NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

As of March
2024

Accounting Practices & Procedures Manual

VOL 1

Preamble

Statements of Statutory Accounting Principles

Appendices A and B

VOL 2

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NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Accounting Practices and Procedures Manual

As of March 2024

VOLUME I

PREAMBLE

STATEMENTS OF STATUTORY ACCOUNTING PRINCIPLES

APPENDIX A – EXCERPTS OF NAIC MODEL LAWS

APPENDIX B – INTERPRETATIONS OF STATUTORY ACCOUNTING PRINCIPLES

NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

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ISBN: 978-1-64179-383-4

Printed in Canada

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MAINTENANCE PROCESS

The Statutory Accounting Principles (E) Working Group maintains codified statutory accounting principles (SAP) by concluding on generally accepted accounting principles (GAAP) or addressing new statutory accounting issues. As revisions are adopted, the corresponding agenda items and issue papers are added to the "Updates" section of the current year's digital version of the *Accounting Practices and Procedures Manual* (Manual).

Email Notification
To receive notification when updates to the Manual are made available, navigate to *https://naicforum.naic.org/statacctupdates.htm* to subscribe to the Statutory Accounting Electronic Updates. The NAIC will retain this database; therefore, if you have previously registered to receive update notices, there is no need to resubmit your request on an annual basis.

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DEDICATION

The *Accounting Practices and Procedures Manual* is dedicated to Norris Clark, California Department of Insurance (retired), Chair of the Codification of Statutory Accounting Principles Working Group, and its successors, the Statutory Accounting Principles and Emerging Accounting Issues (E) Working Groups from September 1994 through July 2004, and to Joseph Fritsch, New York Department of Financial Services (retired), Chair of the Statutory Accounting Principles (E) Working Group from 2004 through December 2012.

Your dedication, leadership, intelligence, and passion were the driving forces behind the creation and continued development of the comprehensive statutory accounting and financial reporting model presented in this publication. Your contributions throughout the years are appreciated and will not be forgotten.

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109	Depreciation of Nonoperating System Software – An Amendment to SSAP No. 16—Electronic Data Processing Equipment and Software
110	Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts, and SSAP No. 56—Separate Accounts
111	Software Revenue Recognition
112	Accounting for the Costs of Computer Software Developed or Obtained for Internal Use and Web Site Development Costs
113	Mezzanine Real Estate Loans
114	Accounting for Derivative Instruments and Hedging Activities
116	Claim Adjustment Expenses, Amendments to SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses
118	Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46
119	Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29, 73, 79 and 82
121	Accounting for the Impairment or Disposal of Real Estate Investments
122	Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
123	Accounting for Pensions, A Replacement of SSAP No. 8
124	Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43

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126	Accounting for Transferable State Tax Credits
127	Exchanges of Nonmonetary Assets, A Replacement of SSAP No. 28—Nonmonetary Transactions
128	Settlement Requirements for Intercompany Transactions, An Amendment to SSAP No.25—Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties
129	Share-Based Payment, A Replacement of SSAP No. 13—Stock Options and Stock Purchase Plans
131	Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment
132	Accounting for Pensions, A Replacement of SSAP No. 89
133	Accounting for Postretirement Benefits Other Than Pensions, A Replacement of SSAP No. 14
134	Servicing Assets/Liabilities, An Amendment of SSAP No. 91
135	Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others
137	Transfer of Property and Casualty Reinsurance Agreements in Run-off
138	Fair Value Measurements
140	Substantive Revisions to SSAP No. 43—Loan-Backed and Structured Securities
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147	Working Capital Finance Investments
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151	Valuation for Holders of Surplus Notes
152	Short Sales
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Appendix H – Superseded SSAPs and Nullified Interpretations

Completely superseded SSAPs and nullified interpretations (INTs) are retained in *Appendix H – Superseded SSAPs and Nullified Interpretations*, which is posted for public reference on the Statutory Accounting Principles (E) Working Group web page at https://content.naic.org/cmte_e_app_sapwg.htm.

SSAP No.	Title
8	Pensions
10	Income Taxes
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13	Stock Options and Stock Purchase Plans
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18	Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
28	Nonmonetary Transactions
31	Derivative Instruments
33	Securitization
45	Repurchase Agreements, Reverse Repurchase Agreements and Dollar Repurchase Agreements
46	Investments in Subsidiary, Controlled, and Affiliated Entities
75	Reinsurance Deposit Accounting—An Amendment to SSAP No. 62R—Property and Casualty Reinsurance
77	Real Estate Sales—An Amendment to SSAP No. 40—Real Estate Investment
79	Depreciation of Nonoperating System Software—An Amendment to SSAP No. 16—Electronic Data Processing Equipment and Software

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SSAP No.	Title
80	Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts, and SSAP No. 56—Separate Accounts
81	Software Revenue Recognition
82	Accounting for the Costs of Computer Software Developed or Obtained for Internal Use and Web Site Development Costs
85	Claim Adjustment Expenses, Amendments to SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses
87	Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29 and 73
88	Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46
89	Accounting for Pensions, A Replacement of SSAP No. 8
91R	Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
96	Settlement Requirements for Intercompany Transactions, An Amendment to SSAP No. 25—Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties
98	Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43
99	Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment
106	Affordable Care Act Section 9010 Assessment

INT No.	Title
99-00	Compilation of Rejected EITFs
99-01	Accounting for Tax Benefits of Operating Losses and Tax Credits in Quasi-Reorganizations
99-02	Accounting for Collateral in Excess of Debt Principal
99-03	Accounting for Investment in Subsidiary, Controlled or Affiliated (SCA) Entities with Subsequent Downstream Investment in an Insurance Company
99-04	Recognition of Prepayment Penalties Upon Adoption of Codification
99-10	EITF 97-8: Accounting for Contingent Consideration Issued in a Purchase Business Combination
99-14	EITF 96-19: Debtor's Accounting for a Modification or Exchange of Debt Instruments
99-16	EITF 97-11: Accounting for Internal Costs Relating to Real Estate Property Acquisitions
99-17	EITF 97-12: Accounting for Increased Share Authorizations in an IRS Section 423 Employee Stock Purchase Plan under APB Opinion No. 25
99-18	EITF 97-13: Accounting for Costs Incurred in Connection with a Consulting Contract or an Internal Project That Combines Business Process Reengineering and Information Technology Transformation
99-21	EITF 98-7: Accounting for Exchanges of Similar Equity Method Investments
99-22	EITF 98-8: Accounting for Transfers of Investments That Are in Substance Real Estate
99-23	Disclosure of Premium Deficiency Reserves
99-24	Accounting for Restructuring Charges
99-25	Accounting for Capital Improvements
99-26	Offsetting Pension Assets and Liabilities
99-27	Nonadmitting Installment Receivables
99-28	Accounting for SCA Mutual Funds, Broker-Dealers and Similar Entities Under SSAP No. 46
99-29	Classification of Step-Up Preferred Stock
00-01	Investment in Foreign SCA Entity
00-02	Accounting for Leveraged Leases Involving Commercial Airplanes Under SSAP No. 22—Leases
00-04	Student Loan Insurance
00-05	Exemption to Merger Disclosure in SSAP No. 3

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INT No.	Title
00-06	EITF 97-14: Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested
00-08	EITF 98-5: Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios
00-10	EITF 98-14: Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements
00-11	EITF 98-15: Structured Notes Acquired for a Specified Investment Strategy
00-12	EITF 99-4: Accounting for Stock Received from the Demutualization of a Mutual Insurance Company
00-21	Disclose Requirement of SSAP No. 10 Paragraphs 17 & 18
00-22	Application of SSAP No. 10 to Admissibility of Deferred Tax Assets
00-23	Reinsurance of Deposit Type Contracts
00-27	EITF 98-9: Accounting for Contingent Rent
00-29	EITF 99-17: Accounting for Advertising Barter Transactions
00-30	Application of SSAP No. 51 Paragraph 6 to Waiver of Deduction on Flexible Premium Universal Life Insurance Policies
00-31	Application of SSAP No. 55 Paragraph 13 to Health Entities
00-32	EITF 00-8: Accounting by a Grantee for an Equity Instrument to Be Received in Conjunction with Providing Goods or Services
01-01	Application of SSAP No. 6 Paragraph 9.a. to de minimus Receivable Balances of Group Accident and Health Policies
01-03	Assets Pledged as Collateral or Restricted for the Benefit of a Related Party
01-04	SSAP Nos. 18 and 33 and Issues Surrounding Securitizations
01-05	Classification of Accrued Interest on Policy Loans
01-07	EITF 98-2: Accounting by a Subsidiary or Joint Venture for an Investment in the Stock of Its Parent Company or Joint Venture Partner
01-10	EITF 00-1: Investor Balance Sheet and Income Statement Display under the Equity Method for Investments in Certain Partnerships and Other Ventures
01-11	EITF 00-10: Accounting for Shipping and Handling Fees and Costs
01-12	EITF 00-14: Accounting for Certain Sales Incentives
01-14	EITF 00-16: Recognition and Measurement of Employer Payroll Taxes on Employee Stock-Based Compensation
01-16	Measurement Date for SSAP No. 8 Actuarial Valuations
01-17	Accounting for Nonqualified Retirement Plans, Nonvested Ancillary Benefits Within Retirement Plans, and Protected Benefits Such as Early Retirement Subsidies in Retirement Plans
01-19	Measurement of Deferred Tax Assets Associated with Nonadmitted Assets
01-20	Utilization of Tax Planning Strategies for the Admissibility of Deferred Tax Assets
01-21	SSAP Nos. 16R, 19, 68 and 79 – Reestablishment of Previously Expensed Software and Furniture, Fixtures and Equipment and Goodwill
01-22	Use of Interim Financial Statements in Computing Reporting Entity's Investment in Subsidiary Under the GAAP Equity Method
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01-24	Application of SSAP No. 46 and 48 to Certain Noninsurance Subsidiary, Controlled or Affiliated Entities
01-26	SSAP No. 51 and Reserve Minimum or Required Amount
01-27	Accounting Change versus Correction of Error
01-28	Margin for Adverse Deviation in Claim Reserve
01-29	SSAP No. 59 and Application to Credit Life
01-32	EITF 01-10: Accounting for the Impact of the Terrorist Attacks of September 11, 2001
01-33	Extension of 9-Month Rule in SSAP No. 62R
02-01	Disclosure Requirements Under SSAP for Differences Between A-785 and Individual State Requirements as a Result of September 11

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INT No.	Title
02-02	SSAP No. 6 and Billing of Premium Before Effective Date
02-03	Accounting for the Impact of the Terrorist Attacks of September 11th on Commercial Mortgage Loans
02-04	Recognition of CARVM and CRVM Expense Allowances by the Assuming Reinsurer in a Modified Coinsurance Agreement
02-05	Accounting for Zero Coupon Convertible Bonds
02-06	Indemnification in Modeled Trigger Transactions
02-07	Definition of Phrase "Other Than Temporary"
02-08	Application of A-791 to YRT Reinsurance of a Block of Business
02-09	A-785 and Syndicated Letters of Credit
02-10	Statutory Audit Report Notes and the Reporting Requirements Related to Disclosures Containing Multiple Year Information
02-11	Recognition of Amounts Related to Earned but Unbilled Premium
02-15	EITF 00-11: Lessors' Evaluation of Whether Leases of Certain Integral Equipment Meet the Ownership Transfer Requirements of FASB Statement 13
02-17	EITF 01-13: Income Statement Display of Business Interruption Insurance Recoveries
02-18	Accounting for the Intangible Asset as Described in SSAP No. 8 Paragraphs 9.d.v. and 9.f.
02-19	EITF 01-1: Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash
02-20	Due Date for Installment Premium Under an Agency Relationship
02-21	Accounting for Prepaid Loss Adjustment Expenses and Claim Adjustment Expenses
03-01	Application of SSAP No. 35 to the Florida Hurricane Catastrophe Fund
03-03	Admissibility of Investments Recorded Based on the Audited GAAP Equity of the Investee when a Qualified Opinion is Provided
03-05	EITF 01-07: Creditor's Accounting for a Modification or Exchange of Debt Instruments
03-12	EITF 02-4: Determining Whether a Debtor's Modification or Exchange of Debt Instruments is within the Scope of FASB Statement No. 15
03-16	Contribution of Stock
03-17	Classification of Liabilities from Extra Contractual Obligation Lawsuits
03-18	Accounting for a Change in the Additional Minimum Liability in SSAP No. 8—Pensions (SSAP No. 8)
04-01	Applicability of New GAAP Disclosures Prior to NAIC Consideration
04-02	Surplus Notes Issued by Entities Under Regulatory Action
04-03	Clarification for Calculating the Additional Minimum Pension Liability Under SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8, paragraph 16.f.
04-05	Clarification of SSAP No. 5R Guidance on when a Judgment is Deemed Rendered
04-07	EITF 02-15: Determining Whether Certain Conversions of Convertible Debt to Equity Securities Are Within the Scope of FASB Statement No. 84
04-10	EITF 02-18: Accounting for Subsequent Investments in an Investee after Suspension of Equity Method Loss Recognition
04-12	EITF 03-4: Determining the Classification and Benefit Attribution Method for a "Cash Balance" Pension Plan
04-13	EITF 03-5: Applicability of AICPA Statement of Position 97-2 to Non-Software Deliverables in an Arrangement Containing More-Than-Incidental Software
04-15	EITF 03-07: Accounting for the Settlement of the Equity-Settled Portion of a Convertible Debt Instrument That Permits or Requires the Conversion Spread to Be Settled in Stock (Instrument C of Issue No. 90-19)
04-18	EITF 00-21: Revenue Arrangements with Multiple Deliverables
04-20	EITF 01-08: Determining Whether an Arrangement Contains a Lease
05-04	Extension of Ninety-day Rule for the Impact of Hurricane Katrina, Hurricane Rita and Hurricane Wilma
05-06	Earned But Uncollected Premium

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INT No.	Title
06-14	Reporting of Litigation Costs Incurred for Lines of Business in which Legal Expenses Are the Only Insured Peril
07-03	EITF 06-3: How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation)
08-02	EITF 06-8: Applicability of the Assessment of a Buyer's Continuing Investment under FASB Statement No. 66 for Sales of Condominiums
08-03	EITF 06-9: Reporting a Change in (or the elimination of) a Previously Existing Difference between the fiscal Year-End of a Parent Company and That of a Consolidated Entity or between the Reporting Period of an Investor and That of an Equity Method Investee
08-04	EITF 07-3: Accounting for Nonrefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities
08-06	FSP EITF 00-19-2: Accounting for Registration Payment Arrangements
08-07	EITF 07-6: Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66 When the Agreement Includes a Buy-Sell Clause
08-08	Balance Sheet Presentation of Funding Agreements Issued to a Federal Home Loan Bank
08-10	Contractual Terms of Investments and Investor Intent
09-03	EITF 08-7: Accounting for Defensive Intangible Assets
09-04	Application of the Fair Value Definition
09-05	EITF 08-3: Accounting by Lessees for Maintenance Deposits
09-08	Accounting for Loans Received under the Federal TALF Program
13-01	Extension of Ninety-Day Rule for the Impact of Hurricane/Superstorm Sandy
13-03	Clarification of Surplus Deferral in SSAP No. 92 & SSAP No. 102
13-04	Accounting for the Risk-Sharing Provisions of the Affordable Care Act
16-01	ACA Section 9010 Assessment 2017 Moratorium
17-01	Extension of Ninety-Day Rule for the Impact of Hurricane Harvey, Hurricane Irma and Hurricane Maria
18-01	Updated Tax Estimates Under the Tax Cuts and Jobs Act
18-02	ACA Section 9010 Assessment Moratoriums
18-04	Extension of Ninety-Day Rule for the Impact of Hurricane Florence and Hurricane Michael
19-01	Extension of Ninety-Day Rule for the Impact of California Camp Fire, Hill Fire and Woolsey Fire
20-02	Extension of Ninety-Day Rule for the Impact of COVID-19
20-03	Troubled Debt Restructuring Due to COVID-19
20-04	Mortgage Loan Impairment Assessment Due to COVID-19
20-05	Investment Income Due and Accrued
20-07	Troubled Debt Restructuring of Certain Debt Investments Due to COVID-19
20-08	COVID-19 Premium Refunds, Limited-Time Exception, Rate Reductions and Policyholder Dividends
20-10	Reporting Nonconforming Credit Tenant Loans
20-11	Extension of Ninety-Day Rule for the Impact of 2020 Hurricanes, California Wildfires and Iowa Windstorms
21-02	Extension of Ninety-Day Rule for the Impact of Hurricane Ida
23-02	Third Quarter 2023 Inflation Reduction Act – Corporate Alternative Minimum Tax

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How to Use This Manual

The contents of this Manual are arranged as follows:

Introduction

Maintenance Process and Ordering Information
Table of Contents
How to Use This Manual
Summary of Changes to Prior Edition of the Manual

Volume I:

Preamble
Statements of Statutory Accounting Principles
Index and Glossary to Statements of Statutory Accounting Principles
Appendix A – Excerpts of NAIC Model Laws
Appendix B – Interpretations of Statutory Accounting Principles

Volume II:

Appendix C – Actuarial Guidelines
Appendix D – GAAP Cross-Reference to SAP
Appendix E – Issue Papers Associated with SSAPs Adopted in 2023
Appendix F – Policy Statements
Appendix G – Implementation Guide for the Model Audit Rule

Historical Contents:

(Posted for public reference on the Statutory Accounting Principles (E) Working Group web page at *https://content.naic.org/cmte_e_app_sapwg.htm.)*

Appendix E – Issue Papers Associated with SSAPs Adopted Prior to 2023
Appendix H – Superseded SSAPs and Nullified Interpretations

The arrangement of material as indicated above is included in the Table of Contents found at the front of each volume of the Manual. A table of contents also precedes each appendix referencing the material within.

Summary of Changes:

The Summary of Changes outlines changes made to the prior edition of the Manual to create the current year's version. It is divided into three sections: 1) the development of new SSAPs or new SAP concepts to existing SSAPs; 2) SAP clarifications; and 3) revisions to the appendices included in the Manual. The Summary of Changes is a key resource for readers who are looking to identify changes from the prior edition.

Preamble:

Many state insurance regulators consider the Preamble one of the most important sections of the Manual as it provides the foundation for statutory accounting principles (SAP). Some of the significant topics covered in the Preamble include codification project background, statement of concepts, statutory hierarchy, materiality and disclosures.

Statements of Statutory Accounting Principles:

As indicated by the Statutory Hierarchy, the Statements of Statutory Accounting Principles (SSAPs) are the primary authoritative statutory accounting practices and procedures promulgated by the NAIC. These statements are the result of issue papers that have been exposed for public comment and finalized. Finalized issue papers are found in Appendix E and ARE NOT authoritative. While it is not intended that there be any significant differences between an underlying issue paper and the resultant

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SSAP, if differences exist, the SSAP prevails and shall be considered definitive. Readers may use the NAIC website to keep abreast of adopted revisions to the SSAPs. Completely superseded SSAPs that are no longer authoritative are moved from the Manual into *Appendix H – Superseded SSAPs and Nullified Interpretations*, which is posted for public reference on the Statutory Accounting Principles (E) Working Group web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

Prior to January 1, 2022, the term used to describe a new SAP concept or a new SAP concept in an existing SSAP was "substantive" and the term used to describe a SAP clarification was "nonsubstantive." The new terms will be reflected in materials to describe revisions to statutory accounting principles on a prospective basis and historical documents will not be updated to reflect the revised terms.

The cover page of each SSAP contains a STATUS section that can affect the implementation of each SSAP. The STATUS section contains the following:

TYPE OF ISSUE – SSAPs designated as Common Area apply to all insurers. Although the nomenclature or terms provided in the prescribed annual statement forms may vary among different types of insurers, only one set of nomenclature or terms may have been used in the SSAP. For example, the Statement of Income found in the Property and Casualty Annual Statement shall be considered as synonymous with the Summary of Operations found in the Life and Health Annual Statement.

ISSUED – Date when the SSAP was adopted by the NAIC. SSAPs designated with Initial Draft were adopted by the NAIC Plenary in March 1998 as part of the Codification Project (SSAP Nos. 1-73). The date included for SSAP No. 74, and subsequent SSAPs, denotes when the Statutory Accounting Principles (E) Working Group adopted the SSAP.

EFFECTIVE DATE – Date representing when the SSAP is effective. Many times, there are additional details relative to the transition provided within the SSAP.

AFFECTS/AFFECTED BY – A useful tool for tracking relationships between statements and interpretations is contained within these sections. The "affects" section is used when a SSAP has previously been amended to reflect new SAP concepts or superseded by other issued SSAPs. Nullified INTs are also noted in this section. Readers are referenced to another SSAP in the "affected by" section if the SSAP has been superseded or amended with a new SAP concept or with the issuance of a new SSAP. Text within paragraphs amended with new SAP concepts or superseded may also be "shaded" to notify readers that revised guidance is available.

INTERPRETED BY – This section includes a reference to the applicable interpretation (INT) of statutory accounting principles contained within Appendix B of the Manual which provides interpretative guidance as a result of issues raised by users of the Manual or related GAAP guidance. INTs are generally effective when adopted. Readers should note that the Manual only contains the INTs finalized through year end prior to publication, due to the fact that the Manual is published annually. Readers may use the NAIC website, as indicated on the inside front cover of the Manual, to keep abreast of recently issued INTs.

RELEVANT APPENDIX A GUIDANCE – This section identifies the relevant *Appendix A—Excerpts from NAIC Model Laws* guidance referenced within the SSAP.

Refer to the Relevant Literature and Effective Date and Transition sections of each SSAP for details of the development of new SSAPs or new SAP concepts, as well as changes as the result of SAP clarifications.

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Appendix A – Excerpts of NAIC Model Laws:

In most cases, the source document for information included in Appendix A is an NAIC Model Regulation or Law. These Appendices are referenced by specific SSAPs and should only be used in context of the Appendix and the SSAP that references it.

Appendix B – Interpretations of Statutory Accounting Principles:

The Statutory Accounting Principles (E) Working Group (SAPWG) is responsible for responding to SAP questions that generally relate to application, interpretation and clarification. Appendix B includes the final interpretations (INTs) of statutory accounting principles through year end prior to publication. Once an INT is finalized, the related SSAP will contain reference to the applicable INT. Nullified INTs are moved from the Manual into *Appendix H – Superseded SSAPs and Nullified Interpretations*, which is posted for public reference on the SAPWG web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

Appendix C – Actuarial Guidelines:

The NAIC Life Actuarial (A) Task Force and Health Actuarial (B) Task Force have been asked on many occasions to assist a particular state insurance department in interpreting a statute dealing with an actuarial topic relative to an unusual policy form or situation not contemplated at the time of original drafting of a particular statute. The Life Actuarial (A) Task Force and Health Actuarial (B) Task Force, in developing interpretations or guidelines, must often consider the intent of the statute, the reasons for initially adopting the statute and the current situation. The Life Actuarial (A) Task Force and Health Actuarial (B) Task Force feel that for those situations which are sufficiently common to all states, the publishing of actuarial guidelines on these topics would be beneficial to the regulatory officials in each state and would promote uniformity in regulation which is beneficial to everyone. To this end, the Life Actuarial (A) Task Force and Health Actuarial (B) Task Force have developed certain actuarial guidelines and will continue to do so as the need arises. The guidelines are not intended to be viewed as statutory revisions but merely a guide to be used in applying a statute to a specific circumstance.

Appendix D – GAAP Cross-Reference to SAP:

As expressed in the Statement of Concepts, SAP utilizes the framework established by U.S. Generally Accepted Accounting Principles (GAAP). Appendix D includes GAAP pronouncements that have been considered in the development of SAP. This listing includes GAAP pronouncements issued through year end prior to publication. This Appendix is a valuable and efficient tool for readers who are interested in the status of a particular GAAP pronouncement in the SAP model.

Appendix E – Issue Papers:

Appendix E includes issue papers associated with SSAPs adopted through year end prior to publication of the Manual. Issue papers are used as the first step in developing new SSAPs and contain a recommended conclusion, discussion and relevant literature section. Issue papers **DO NOT** constitute an authoritative level of statutory accounting, as supported by the statutory hierarchy, and should only be used as reference material. Nevertheless, issue papers are important because they reference the history and discussion of a related SSAP. The "Relevant Statutory Accounting and GAAP Guidance" section of the issue paper contains excerpts of accounting guidance considered, but not necessarily adopted, by the Statutory Accounting Principles (E) Working Group (SAPWG) when forming the conclusions reached in the resultant SSAP. Historical issue papers associated with SSAPs adopted prior to the current year are posted for public reference on the SAPWG web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

Appendix F – Policy Statements:

Appendix F includes NAIC policy statements applicable to SAP. These statements provide the basis by which SAP is maintained, documentation of the agenda process and other important issues that affect the Manual.

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Appendix G – Implementation Guide for Model Audit Rule:

Appendix G contains the NAIC Implementation Guide for the Model Audit Law. The Implementation Guide has been included for informational purposes only and should not be viewed as a requirement of complying with the *Accounting Practices and Procedures Manual*.

Appendix H – Superseded SSAPs and Nullified Interpretations:

Appendix H contains superseded SSAPs and nullified interpretations and is posted for public reference on the Statutory Accounting Principles (E) Working Group web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

How to Use This Manual …

... to account for a certain item under NAIC SAP

As the SSAPs represent the highest level of NAIC statutory authority, readers should begin their search there. The Index to SSAPs is a useful tool to identify which SSAP(s) address the issue. Once the pertinent SSAP has been identified, it can be used to locate other documents that may also address the issue. On the SSAP cover page, readers will be referred to other SSAPs if there have been substantive changes made to it or INTs if there have been interpretations of the SSAP. Within the body of the SSAP, readers may be referred to Appendix A or C for further guidance. There is a reference located at the end of each SSAP to issue paper(s) used in the development of the SSAP. The DISCUSSION section of the issue paper provides documentation supporting the conclusions reached in the SSAP. As supported by the statutory hierarchy, readers should only utilize the issue papers as support to the SSAP as they ARE NOT authoritative. The Statutory Hierarchy contains a detailed listing of levels of authoritative literature.

... to compare SAP to GAAP for a particular issue

Appendix D is an excellent reference for readers who are interested in determining how SAP addresses an issue that has been adopted by GAAP. Appendix D provides a reference to the SSAP or INT that addresses a particular GAAP pronouncement. As indicated in the Preamble, readers should not utilize GAAP until and unless adopted by the NAIC. Within the body of the applicable SSAP or INT, readers will find documentation as to the reason for adoption, rejection, or adoption with modification of a particular GAAP pronouncement.

... to identify the relationship between the Manual and State law

Once a reader has identified the accounting treatment for a particular transaction or issue within the Manual, one must consider the effect of state law. That is, the Manual is not intended to preempt states' legislative and regulatory authority. It is intended to establish a comprehensive basis of accounting recognized and adhered to if not in conflict with state statutes and/or regulations, or when the state statutes and/or regulations are silent. For instance, if a state prohibits the admission of goodwill, insurers domiciled in that state are required to nonadmit all goodwill instead of following the NAIC guidance contained within *SSAP No. 68—Business Combinations and Goodwill*. Insurers should refer to their state laws and regulations regarding deviations from the Manual.

... to obtain updates to the latest published Manual

Each year there will be modifications to the accounting pronouncements included in the Manual. As such, guidance is subject to the maintenance process. To address this, the NAIC provides updates on the latest information impacting statutory accounting. To learn more about how to obtain updates to the latest published Manual, refer to the Maintenance Process page, which precedes the Table of Contents.

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... to learn how changes are made to the Manual and how to stay abreast of such changes

Appendix F contains several NAIC policy statements that document the process by which the Manual will be modified. It also outlines the process by which the Statutory Accounting Principles (E) Working Group (SAPWG) will conduct its business. Users of the Manual can track the development of SAP by attending the national meetings of the SAPWG or through use of the NAIC website at *https://content.naic.org*.

... to contact the NAIC regarding questions about the Manual

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Summary of Changes to the *As of March 2023 Accounting Practices and Procedures Manual* included in the As of March 2024 Manual

The following summarizes changes made to the *As of March 2023 Accounting Practices and Procedures Manual* (Manual) and shown in the As of March 2024 version.

Section 1 summarizes revisions that result in a new SSAP or new SAP concept to statutory accounting principles. Revisions that introduce original or modified accounting principles can be reflected in an existing or new SSAP. When revisions that result in a new SAP concept are made to an existing SSAP, the effective date is identified in the Status section, New SSAPs and new SAP concepts that revise existing SSAPs are commonly accompanied by a corresponding issue paper that reflects the tracked revisions for historical purposes. If language in an existing SSAP is superseded, that language is shaded and the new or revised SSAP is referenced. Completely superseded SSAPs and nullified interpretations are included in Appendix H.

Section 2 summarizes revisions that clarify existing statutory accounting principles. These revisions are characterized as language clarifications which do not modify the original intent of a SSAP, or changes to reference material. Such revisions are depicted by underlines (new language) and strikethroughs (removed language) and will not be tracked in subsequent manuals. Revisions that clarify existing statutory accounting principles are effective when adopted unless a specific effective date is noted.

Section 3 summarizes revisions to the Manual appendices.

PENDING CONTENT ALERT – BOND PROJECT - Effective January 1, 2025
Adopted revisions in 2023 which are effective January 1, 2025, as a result of the ongoing Principles-Based Bond Project are available on the Statutory Accounting Principles (E) Working Group web page at https://content.naic.org/cmte_e_app_sapwg.htm. Revisions specifically impacting *SSAP No. 26R—Bonds*, *SSAP No. 43R—Loan-Backed and Structured Securities*, various other SSAPS, and the annual statement instructions will be documented in the *As of March 2025 Accounting Practices and Procedures Manual*.

1. Revisions that Resulted in a New SSAP or New SAP Concept – Statutory Accounting Principles		
Section	**Reference**	**Description**
No revisions that resulted in a new SSAP or new SAP concept were adopted in 2023.		
2. Revisions that Resulted in a SAP Clarification – Statutory Accounting Principles		
Section	**Reference**	**Description**
SSAP No. 2R	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 5R	2022-01	Revisions clarify the definition of a liability under statutory accounting to be more consistent with recent FASB revisions and are historically documented in *Issue Paper No. 168—Updates to the Definition of a Liability.*
	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
	2023-18	Revisions adopt with modification *ASU 2016-19, Technical Corrections and Improvements* and standardize the terminology used for insurance contracts regarding pension and other post-retirement benefits.

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	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 16R	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 20 SSAP No. 21R	2022-11	Revisions include consistency revisions to SSAP No. 20. Revisions to SSAP No. 21R provide more detail on qualifying collateral for collateral loans, require information to support fair value of collateral to be available on request, and provide audit transition guidance for equity collateral.
SSAP No. 22R	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 24	2023-06	Revisions reject *ASU 2021-10, Government Assistance* while incorporating certain disclosures regarding government assistance.
SSAP No. 25	2022-15	Revisions clarify that any invested asset held by a reporting entity which is issued by an affiliated entity, or which includes the obligations of an affiliated entity, is an affiliated investment.
	2023-11EP	Revisions streamline citations to *the Purposes and Procedures Manual of the NAIC Investment Analysis Office* so they do not reflect a specific location in the P&P Manual or a webpage.
SSAP No. 26R	2023-11EP	Revisions streamline citations to *the Purposes and Procedures Manual of the NAIC Investment Analysis Office* so they do not reflect a specific location in the P&P Manual or a webpage.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 30R	2023-11EP	Revisions streamline citations to *the Purposes and Procedures Manual of the NAIC Investment Analysis Office* so they do not reflect a specific location in the P&P Manual or a webpage.
	2023-23	Revisions clarify that investments that are in-substance residual interests shall be reported on Schedule BA on the dedicated reporting line for residuals.
SSAP No. 32R	2023-11EP	Revisions streamline citations to *the Purposes and Procedures Manual of the NAIC Investment Analysis Office* so they do not reflect a specific location in the P&P Manual or a webpage.
	2023-23	Revisions clarify that investments that are in-substance residual interests shall be reported on Schedule BA on the dedicated reporting line for residuals.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.

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SSAP No. 34	2022-17	Revisions add additional disclosures in SSAP No. 34 to data capture the gross, nonadmitted and admitted amounts of interest income due and accrued, and to reflect the cumulative amount of paid-in-kind (PIK) interest income included in the current principal balance.
	2023-13	Revisions clarify and incorporate a practical expedient to the paid-in-kind (PIK) interest aggregate disclosure for *SSAP No. 34—Investment Income Due and Accrued* and proposed annual statement instructions.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 37 SSAP No. 39 SSAP No. 41R	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 43R	2023-02	Revisions incorporate changes to add collateralized loan obligations (CLOs) to the financial modeling guidance and to clarify that CLOs are not captured as legacy securities.
	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
	2023-12	Revisions for the reporting of residual interests, so that all residuals are captured on the dedicated Schedule BA – Other Long-Term Invested Assets reporting lines.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 47	2023-07	Revisions adopt with modification *ASU 2019-08, Stock Compensation and Revenue with Contracts from Customers* to provide guidance on share-based consideration payable to customers.
SSAP No. 48	2023-12	Revisions for the reporting of residual interests, so that all residuals are captured on the dedicated Schedule BA – Other Long-Term Invested Assets reporting lines.
SSAP No. 50 SSAP No. 51R SSAP No. 52	2023-10	Revisions reject *ASU 2022-05, Transition for Sold Contracts* as not applicable for statutory accounting.
SSAP No. 54R	2023-22	Revisions clarify that gross premium valuation (under *A-010, Minimum Reserve Standards for Individual and Group Health*) and cash-flow testing (under *Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves*) are both required if indicated.
SSAP No. 56	2023-10	Revisions reject *ASU 2022-05, Transition for Sold Contracts* as not applicable for statutory accounting.
SSAP No. 57 SSAP No. 60	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 61R	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.

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SSAP No. 62R	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 65	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 71	2023-10	Revisions reject *ASU 2022-05, Transition for Sold Contracts* as not applicable for statutory accounting.
SSAP No. 78	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 86	2023-11EP	Revisions change SSAP No. 86 references of "Intrinsic Value" to reflect "Volatility Value". In addition, "percent" is changed to "%" to maintain consistency throughout the Manual.
	2023-10	Revisions reject *ASU 2022-05, Transition for Sold Contracts* as not applicable for statutory accounting.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 92	2023-18	Revisions adopt with modification *ASU 2016-19, Technical Corrections and Improvements* and standardize the terminology used for insurance contracts regarding pension and other post-retirement benefits.
	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
	2023-21	Revisions to remove the initial transition guidance as the 10-year effective period of the guidance has expired.
SSAP No. 93	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 95	2023-07	Revisions adopt with modification *ASU 2019-08, Stock Compensation and Revenue with Contracts from Customers* to provide guidance on share-based consideration payable to customers.
SSAP No. 97	2023-11EP	Revisions streamline citations to *the Purposes and Procedures Manual of the NAIC Investment Analysis Office* so they do not reflect a specific location in the P&P Manual or a webpage.
SSAP No. 100R	2022-16	Revisions adopt with modification the fair value measurement guidance from *ASU 2022-03, Fair Value Measurement of Restricted Securities* to incorporate updated guidance for restricted securities for statutory accounting. The disclosures from ASU 2022-03 were not adopted.
	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 101	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
SSAP No. 102	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.

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	2023-18	Revisions adopt with modification *ASU 2016-19, Technical Corrections and Improvements* and standardize the terminology used for insurance contracts regarding pension and other post-retirement benefits.
	2023-21	Revisions to remove the initial transition guidance as the 10-year effective period of the guidance has expired.
SSAP No. 103R	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
	2023-18	Revisions adopt with modification *ASU 2016-19, Technical Corrections and Improvements* and standardize the terminology used for insurance contracts regarding pension and other post-retirement benefits.
SSAP No. 104R	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.
	2023-07	Revisions adopt with modification *ASU 2019-08, Stock Compensation and Revenue with Contracts from Customers* to provide guidance on share-based consideration payable to customers.
SSAP No. 105R	2022-18	Revisions reject *ASU 2022-04, Disclosure of Supplier Finance Program Obligations* for statutory accounting.
	2023-24	Revisions reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
SSAP No. 108	2023-11EP	Revisions change "percent" to "%" to maintain consistency throughout the Manual.

3. Revisions to the Appendices

Section	Reference	Description
Appendix A		*No revisions impacting this appendix were adopted in 2023.*
Appendix B	2023-24 INT 06-07	Revisions to *INT 06-07: Definition of Phrase "Other Than Temporary"* reject *ASU 2016-13, Financial Instruments—Credit Losses* and related subsequent ASUs. These revisions reject current expected credit losses (CECL) for statutory accounting.
	2023-05 INT 20-01	Revisions to *INT 20-01: ASUs 2020-04, 2021-01 & 2022-06 – Reference Rate Reform* which provides a temporary (optional) expedient and exception interpretative guidance to revise the expiration date of the guidance in INT 20-01 to December 31, 2024.
	INT 22-02	Revisions to *INT 22-02: Third Quarter 2022 through Second Quarter 2023 Reporting of the Inflation Reduction Act – Corporate Alternative Minimum Tax* extend this interpretation for the second quarter 2023 statutory financial statements.
	2022-19 INT 23-01	*INT 23-01: Net Negative (Disallowed) Interest Maintenance Reserve* provides an optional, limited-time guidance, which allows the admittance of net negative (disallowed) interest maintenance reserve (IMR) up to 10% of adjusted capital and surplus. INT 23-01 will be automatically nullified on January 1, 2026.

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	2023-04 INT 23-03	*INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax* provides guidance for CAMT reporting on or after year-end 2023 and addresses accounting, the statutory valuation allowance, admissibility, disclosures, and year-end 2023 transition.
	INT 23-04	*INT 23-04: Scottish Re Life Reinsurance Liquidation Questions* provides accounting and reporting guidance for entities ceding to the life reinsurer in liquidation.
Appendix C	AG 49-A	Revisions to AG 49-A improve illustrations for indexed universal life (IUL) products with uncapped volatility-controlled funds and a fixed bonus. The guideline applies to policies sold on or after May 1, 2023.
	AG 54	This new guideline specifies the conditions under which an Index-Linked Variable Annuity (ILVA) is consistent with the definition of a variable annuity and exempt from *Standard Nonforfeiture Law for Individual Deferred Annuities* (#805) and specifies nonforfeiture requirements consistent with variable annuities. The guideline applies to all contracts (including associated riders, endorsements, or amendments) issued on or after July 1, 2024.
Appendix D	Rejected as Not Applicable to Statutory Accounting:	
	2023-08	*ASU 2019-07, Codification Updates to SEC Sections*
	2023-09	*ASU 2020-09, Amendments to SEC Paragraphs Pursuant to SEC Release No. 33-10762, Debt (Topic 470)*
	2023-19	*ASU 2018-09, Codification Improvements*
	2023-20	*ASU 2020-10, Codification Improvements*
Appendix E	IP No. 167	*Issue Paper No. 167—Derivatives and Hedging* details the historical actions of the authoritative guidance resulting in new SAP concepts adopted in August 2022 within *SSAP No. 86—Derivatives*.
	IP No. 168	*Issue Paper No. 168—Updates to the Definition of a Liability* documents revisions to *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets* to align the definition of a liability with the term utilized by the Financial Accounting Standards Board (FASB).
Appendix F		*No revisions impacting this appendix were adopted in 2023.*
Appendix G		*No revisions impacting this appendix were adopted in 2023.*
Appendix H	INT 23-02	*INT 23-02: Third Quarter 2023 Inflation Reduction Act – Corporate Alternative Minimum Tax*; Adoption provided guidance for third quarter 2023 CAMT reporting and required disclosures, but not accrual of a liability; automatically nullified on November 16, 2023.

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NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Accounting Practices and Procedures Manual

As of March 2023

VOLUME I

PREAMBLE

STATEMENTS OF STATUTORY ACCOUNTING PRINCIPLES

APPENDIX A – EXCERPTS OF NAIC MODEL LAWS

APPENDIX B – INTERPRETATIONS OF STATUTORY ACCOUNTING PRINCIPLES

Statutory Accounting Principles
Preamble

Section VII Interpreted by: INT 00-20

I. History of Accounting Practices and Procedures Promulgated by the NAIC

A. Background

1. The NAIC, through its committees and working groups, facilitated many projects of importance to the insurance regulators, industry and users of statutory financial information. That was evidenced by the mission statement and charges of the NAIC Accounting Practices and Procedures (E) Task Force of the Financial Condition (E) Committee.

2. The mission of the Accounting Practices and Procedures (E) Task Force was to identify, investigate and develop solutions to accounting problems with the ultimate goal of guiding insurers in properly accounting for various aspects of their operations and to modify the NAIC *Accounting Practices and Procedures Manuals for Property and Casualty Insurance Companies*, *for Life, Accident and Health Insurance Companies*, and *for Health Maintenance Organizations* (Accounting Practices and Procedures manuals) to reflect changes necessitated by task force action and to study innovative insurer accounting practices which affect the ability of regulators to determine the true financial condition of insurers.

3. To carry out the mission, the Accounting Practices and Procedures (E) Task Force was charged with carrying out the following initiatives:

- Provide authoritative guidance to insurance regulators on current statutory accounting issues.
- Continue evaluation of statutory accounting principles for purposes of development, expansion and codification.
- Extend evaluation of statutory accounting principles to address areas specific to health entities.
- The Codification of Statutory Accounting Principles (E) Working Group (Statutory Accounting Principles (E) Working Group as of January 1, 2000) will maintain codified statutory accounting principles by providing periodic updates to the guidance which address new statutory issues and new generally accepted accounting principles (GAAP) pronouncements as they develop.

4. The comprehensive guide to statutory accounting principles, composed of the Preamble, the Statements of Statutory Accounting Principles (SSAPs), and the Appendices, was intended to respond to the initiatives noted above. The guide and interpretations of the Emerging Accounting Issues (E) Working Group was referred to as the *Accounting Practices and Procedures Manual* - version effective January 1, 2001 (during the transition period until the 1998 version was no longer maintained and updated by the NAIC). The 1998 version of the *Accounting Practices and Procedures Manual* was maintained and

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published until December 31, 2000. However, the Manual was not intended to preempt states' legislative and regulatory authority. It was intended to establish a comprehensive basis of accounting recognized and adhered to if not in conflict with state statutes and/or regulations, or when the state statutes and/or regulations are silent.

B. Purpose of Codification

5. The purpose of the codification of statutory accounting principles was to produce a comprehensive guide to SAP for use by insurance departments, insurers, and auditors. Statutory accounting principles, as they existed prior to codification did not always provide a consistent and comprehensive basis of accounting and reporting. The prescribed or permitted statutory accounting model resulted in practices that could have varied from state to state. Insurance companies were sometimes uncertain about what rules to follow and regulators were sometimes unfamiliar with the accounting rules followed by insurers in other states. As a result, insurers' financial statements were not always prepared on a comparable basis.

6. As part of the codification project, it was necessary to revisit principles that had been developed over a long period of time and to consider identified accounting issues not addressed by SAP. In many cases, previously available choices of accounting methods were eliminated. Also considered was the current state of the regulatory environment and the tools developed, such as risk-based capital (RBC). Those financial analytical tools allowed for a reconsideration of the level of conservatism necessary to achieve regulatory objectives.

7. The Codification project resulted in more complete disclosures and more comparable financial statements, making the insurance departments' analysis techniques more meaningful and effective. The project provided examiners and analysts with uniform accounting rules against which companies' financial statements could be evaluated. RBC, an important tool used by the states to measure solvency of insurers, is reported more consistently with the benefit of codification.

C. History of Codification

8. In 1989, the NAIC adopted a Solvency Agenda designed to enhance the ability of state regulators to protect insurance consumers from the financial trauma of insurer insolvency. In recognition of the fact that enhancement of solvency regulation is an ongoing process, the agenda was updated in 1991. Since 1991, most major initiatives of the 1991 Solvency Agenda have been accomplished. They include: 1) revision of the NAIC *Financial Condition Examiners Handbook*, 2) development of a risk-based capital approach to define required levels of capital and surplus, 3) development of a model law on authorized insurer investments, 4) creation of a centralized financial analysis unit to perform comprehensive analysis of insurance companies who may be troubled, 5) development of computerized analytical routines for use by state insurance departments, and 6) creation of an NAIC education fund.

9. The codification project was a direct result of the 1991 Solvency Agenda. The goal was "evaluation of existing statutory accounting principles as presently outlined in the *Accounting Practices and Procedures Manual* for purposes of further development, expansion, and codification."

10. Beginning in 1994, the NAIC's efforts to codify SAP were strengthened and reorganized recognizing the need for expediency. There was both a commitment of substantial financial resources as well as the selection of a team of dedicated regulators who were willing to commit the time and effort necessary to accomplish one of the most significant undertakings that has been faced by the NAIC.

11. Recognition of this effort was given by the AICPA when in 1995 they issued *Statement of Position 95-5—Auditor's Report on Statutory Financial Statements of Insurance Enterprises* (SOP 95-5) so that an auditor's opinion on a "prescribed or permitted" basis could continue until codification was completed. SOP 95-5 states "The codification is expected to result in a hierarchy of statutory accounting

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practices that will provide a comprehensive basis of accounting that can be applied consistently to all insurance enterprises." At that time, it was believed that once Codification was effective, in order for certified public accountants (CPAs) to issue opinions on statutory statements, SAP had to be considered an "Other Comprehensive Basis of Accounting" (OCBOA) by the American Institute of Certified Public Accountants (AICPA).

12. Codification is not intended to preempt state legislative and regulatory authority. While Codification is expected to be the foundation of a state's statutory accounting practices, it may be subject to modification by practices prescribed or permitted by a state's insurance commissioner. Statutory financial statements will continue to be prepared on the basis of accounting practices prescribed or permitted by the states. As a result, in 1998 the AICPA's Insurance Companies Committee determined that it will not be necessary for the Auditing Standards Board to grant the Codification status as an OCBOA since it will not be the sole basis for preparing statutory financial statements. Further, auditors will be permitted to continue to provide audit opinions on practices prescribed or permitted by the insurance department of the state of domicile.

D. Result of Codification Project

13. The conceptual framework used in developing and maintaining statutory accounting principles for insurance companies was summarized in the Statutory Accounting Principles Statement of Concepts (Section IV of Preamble). The application of the concepts of conservatism, consistency and recognition assured that guidance developed and codified as part of this project was consistent with the underlying objectives of statutory accounting.

14. The inaugural NAIC Practices and Procedures Manual was developed using the body of statutory accounting principles as prescribed in the statutory hierarchy of accounting guidance (Section V of Preamble), which is incorporated into the Statement of Concepts. The hierarchy provides the guidance for judging the presentation of statutory financial statements in conformance with statutory accounting principles.

15. The principles established through codification were effective January 1, 2001. Accounting changes adopted to conform to the provisions of these statements were reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle; however, specific effective dates, and transition or grandfathering rules, if any, are contained in each SSAP. Subsequent revisions or the adoption of new SSAPs subsequent to original codification shall follow the adoption and transition guidance detailed within each individual SSAP.

II. Accounting for Insurance Companies

A. Environment

16. Accounting is the process of accumulating and reporting financial information about an economic unit or group of units. Relative to commercial enterprises, the users of accounting information include management, investors, potential investors, lenders, investment analysts, regulators and customers. Although customers of most commercial enterprises have no direct financial interest therein and generally are only concerned with the price to be paid for the product or service purchased, they may use accounting information to make choices as to the entity with which they engage in a business transaction. This is particularly relevant to purchases of insurance products as insurance contracts involve a promise to pay which may extend years into the future. Insurance products may provide benefits well in excess of the purchase price or premium. The benefits ultimately received are almost always greater than the price (premium) paid and can only be estimated at the time the product (policy) is purchased.

17. Insurance is regulated on a state-by-state basis in the United States. Each state has its own regulatory framework generally led by an insurance commissioner. Insurance commissioners are charged

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with overseeing the financial condition of insurance companies doing business in their jurisdictions and they require meaningful financial, statistical, and operating information about the companies. This financial oversight is designed to help ensure that policyholders and claimants receive the requisite benefits from the policies sold, often times such products having been sold years or decades prior to when the benefits are due. Frequently, this regulatory perspective differs markedly from the perspectives of other users of insurers' accounting information. In recognition of these special concerns and responsibilities, statutory accounting principles have been established by statute, regulation and practice.

B. Statutory Accounting Principles (SAP)

18. In simplest terms, SAP has been those accounting principles or practices prescribed or permitted by an insurer's domiciliary state. Statutory accounting practices have been interspersed in the insurance laws, regulations, and administrative rulings of each state, the accounting practices and procedures manuals, the annual statement instructions, the NAIC *Financial Condition Examiners Handbook,* the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and NAIC committee, task force, and working group minutes. In addition, there are many statutory practices widely accepted by both insurers and regulators which have never been codified.

19. SAP is conservative in some respects but not unreasonably conservative over the span of economic cycles, or in recognition of the primary statutory responsibility to regulate for financial solvency. SAP attempts to determine at the financial statement date an insurer's ability to satisfy its obligations to its policyholders and creditors.

C. Comparison of U.S. Generally Accepted Accounting Principles (GAAP) and SAP

20. The objectives of GAAP reporting differ from the objectives of SAP. GAAP is designed to meet the varying needs of the different users of financial statements. SAP is designed to address the concerns of regulators, who are the primary users of statutory financial statements. As a result, GAAP stresses measurement of emerging earnings of a business from period to period, (i.e., matching revenue to expense), while SAP stresses measurement of ability to pay claims in the future. This difference is illustrated by the fact that statutory policy reserves are intentionally established on a conservative basis emphasizing the long-term nature of the liabilities. Under GAAP, the experience expected by each company is used to determine the reserves it will establish for its policies. GAAP reserves may be more or less than the statutory policy reserves. In addition, another primary difference is that GAAP has recognized certain assets which, for statutory purposes, have been either nonadmitted or immediately expensed. For example, policy acquisition costs are expensed as incurred under SAP since the funds so expended are no longer available to pay future liabilities. Insurance company financial statements prepared in accordance with GAAP defer qualifying costs incurred in the successful acquisition of new or renewal insurance contracts and amortize them over the expected life of the insurance contract.

III. Development of Ongoing Accounting Practices and Procedures

21. The mission of the Accounting Practices and Procedures (E) Task Force is to identify, investigate and develop solutions to accounting problems with the ultimate goal of guiding insurers in properly accounting for various aspects of their operations, to modify the NAIC *Accounting Practices and Procedures Manual* to reflect changes necessitated by Task Force action, and to study innovative insurer accounting practices which affect the ability of regulators to determine the true financial condition of insurers.

22. The role of the Accounting Practices and Procedures (E) Task Force is further defined in *Appendix F—Policy Statements* of this Manual.

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23. The Accounting Practices and Procedures (E) Task Force will accomplish its mission through charges assigned to the following working groups:

- Statutory Accounting Principles (E) Working Group: Responsible for developing and adopting revisions to the Statements of Statutory Accounting Principles (SSAPs). Statutory accounting principles provide the basis for insurers to prepare financial statements for financial regulation purposes, and SSAPs are considered level 1 (highest authority) in the statutory accounting hierarchy. Refer to the Statutory Accounting Principles (E) Working Group Web page (*https://content.naic.org/cmte_e_app_sapwg.htm*) for specific information and charges.

- Blanks (E) Working Group: Considers improvements and revisions to various annual/quarterly statement blanks to conform to changes made in other areas of the NAIC to promote uniformity in reporting of financial information by insurers and develop reporting formats for other entities subject to the jurisdiction of state insurance departments. Refer to the Blanks (E) Working Group webpage (*https://content.naic.org/cmte_e_app_blanks.htm*) for specific information and charges.

24. This comprehensive guide to statutory accounting principles, composed of the Preamble, the Statements of Statutory Accounting Principles (SSAPs) and the Appendices, is intended to respond to the mission of the Accounting Practices and Procedures (E) Task Force and the charges of its affiliated working groups as noted above. The Manual is not intended to preempt states' legislative and regulatory authority. It is intended to establish a comprehensive basis of accounting recognized and adhered to if not in conflict with state statutes and/or regulations, or when the state statutes and/or regulations are silent.

IV. Statutory Accounting Principles Statement of Concepts

A. Purpose

25. This document states the fundamental concepts on which statutory financial accounting and reporting standards are based. These concepts provide a framework to guide the National Association of Insurance Commissioners (NAIC) in the continued development and maintenance of statutory accounting principles ("SAP" or "statutory basis") and, as such, these concepts and principles constitute an accounting basis for the preparation and issuance of statutory financial statements by insurance companies in the absence of state statutes and/or regulations.[1]

26. The NAIC and state insurance departments are primarily concerned with statutory accounting principles that differ from GAAP reflective of the varying objectives of regulation. Recodification of areas where SAP and GAAP are parallel is an inefficient use of limited resources.

27. SAP utilizes the framework established by GAAP.[2] This document integrates that framework with objectives exclusive to statutory accounting. The NAIC's guidance on SAP is comprehensive for

[1] As stated in the NAIC's constitution, the NAIC is an association of chief insurance regulatory officials of the 50 states, the District of Columbia, American Samoa, Guam, Northern Mariana Islands, Puerto Rico, and U.S. Virgin Islands whose objective is to serve the public by assisting several state insurance supervisory officials, individually and collectively, in achieving the following fundamental insurance regulatory objectives:

1. Maintenance and improvement of state regulation of insurance in a responsive and efficient manner;
2. Reliability of the insurance institution as to financial solidity and guaranty against loss;
3. Fair, just, and equitable treatment of policyholders and claimants.

[2] The GAAP framework applicable to insurance accounting is set forth in *Statements of Financial Accounting Concepts Five and Eight*. These documents, promulgated by the Financial Accounting Standards Board, set forth the objectives and concepts which are used in developing accounting and reporting standards.

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those principles that differ from GAAP based on the concepts of statutory accounting outlined herein. Those GAAP pronouncements that are not applicable to insurance companies will not be adopted by the NAIC. For those principles that do not differ from GAAP, the NAIC must specifically adopt those GAAP Pronouncements to be included in statutory accounting. GAAP Pronouncements do not become part of SAP until and unless adopted by the NAIC.

28. The body of statutory accounting principles is prescribed in the statutory hierarchy of accounting guidance. This hierarchy provides the framework for judging the presentation of statutory financial statements in conformance with statutory accounting principles.

29. Statutory requirements vary from state to state. While it is desirable to minimize these variations, to the extent that they exist it is the objective of NAIC statutory accounting principles to provide the standard against which the exceptions will be measured and disclosed if material.

B. Objectives of Statutory Financial Reporting

30. The primary responsibility of each state insurance department is to regulate insurance companies in accordance with state laws with an emphasis on solvency for the protection of policyholders. The ultimate objective of solvency regulation is to ensure that policyholder, contract holder and other legal obligations are met when they come due and that companies maintain capital and surplus at all times and in such forms as required by statute to provide an adequate margin of safety. The cornerstone of solvency measurement is financial reporting. Therefore, the regulator's ability to effectively determine relative financial condition using financial statements is of paramount importance to the protection of policyholders. An accounting model based on the concepts of conservatism, consistency, and recognition is essential to useful statutory financial reporting.

31. Statutory reporting applies to all insurers authorized to do business in the United States and its territories, and requires sufficient information to meet the statutory objectives. However, statutory reporting as contained in this guide is not intended to preempt state legislative and regulatory authority. The SAP financial statements include the balance sheet and related summary of operations, changes in capital and surplus, and cash flow statements. Because these basic financial statements cannot be expected to provide all of the information necessary to evaluate an entity's short-term and long-term stability, management must supplement the financial statements with sufficient disclosures (e.g., notes to financial statements, management's discussion and analysis, and supplementary schedules and exhibits) to assist financial statement users in evaluating the information provided.

C. Concepts

Conservatism

32. Financial reporting by insurance enterprises requires the use of substantial judgments and estimates by management. Such estimates may vary from the actual amounts for numerous reasons. To the extent that factors or events result in adverse variation from management's accounting estimates, the ability to meet policyholder obligations may be lessened. In order to provide a margin of protection for policyholders, the concept of conservatism should be followed when developing estimates as well as establishing accounting principles for statutory reporting.

33. Conservative valuation procedures provide protection to policyholders against adverse fluctuations in financial condition or operating results. Statutory accounting should be reasonably conservative over the span of economic cycles and in recognition of the primary responsibility to regulate for financial solvency. Valuation procedures should, to the extent possible, prevent sharp fluctuations in surplus.

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Consistency

34. The regulators' need for meaningful, comparable financial information to determine an insurer's financial condition requires consistency in the development and application of statutory accounting principles. Because the marketplace, the economic and business environment, and insurance industry products and practices are constantly changing, regulatory concerns are also changing. An effective statutory accounting model must be responsive to these changes and address emerging accounting issues. Precedent or historically accepted practice alone should not be sufficient justifications for continuing to follow a particular accounting principle or practice which may not coincide with the objectives of regulators.

Recognition

35. The principal focus of solvency measurement is determination of financial condition through analysis of the balance sheet. However, protection of the policyholders can only be maintained through continued monitoring of the financial condition of the insurance enterprise. Operating performance is another indicator of an enterprise's ability to maintain itself as a going concern. Accordingly, the income statement is a secondary focus of statutory accounting and should not be diminished in importance to the extent contemplated by a liquidation basis of accounting.

36. The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third party interests should not be recognized on the balance sheet but rather should be charged against surplus when acquired or when availability otherwise becomes questionable.

37. Liabilities require recognition as they are incurred. Certain statutorily mandated liabilities may also be required to arrive at conservative estimates of liabilities and probable loss contingencies (e.g., interest maintenance reserves, asset valuation reserves, and others).

38. Revenue should be recognized only as the earnings process of the underlying underwriting or investment business is completed. Accounting treatments which tend to defer expense recognition do not generally represent acceptable SAP treatment.

39. SAP income reflects the extent that changes have occurred in SAP assets and liabilities for current period transactions, except changes in capital resulting from receipts or distributions to owners. SAP income also excludes certain other direct charges to surplus which are not directly attributable to the earnings process (e.g., changes in nonadmitted assets).

D. Conclusion

40. This document states the fundamental concepts for financial statements presented on the basis of SAP. These concepts summarize the conceptual framework that the NAIC uses in developing and maintaining statutory accounting principles for insurance companies. These concepts will also assure that guidance will be provided consistently with the underlying objectives of statutory accounting and will aid in the review of emerging accounting issues.

41. The multitude of unique circumstances and individual transactions makes it virtually impossible for any codification of accounting principles to be totally comprehensive. Application of SAP, either contained in the SSAPs or defined as GAAP and adopted by the NAIC, to unique circumstances or individual transactions should be consistent with the concepts of conservatism, consistency, and recognition.

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V. Statutory Hierarchy

42. The following Hierarchy is not intended to preempt state legislative and regulatory authority.

Level 1

- SSAPs, including U.S. GAAP reference material to the extent adopted by the NAIC from the FASB Accounting Standards Codification[3] (FASB Codification or GAAP guidance)

Level 2

- Consensus positions of the Emerging Accounting Issues (E) Working Group as adopted by the NAIC (INTs adopted before 2016)
- Interpretations of existing SSAPs as adopted by the Statutory Accounting Principles (E) Working Group (INTs adopted in 2016 or beyond)

Level 3

- NAIC Annual Statement Instructions
- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*

Level 4

- Statutory Accounting Principles Preamble and Statement of Concepts[4]

Level 5

- Sources of nonauthoritative GAAP accounting guidance and literature, including: (a) practices that are widely recognized and prevalent either generally or in the industry, (b) FASB Concept Statements, (c) AICPA guidance not included in FASB Codification, (d) International Financial Reporting Standards, (e) Pronouncements of professional associations or regulatory agencies, (f) Technical Information Service Inquiries and Replies included in the AICPA Technical Practice Aids, and (g) Accounting textbooks, handbooks and articles

43. If the accounting treatment of a transaction or event is not specified by the SSAPs, preparers, regulators and auditors of statutory financial statements should consider whether the accounting treatment is specified by another source of established statutory accounting principles. If an established statutory accounting principle from one or more sources in Level 2 or 3 is relevant to the circumstances, the preparer, regulator or auditor should apply such principle. If there is a conflict between statutory accounting principles from one or more sources in Level 2 or 3, the preparer, regulator or auditor should follow the treatment specified by the source in the higher level—that is, follow Level 2 treatment over Level 3. Revisions to guidance in accordance with additions or revisions to the NAIC statutory hierarchy

[3] Effective September 15, 2009, the FASB Codification is the source of authoritative U.S. generally accepted accounting principles. As of that date, the FASB Codification superseded all then-existing non-SEC accounting and reporting standards. All other nongrandfathered, non-SEC accounting literature not included in the FASB Codification is nonauthoritative. As of September 15, 2009, AICPA Statements of Position are no longer reviewed as part of the statutory maintenance process as they are no longer considered authoritative GAAP literature. If the AICPA were to address an issue that affects the FASB Codification, an accounting standard update (ASU) would be issued and reviewed for applicability to statutory accounting.

[4] The Statutory Accounting Principles Statement of Concepts incorporates by reference FASB Concepts Statements Five and Eight to the extent they do not conflict with the concepts outlined in the statement. However, for purposes of applying this hierarchy the FASB Concepts Statements shall be included in Level 5 and only those concepts unique to statutory accounting as stated in the statement are included in Level 4.

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should be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

44. Because of developments such as new legislation or the evolution of a new type of business transaction, there sometimes are no established statutory accounting principles for reporting a specific transaction or event. In those instances, it might be possible to report the event or transaction on the basis of its substance by selecting a statutory accounting principle that appears appropriate when applied in a manner similar to the application of an established statutory principle to an analogous transaction or event. In the absence of a SSAP or another source of established statutory accounting principles, the preparer, regulator or auditor of statutory financial statements may consider other accounting literature, depending on its relevance in the circumstances. Other accounting literature includes the Statutory Accounting Principles Statement of Concepts and GAAP reference material and accounting literature identified in Level 5. The appropriateness of other accounting literature depends on its relevance to the particular circumstances, the specificity of the guidance, and the general recognition of the issuer or author as an authority. For example, the Statutory Accounting Principles Statement of Concepts would be more authoritative than any other sources of accounting literature. Similarly, FASB Concepts Statements would normally be more influential than other sources of nonauthoritative GAAP pronouncements.

VI. Statements of Statutory Accounting Principles

45. This Manual consists primarily of Statements of Statutory Accounting Principles (SSAPs). SSAPs are the primary Accounting Practices and Procedures promulgated by the NAIC. These statements are the result of issue papers that have been exposed for public comment and finalized. Finalized issue papers are in Appendix E. While it is not intended that there be any significant differences between an underlying issue paper and the resultant SSAP, if differences exist, the SSAP prevails and shall be considered definitive.

46. SSAPs designated as Common Area apply to all insurers. Although the nomenclature or terms provided in the prescribed annual statement forms may vary among different types of insurers, only one set of nomenclature or terms may have been used in the SSAP. For example, the Statement of Income found in the Property and Casualty Annual Statement shall be considered as synonymous with the Summary of Operations found in the Life and Health Annual Statement.

47. Once promulgated, statements will only be amended or superseded through the issuance of new SSAP pronouncements. If it is necessary to introduce a new SAP concept that will modify or augment the guidance in an existing SSAP, a new statement will be promulgated and/or the statement will be reissued with “revised” in the title. Changes as a result of clarifying an existing SAP will be included in the existing statement with changes tracked (i.e., new text will be underlined and deleted text as strikethrough) in the next published Manual. Then no changes will be shown after the initial year. A useful tool for tracking of the relationships between statements is contained in the “Status” section of each statement which includes sections labeled “Affects” and “Affected By.” As SSAPs are issued in the future that modify or augment the guidance previously provided, these sections will identify the relationships between statements.

VII. Materiality

48. Those who make accounting decisions and those who make judgments as regulators and auditors continually confront the need to make judgments about materiality. Materiality judgments are primarily quantitative in nature. They pose the question: Is this item large enough for users of the information to be influenced by it? However, the answer to that question will usually be affected by the nature of the item; items too small to be thought material if they result from routine transactions may be considered material if they arise in abnormal circumstances.

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49. Materiality judgments are concerned with screens or thresholds. Is an item, an error, or an omission large enough, considering its nature and the attendant circumstances, to pass over the threshold that separates material from immaterial items? The more important a judgment item is, the finer the screen should be that will be used to determine whether it is material. For example:

- Circumstances where an accounting adjustment puts an insurer in danger of being in breach of a covenant or regulatory requirement may justify a lower materiality threshold than if its position were stronger. For example, an error resulting from an insurer incorrectly reporting certain nonadmitted assets as admitted assets might be considered material if the classification of those assets as nonadmitted would cause the insurer to trigger an event under the Risk-Based Capital requirements.

- A failure to disclose separately a nonrecurrent item of revenue may be material at a lower threshold than would otherwise be the case if the revenue turns a loss into a profit or reverses the trend of earnings from a downward to an upward trend.

- A miscategorization of assets or liabilities that would not be material in amount to the basic financial statements, but would cause the insurer to trigger an event under the Risk-Based Capital requirements, might be material.

- Amounts too small to warrant disclosure or correction in normal circumstances may be considered material if they arise from abnormal or unusual transactions or events.

50. Almost always, the relative rather than the absolute size of a judgment item determines whether it should be considered material in a given situation. Losses from bad debts that could be shrugged off as routine by a large insurer may threaten the continued existence of a small one. An error in reserve valuation may be material in a small insurer for which it cut earnings in half but immaterial in an insurer for which it might make a barely perceptible ripple in the earnings.

51. Another factor in materiality judgments is the degree of precision that is attainable in estimating the judgment item. The amount of deviation that is considered immaterial may increase as the attainable degree of precision decreases. For example, accounts payable usually can be estimated more accurately than can contingent liabilities arising from litigation or threats of it, and a deviation considered to be material in the first case may be quite trivial in the second.

52. Individual judgments are required to assess materiality. The essence of the materiality concept is clear. The omission or misstatement of an item in a statutory financial statement is material if, in the light of surrounding circumstances, the magnitude of the item is such that it is probable that the judgment of a reasonable person relying upon the statutory financial statement would have been changed or influenced by the inclusion or correction of the item.

53. The provisions of this Manual need not be applied to immaterial items. *INT 00-20: Application of SEC SAB No. 99, Materiality to the Preamble of the AP&P Manual* provides further information on the application of the concept of materiality.

VIII. Relationship to GAAP

54. As expressed in the Statement of Concepts, SAP utilizes the framework established by GAAP. This Manual integrates that framework with objectives exclusive to statutory accounting. The NAIC's guidance on SAP is comprehensive for those principles that differ from GAAP based on the concepts of statutory accounting outlined herein. GAAP guidance that is not applicable to insurance companies will not be adopted by the NAIC. For those principles that do not differ from GAAP, the NAIC may specifically adopt GAAP guidance to be included in statutory accounting. Elements of the FASB Codification do not become part of SAP until and unless adopted by the NAIC. Future SAP

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pronouncements will specifically identify any element of the FASB Codification that is to be included in SAP whether in whole, in part, or with modification as well as any rejected GAAP guidance. GAAP guidance which SAP has not yet addressed shall not be considered as providing authoritative statutory guidance.

IX. Relationship to Developments within NAIC

55. Various NAIC committees and their working groups will be involved in issues, at any point in time, which could impact accounting guidance. Recommendations that affect accounting guidance must be referred to the Accounting Practices and Procedures (E) Task Force which has the responsibility for the maintenance of this Manual for determination of appropriate inclusion in SAP.

56. There are instances where the Codification of Statutory Accounting Principles (E) Working Group (Statutory Accounting Principles (E) Working Group as of January 1, 2000) has established an accounting principle in a SSAP but deferred maintenance and update of the detailed guidance to other NAIC task forces and their working groups. Those instances are specifically set forth in the individual SSAPs and include specific guidance for calculation of the Interest Maintenance Reserve (IMR), the Asset Valuation Reserve (AVR), the provision for overdue reinsurance, and periodic update to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*.

57. Changes to statutory accounting principles are not authoritative until approved by the general membership of the NAIC.

X. Permitted Accounting Practices

58. In instances where the domiciliary state regulator is considering approval of a request for an accounting practice that departs from the NAIC *Accounting Practices and Procedures Manual* (Manual) and state prescribed accounting practices, the domiciliary regulator must provide Notice as defined in paragraphs 59-61.

59. No domiciliary state regulatory authority shall grant an approval to use an accounting practice, as described in paragraph 58, unless it provides Notice at least 5 days in advance of such approval.

60. This Notice must disclose the following information regarding the requested accounting practice request to all other states in which the insurer is licensed prior to the financial statement filing date:

a. The nature and a clear description of the permitted accounting practice request;

b. The quantitative effect of the permitted accounting practice request with all other approved permitted accounting practices currently in effect as disclosed in *Appendix A-205—Illustrative Disclosure of Differences Between NAIC Statutory Accounting Practices and Procedures and Accounting Practices Prescribed or Permitted by the State of Domicile*, for that insurer in the domiciliary state;

c. The effect of the requested permitted accounting practice on a legal entity basis and on all parent and affiliated United States insurance companies, if applicable; and

d. Identify any potential effects on and quantify the potential impact to each financial statement line item affected by the request. The potential impact may be determined by comparing the financial statements prepared in accordance with NAIC SAP and the financial statements incorporating the requested permitted accounting practice.

61. The granting of approval for an accounting practice request by the domiciliary state regulator does not preempt or in any way limit any individual state's legislative and regulatory authority.

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XI. Financial Statements

A. Annual Financial Statement

62. Each state requires all insurance companies doing business in that state to file an annual financial statement. All states use the annual statement blank promulgated by the NAIC, but each state retains the authority to make changes in those statements. Changes made by states generally require only supplemental information and do not change the basic financial information.

63. To the extent that disclosures required by a SSAP are made within specific notes, schedules, or exhibits to the annual statement, those disclosures are not required to be duplicated in a separate note. Annual statutory financial statements which are not accompanied by annual statement exhibits and schedules (e.g., annual audit report) shall include all disclosures required by the SSAPs based on the applicability, materiality and significance of the item to the insurer. Certain disclosures, as noted in individual SSAPs, are required in the annual audited statutory financial statements only.

B. Interim Financial Statements

64. Interim financial statements, including quarterly statements, shall follow the form and content of presentation prescribed by the domiciliary state for the quarterly financial statements. The NAIC quarterly statement form has been adopted by each state with minor variations as required by certain states.

65. The interim financial information shall include disclosures sufficient to make the information presented not misleading. It may be presumed that the users of the interim financial information have read or have access to the annual statement for the preceding period and that the adequacy of additional disclosure needed for a fair presentation, except in regard to material contingencies may be determined in that context. Accordingly, footnote disclosure which would substantially duplicate the disclosure contained in the most recent annual statement or audited financial statements, such as a statement of significant accounting policies and practices, details of accounts which have not changed significantly in amount or composition since the end of the most recently completed fiscal year, may be omitted. However disclosure shall be provided where events subsequent to the end of the most recent fiscal year have occurred which have a material impact on the insurer. Disclosures shall encompass, for example, significant changes since the end of the period reported on the last annual statement in such items as: statutory accounting principles and practices, estimates inherent in the preparation of financial statements, status of long term contracts, capitalization including significant new borrowings or modifications of existing financial arrangements, and the reporting entity resulting from business combinations or dispositions. Notwithstanding the above, where material noninsurance contingencies exist, disclosure of such matters shall be provided even though a significant change since year end may not have occurred.

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Permitted Practices Advance Notification Requirement Implementation Questions and Answers

1. Q: Why is the issue of permitted accounting practices important?

A: Since the Codification of the NAIC *Accounting Practices and Procedures Manual* (AP&P Manual), there has been continued emphasis on uniformity among the states. With the adoption of Codification, the belief was that permitted accounting practices would be limited. The intent of the policy statement on permitted accounting practices is to provide notification prior to granting permitted accounting practices to other states in which an insurer is licensed. Proactive notification encourages communication between state insurance regulators who share a common interest in the solvency of insurance companies writing business in their state.

2. Q: What is the difference between a permitted accounting practice and a prescribed practice?

A: **Permitted** accounting practices include practices specifically requested by an insurer that depart from NAIC Statutory Accounting Principles (SAP) and state prescribed accounting practices, as described below, and have received approval from the insurer's domiciliary state regulatory authority.

Prescribed accounting practices are those practices that are incorporated directly or by reference by state laws, regulations and general administrative rules applicable to all insurance enterprises domiciled and/or licensed in a particular state. The NAIC AP&P Manual is not intended to preempt states' legislative and regulatory authority. Prescribed accounting practices of the domiciliary state shall be reflected in the statutory financial statements filed with the NAIC. Non-domiciliary states may additionally require insurance entities licensed in their state to file supplementary financial information that details the use of different accounting practices required or allowed by the non-domiciliary state that differs from the AP&P Manual.

If a reporting entity requests an accounting practice that differs from state prescribed accounting practices, but is in accordance with NAIC SAP, advance notice of approval is not required.

3. Q: Does a permitted accounting practice request require approval/consensus from other states before it is granted by the domiciliary state?

A: No, the domiciliary state regulatory authority does not need approval or consensus from other state regulatory authorities to grant a permitted accounting practice. The granting of approval for an accounting practice request by the domiciliary state regulator does not preempt or in any way limit any individual state's legislative and regulatory authority.

If a state does not comply with the advance notice provision but approves a permitted practice, the lack of notice does not invalidate the permitted practice for the reporting entity. In addition, the reporting entity is required to disclose accounting practices that depart from the NAIC accounting practices and procedures, which affect statutory surplus or risk based capital pursuant to *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*.

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4. Q: How does the domestic regulator communicate an insurer's request for a permitted accounting practice to other states?

A: The NAIC can facilitate the communication of this information through the Permitted Practice Database within the Exam Tracking System. In order to develop a repository of all permitted accounting practice notifications, all regulatory authorities should distribute permitted accounting practice notifications using the procedures prescribed by the NAIC members. When providing permitted accounting practice notifications, the regulatory authority will provide the following information in instances where they are considering approval of a request:

- Detailed description of the permitted accounting practice request, including the specific NAIC Statutory Accounting Principles or state prescribed practices from which the practice departs
- Whether the permitted accounting practice was granted the previous year
- The financial statement filing date in which the permitted accounting practice will be reflected and the timeframe for which the permitted accounting practice is granted (e.g., indefinitely, until withdrawn, specific date – month, day, year)
- Explanation for providing less than the required advance notice
- The financial statement line items the permitted accounting practice will affect and the respective financial impact for each line item identified
- The total financial impact to capital and surplus for all approved/requested permitted accounting practices
- The effect of the permitted accounting practice on a legal entity basis and on all parent and affiliated U.S. insurance companies, if applicable
- Whether the permitted accounting practice is approved or the decision is pending

Grandfather Clause: Please note that those permitted accounting practices that have been granted prior to December 2004 for an indefinite time period do not require a new notice to other states and are not required to be filed through the ETS system. If the permitted accounting practice is considered by the state for reaffirmation annually then annual advance notice is required.

5. Q: If a Department of Insurance received a request for a permitted accounting practice from an insurer licensed in only one state, is the Department required to comply with communication requirements outlined in the Preamble?

A: No, an insurer licensed in only one state is not subject to the permitted accounting practices communication policy included in the Preamble. The goal of the permitted accounting practices communication policy is to encourage open communication between state regulatory authorities and promote uniformity. As permitted accounting practices granted to an insurer licensed in only one state would not impact states outside of the domiciliary state, they do not need to be communicated to other regulatory authorities.

6. Q: Are requests for permitted accounting practices kept confidential?

A: The communication of permitted accounting practices will be facilitated through the NAIC's Permitted Practice Database of the Exam Tracking System, which is a confidential, regulator-only system and/or through regulator-to-regulator e-mail exchange.

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7. Q: Is a state required to provide advance notification for accounting practices that are explicitly permitted under the AP&P Manual, with the approval of the commissioner?

A: No, for example, a reporting entity is required to obtain domiciliary commissioner approval for a capital contribution as described in *SSAP No. 72—Surplus and Quasi-Reorganizations*, paragraph 8:

> 8. Notes or other receivables received as additional capital contributions satisfied by receipt of cash or readily marketable securities prior to filing of the statutory financial statement shall be treated as a Type I subsequent event in accordance with SSAP No. 9 and as such shall be considered an admitted asset based on the evidence of collection and approval of the domiciliary commissioner. To the extent that the notes or other receivables are not satisfied, they shall be nonadmitted.

These types of transactions are not a departure from NAIC SAP and do not require a request for a permitted accounting practice.

8. Q: When will the permitted accounting practices communication policy become effective?

A: The Statutory Accounting Principles (E) Working Group, the Accounting Practices and Procedures (E) Task Force and the Financial Condition (E) Committee held a joint conference call to approve the guidance on November 30, 2004. The policy became effective in December 2004 upon approval by the Executive/Plenary Committee. The policy will be incorporated into the *Accounting Practices and Procedures Manual* and the Financial Regulation Standards and Accreditation (F) Committee will consider such changes to the *NAIC Financial Regulations Standards and Accreditation Manual* during the normal maintenance process.

9. Q: When submitting a permitted accounting practice request, is the financial statement effect quantified for all affiliates, or only those materially affected?

A: It is important that the insurer identify any potential effects on and quantify the potential impact to each financial statement line item on a legal entity basis and on all parent and affiliated U.S. insurance companies, if applicable. The notification from the regulator should only include the effect on a legal entity basis for those entities materially affected positively or negatively by the permitted accounting practice.

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Statement of Statutory Accounting Principles No. 1

Accounting Policies, Risks & Uncertainties, and Other Disclosures

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-001; A-205

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the disclosure of accounting policies, risks and uncertainties, the use of accounting practices which depart from NAIC statutory accounting practices and procedures, and other disclosures.

2. Separate statements of statutory accounting principles have disclosure requirements specific to the topics addressed in those statements. Additional disclosure requirements not addressed in other statements are included herein.

SUMMARY CONCLUSION

3. Refer to the Preamble for further discussion of disclosure requirements. The disclosures required under paragraph 6 concerning changes in accounting policies shall be made for each financial statement presented. The disclosures required under paragraphs 9, 10, 12, 13, 15 and 16 shall be included in the annual audited statutory financial reports only.

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Accounting Policies and Practices

4. Accounting policies are defined as the specific accounting principles and the methods of applying those principles that are utilized in preparing the statutory financial statements.

5. Disclosure shall be made of all accounting policies that affect the assets, liabilities, capital and surplus or results of operations of the reporting entity. The disclosure shall encompass important judgments as to the appropriateness of principles relating to recognition of revenue particularly when selecting between acceptable alternatives, or methods particular to the business.

6. Disclosure of accounting policies shall be made in a separate Summary of Significant Accounting Policies as the initial note in the notes to the financial statements. If the reporting entity has changed the accounting policies since the end of its preceding year, the changes shall be disclosed in the quarterly financial statements.

7. NAIC statutory accounting practices and procedures are those that are set forth in the *Accounting Practices and Procedures Manual*. If a reporting entity employs accounting practices that depart from the NAIC accounting practices and procedures, disclosure of the following information about those accounting practices that affect statutory surplus or risk-based capital, or that result in different statutory accounting reporting (e.g., gross or net presentation, financial statement reporting lines, etc.), shall be made at the date each financial statement is presented:

a. A description of the accounting practice;

b. A statement that the accounting practice differs from NAIC statutory accounting practices and procedures[1];

c. The monetary effect on net income and statutory surplus of using an accounting practice which differs from NAIC statutory accounting practices and procedures; and

d. If an insurance enterprise's risk-based capital would have triggered a regulatory event had it not used a prescribed or permitted practice, that fact should be disclosed in the financial statements.

These disclosures shall be disclosed in Note 1 as illustrated in Appendix A-205—*Illustrative Disclosure of Differences Between NAIC Statutory Accounting Practices and Procedures and Accounting Practices Prescribed or Permitted by the State of Domicile*. Additionally, a reference to Note 1 shall be included in the individual notes to financial statements impacted by the prescribed or permitted practices as applicable.

8. Disclosure of the following information shall be made about accounting practices when NAIC statutory accounting practices and procedures do not address the accounting for the transaction:

a. A description of the transaction and of the accounting practice used; and

b. A statement that NAIC statutory accounting practices and procedures do not address the accounting for the transaction.

[1] This disclosure shall identify whether the practice is a departure from NAIC SSAP or from a state prescribed practice and include the financial statement reporting line(s) predominantly impacted by the permitted or prescribed practice. (Although most practices impact net income or surplus, direct reference to those lines should be avoided. The intent is to capture the financial statement line(s) reflecting the practice which ultimately impacts net income or statutory surplus.) For example, although a permitted practice to admit furniture would increase surplus, this should be disclosed as a permitted practice to *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*, impacting line 21 of the asset page (furniture and equipment) and not line 37 (surplus) of the liabilities and surplus page.

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Risks and Uncertainties

9. Companies shall make disclosures in their financial statements about risks and uncertainties existing as of the date of those statements in the following areas:

a. Nature of operations;

b. Use of estimates in the preparation of financial statements;

c. Certain significant estimates; and

d. Current vulnerability due to certain concentrations.

Nature of Operations

10. Financial statements shall include a summary of the ownership and relationships of the reporting entity and all affiliated companies, and a description of the major products or services the reporting entity sells or provides and its principal markets, including the locations of those markets. If the entity operates in more than one business, the disclosure should also indicate the relative importance of its operations in each business and the basis for the determination (e.g., assets, revenues, or earnings). Disclosures about the nature of operations need not be quantified; relative importance could be conveyed by use of terms such as predominately, about equally, or major.

Use of Estimates in the Preparation of Financial Statements

11. Financial statements shall include an explanation that the preparation of financial statements in conformity with the annual statement instructions and the *Accounting Practices and Procedures Manual* requires the use of management's estimates.

Certain Significant Estimates

12. Disclosure regarding an estimate shall be made when known information available prior to issuance of the financial statements indicates that both of the following criteria are met:

a. It is at least reasonably possible that the estimate of the effect on the financial statements of a condition, situation, or set of circumstances that existed at the date of the financial statements will change in the near term due to one or more future confirming events; and

b. The effect of the change would be material to the financial statements.

13. The disclosure shall indicate the nature of the uncertainty and include an indication that it is at least reasonably possible that a change in the estimate will occur in the near term (generally a period of time not to exceed one year from the date of the financial statements). If the estimate involves a loss contingency as defined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, the disclosure shall include an estimate of the possible loss or range of loss, or state that such an estimate cannot be made. Reporting entities shall disclose the factors that cause the estimate to be sensitive to change.

Current Vulnerability Due to Certain Concentrations

14. Vulnerability from concentrations arises because an entity is exposed to risk of loss greater than it would have had it mitigated its risk through diversification. Such risks manifest themselves differently, depending on the nature of the concentration, and vary in significance.

15. Financial statements shall disclose the concentrations described in paragraph 16 of this statement if, based on information known to management prior to issuance of the financial statements, all of the following criteria are met:

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a. The concentration exists at the date of the financial statements;

b. The concentration makes the enterprise vulnerable to the risk of a near-term severe (more than material but less than catastrophic) impact; and

c. It is at least reasonably possible that the events that could cause the severe impact will occur in the near term.

16. Concentrations, including known group concentrations, described below require disclosure if they meet the criteria of paragraph 15 of this statement. (Group concentrations exist if a number of counterparties or items that have similar economic characteristics collectively expose the reporting entity to a particular kind of risk.) Some concentrations may fall into more than one category:

a. Concentrations in the volume of business transacted with a particular customer, supplier, or lender. The potential for the severe impact can result, for example, from total or partial loss of the business relationship. For the purposes of this statement, it is always considered at least reasonably possible that any customer will be lost in the near term;

b. Concentrations in revenue from particular products or services. The potential for severe impact can result, for example, from volume or price changes for a particular source of revenue;

c. Concentrations in the available sources of labor, services, licenses, or other rights used in the entity's operations;

d. Concentrations in the market or geographic area in which an entity conducts its operations. The potential for severe impact can result, for example, from negative effects of the economic and political forces within the market or geographic area. For the purposes of this statement, it is always considered at least reasonably possible that operations located outside an entity's home country will be disrupted in the near term.

Going Concern

17. Management for each reporting entity shall evaluate whether there is substantial doubt about an entity's ability to continue as a going concern. Such substantial doubt is determined when relevant conditions and events, considered in the aggregate, indicate that it is probable that an entity will be unable to meet its obligations as they become due within one year after the date that the financial statements are issued. This initial evaluation shall not take into consideration the potential mitigating effect of management's plans that have not been fully implemented as of that date.

18. Pursuant to paragraph 17, when relevant conditions or events have raised substantial doubt of the reporting entity's ability to continue as a going concern, management for the reporting entity shall evaluate whether its plans to mitigate those concerns and events, when implemented, will alleviate the substantial doubt about the entity's ability to continue as a going concern. The mitigating effect of management's plans shall be considered in evaluating whether the substantial doubt is alleviated only to the extent that information available as of the date that the financial statements are issued indicates both of the following:

a. It is probable that management's plans will be effectively implemented within one year after the date that the financial statements are issued.

b. It is probable that management's plans, when implemented, will mitigate the relevant conditions or events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued.

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19. If after considering management's plans, substantial doubt about an entity's ability to continue as a going concern is alleviated, the reporting entity shall disclose in the notes to the financial statements the following information:

a. Principal conditions and events that raised substantial doubt about the entity's ability to continue as a going concern (before consideration of management's plans).

b. Management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations.

c. Management's plans that alleviated substantial doubt about the entity's ability to continue as a going concern.

20. If after considering management's plans, substantial doubt about an entity's ability to continue as a going concern is not alleviated, the entity shall include a statement in the notes to the financial statements indicating that there is substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. Additionally, the reporting entity shall disclose the information in paragraphs 19.a. and 19.b., as well as the management's plans that are intended to mitigate the conditions or events that raise substantial doubt about the entity's ability to continue as a going concern.

21. The going concern evaluation and going concern disclosures discussed in paragraphs 17-19 are required for both interim and annual financial statements. If substantial doubt was determined, and the conditions or events continue to raise substantial doubt about an entity's ability to continue as a going concern in subsequent annual or interim reporting periods, the entity shall continue to provide the disclosures in each subsequent reporting period. In these subsequent periods the disclosures should become more extensive as additional information becomes available about the relevant conditions or events and about management's plans. The entity shall provide appropriate context and continuity in explaining how conditions or events have changed between reporting periods.

22. For the period in which substantial doubt no longer exists (before or after consideration of management's plans), an entity shall disclose how the relevant conditions or events that raised substantial doubt were resolved.

Other Disclosures

23. Reporting entities shall disclose[2] the following information in the financial statements:

a. Amounts not recorded in the financial statements that represent segregated funds held for others, the nature of the assets and the related fiduciary responsibilities associated with such assets. One example of such an item is escrow accounts held by title insurance companies; and

b. The total combined (admitted and nonadmitted) amount of restricted assets by category, with separate identification of the admitted and nonadmitted restricted assets by category, and nature of any assets pledged to others as collateral or otherwise restricted (e.g., not under the exclusive control, assets subject to a put option contract, etc.)[3] in the general and

[2] Disclosure of restricted assets shall be included in the annual financial statements and, pursuant to the Preamble, in the interim financial statements if significant changes have occurred since the annual statement. If significant changes have occurred, the entire disclosure shall be reported in the interim financial statements.

[3] The aggregate information captured within this disclosure is intended to reflect the information reported in the Annual Statement Investment Schedules in accordance with the coding of investments that are not under the exclusive control of the reporting entity, including assets loaned to others and the information reported in the General Interrogatories, as well as information on restricted cash, cash equivalents and short-term investments.

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separate accounts[4] by the reporting entity in comparison to total assets and total admitted assets. (Pursuant to SSAP No. 4, paragraph 6, all assets pledged as collateral or otherwise restricted shall be reported in this disclosure regardless if the asset is considered an admitted asset.) This disclosure shall include the following restricted asset categories:

i. Reported assets subject to contractual obligation for which liability is not shown;

ii. Collateral held under security lending agreements;

iii. Assets subject to repurchase agreements;

iv. Assets subject to reverse repurchase agreements;

v. Assets subject to dollar repurchase agreements;

vi. Assets subject to dollar reverse repurchase agreements;

vii. Assets placed under option contracts;

viii. Letter stock or securities restricted as to sale[5] – excluding FHLB stock;

ix. FHLB capital stock;

x. Assets on deposit with states;

xi. Assets on deposit with other regulatory bodies;

xii. Pledged as collateral to the FHLB (including assets backing funding agreements);

xiii. Assets pledged as collateral not captured in other categories; and

xiv. Other restricted assets.

c. The amount and nature of any assets received as collateral, reflected as assets within the reporting entity's financial statements, and the recognized liability to return these collateral assets, in the general and separate accounts in comparison to total assets and admitted assets.

24. The financial statements shall disclose forward commitments which are not derivative instruments (e.g., the commitment to purchase a GNMA security two months after the commitment date, or a private placement six months after the commitment date).

Insurance-Linked Securities

25. Reporting entities shall disclose information when they may receive possible proceeds as the issuer, ceding insurer, or counterparty of insurance-linked securities. Insurance-linked securities (ILS) are securities whose performance is linked to the possible occurrence of pre-specified events that relate to insurance risks. While catastrophe bonds (cat bonds) may be the most well-known type of ILS, there are other non-cat-bond ILS, including those based on mortality rates, longevity and medical-claim costs. ILS

[4] Restricted assets in the separate account are not intended to reflect amounts "restricted" only because they are insulated from the general account or because they are attributed to specific policyholders. Separate account assets shall be captured in this disclosure only if they are restricted outside of these characteristics.

[5] The nature, description and amount of the restriction are required in the disclosure.

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securities may be used by an insurer, or any other risk-bearing entity, in addition to (or as an alternative to) the purchase of insurance or reinsurance. This disclosure shall specifically identify the following:

a. Whether the reporting entity may receive possible proceeds as the issuer, ceding insurer or counterparty of insurance-linked securities as a way of managing risks related to directly-written insurance risks. This disclosure shall include the number of outstanding ILS contracts, and the aggregate maximum proceeds that could be received as of the reporting date under the terms of the ILS.

b. Whether the reporting entity may receive possible proceeds as the issuer, ceding insurer, or counterparty of insurance-linked securities as a way of managing risk related to assumed insurance risks. This disclosure shall include the number of outstanding ILS contracts, and the aggregate maximum proceeds that could be received as of the reporting date under the terms of the ILS.

Supplemental Investment Disclosure

26. For the current year, reporting entities shall disclose the information required by *Appendix A-001—Investments of Reporting Entities*. A Summary Investment Schedule and Investment Risk Interrogatories shall be filed with the audited statutory financial statements. The Summary Investment Schedule shall be filed with the annual statement whereas the interrogatories shall be filed as a supplement to the annual statement by April 1 for the applicable reporting period.

27. The Life, Accident and Health and Fraternal annual statement instructions include instructions for completing Schedule 1 Selected Financial Data. This Supplemental schedule is required to be included in the annual audit report for Life, Accident and Health and Fraternal reporting entities.

5GI Security Disclosure

28. For each annual reporting period, include a comparable disclosure to the prior annual reporting period of the number of 5GI securities, by investment type, and the book adjusted carrying value and fair value for those securities. This disclosure is required in the interim, pursuant to the Preamble, if there have been significant changes from the prior annual reporting statement. If significant changes require inclusion in more than one quarterly reporting statement in a single annual reporting year, the comparison period shall continue to reflect the prior annual reporting period.

Subprime Mortgage Related Risk Exposure

29. Reporting entities shall disclose information pertaining to subprime mortgage related risk exposure and related risk management practices, regardless of the materiality of the exposure, in the statutory financial statements. These disclosures are not required in the annual audited financial statements. Although definitions may differ among reporting entities, the following features are commonly recognized characteristics of subprime mortgage loans:

a. An interest rate above prime to borrowers who do not qualify for prime rate loans;

b. Borrowers with low credit ratings (FICO scores);

c. Interest-only or negative amortizing loans;

d. Unconventionally high initial loan-to-value ratios;

e. Low initial payments based on a fixed introductory rate that expires after a short initial period, then adjusts to a variable index rate plus a margin for the remaining term of the loan;

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f. Borrowers with less than conventional documentation of their income and/or net assets;

g. Very high or no limits on how much the payment amount or the interest rate may increase at reset periods, potentially causing a substantial increase in the monthly payment amount, and/or;

h. Include substantial prepayment penalties and/or prepayment penalties that extend beyond the initial interest rate adjustment period.

30. To the extent such information is available, reporting entities shall consider exposure to subprime mortgage related risk through the following sources:

a. Direct investments in subprime mortgage loans;

b. Direct investments in securities with underlying subprime exposure, such as residential mortgage backed securities, commercial mortgage backed securities, collateralized debt obligations, structured securities (including principal protected notes), hedge funds, credit default swaps, and special investment vehicles;

c. Equity investments in subsidiary, controlled or affiliated entities with significant subprime related risk exposure;

d. Underwriting risk on policies issued for Mortgage Guaranty or Financial Guaranty insurance coverage.

31. As it relates to the exposure described above, reporting entities shall provide the following information:

a. A narrative description of the manner in which the reporting entity specifically defines its exposure to subprime mortgage related risk in practice. Disclose the general categories of information considered in determining exposure to subprime mortgage related risk. Differentiation should be made between exposure to unrealized losses due to changes in asset values versus exposure to realized losses resulting from receiving less than anticipated cash flows or due to potential sale of assets to meet future cash flow requirements. Risk management or mitigation strategies shall also be disclosed.

b. Direct exposure through investments in subprime mortgage loans. Disclose the following information for the aggregate amount of directly held subprime mortgage loans: book adjusted carrying value (excluding accrued interest); fair value; value of land and buildings; any other-than-temporary impairment losses recognized to date; default rate for the subprime portion of the loan portfolio. This information shall be segregated by the categories of Mortgages in the Process of Foreclosure, Mortgages in Good Standing and Mortgages with Restructured Terms.

c. Direct exposure through other investments. Reporting entities shall consider subprime mortgage related risk exposure through other investments for the following types of investments:

i. Residential mortgage backed securities

ii. Commercial mortgage backed securities

iii. Collateralized debt obligations

iv. Structured securities (including principal protected notes)

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v. Equity investments in subsidiary, controlled or affiliated entities with significant subprime mortgage related risk exposure (a general description of the nature and extent of the SCAs exposure should be included)

vi. Other assets (including but not limited to hedge funds, credit default swaps, special investment vehicles)

Aggregated by the above investment types, reporting entities shall disclose the following: actual cost; book adjusted carrying value; fair value; any other-than-temporary impairment losses recognized to date.

d. Underwriting exposure to subprime mortgage risk through Mortgage Guaranty or Financial Guaranty insurance coverage. Disclose the following information, by coverage type, related to underwriting exposure on policies issued for Mortgage Guaranty coverage or Financial Guaranty coverage and any other lines of insurance expected to be impacted: the aggregate amount of subprime related losses paid in the current year; the aggregate amount of subprime related losses incurred in the current year; the aggregate amount of subprime related case reserves at the end of the current period; the aggregate amount of subprime related IBNR reserves at the end of the current period.

Stress Liquidity Risks

32. Reporting entities may be requested to complete disclosures pertaining to stress liquidity risks pursuant to inquiries and templates, or variations thereof, included in the *NAIC Financial Condition Examiners Handbook*. These disclosures may be considered confidential, therefore are not captured within the statutory financial statements. As noted in the *NAIC Financial Condition Examiners Handbook,* requests for reporting entities to complete these templates may occur at any time and are not limited to instances of comprehensive statutory examinations.

Relevant Literature

33. This statement adopts *Accounting Principles Board Opinion No. 22, Disclosure of Accounting Policies, Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins, Chapter 2A, "Comparative Financial Statements," AICPA Statement of Position No. 94-5, Disclosures of Certain Matters in the Financial Statements of Insurance Enterprises*, and *AICPA Statement of Position No. 94-6, Disclosures of Certain Significant Risks and Uncertainties*. The disclosure of certain accounting policies within specific notes to the annual statement is required by the annual statement instructions. This statement also adopts *ASU 2014-15, Presentation of Financial Statements – Going Concern, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern.*

Effective Date and Transition

34. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in paragraphs 17-22, requiring evaluation and disclosure of substantial doubt about an entity's ability to continue as a going concern is effective December 31, 2016, and is required for interim and annual reporting periods thereafter. Early application is permitted. The update to Section 3, Summary Investment Schedule, of Appendix A-001 is effective January 1, 2019.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 77—Disclosure of Accounting Policies, Risks & Uncertainties, and Other Disclosures*

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Statement of Statutory Accounting Principles No. 2 – Revised

Cash, Cash Equivalents, Drafts, and Short-Term Investments

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised December 10, 2016
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 155 effective December 31, 2017
Affects	Nullifies and incorporates INT 08-10
Affected by	No other pronouncements
Interpreted by	INT 21-01
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Cash 1
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REFERENCES **6**

Other 6
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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles and related reporting for cash, cash equivalents, drafts and short-term investments.

SUMMARY CONCLUSION

Cash

2. Cash constitutes a medium of exchange that a bank or other similar financial institution will accept for deposit and allow an immediate credit to the depositor's account.

3. Cash meets the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and is an admitted asset to the extent it conforms to the requirements of this statement.

4. If a reporting entity has multiple cash accounts, the net amount of all accounts shall be reported jointly. Cash accounts with positive balances shall not be reported separately from cash accounts with

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negative balances. If in the aggregate, the reporting entity has a net negative cash balance, it shall be reported as a negative asset and shall not be recorded as a liability.

5. Also classified as cash for financial statement purposes, although not falling within the definition of cash, are savings accounts and certificates of deposit in banks or other similar financial institutions with maturity dates within one year or less from the acquisition date.

Cash Equivalents

6. Cash equivalents are short-term, highly liquid investments that are both (a) readily convertible to known amounts of cash, and (b) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Only investments with original maturities[1] of three months or less can qualify under this definition, with the exception of money market mutual funds, as detailed in paragraph 8, and cash pooling, as detailed in paragraph 9. Regardless of maturity date, derivative instruments shall not be reported as cash equivalents and shall be reported as derivatives on Schedule DB. Securities with terms that are reset at predefined dates (e.g., an auction-rate security that has a long-term maturity and an interest rate that is regularly reset through a Dutch auction) or have other features an investor may believe results in a different term than the related contractual maturity shall be accounted for based on the contractual maturity at the date of acquisition, except where other specific rules within the statutory accounting framework currently exist.

7. Regardless of maturity date, related party or affiliated investments that would be in scope of *SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities,* or that would be reported as "Other Invested Assets" shall be reported as long-term investments if any of the following conditions apply,[2] unless the reporting entity has re-underwritten the investment, maintained appropriate re-underwriting documentation, and each participating party had the ability to independently review the terms and can terminate the transaction prior to renewal.

a. The reporting entity does not reasonably expect the investment to terminate on the maturity date. This provision includes investments that are expected to be renewed (or rolled) with a maturity date that ends subsequent to the initial 90-day timeframe.

b. The investment was previously reported as a cash equivalent investment and the initial maturity timeframe has passed. If an investment is reported as a cash equivalent and it is unexpectedly renewed/rolled, the reporting entity is not permitted to continue to report the held security as a cash equivalent, regardless of the updated maturity date, and shall report the security as a long-term investment. An investment is only permitted to be reported as a cash equivalent for one quarter reporting period. Meaning, if an investment was reported as a cash equivalent in the first quarter, it is not permitted to be reported as a cash equivalent in the second quarter.

c. The reporting entity reacquired the investment (or a substantially similar investment) within one year after the original security matured or was terminated. These reacquired securities shall be reported as long-term investments. (These securities are also not permitted to be reported as short-term investments, regardless of the maturity date of the reacquired investment.)

[1] Original maturity means original maturity to the entity holding the investment. For example, both a three-month U.S. Treasury bill and a three-year Treasury note purchased three months from maturity qualify as cash equivalents. However, a Treasury note purchased three years ago does not become a cash equivalent when its remaining maturity is three months.

[2] Cash equivalents subject to the provisions of paragraph 7 are not permitted to be subsequently reported as short-term investments, even if the updated/reacquired maturity date is within one year. These investments shall be reported as long-term investments. To avoid changes in reporting schedules, reporting entities are permitted to report securities as long-term investments at initial acquisition, regardless of the initial maturity date.

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8. Money market mutual funds registered under the Investment Company Act of 1940 and regulated under rule 2a-7 of the Act shall be accounted for and reported as cash equivalents for statutory accounting. Investments in money market mutual funds shall be valued at fair value or net asset value (NAV) as a practical expedient. For reporting entities required to maintain an asset valuation reserve (AVR), the accounting for unrealized capital gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities not required to maintain an AVR, unrealized capital gains and losses shall be recorded as a direct credit or charge to surplus. Sales/reinvestments in money market mutual funds are excluded from the wash sale disclosure in SSAP No. 103R.

9. Cash pooling is a technique utilized by some companies under common control by which several entities' cash accounts are aggregated for numerous purposes, including liquidity management, optimizing interest or investment returns and reducing investment or banking transaction fees. Cash pools can have numerous functions and structures; however, only those that have obtained domiciliary regulator approval and meet the following requirements are in scope of this statement.

a. Members or participants in the pool are limited to affiliated entities as defined in *SSAP No. 25—Affiliates and Other Related Parties*.

b. Investments held by the pool are limited to non-affiliated entities investments (non-affiliated to the insurance reporting entity).

c. The pool must permit each participant to withdraw, at any time, cash up to the amount it has contributed to the pool. Each participant must own an undivided interest in the underlying assets of the pool in proportion to the aggregate amount of cash contributed. All affiliates' interests in the pool shall be of the same class, with equal rights, preferences, and privileges. All membership interests shall be fully paid and non-assessable and shall have no preemptive, conversion or exchange rights. The liability of a participant's debts and obligations of the pool shall be limited to the amount of its contributions and no participant shall be obligated to contribute money to the pool for any reason other than to participate in the pool's investments. Additionally, participants shall not cover the debits or credits of another participant (commonly referred to as notional cash pooling).

d. A reporting entity shall receive monthly reports from the pool manager, which identifies the participant's investment (share) in the cash pool and the dollar value of its share of cash, cash equivalents and short-term investments. The reporting entity shall report their total balances in the cash pool on Schedule E – Part 2, utilizing the line number as specified in the annual statement instructions. The reporting entity shall independently if the investments would have qualified as cash, cash equivalents or short-term investments had the entity independently acquired the investments. To the extent the pool holds investments that do not meet the definition of cash, cash equivalents, short-term investments, the pool does not qualify within scope of this statement.

e. Valuation of assets in the pool shall remain consistent with the valuations required by reported asset type as stipulated in this statement.

Drafts

10. A draft is defined as an order to pay a sum certain in money. It is signed by the drawer (e.g., the insurance company or its agent), and payable to order or bearer (e.g., the policyholder). When the draft is presented to the drawee (i.e., the bank), it is paid only upon approval by the reporting entity.

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11. Drafts and checks have different legal characteristics. A check is payable on demand, whereas a draft must be approved for payment by the reporting entity before it is honored by the bank. Because of these different characteristics, a draft meets the definition of a liability as defined by *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Outstanding checks are accounted for as a reduction of cash.

12. A reporting entity that utilizes instruments meeting the definition of drafts shall elect one of the following accounting methods:

a. Draft Issued Method—When a draft is issued, an increase in paid losses and a related decrease in loss reserves is recorded. Drafts that have not been presented for payment and remain outstanding at the balance sheet date are reflected as a liability.

b. Draft Honored Method—An increase in paid losses and a related decrease in loss reserves is recorded when the draft is presented by the bank to the reporting entity for approval and reimbursement. Consequently, under a draft honored method there is no liability for outstanding drafts.

13. The method elected by a reporting entity to account for drafts issued and outstanding shall remain consistent from year to year. Procedures for changes in the accounting method shall be governed by *SSAP No. 3—Accounting Changes and Corrections of Errors*.

Short-Term Investments

14. Short-term investments are investments that do not qualify as cash equivalents with remaining maturities (or repurchase dates under reverse repurchase agreements) of one year or less at the time of acquisition. Short-term investments can include, but are not limited to bonds, commercial paper, reverse repurchase agreements, and collateral and mortgage loans which meet the noted criteria. Short-term investments shall not include investments specifically classified as cash equivalents as defined in this statement, certificates of deposit, or derivatives. Regardless of maturity date, derivative instruments shall not be reported as short-term investments and shall be reported as derivatives on Schedule DB.

15. Regardless of maturity date, related party or affiliated investments in scope of *SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities,* or that would be reported as "Other Invested Assets" shall be reported as long-term investments if any of the following conditions apply,[3, 4] unless the reporting entity has re-underwritten the investment, maintained appropriate re-underwriting documentation, and each participating party had the ability to independently review the terms and can terminate the transaction prior to renewal.

a. The reporting entity does not reasonably expect the investment to terminate on the maturity date. This provision includes investments that are expected to be renewed (or rolled) with a maturity date that ends subsequent to the initial "less than one year" timeframe.

b. The investment was previously reported as a short-term investment and the initial maturity timeframe has passed. If an investment is reported as a short-term investment and it is unexpectedly renewed/rolled, the reporting entity is not permitted to continue to report the held security as a short-term investment (or as a cash equivalent) regardless of

[3] Reverse repurchase transactions are excluded from these provisions if admitted in accordance with collateral requirements pursuant *to SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.*

[4] Short-term investments subject to the provisions of paragraph 15 are not permitted to be subsequently reported as cash equivalents, even if the updated/reacquired maturity date is within 90 days. These investments shall be reported as long-term investments. To avoid changes in reporting schedules, reporting entities are permitted to report securities as long-term investments at initial acquisition, regardless of the initial maturity date.

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the updated maturity date and shall report the security as a long-term investment. An investment is only permitted to be reported as a short-term investment for one annual reporting period. Meaning, if an investment was reported as a short-term investment as of December 31, 2018, it is not permitted to be reported as short-term investment as of December 31, 2019.

c. The reporting entity reacquired the investment (or a substantially similar investment) within one year after the original security matured or was terminated. These reacquired securities shall be reported as long-term investments. (These securities are also not permitted to be reported as cash equivalent investments regardless of the maturity date of the reacquired investment.)

16. All short-term investments shall be accounted for in the same manner as similar long-term investments.

17. Short-term investments meet the definition of assets as defined in SSAP No. 4 and are admitted assets to the extent they conform to the requirements of this statement.

Disclosures

18. The following disclosures shall be made for short-term investments in the financial statements:

a. Fair values in accordance with *SSAP No. 100R—Fair Value*;

b. Concentrations of credit risk in accordance with *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures*;

c. Basis at which the short-term investments are stated.

d. The items in the scope of this statement are also subject to the annual audited disclosures in *SSAP No. 26R—Bonds*, paragraph 30.f.

e. Identification of cash equivalents (excluding money market mutual funds as detailed in paragraph 8) and short-term investments (or substantially similar investments), which remain on the same reporting schedule for more than one consecutive reporting period. This disclosure is satisfied by use of a designated code in the investment schedules of the statutory financial statements.

19. The financial statements shall disclose the reporting entity's share of the cash pool by asset type (cash, cash equivalents or short-term investments).

20. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures in paragraph 18.b. and paragraph 18.d. of this statement shall be included in the annual audited statutory financial reports only.

Relevant Literature

21. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment

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guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~21.~~22. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. Guidance in paragraph 6 of this statement related to terms reset at predefined dates was previously included within *INT 08-10: Contractual Terms of Investments and Investor Intent* and was effective for periods beginning December 5, 2008. This substantively revised statement, as detailed in Issue Paper No. 155 regarding treatment of money market mutual funds as cash equivalents, is effective on a prospective basis beginning December 31, 2017.

~~22.~~23. Revisions permitting cash liquidity pools that meet the specific criteria are effective May 20, 2020, for reporting entities with qualifying cash pools. Reporting entities with cash liquidity pools that do not meet the requirements for reporting within scope of this standard are not permitted to be reported as cash equivalents or short-term investments and shall be reported as a prescribed or permitted practice. (Prior to this adoption date, there was no guidance permitting cash liquidity pools to be captured in scope of this standard.) For reporting entities that will have to reclassify qualifying cash liquidity pools to a cash equivalent from a different investment schedule, the reporting entity may elect to complete these reclassifications effective January 1, 2021, with early adoption permitted.

REFERENCES

Other

- Purposes and Procedures Manual of the NAIC Investment Analysis Office

Relevant Issue Papers

- Issue Paper No. 2—Definition of Cash
- Issue Paper No. 12—Accounting for Drafts Issued and Outstanding
- Issue Paper No. 28—Short-Term Investments
- Issue Paper No. 155—Classification of Money Market Mutual Funds as Cash Equivalents

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Statement of Statutory Accounting Principles No. 3

Accounting Changes and Corrections of Errors

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 00-05 and INT 01-27
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Change in Accounting Principle 2
Change in Accounting Estimate 2
Correction of an Error 2
Impact on Historical Schedules 3
Mergers 3
Disclosures 3
Relevant Literature 4
Effective Date and Transition 4

REFERENCES **4**

Relevant Issue Papers 4

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for changes in accounting, which include changes in accounting principles, estimates, and reporting entities, and for corrections of errors in previously issued financial statements.

SUMMARY CONCLUSION

2. An accounting change is defined as a change in an accounting principle, an accounting estimate, or the reporting entity. The correction of an error in previously issued financial statements is not deemed to be an accounting change. The treatment of a change resulting from an insurance department examination will depend on whether the change resulted from a correction of an error, a change in accounting principle, or a change in estimate.

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Change in Accounting Principle

3. A change in accounting principle results from the adoption of an accepted accounting principle, or method of applying the principle, which differs from the principles or methods previously used for reporting purposes. A change in the method of applying an accounting principle shall be considered a change in accounting principle.

4. A characteristic of a change in accounting principle is that it concerns a choice from among two or more statutory accounting principles. However, a change in accounting principle is neither (a) the initial adoption of an accounting principle in recognition of events or transactions occurring for the first time or previously immaterial in their effect, nor (b) the adoption or modification of an accounting principle necessitated by transactions or events that are clearly different in substance from those previously occurring.

5. The cumulative[1] effect of changes in accounting principles shall be reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle. The cumulative effect is the difference between the amount of capital and surplus at the beginning of the year and the amount of capital and surplus that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods.

Change in Accounting Estimate

6. Changes in estimates used in accounting are necessary consequences of periodic presentations of financial statements which require estimating the effects of future events. Examples of items for which estimates are necessary include service lives of depreciable assets and changes in loss reserve estimates for property and casualty companies. Accounting estimates change as new events occur, as more experience is acquired, or as additional information is obtained.

7. A change in accounting estimate shall be included in the statement of income in the period when the change becomes known.

8. If the effect of a change in accounting principle is inseparable from the effect of a change in accounting estimate, then the change shall be considered as a change in accounting estimate for purposes of applying the accounting principles set forth in this statement.

Correction of an Error

9. Accounting errors in financial statements result from mathematical mistakes, mistakes in the application of accounting principles, or oversight or misuse of facts that existed at the time the financial statements were prepared. In contrast, a change in accounting estimate results from new information, or subsequent developments and, accordingly, from better insight or improved judgment. Thus, an error is distinguished from a change in estimate.

10. If a reporting entity becomes aware of a material accounting error in a previously filed financial statement after it has been submitted to the appropriate regulatory agency, the entity shall file an amended financial statement unless otherwise directed by the domiciliary regulator. Correction of all accounting

[1] If additional changes are identified in subsequent quarters of a fiscal year related to a change in accounting principles recognized initially during the first quarter, such changes shall be considered part of the cumulative effect of the change in accounting principle. The cumulative effect is the difference between the amount of capital and surplus at the beginning of the year and the amount of capital and surplus that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods. For example, adjustments to an amount recorded as of January 1, 2001, would be recorded as changes in accounting principle rather than corrections of an error through the period of 2001.

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errors in previously issued financial statements, for which an amended financial statement was not filed, shall be reported as adjustments to unassigned funds (surplus) in the period an error is detected.

Impact on Historical Schedules

11. Changes which do not affect assets, liabilities, revenues, expenses, or surplus but which materially affect historical information in the financial statement supplemental schedules (e.g., Schedule P for property and casualty insurers or Schedule O for life and accident and health insurers) shall be reflected in the current year's schedules with appropriate notations made directly to the affected schedules and in the notes to the financial statements.

Mergers

12. For mergers, prior years' amounts in the annual statement shall be restated as if the merger had occurred as of January 1 of the prior year. Additionally, restatement shall be required for the two most recent years included in the Five-Year Historical Summary. The Five-Year Historical Summary shall include a footnote indicating that the other three years have not been restated. A reporting entity that merges with an entity which effectively is a shell company[2] (i.e., the reporting entity has no outstanding underwriting liabilities) shall be exempt from prior year restatement.

Disclosures

13. Disclosure of material changes in accounting and correction of errors shall include:

a. A brief description of the change, encompassing a general disclosure of the reason and justification for change or correction;

b. The impact of the change or correction on net income, surplus, total assets, and total liabilities for the two years presented in the financial statements (i.e., the balance sheet and statement of income and operations);

c. The effect on net income of the current period for a change in estimate that affects several future periods, such as a change in the service lives of depreciable assets or actuarial assumptions affecting pension costs. Disclosure of the effect on those income statement amounts is not necessary for estimates made each period in the ordinary course of accounting for items such as uncollectible accounts; however, disclosure is recommended if the effect of a change in the estimate is material;

d. Changes in accounting that are changes in reserve valuation basis as described in *SSAP No. 51R—Life Contracts,* which have elected phase-in provided for in the *Valuation Manual*, Section VM 21, shall also include in the change in accounting disclosures information regarding the application of any phase-in as provided for in SSAP No. 51R; and

e. When subsequent financial statements are issued containing comparative restated results as a result of the filing of an amended financial statement, the reporting entity shall disclose that the prior period has been restated and the nature and amount of such restatement.

14. Refer to the Preamble for further discussion regarding disclosure requirements.

[2] When one of the entities is a "shell company," the prior year amounts shall only consist of the "non-shell company." The merger with a shell entity shall be reflected as of January 1 of the current year.

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Relevant Literature

15. This statement rejects *ASU 2016-03, Intangibles—Goodwill and Other, Business Combinations, Consolidation, Derivatives and Hedging; Accounting Research Bulletin No. 51, Consolidated Financial Statements; FASB Interpretation No. 46, Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51;* and *FASB Statement No. 94, Consolidation of All Majority-Owned Subsidiaries, an amendment of ARB 51, with related amendments of APB Opinion No. 18 and ARB No. 43, Chapter 12*.

16. This statement rejects paragraphs 1-19 and 26-27 of *Accounting Principles Board Opinion No. 9, Reporting the Results of Operations,* which address the treatment of extraordinary items and prior period adjustments and the related *AICPA Accounting Interpretations, Reporting the Results of Operations: Unofficial Accounting Interpretations of APB Opinion No. 9*. This statement also rejects *Accounting Principles Board Opinion No. 20*, *Accounting Changes, AICPA Accounting Interpretations, Accounting Changes: Accounting Interpretations of APB Opinion No. 20, FASB Interpretation No. 20, Reporting Accounting Changes under AICPA Statements of Position, an interpretation of APB Opinion No. 20* and *FASB Statement No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3 (FAS 154). FASB Statement No. 16*, *Prior Period Adjustments,* is rejected as corrections of errors in previously issued financial statements are reported as adjustments to unassigned funds (surplus).

Effective Date and Transition

17. This statement is effective for years beginning January 1, 2001. The guidance in the footnote to paragraph 5 was originally contained within *INT 01-27: Accounting Change versus Correction of Error* and was effective October 16, 2001. The guidance in the footnote to paragraph 12 was originally contained within *INT 00-05: Exemption to Merger Disclosure in SSAP No. 3* and was effective June 12, 2000.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 1—Consolidation of Majority-owned Subsidiaries*
- *Issue Paper No. 3—Accounting Changes*

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Statement of Statutory Accounting Principles No. 4

Assets and Nonadmitted Assets

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 87 with guidance incorporated August 2011; Nullifies and incorporates INT 01-03
Affected by	No other pronouncements
Interpreted by	INT 01-31; INT 23-03
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Assets Pledged as Collateral or Otherwise Restricted 2
Disclosure 3
Relevant Literature 3
Effective Date and Transition 3

REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes the definition of an "asset" for use in statutory accounting and establishes the criteria for consistent treatment of nonadmitted assets.

SUMMARY CONCLUSION

2. For purposes of statutory accounting, an asset shall be defined as: a present right of an entity to an economic benefit. An asset has two essential characteristics: (a) it is a present right, and (b) the right is to an economic benefit.[1] These assets shall then be evaluated to determine whether they are admitted.[2] The criteria used is outlined in paragraph 3.

[1] *FASB Statement of Financial Accounting Concepts No. 8, Elements of Financial Statements*, states that the combination of these two characteristics allows an entity to obtain the economic benefit and control others' access to the benefit. A present right of an entity to an economic benefit entitles the entity to the economic benefit and the ability to restrict others' access to the benefit to which the entity is entitled.

[2] If assets of an insurance entity are pledged or otherwise restricted by the action of a related party, the assets are not under the exclusive control of the insurance entity and are not available to satisfy policyholder obligations due to these encumbrances or other third-party interests. Thus, pursuant to paragraph 2, such assets shall not be recognized as an admitted asset on the balance sheet. Additional guidance for assets pledged as collateral is included in INT 01-31.

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3. As stated in the Statement of Concepts, "The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third-party interests should not be recognized on the balance sheet," and are, therefore, considered nonadmitted. For purposes of statutory accounting principles, a nonadmitted asset shall be defined as an asset meeting the criteria in paragraph 2, which is accorded limited or no value in statutory reporting, and is one which is:

a. Specifically identified within the *Accounting Practices and Procedures Manual* as a nonadmitted asset; or

b. Not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*.

If an asset meets one of these criteria, the asset shall be reported as a nonadmitted asset and charged against surplus unless otherwise specifically addressed within the *Accounting Practices and Procedures Manual*. The asset shall be depreciated or amortized against net income as the estimated economic benefit expires. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of furniture, fixtures, equipment, or supplies, shall be expensed when purchased.

4. Transactions which do not give rise to assets as defined in paragraph 2 shall be charged to operations in the period the transactions occur. Those transactions which result in amounts which may meet the definition of assets, but are specifically identified within the *Accounting Practices and Procedures Manual* as not giving rise to assets (e.g., policy acquisition costs), shall also be charged to operations in the period the transactions occur.

5. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Assets Pledged as Collateral or Otherwise Restricted

6. Assets that are pledged to others as collateral or otherwise restricted (not under the exclusive control of the insurer, subject to a put option contract, etc.) shall be identified in the investment schedules pursuant to the codes in the annual statement instructions, disclosed in accordance with *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*, reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for assets pledged as collateral or otherwise restricted. Restricted assets should be reviewed to determine admitted or nonadmitted assets status in the statutory financial statements per the terms of their respective SSAPs. Asset restrictions may be a factor in determining the admissibility of an asset under a respective SSAP[3]. However, determining that a restricted asset is an admitted asset does not eliminate the statutory requirements to document and identify the asset as one that is pledged as collateral or otherwise restricted.

7. Assets pledged as collateral are one example of assets that are not under the exclusive control of the insurer, and are therefore restricted, even if the assets are admitted under statutory accounting guidelines (e.g., the asset is substitutable and/or other related SSAP conditions are met). As such, the asset shall be coded as pledged in the investment schedules pursuant to the annual statement instructions, disclosed in accordance with SSAP No. 1, reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for assets pledged as collateral or otherwise restricted.

[3] An example of such a situation is detailed in footnote 2 pertaining to assets restricted by the action of a related party. This is only a single example and each restricted asset would need to be reviewed to ensure it qualifies as an admitted asset.

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Disclosure

8. The financial statements shall disclose if the written capitalization policy and the resultant predefined thresholds changed from the prior period and the reason(s) for such change.

Relevant Literature

9. This statement incorporates the definition of an asset from *FASB Statement of Financial Accounting Concepts No. 8, Chapter 4, Elements of Financial Statements,* paragraphs E16-E18.

Effective Date and Transition

10. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance reflected in paragraphs 3, 5 and 8, incorporated from SSAP No. 87, was originally effective for years beginning on and after January 1, 2004. The guidance in footnote 2 to paragraph 2 was originally contained within *INT 01-03: Assets Pledged as Collateral or Restricted for the Benefit of a Related Party* and was effective June 11, 2001.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*
- *Issue Paper No. 119—Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29, 73, 79 and 82*
- *Issue Paper No. 166—Updates to the Definition of an Asset*

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Statement of Statutory Accounting Principles No. 5 – Revised

Liabilities, Contingencies and Impairments of Assets

STATUS

Type of Issue	Common Area
Issued	Initial draft; Substantively revised October 18, 2010
Effective Date	January 1, 2001; Substantive revisions December 31, 2011
Affects	Nullifies and incorporates INT 04-01 and INT 08-06
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SUMMARY CONCLUSION **1**

Liabilities 1
Joint and Several Liabilities 2
Loss Contingencies or Impairments of Assets 2
Tax Contingencies 3
Gain Contingencies 4
Guarantees 4
Financial Instruments with Characteristics of Both Liabilities and Equity 7
Disclosures 8
Relevant Literature 10
Effective Date and Transition 11

REFERENCES **12**

Relevant Issue Papers 12

SCOPE OF STATEMENT

1. This statement defines and establishes statutory accounting principles for liabilities, contingencies and impairments of assets.

SUMMARY CONCLUSION

Liabilities

2. A liability is defined as a present obligation of an entity to transfer an economic benefit.~~certain or probable[1] future sacrifices of economic benefits arising from present obligations of a particular entity to~~

[1] ~~*FASB Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements*, states: Probable is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in *FASB Statement 5, Accounting for Contingencies*, paragraph 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved.~~

~~transfer assets or to provide services to other entities in the future as a result of a past transaction(s) or event(s).~~

3. A liability[2] has ~~three~~two essential characteristics: (a) it is a present obligation~~embodies a present duty or responsibility to one or more other entities that entails settlement by probable[1] future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand~~, and (b) the obligation requires an entity to transfer or otherwise provide economic benefit to others.~~duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice, and (c) the transaction or other event obligating the entity has already happened.~~ This includes, but is not limited to, liabilities arising from policyholder obligations (e.g., policyholder benefits, reported claims and reserves for incurred but not reported claims). Liabilities shall be recorded on a reporting entity's financial statements when incurred.

4. Estimates (e.g., loss reserves) are required in financial statements for many ongoing and recurring activities of a reporting entity. The mere fact that an estimate is involved does not of itself constitute a loss contingency. For example, estimates of losses utilizing appropriate actuarial methodologies meet the definition of liabilities as outlined above and are not loss contingencies.

Joint and Several Liabilities

5. Joint and several liability arrangements for which the total obligation amount under the arrangement is fixed[3] at the reporting dates shall be measured and reported as the sum of:

a. The amount the reporting entity agreed to pay on the basis of the agreements among its co-obligors, and

b. Any additional amount the reporting entity expects to pay on behalf of its co-obligors. When an amount within management's estimate of the range of a loss appears to be a better estimate than any other amount within the range, that amount shall be the additional amount included in the measurement of the obligation. If no amount within the range is a better estimate than any other amount, then the midpoint shall be used.

6. Although the total amount of the obligation of the entity and its co-obligors must be fixed at the reporting date to be within the scope of this statement, the amount that the reporting entity expects to pay on behalf of its co-obligors may be uncertain at the reporting date.

Loss Contingencies or Impairments of Assets

~~6.~~7. For purposes of implementing the statutory accounting principles of loss contingency or impairment of an asset described below, the following additional definitions shall apply:

a. Probable—The future event or events are likely to occur;

b. Reasonably Possible—The chance of the future event or events occurring is more than remote but less than probable;

[2] The guidance in this statement regarding the definition of a liability is applicable unless another authoritative statement of statutory accounting principles (SSAP) provides more topic-specific, contradictory guidance. In such cases the topic-specific guidance shall apply.

[3] Examples of items within the scope of this guidance include debt arrangements, other contractual obligations, and settled judicial litigation and judicial rulings. Loss contingencies, guarantees, pension and other postretirement benefit obligations and taxes are excluded from this guidance and shall be accounted for under the statutory accounting provisions specific to those topics.

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c. Remote—The chance of the future event or events occurring is slight.

~~7.~~8. A loss contingency or impairment of an asset is defined as an existing condition, situation, or set of circumstances involving uncertainty as to possible loss to an enterprise that will ultimately be resolved when one or more future event(s) occur or fail to occur (e.g., collection of receivables).

~~8.~~9. An estimated loss from a loss contingency or the impairment of an asset shall be recorded by a charge to operations if both of the following conditions are met:

a. Information available prior to issuance of the statutory financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the statutory financial statements. It is implicit in this condition that it is probable that one or more future events will occur confirming the fact of the loss or incurrence of a liability; and

b. The amount of loss can be reasonably estimated.

~~9.~~10. This accounting shall be followed even though the application of other prescribed statutory accounting principles or valuation criteria may not require, or does not address, the recording of a particular liability or impairment of an asset (e.g., a known impairment of a bond even though the VOS manual has not recognized the impairment).

~~10.~~11. Additionally, in instances where a judgment, assessment or fine has been rendered against a reporting entity, there is a presumption that the criteria in paragraph ~~8~~9.a. and ~~8~~9.b. have been met. A judgment is considered "rendered" when a court enters a verdict, notwithstanding the entity's ability to file post-trial motions and to appeal. The amount of the liability shall include the anticipated settlement amount, legal costs, insurance recoveries and other related amounts and shall take into account factors such as the nature of the litigation, progress of the case, opinions of legal counsel, and management's intended response to the litigation, claim, or assessment.

~~11.~~12. When the condition in paragraph ~~8~~9.a. is met with respect to a particular loss contingency, and the reasonable estimate of the loss is a range, which meets the condition in paragraph ~~8~~9.b., an amount shall be accrued for the loss. When an amount within management's estimate of the range of a loss appears to be a better estimate than any other amount within the range, that amount shall be accrued. When, in management's opinion, no amount within management's estimate of the range is a better estimate than any other amount, however, the midpoint (mean) of management's estimate in the range shall be accrued. For purposes of this paragraph, it is assumed that management can quantify the high end of the range. If management determines that the high end of the range cannot be quantified, then a range does not exist, and management's best estimate shall be used.

~~12.~~13. The use of the midpoint in a range will be applicable only in the rare instance where there is a continuous range of possible values, and no amount within that range is any more probable than any other. This guidance is not applicable when there are several point estimates which have been determined as equally possible values, but those point estimates do not constitute a range. If there are several point estimates with equal probabilities, management should determine their best estimate of the liability.

Tax Contingencies

~~13.~~14. As directed by *SSAP No. 101—Income Taxes*, tax loss contingencies (including related interest and penalties) for current and all prior years, shall be computed in accordance with this SSAP, with the following modifications:

a. The term "probable" as used in this standard shall be replaced by the term "more likely than not (a likelihood of more than 50% ~~percent~~)" for federal and foreign income tax loss contingencies only.

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b. For purposes of the determination of a federal and foreign income tax loss contingency, it shall be presumed that the reporting entity will be examined by the relevant taxing authority that has full knowledge of all relevant information.

c. If the estimated tax loss contingency is greater than 50% ~~percent~~ of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% ~~percent~~ of the original tax benefit recognized.

As noted in SSAP No. 101, state taxes (including premium, income and franchise taxes) shall also be computed in accordance with this SSAP. These items (as detailed in SSAP No. 101) are not impacted by the modifications detailed in paragraphs ~~13~~14.a.-~~13~~14.c.

Gain Contingencies

~~14.~~15. A gain is defined as an increase in surplus which results from peripheral or incidental transactions of a reporting entity and from all other transactions and other events and circumstances affecting the reporting entity except those that result from revenues or investments by owners. If, on or before the balance sheet date, (a) the transaction or event has been fully completed, and (b) the amount of the gain is determinable, then the transaction or event is considered a gain, and is recognized in the financial statements. The definition of a gain excludes increases in surplus that result from activities that constitute a reporting entity's ongoing major or central operations or activities. Because investment activities are central to an insurer's operations, increases in surplus that result from such investment activities are excluded from the definition of gains. Revenues are inflows or other enhancements of assets of a reporting entity or settlements of its liabilities (or a combination of both) from providing products, rendering services, or other activities that constitute the reporting entity's ongoing major or central operations. Investments by owners include any type of capital infused into the surplus of the reporting entity.

~~15.~~16. A gain contingency is defined as an existing condition, situation, or set of circumstances involving uncertainty as to possible gain (as defined in the preceding paragraph) to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur (e.g., a plaintiff has filed suit for damages associated with an event occurring prior to the balance sheet, but the outcome of the suit is not known as of the balance sheet date). Gain contingencies shall not be recognized in a reporting entity's financial statements. However, if subsequent to the balance sheet date but prior to the issuance of the financial statements, the gain contingency is realized, the gain shall be disclosed in the notes to financial statements and the unissued financial statements should not be adjusted to record the gain. A gain is generally considered realizable when noncash resources or rights are readily convertible to known amounts of cash or claims to cash.

Guarantees

~~16.~~17. A guarantee contract is a contract that contingently requires the guarantor to make payments (either in cash, financial instruments, other assets, shares of its stock, or provision of services) to the guaranteed party based on changes in the underlying that is related to an asset, a liability, or an equity security of the guaranteed party. Commercial letters of credit and loan commitments, by definition, are not considered guarantee contracts. Also excluded from the definition are indemnifications or guarantees of an entity's own performance, subordination arrangements or a noncontingent forward contract. This definition could include contingent forward contracts if the characteristics of this paragraph are met.

~~17.~~18. The following guarantee contracts are not subject to the guidance in paragraphs ~~20-26~~21-27 and paragraphs ~~33-36~~34-37:

a. Guarantees already excluded from the scope of SSAP No. 5R;

b. Guarantee contracts accounted for as contingent rent;

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c. Insurance contract guarantees, including guarantees embedded in deposit-type contracts;

d. Contracts that provide for payments that constitute a vendor rebate by the guarantor based on either the sales revenue or the number of units sold by the guaranteed party;

e. A guarantee or indemnification whose existence prevents the guarantor from being able to either account for a transaction as the sale of an asset that is related to the guarantee's underlying or recognize in earnings the profit from that sale transaction;

f. Registration payment arrangements; and

g. A guarantee that is accounted for as a credit derivative instrument at fair value under *SSAP No. 86—Derivatives*, as described in paragraph 62.e. of SSAP No. 86.

~~18.~~19. The following types of guarantees are exempted from the initial liability recognition in paragraphs ~~20-26~~21-27, but are subject to the disclosure requirements in paragraphs ~~33-36~~34-37:

a. Guarantee that is accounted for as a derivative instrument, other than credit derivatives within SSAP No. 86;

b. Guarantee for which the underlying is related to the performance of nonfinancial assets that are owned by the guaranteed party, including product warranties;

c. Guarantee issued in a business combination that represents contingent consideration;

d. Guarantee in which the guarantor's obligation would be reported as an equity item;

e. Guarantee by an original lessee that has become secondarily liable under a new lease that relieved the original lessee from being the primary obligator;

f. Guarantees (as defined in paragraph ~~16~~17) made to/or on behalf of directly or indirectly wholly-owned insurance or non-insurance subsidiaries[4]; and

g. Intercompany and related party guarantees that are considered "unlimited" (e.g., typically in response to a rating agency's requirement to provide a commitment to support).

The exemptions for paragraphs ~~18~~19.f. and ~~18~~19.g. do not apply in situations in which a reporting entity has provided a financial guarantee or commitment to support a subsidiary, controlled or affiliated entity (SCA), and the SCA's equity is negative (see paragraph ~~25~~26).

~~19.~~20. With the exception of the provision for guarantees made to/or on behalf of a wholly-owned subsidiaries in paragraph ~~18~~19.f. and "unlimited" guarantees in paragraph ~~18~~19.g., this guidance does not exclude guarantees issued as intercompany transactions or between related parties from the initial liability recognition requirement. Thus, unless the guarantee is provided on behalf of a wholly-owned subsidiary or considered "unlimited," guarantees issued between the following parties are subject to the initial recognition and disclosure requirements:

[4] The exclusion for wholly-owned subsidiaries includes guarantees from a parent to, or on behalf of, a direct wholly-owned insurance or non-insurance subsidiary as well as guarantees made from a parent to, or on behalf of, an indirect wholly-owned insurance or non-insurance subsidiary. The "wholly-owned" exclusion in paragraph 18.f. does not include guarantees issued from one subsidiary to another subsidiary, regardless if both subsidiaries are wholly-owned (directly or indirectly) by a parent company.

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a. Guarantee issued either between parents and their subsidiaries or between corporations under common control;

b. A parent's guarantee of its subsidiary's debt to a third party; and

c. A subsidiary's guarantee of the debt owed to a third party by either its parent or another subsidiary of that parent.

~~20.~~21. At the inception of a guarantee, the guarantor shall recognize in its statement of financial position a liability for that guarantee. Except as indicated in paragraph ~~22~~23, the objective of the initial measurement of the liability is the fair value[5] of the guarantee at its inception.

~~21.~~22. The issuance of a guarantee obligates the guarantor (the issuer) in two respects: (a) the guarantor undertakes an obligation to stand ready to perform over the term of the guarantee in the event that the specified triggering events or conditions occur (the noncontingent aspect) and (b) the guarantor undertakes a contingent obligation to make future payments if those triggering events or conditions occur (the contingent aspect). Because the issuance of a guarantee imposes a noncontingent obligation to stand ready to perform in the event that the specified triggering event occurs, the provisions of paragraph ~~8~~9 should not be interpreted as prohibiting the guarantor from initially recognizing a liability for that guarantee even though it is not probable that payments will be required under that guarantee.

~~22.~~23. In the event that, at the inception of the guarantee, the guarantor is required to recognize a liability under paragraph ~~8~~9 for the related contingent loss, the liability to be initially recognized for that guarantee shall be the greater of (a) the amount the satisfies the fair value objective as discussed in paragraph ~~20~~21 or (b) the contingent liability amount required to be recognized at inception of the guarantee by paragraph ~~8~~9. For many guarantors, it would be unusual for the contingent liability under (b) to exceed the amount that satisfies the fair value objective at the inception of the guarantee.

~~23.~~24. The offsetting entry pursuant to the liability recognition at the inception of the guarantee depends on the circumstances in which the guarantee was issued. Examples include:

a. If the guarantee was issued in a standalone transaction for a premium, the offsetting entry would the consideration received.

b. If the guarantee was issued in conjunction with the sale of assets, a product, or a business, the overall proceeds would be allocated between the consideration being remitted to the guarantor for issuing the guarantee and the proceeds from that sale. That allocation would affect the calculation of the gain or loss on the sale transaction.

c. If a residual value guarantee were provided by a lessee-guarantor when entering into an operating lease, the offsetting entry would be reflected as prepaid rent, which would be nonadmitted under SSAP No. 29.

d. If a guarantee were issued to an unrelated or related party for no consideration on a standalone basis, the offsetting entry would be to expense.

~~24.~~25. Except for the measurement and recognition of continued guarantee obligations after the settlement of a contingent guarantee liability described in paragraph ~~26~~27, this standard does not describe

[5] As practical expedients, when a guarantee is issued in a standalone arm's-length transaction, the liability recognized at the inception of the guarantee should be the premium received or receivable by the guarantor. When a guarantee is issued as part of a transaction with multiple elements, the liability recognized at the inception of the guarantee should be an estimate of the guarantee's fair value. In that circumstance, guarantors should consider what premium would be required by the guarantor to issue the same guarantee in a standalone arm's-length transaction.

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in detail how the guarantor's liability for its obligations under the guarantee would be measured subsequent to initial recognition. The liability that the guarantor initially recognized in accordance with paragraph ~~20~~21 would typically be reduced (as a credit to income) as the guarantor is released from risk under the guarantee. Depending on the nature of the guarantee, the guarantor's release from risk has typically been recognized over the term of the guarantee (a) only upon either expiration or settlement of the guarantee, (b) by a systematic and rational amortization method, or (c) as the fair value of the guarantee changes (for example, guarantees accounted for as derivatives). The reduction of liability does not encompass the recognition and subsequent adjustment of the contingent liability recognized under paragraph ~~8~~9 related to the contingent loss for the guarantee. If the guarantor is required to subsequently recognize a contingent liability for the guarantee, the guarantor shall eliminate any remaining noncontingent liability for that guarantee and recognize a contingent liability in accordance with paragraph ~~8~~9.

~~25.~~26. In situations in which a reporting entity has provided a financial guarantee or commitment to support a subsidiary, controlled or affiliated entity (SCA), and the reporting entity's share of losses in the SCA exceed the equity method carrying amount of the SCA (resulting in a negative equity value in the SCA), the reporting entity shall recognize the greater impact of (i) the then-current fair value liability for the guarantee, or (ii) the negative equity position, limited to the maximum amount of the financial guarantee or commitment provided by the reporting entity. (This guidance requires the recognition of a guarantee liability for guarantees captured in paragraphs ~~18~~19.f. and ~~18~~19.g. when negative equity exists in an SCA.) The guidance in paragraphs ~~20~~21 through ~~26~~27 shall be followed for the recognition of a contingent liability and a noncontingent liability, as applicable.

~~26.~~27. After recognition and settlement of a contingent guarantee liability in accordance with paragraph ~~8~~9, a guarantor shall assess whether remaining potential obligations exist under the guarantee agreement. If the guarantor still has potential obligations under the guarantee contract, the guarantor shall recognize the remaining noncontingent guarantee that represents the current fair value of the potential obligation remaining under the guarantee agreement. This noncontingent guarantee liability shall be released in accordance with paragraph ~~24~~25.

Financial Instruments with Characteristics of Both Liabilities and Equity

~~27.~~28. Issued, free-standing financial instruments with characteristics of both liability and equity shall be reported as a liability to the extent the instruments embodies an unconditional obligation of the issuer. (Pursuant to SSAP No. 86, embedded features in derivative contracts shall not be separated from the host contract for separate recognition.) Free-standing financial instruments that meet any of the criteria below meet the definition of a liability:

a. A mandatorily redeemable financial instrument shall be classified as a liability unless the redemption is required to occur only upon the liquidation or termination of the issuing reporting entity.

b. A financial instrument, other than an outstanding share, that at inception both: 1) embodies an obligation to repurchase the issuer's equity shares or is indexed to such an obligation, and 2) requires or may require the issuer to settle the obligation by transferring assets.

c. Obligations that permit the holder to require the issuer to transfer assets.

d. A financial instrument is a liability if the issuer must settle the obligation by issuing a variable number of its equity shares and the obligation's monetary value is based solely or predominantly on: 1) a fixed monetary amount, 2) variation in something other than the fair value of the issuer's equity shares, or 3) variations inversely related to changes in the fair value of the issuer's equity shares.

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e. Instruments in which the counterparty (holder) is not exposed to the risks and benefits that are similar to those of a holder of an outstanding share of the entity's equity shall be classified as a liability.

~~28.~~29. If a free-standing financial instrument will be redeemed only upon the occurrence of a conditional event, redemption of that instrument is conditional and, therefore, the instrument does not meet the definition of mandatorily redeemable financial instrument. However, that financial instrument shall be assessed each reporting period to determine whether circumstances have changed such that the instrument meets the definition of a mandatorily redeemable instrument (that is, the event is no longer conditional). If the event has occurred, the condition is resolved, or the event has become certain to occur, the financial instrument shall be reclassified as a liability.

~~29.~~30. The classification of a free-standing financial instrument as a liability or equity shall only apply to the instrument issuer. Holders or purchasers of such instruments shall refer to the appropriate investment statement for valuation and reporting.

Disclosures

~~30.~~31. Disclose the following information for each joint and several liability arrangements accounted for under paragraph 5. If co-obligors are related parties, disclosure requirements in *SSAP No. 25—Affiliates and Other Related Parties* also apply.

a. The nature of the arrangement including: 1) how the liability arose, 2) the relationship with co-obligors, and 3) the terms and conditions of the arrangements.

b. The total outstanding amount under the arrangement, which shall not be reduced by the effect of any amounts that may be recoverable from other entities.

c. The carrying amount, if any, of the entity's liability and the carrying amount of a receivable recognized, if any.

d. The nature of any recourse provisions that would enable recovery from other entities of the amounts paid, including any limitations on the amounts that might be recovered.

e. In the period the liability is initially recognized and measured or in a period the measurement changes significantly: 1) the corresponding entry, and 2) where the entry was recorded in the financial statements.

~~31.~~32. If a loss contingency or impairment of an asset is not recorded because only one of the conditions in paragraph ~~8~~9.a. or ~~8~~9.b. is met, or if exposure to a loss exists in excess of the amount accrued pursuant to the provisions described above, disclosure of the loss contingency or impairment of the asset shall be made in the financial statements when there is at least a reasonable possibility that a loss or an additional loss may have been incurred. The disclosure shall indicate the nature of the contingency and shall give an estimate of the possible loss or range of loss or state that such an estimate cannot be made. (Disclosures for tax contingencies as identified in paragraph ~~13~~14 shall be completed as instructed within SSAP No. 101.)

~~32.~~33. Disclosure is not required of a loss contingency involving an unasserted claim or assessment when there has been no manifestation by a potential claimant of an awareness of a possible claim or assessment unless it is considered probable that a claim will be asserted and there is a reasonable possibility that the outcome will be unfavorable.

~~33.~~34. Certain loss contingencies, the common characteristic of each being a guarantee, shall be disclosed in financial statements even though the possibility of loss may be remote. Examples include (a) guarantees of indebtedness of others, and (b) guarantees to repurchase receivables (or, in some cases,

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to repurchase related properties) that have been sold or otherwise assigned. The disclosure of those loss contingencies, and others that in substance have the same characteristics, shall be applied to statutory financial statements. The disclosure shall include the nature and amount of the guarantee. Consideration shall be given to disclosing, if estimable, the value of any recovery that could be expected to result, such as from the guarantor's right to proceed against an outside party.

~~34.~~35. A guarantor shall disclose the following information about each guarantee, or each group or similar guarantees (except product warranties addressed in paragraph ~~36~~37), even if the likelihood of the guarantor's having to make any payments under the guarantee is remote. In addition, the nature of the relationship to the beneficiary of the guarantee or undertaking (affiliated or unaffiliated) shall also be disclosed:

a. The nature of the guarantee, including the approximate term of the guarantee, how the guarantee arose, and the events and circumstances that would require the guarantor to perform under the guarantee, the ultimate impact to the financial statements (specific financial statement line item) after the settlement of the contract guarantee if action under the guarantee was required (e.g., increase to the investment, dividends to stockholder, etc.) and the current status (that is, as of the date of the statement of financial position) of the payment/performance risk of the guarantee. For example, the current status of the payment/performance risk of a credit-risk-related guarantee could be based on either recently issued external credit ratings or current internal groupings used by the guarantor to manage its risk. An entity that uses internal groupings shall disclose how those groupings are determined and used for managing risk.

b. The potential amount of future payments (undiscounted) the guarantor could be required to make under the guarantee. That maximum potential amount of future payments shall not be reduced by the effect of any amounts that may possibly be recovered under recourse or collateralization provisions in the guarantee (which are addressed under (d) below). If the terms of the guarantee provide for no limitation to the maximum potential future payments under the guarantee, that fact shall be disclosed. If the guarantor is unable to develop an estimate of the maximum potential amount of future payments under its guarantee, the guarantor shall disclose the reasons why it cannot estimate the maximum potential amount.

c. The current carrying amount of the liability, if any, for the guarantor's obligations under the guarantee (including the amount, if any, recognized under paragraph ~~8~~9), regardless of whether the guarantee is freestanding or embedded in another contract.

d. The nature of (1) any recourse provisions that would enable the guarantor to recover from third parties any of the amounts paid under the guarantee and (2) any assets held either as collateral or by third parties that, upon the occurrence of any triggering event or condition under the guarantee, the guarantor can obtain and liquidate to recover all or a portion of the amounts paid under the guarantee. The guarantor shall indicate, if estimable, the approximate extent to which the proceeds from liquidation of those assets would be expected to cover the maximum potential amount of future payments under the guarantee.

~~35.~~36. An aggregate compilation of guarantee obligations shall include the maximum potential of future payments of all guarantees (undiscounted), the current liability (contingent and noncontingent) reported in the financial statements, and the ultimate financial statement impact based on maximum potential payments (undiscounted) if performance under those guarantees had been triggered.

~~36.~~37. As product warranties are excluded from the initial recognition and initial measurement requirements for guarantees, a guarantor is not required to disclose the maximum potential amount of

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future payments. Instead the guarantor is required to disclose for product warranties the following information:

a. The guarantor's accounting policy and methodology used in determining its liability for product warranties (Including any liability associated with extended warranties).

b. A tabular reconciliation of the changes in the guarantor's aggregate product warranty liability for the reporting period. That reconciliation should present the beginning balance of the aggregate product warranty liability, the aggregate reductions in that liability for payments made (in cash or in kind) under the warranty, the aggregate changes in the liability for accruals related to product warranties issued during the reporting period, the aggregate changes in the liability for accruals related to preexisting warranties (including adjustments related to changes in estimates), and the ending balance of the aggregate product warranty liability.

~~37.~~38. The financial statements shall contain adequate disclosure about the nature of any gain contingency. However, care should be exercised to avoid misleading implications as to the likelihood of realization.

~~38.~~39. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

~~39.~~40. This statement adopts *FASB Statement No. 5, Accounting for Contingencies* (FAS 5), and *FASB Statement 114, Accounting by Creditors for Impairment of a Loan* only as it amends in part FAS 5 ~~and paragraphs 35 and 36 of *FASB Statement of Financial Accounting Concepts No. 6—Elements of Financial Statements*~~. *FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss, An Interpretation of FASB Statement No. 5* (FIN No. 14) is adopted with the modification to accrue the loss amount as the midpoint of the range rather than the minimum as discussed in paragraph 3 of FIN No. 14. This statement adopts with modification *ASU 2013-04, Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date* with the same statutory modification adopted for FIN 14. This statement incorporates the definition of a liability from *FASB Statement of Financial Accounting Concepts No. 8, Chapter 4, Elements of Financial Statements,* paragraphs E37 and E38, with modification reflected in this statement regarding topic-specific guidance.

~~40.~~41. This statement adopts with modification *FASB Interpretation No. 45: Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FASB Interpretation No. 34* (FIN 45), *FASB Interpretation No. 45-3, Application of FASB Interpretation No. 45 to Minimum Revenue Guarantees Grated to a Business or Owner* (FSP FIN 45-3)*, and FASB Staff Position FAS 133-1 and FIN 45-4, Disclosures about Credit Derivatives and Certain Guarantees, An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45* (FSP FAS 133-1 and FIN 45-4). Statutory Modifications to FIN 45 include initial liability recognition for guarantees issued as part of intercompany or related party transactions, assessment and recognition of non-contingent guarantee obligations after recognition and settlement of a contingent obligation and revise the GAAP guidance to reflect statutory accounting terms and restrictions. Under this statement, intercompany and related party guarantees (including guarantees between parents and subsidiaries) should have an initial liability recognition unless the guarantee is considered "unlimited" or is made to/or on behalf of a wholly-owned subsidiary. (An example of an intercompany "unlimited" guarantee would be a guarantee issued in response to a rating agency's requirement to provide a commitment to support.) In instances in which an "unlimited" guarantee exists or a guarantee has been made to/or on behalf of a wholly-owned subsidiary, this statement requires disclosure, pursuant to the disclosure requirements adopted from FIN 45. The adoption of FIN 45 superseded the previously adopted guidance *in FASB Interpretation No. 34, Disclosure of Indirect*

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Guarantees of Indebtedness of Others, An interpretation of FASB Statement No. 5. This statement also adopts Accounting Principles Board Opinion No. 12, Omnibus Opinion—1967, paragraphs 2 and 3 with the modification that AVR, IMR and Schedule F Penalty shall be shown gross. Appropriation of retained earnings discussed in paragraph 15 of FAS 5 is addressed in *SSAP No. 72—Surplus and Quasi-Reorganizations.*

~~41.~~42. This statement adopts with modification the guidance in paragraphs 7-11 of *FSP EITF 00-19-2, Accounting for Registration Payment Arrangements*. This guidance specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision for a financial instrument, other agreement, should be separately recognized and measured in accordance with *FAS 5, Accounting for Contingencies*. The guidance in FSP EITF 00-19-2 is modified as follows:

a. Registration payment arrangements meet the definition of a loss contingency in accordance with paragraph ~~7~~8.

b. Financial instruments shall be accounted for in accordance with the statutory accounting principles for that specific asset type. Registration payment arrangement obligations shall be separate from the measurement and recognition of financial instruments subject to such arrangements.

c. Transition revisions resulting from application of this guidance shall be accounted for as a change in accounting principle pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors*. In accordance with SSAP No. 3, the cumulative effect of changes in accounting principles shall be reported as adjustments to unassigned funds in the period of change in the accounting principles.

~~42.~~43. This statement rejects *ASU 2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40), Accounting for Convertible Instruments and Contracts in an Entity's Own Equity.*

44. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~43.~~45. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

~~44.~~46. The guidance in paragraph ~~10~~11 related to when a judgment is considered rendered was originally contained in *INT 04-05: Clarification of SSAP No. 5R Guidance on when a Judgment is Deemed Rendered* and was effective September 12, 2004. The guidance for guarantees included within paragraphs ~~16-26~~17-27 and ~~34-36~~35-37 shall be applicable to all guarantees issued or outstanding as of December 31, 2011. Thereafter, disclosure of all guarantees shall be annually reported, with interim reporting required for new guarantees issued, and/or existing guarantees when significant changes are made. Guidance in

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paragraph ~~41~~42 was previously reflected within *INT 08-06: FSP EITF 00-19-2, Accounting for Registration Payment Arrangements* and was effective September 22, 2008.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets*
- *Issue Paper No. 20—Gain Contingencies*
- *Issue Paper No. 135—Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*
- *Issue Paper No. 168—Updates to the Definition of a Liability*

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Statement of Statutory Accounting Principles No. 6

Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 99-27, INT 01-01, INT 02-02 and INT 02-20
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Determination of Due Date 2
Impairment 2
Wash Transactions 3
Disclosures 3
Effective Date and Transition 3

REFERENCES **4**

Relevant Issue Papers 4

EXHIBIT A – NONADMITTANCE OF PREMIUM RECEIVABLES (PARAGRAPH 9.a.) **5**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for direct and group billed uncollected premiums, bills receivable for premiums, and amounts due from agents and brokers (collectively referred to as agents).

2. This statement does not address uncollected and deferred premiums for life considerations.

SUMMARY CONCLUSION

3. Premium transactions conducted directly with the insured result in uncollected premium balances.

4. Bills receivable, which are generally interest bearing, are used by reporting entities as a method of financing premiums.

5. Amounts due from agents result from various transactions ranging from premiums collected by the agents on behalf of the reporting entity to amounts advanced to the agent by the reporting entity to finance agency operations.

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6. Uncollected premium balances, bills receivable for premiums, and amounts due from agents meet the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement[1]. Premiums owed by agents shall be reflected net of commissions, if permitted by the contract. Balances resulting from advances to agents, which are primarily encountered in the life insurance industry, are nonadmitted if (a) the amounts are in the form of unsecured loans or advances, (b) the contractual terms for repayment are through application of future renewal commissions and/or other credits, or (c) the terms of repayment do not provide readily available cash for the satisfaction of policyholder liabilities.

Determination of Due Date

7. The due date for all premium balances addressed by this statement is determined as follows:

a. Original and deposit premiums—governed by the effective date of the underlying insurance contract and not the agent/reporting entity contractual relationship;

b. Endorsement premiums—governed by the effective date of the insurance policy endorsement;

c. Installment premiums—governed by the contractual due date of the installment from the insured;

d. Audit premiums and retrospective premiums—governed by insurance policy or insurance contract provisions. If the due date for receivables relating to these policies is not addressed by insurance policy provisions or insurance contract provisions, any uncollected audit premium (either accrued or billed) is nonadmitted.

8. The provisions of paragraph 7 shall be applied to all balances due except those arising from force placed insurance obtained by a lender for collateral protection, certain policies, known as Trustee Sales Guarantees (TSGs), issued by title insurance companies to lenders on defaulted real estate loans and crop/hail policies. For forced placed insurance policies, the due date for purposes of applying paragraph 9 shall be the date of billing. For TSGs, the due date for purposes of applying paragraph 9 shall be the expiration of the grace period given to the defaulted debtor, which is provided by statute. Crop/hail premiums are considered installment premiums in accordance with paragraph 7 and accordingly, the due date for purposes of applying paragraph 9 shall be governed by the contractual due date of the installment.

Impairment

9. Nonadmitted amounts are determined as follows:

a. Uncollected Premium—To the extent that there is no related unearned premium, any uncollected premium balances which are over ninety days due shall be nonadmitted. If an installment premium is over ninety days due, the amount over ninety days due plus all future installments that have been recorded on that policy shall be nonadmitted[2];

[1] Premiums billed prior to the effective date do not meet the definition of an asset per SSAP No. 4. Therefore, an asset/receivable should not be recognized on the financial statements until the effective date of the underlying policy/contract (i.e. the effective date of the contract gives rise to the entity's right). The mailing of a premium billing has no determination in the reporting of such premiums as an asset. Additionally, advance premiums are only recognized when the reporting entity receives cash payment for premiums prior to the effective date of the contract. In the event that the reporting entity bills and receives payment for premiums prior to the effective date, the reporting entity will recognize the receipt of cash with a corresponding credit to advance premiums (in this case a receivable is not recognized as the payment is received prior to the effective date).

[2] Installment premiums include monthly billed premiums on group accident and health policies. For group accident and health contracts, the existence of a nonadmitted *de minimus* over ninety-day balance would not cause future installments that have been recorded on that policy to also be nonadmitted. The *de minimus* over ninety-day balance itself shall be treated as nonadmitted as it is over ninety days old, and pursuant to paragraph 10, the entire current balance is subject to a collectability analysis.

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b. Bills Receivable—Bills receivable shall be nonadmitted if either of the following conditions are present:

i. If any installment is past due, the entire bills receivable balance from that policy is nonadmitted; or

ii. If the bills receivable balance due exceeds the unearned premium on the policy for which the note was accepted, the amount in excess of the unearned premium is nonadmitted.

c. Agents' Balances—The uncollected agent's receivable on a policy by policy basis which is over ninety days due shall be nonadmitted regardless of any unearned premium;

i. If amounts are both payable to and receivable from an agent on the same underlying policy, and the contractual agreements between the agent and the reporting entity permit offsetting, the nonadmitted portion of amounts due from that agent shall not be greater than the net balance due, by agent;

ii. If reconciling items between a reporting entity's account and an agent's account are over ninety days due, the amounts shall be nonadmitted.

10. After calculation of nonadmitted amounts, an evaluation shall be made of the remaining admitted assets in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, to determine if there is impairment. If, in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. If it is reasonably possible a portion of the balance is uncollectible and is therefore not written off, disclosure requirements outlined in SSAP No. 5R shall be followed.

11. Amounts classified as nonadmitted assets collected subsequent to the date of the statutory financial statements shall not be used to adjust the nonadmitted asset otherwise calculated.

Wash Transactions

12. Amounts due from agents (affiliated or nonaffiliated) that are collected prior to the date of the financial statements and then repaid to the agent by the reporting entity or one of the reporting entity's affiliates subsequent to the date of the financial statements shall be accounted for in accordance with the substance of the transaction (a wash transaction) and not its form. Accordingly, the payments received shall be accounted for as deposits and a liability shall be established for the same amount. The amounts due shall be reestablished as an asset and subjected to asset collectibility and nonadmitted asset calculations using the original due date of the receivable.

13. Short-term financing by third parties shall also be considered a wash transaction if the substance of the transaction is to avoid the nonadmitted asset principle set forth in this statement.

Disclosures

14. Refer to the Preamble for further discussion regarding disclosure requirements.

Effective Date and Transition

15. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in the footnote to paragraph 6 was originally contained within *INT 02-02: SSAP No. 6 and Billing of Premium Before Effective Date*

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and was effective March 18, 2002. The guidance in the footnote to paragraph 9 was originally contained within *INT 01-01: Application of SSAP No. 6 Paragraph 9.a. to de minimus Receivable Balances of Group Accident and Health Policies* and was effective March 26, 2001. Guidance in Exhibit A—Nonadmittance of Premium Receivables (paragraph 9.a.) was originally included in *INT 99-27: Nonadmitting Installment Receivables* and was effective December 6, 1999.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 6—Amounts Due From Agents and Brokers*
- *Issue Paper No. 10—Uncollected Premium Balances*
- *Issue Paper No. 21—Bills Receivable For Premiums*

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EXHIBIT A – NONADMITTANCE OF PREMIUM RECEIVABLES (PARAGRAPH 9.a.)

The application of paragraph 9.a. (uncollected installment premium) can be illustrated through the following journal entries:

Worker's compensation policy written on 1/1/X1 for $120,000 billed on installment basis at the end of each month.

Required Journal Entries:

1/1/X1	Installments booked but deferred and not yet due	120,000	
	Written premium		120,000
	Change in unearned premium reserve	120,000	
	Unearned premium reserve		120,000
	Initial journal entry written on effective date of policy		
1/30/X1	Premiums in course of collection	10,000	
	Installments booked but deferred and not yet due		10,000
	Unearned premium reserve	10,000	
	Change in unearned premium reserve		10,000
	Monthly journal entry to record installments		

Balance of accounts on 4/30/X1:

Installments booked but deferred and not yet due	80,000
Unearned premium reserve	80,000
Premiums in course of collection	40,000
Written premium	120,000
Change in unearned premium reserve	80,000
Earned premium	40,000

If no collections have been made as of 4/30/X1 then paragraph 9.a. would stipulate that the entire balance of $40,000 residing in the premiums in course of collection account would be nonadmitted. As the installments receivable and unearned premium reserve offset one another, no further amounts would be deemed nonadmitted at this point. In fact, as long as any of the premiums in course of collection account are 90 days past the contractual due date of the installment, then all subsequent installment billings would automatically be nonadmitted (i.e., May, June, July receivables of $10,000).

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Statement of Statutory Accounting Principles No. 7

Asset Valuation Reserve and Interest Maintenance Reserve

STATUS

Type of Issue..... Life, Accident and Health
Issued ..... Initial Draft
Effective Date ..... January 1, 2001
Affects..... No other pronouncements
Affected by..... No other pronouncements
Interpreted by..... INT 23-01
Relevant Appendix A Guidance ..... None

STATUS **1**
SCOPE OF STATEMENT **1**
SUMMARY CONCLUSION **1**
Effective Date and Transition 2
REFERENCES **2**
Other 2
Relevant Issue Papers 2

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for an asset valuation reserve (AVR) and an interest maintenance reserve (IMR) for life and accident and health insurance companies, excluding separate accounts. Separate account AVR/IMR reporting is addressed in *SSAP No. 56—Separate Accounts.*

SUMMARY CONCLUSION

2. Life and accident and health insurance companies shall recognize liabilities for an AVR and an IMR. The AVR is intended to establish a reserve to offset potential credit-related investment losses on all invested asset categories excluding cash, policy loans, premium notes, collateral notes and income receivable. The IMR defers recognition of the realized capital gains and losses resulting from changes in the general level of interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the investments sold. The IMR also applies to certain liability gains/losses related to changes in interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the liability released.

3. The IMR and AVR shall be calculated and reported as determined per guidance in the SSAP for the specific type of investment (e.g., SSAP No. 43R for loan-backed and structured securities), or if not specifically stated in the respective SSAP, in accordance with the NAIC *Annual Statement Instructions* for Life and Accident and Health Insurance Companies.

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Effective Date and Transition

4. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Other

- NAIC Annual Statement Instructions for Life and Accident and Health Insurance Companies

Relevant Issue Papers

- *Issue Paper No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*

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Statement of Statutory Accounting Principles No. 9

Subsequent Events

STATUS

Type of Issue..... Common Area
Issued ..... Initial Draft
Effective Date ..... January 1, 2001
Affects..... No other pronouncements
Affected by..... No other pronouncements
Interpreted by..... INT 22-02; INT 23-03
Relevant Appendix A Guidance ..... None

STATUS **1**
SCOPE OF STATEMENT **1**
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SCOPE OF STATEMENT

1. This statement defines subsequent events and establishes the criteria for recording such events in the financial statements and/or disclosing them in the notes to the financial statements. The conclusions in this statement apply to both quarterly and annual statement filings.

SUMMARY CONCLUSION

Key Terms

2. Subsequent events shall be defined as events or transactions that occur subsequent to the balance sheet date, but before the issuance of the statutory financial statements and before the date the audited financial statements are issued, or available to be issued. The issuance of the statutory financial statements includes not only the submission of the quarterly and annual statement but also the issuance of the audit opinion by the reporting entity's certified public accountant.

3. Material subsequent events shall be considered either:

   a. Type I – Recognized Subsequent Events: Events or transactions that provide additional evidence with respect to conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements;

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b. Type II – Nonrecognized Subsequent Events: Events or transactions that provide evidence with respect to conditions that did not exist at the balance sheet date but arose after that date.

4. **Financial statements are issued:** Financial statements are considered issued when they are widely distributed to shareholders and other financial statement users for general use and reliance in a form and format that complies with SAP.

5. **Financial statements are available to be issued:** Financial statements are considered available to be issued when they are complete in a form and format that complies with SAP and all approvals necessary for issuance have been obtained, for example, from management, the board of directors, and/or significant shareholders. The process involved in creating and distributing the financial statements will vary depending on an entity's management and corporate governance structure as well as statutory and regulatory requirements. An entity that has a current expectation of widely distributing its financial statements to its shareholders and other financial statement users shall evaluate subsequent events through the date that the financial statements are issued. All other entities shall evaluate subsequent events through the date that the financial statements are available to be issued.

Recognition Guidance

6. An entity shall recognize in the financial statements the effects of all material Type I subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Any changes in estimates resulting from the use of such evidence shall be recorded in the financial statements unless specifically prohibited, (e.g., subsequent collection of agents balances over 90 days due when determining nonadmitted agents balances as prohibited by *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*).

7. For material Type I subsequent events, the nature and the amount of the adjustment shall be disclosed in the notes to the financial statements only if necessary to keep the financial statements from being misleading.

8. Material Type II subsequent events shall not be recorded in the financial statements, but shall be disclosed in the notes to the financial statements. For such events, an entity shall disclose the nature of the event and an estimate of its financial effect, or a statement that such an estimate cannot be made.

9. An entity also shall consider supplementing the historical financial statements with pro forma financial data. Occasionally, a nonrecognized subsequent event may be so significant that disclosure can best be made by means of pro forma financial data. Such data shall give effect to the event as if it had occurred on the balance sheet date. In some situations, an entity also shall consider presenting pro forma statements. If an event is of such a nature that pro forma disclosures are necessary to keep the financial statements from being misleading, disclosure of supplemental pro forma financial data shall be made including the impact on net income, surplus, total assets, and total liabilities giving effect to the event as if it had occurred on the date of the balance sheet.

10. Identifying events that require adjustment of the financial statements under the criteria stated in the conclusion calls for the management of the entity to exercise judgment and accumulate knowledge of the facts and circumstances surrounding the event. For example, a loss on an uncollectible agent's balance as a result of an agent's deteriorating financial condition leading to bankruptcy subsequent to the balance sheet date would be indicative of conditions existing at the balance sheet date, thereby requiring the recording of such event to the financial statements before their issuance. On the other hand, a similar loss resulting from an agent's major casualty loss such as a fire or flood subsequent to the balance sheet date would not be indicative of conditions existing at the balance sheet date and recording of the event to the

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financial statements would not be appropriate. However, this is a Type II subsequent event which would require disclosure in the notes to the financial statements.

11. The following are examples of Type I recognized subsequent events:

a. If the events that gave rise to litigation had taken place before the balance sheet date and that litigation is settled, after the balance sheet date but before the financial statements are issued or are available to be issued, for an amount different from the liability recorded in the accounts, then the settlement amount should be considered in estimating the amount of liability recognized in the financial statements at the balance sheet date.

b. Subsequent events affecting the realization of assets, such as receivables and inventories or the settlement of estimated liabilities, should be recognized in the financial statements when those events represent the culmination of conditions that existed over a relatively long period of time. For example, a loss on an uncollectible trade account receivable as a result of a customer's deteriorating financial condition leading to bankruptcy after the balance sheet date but before the financial statements are issued or are available to be issued ordinarily will be indicative of conditions existing at the balance sheet date. Thus, the effects of the customer's bankruptcy filing shall be considered in determining the amount of uncollectible trade accounts receivable recognized in the financial statements at the balance sheet date.

12. The following are examples of Type II nonrecognized subsequent events:

a. Sale of a bond or capital stock issued after the balance sheet date but before financial statements are issued or are available to be issued

b. A business combination that occurs after the balance sheet date but before financial statements are issued or are available to be issued

c. Settlement of litigation when the event giving rise to the claim took place after the balance sheet date but before financial statements are issued or are available to be issued

d. Loss of plant or inventories as a result of fire or natural disaster that occurred after the balance sheet date but before financial statements are issued or are available to be issued

e. Losses on receivables resulting from conditions (such as a customer's major casualty) arising after the balance sheet date but before financial statements are issued or are available to be issued

f. Changes in the fair value of assets or liabilities (financial or nonfinancial) or foreign exchange rates after the balance sheet date but before financial statements are issued or are available to be issued

g. Entering into significant commitments or contingent liabilities, for example, by issuing significant guarantees after the balance sheet date but before financial statements are issued or are available to be issued

Disclosures

13. In addition to the disclosure of subsequent events as required throughout this statement, for annual and interim reporting periods, reporting entities shall disclose the dates through which subsequent events have been evaluated for statutory reporting and for audited financial statements along with the dates the statutory reporting statements and the audited financial statements were issued, or available to

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be issued. In the audited financial statements, reporting entities shall specifically identify subsequent events identified after the date subsequent events were reviewed for statutory reporting.

14. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

15. The above guidance was originally adopted to be consistent with the AICPA *Statement on Auditing Standards No. 1*, Section 560, *Subsequent Events*. In 2009, *FASB Statement No. 165, Subsequent Events* (FAS 165), was adopted for statutory accounting. The adoption of this guidance should not result in significant changes in the subsequent events that an entity reports, through either recognition or disclosure, in its financial statements. FAS 165 introduced the concept of available to be issued and requires additional disclosures on the dates for which an entity evaluated subsequent events as well as the date the financial statements were issued, or available to be issued. Guidance within ASU 2010-09 (modifications to Subtopic 855-10 in the FASB Codification) has been rejected for statutory accounting.

Effective Date and Transition

16. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Changes adopted as a result of FAS 165, are effective for years ending on and after December 31, 2009.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 9—Subsequent Events*

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Statement of Statutory Accounting Principles No. 11

Postemployment Benefits and Compensated Absences

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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Sick-Pay Benefits 3
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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for postemployment benefits and for compensated absences.

2. The scope of this statement includes:

   a. All forms of postemployment benefits that meet the conditions in paragraph 5.

   b. Split-dollar life-insurance arrangements if the arrangement is, in substance, an individual deferred compensation contract.

   c. Other deferred compensation contracts.

   d. Compensated Absences.

3. The scope of this statement does not include:

   a. Benefits paid to active employees other than compensated absences.

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b. Benefits paid at retirement or provided through a pension or postretirement benefit plan, including special or contractual termination benefits payable upon termination from a pension or other postretirement plan. Guidance for these benefits is addressed in SSAP No. 102 and SSAP No. 92 respectively.

c. Individual deferred compensation contracts, if those contracts taken together are equivalent to a defined benefit pension plan or other postretirement plan. Guidance for these benefits is addressed in SSAP No. 102 and SSAP No. 92 respectively.

d. Other postemployment benefits that do not meet the conditions in paragraph 5. Such postemployment benefits shall be assessed as contingent liabilities in accordance with SSAP No. 5R.

e. Stock compensation plans accounted for under *SSAP No. 104R—Share-Based Payments.*

SUMMARY CONCLUSION

4. Postemployment benefits are all types of benefits provided by an employer to former or inactive employees or agents, their beneficiaries, and covered dependents, after employment but before retirement. Those benefits include, but are not limited to, salary continuation, supplemental unemployment benefits, severance benefits, disability-related benefits (including workers' compensation), job training and counseling, continuation of benefits such as health care benefits and life insurance coverage, and special or contractual termination benefits payable before retirement and that are not payable from a pension or other postretirement plan. Compensated absences include, but are not limited to, benefits such as vacation, sick pay, sabbatical leave and other similar benefits, and holidays.

5. A reporting entity shall accrue a liability for postemployment benefits and for employees' compensation for future absences if all of the following conditions are met:

a. The reporting entity's obligation relating to compensated absences and postemployment benefits is attributable to employees' services already rendered;

b. The obligation relates to rights that vest[1] or accumulate[2];

c. Payment is probable; and

d. The amount can be reasonably estimated.

6. A liability for amounts to be paid as a result of employees' rights to compensated absences shall be accrued, considering anticipated forfeitures, in the year in which earned. Furthermore, the definition of a liability does not limit an employer's liability for compensated absences solely to rights to compensation for those absences that eventually vest. The definition also encompasses a constructive obligation for reasonable estimable compensation for past services that, based on the employer's past practices, probably shall be paid and can be reasonably estimated.

7. Individual facts and circumstances must be considered in determining when nonvesting rights to compensated absences are earned by services rendered. The requirement to accrue a liability for nonvesting rights to compensated absences depends on whether the unused rights expire at the end of the

[1] In this statement, vested rights are those for which the reporting entity has an obligation to make payment even if an employee terminates; thus, they are not contingent on an employee's future service.

[2] For purposes of this statement, accumulate means that earned but unused rights to compensated absences may be carried forward to one or more periods subsequent to that in which they are earned, even though there may be a limit to the amount that can be carried forward.

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year in which earned, or accumulate and carried forward to succeeding years, thereby increasing the benefits that would otherwise be available in those latter years. If the rights expire, a liability for future absences shall not be accrued at year-end because the benefits to be paid in subsequent years would not be attributable to employee services rendered in prior years. If unused rights do accumulate and increase the benefits otherwise available in subsequent years, a liability shall be accrued to the extent that it is probable that employees will be paid in subsequent years for the increased benefits attributable to the accumulated rights and the amount can be reasonably estimated.

8. A reporting entity shall accrue a liability for employees' compensated absences and postemployment benefits reimbursable under service agreements with an affiliate, if all of the conditions of paragraph 5 are met.

9. Postemployment benefits provided to employees or agents in connection with their termination can include special termination benefits and contractual termination benefits. Special termination benefits are defined as those that are offered only for a short period of time in exchange for employees' voluntary termination of service; contractual termination benefits are defined as those required by the terms of a plan only if a specified event, such as a facility closing, occurs. An employer that offers special termination benefits to employees or agents shall recognize a liability and an expense when the employees or agents accept the offer and the amount can be reasonably estimated. An employer that provides contractual termination benefits shall recognize a liability and an expense when it is probable that employees or agents will be entitled to benefits and the amount can be reasonably estimated. The cost of such termination benefits shall include the amount of any lump-sum payments and the present value of any expected future payments.

Sabbatical Leave and Other Similar Benefits

10. An entity may provide its employees with a benefit in the form of a compensated absence known as a sabbatical leave (sabbatical) whereby the employee is entitled to paid time off after working for an entity for a specified period of time. During the sabbatical, the individual continues to be a compensated employee and is not required to perform any duties for the entity. This issue is limited to those arrangements under which the sabbatical or other similar benefit arrangement is unrestricted (i.e., the employee is not required to perform any direct or indirect services for or on behalf of the entity during the absence). Arrangements in which employees are required to engage in research or public service to enhance the reputation of or otherwise benefit the entity are not within the scope of this statement.

11. An employee's right to a compensated absence under a sabbatical or other similar benefit arrangement (a) that requires the completion of a minimum service period and (b) in which the benefit does not increase with additional years of service accumulates pursuant to paragraph 5.b. of this statement for arrangements in which the individual continues to be a compensated employee and is not required to perform duties for the entity during the absence. Therefore, assuming all of the other conditions of paragraph 5 are met, the compensation cost associated with a sabbatical or other similar benefit arrangement should be accrued over the requisite service period.

Sick-Pay Benefits

12. The employer's actual administration of sick-pay benefits shall determine the appropriate accounting. In accounting for compensated absences, the form of an employer's policy for compensated absences shall not prevail over actual practices. If sick-pay benefits are treated as compensated absences (e.g., employees are paid sick leave benefits even though absences are not the result of illness, or employees are allowed to take compensated terminal leave for accumulated unused sick-pay benefits prior to retirement), they shall be captured within paragraph 5. Otherwise, an employer is not required to accrue a liability for nonvesting accumulating rights to receive sick-pay benefits (compensation for an employee's absence due to illness). This statement does not prevent an employer from accruing a liability for such non-vesting, accumulating sick-pay benefits if the criteria in paragraph 5 is met.

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Deferred Compensation Arrangements Accounted for Individually

13. To the extent the terms of a contract attribute all or a portion of the expected future benefits to an individual year of the employee's service, the cost of those benefits shall be recognized in that year. To the extent the terms of the contract attribute all or a portion of the expected future benefits to a period of service greater than one year, the cost of those benefits shall be accrued over that period of the employee's service in a systematic and rational manner. If elements of both current and future services are present, only the portion applicable to the current services shall be accrued.

14. Some deferred compensation contracts provide for periodic payments to employees or their surviving spouses for life with provisions for a minimum lump-sum settlement in the event of the early death of one or all of the beneficiaries. The estimated amount of future payments to be made under such contracts shall be accrued over the period of active employment from the time the contract is entered into.

15. The amounts to be accrued periodically under paragraph 13 shall result in an accrued amount at the full eligibility date equal to the then present value of all of the future benefits expected to be paid. Such estimates shall be based on the life expectancy of each individual concerned (based on the most recent mortality tables available) or on the estimated cost of an annuity contract rather than on the minimum payable in the event of early death. At the end of that period the aggregate amount accrued shall equal the then present value of the benefits expected to be provided to the employee, any beneficiaries, and covered dependents in exchange for the employee's service to that date.

Consolidated/Holding Company Plans

16. The employees of many reporting entities are eligible for certain compensated absence and postemployment benefits granted by a parent company or holding company. An entity with employees who are eligible for those benefits and is not directly liable for those related obligations shall recognize an expense equal to its allocation from the parent company or holding company of the benefits earned during the period. A liability shall be established for any such amounts due but not yet paid.

17. The reporting entity shall disclose in the financial statements that its employees participate in a plan sponsored by the holding company for which the reporting entity has no legal obligation. The amount of expense incurred and the allocation methodology utilized by the provider of such benefits shall also be disclosed. If the reporting entity is directly liable for the benefits, then the requirements outlined in paragraphs 2-15 shall be applied.

Disclosures

18. If it is not practicable to estimate, and therefore, not accrue the liability under paragraph 5 (i.e., conditions 5.a., 5.b. and 5.c. are met but condition 5.d. is not), that fact and the reasons therefore shall be disclosed in the financial statements.

19. For special or contractual termination benefits within scope of this standard (special or contractual termination benefits outside of SSAP No. 92 or SSAP No. 102), the reporting entity shall complete the disclosures in SSAP No. 92, paragraphs 66.a., 66.b., 66.g. and 66.p., as applicable.

20. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

21. This statement adopts:

a. *FASB Statement No. 43, Accounting for Compensated Absences* (FAS 43),

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b. *FASB Statement No. 112, Employers' Accounting for Postemployment Benefits: an amendment of FASB Statements No. 5 and 43,*

c. *FASB Statement No. 88, Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* as modified by *FAS 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (FAS 158), paragraph 15 regarding guidance for termination benefits,

d. *FASB Statement No. 132(R), Employers' Disclosures about Pensions and Other Postretirement Benefits,* as modified by FAS 158, paragraphs 5(a), 5(b), 5(h), 5(g) and 8(m) to address disclosure requirements related to termination benefits, and

e. *APB 12: Omnibus Opinion*, paragraphs 6, 6A and 7.

22. This statement adopts with modification:

a. FASB *Emerging Issues Task Force Issue No. 06-2—Accounting for Sabbatical Leave and Other Similar Benefits Pursuant to FASB Statement No. 43* with modification that the changes resulting from the adoption of EITF 06-2 are in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors***.**

Effective Date and Transition

23. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 11—Compensated Absences*
- *Issue Paper No. 13—Employers' Accounting for Postemployment Benefits*

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Statement of Statutory Accounting Principles No. 12

Employee Stock Ownership Plans

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Leveraged ESOPs 2
Nonleveraged ESOPs 2
Pension Reversion ESOPs 2
Issues Related to Accounting for Income Taxes 3
Disclosures 3
Relevant Literature 4
Effective Date and Transition 4

REFERENCES **4**

Relevant Issue Papers 4

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the plan sponsors' accounting for Employee Stock Ownership Plans (ESOPs).

SUMMARY CONCLUSION

2. An ESOP is an employee benefit plan that is described by the Employee Retirement Income Security Act of 1974 (ERISA) and the Internal Revenue Code of 1986 as a stock bonus plan, or a combination stock bonus and money purchase pension plan, designed to invest primarily in employer stock. For such plans, reporting entities shall adopt AICPA *Statement of Position 93-6, Employers' Accounting for Employee Stock Ownership Plans* (SOP 93-6) except that debt obligations of ESOPs shall be reported consistent with *SSAP No. 15—Debt and Holding Company Obligations*, and the related income tax effects shall be accounted for consistent with *SSAP No. 101—Income Taxes*, as further clarified in this statement. There are two basic forms of ESOPs: leveraged and nonleveraged. A summary of the financial reporting for each is provided below.

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Leveraged ESOPs

3. A leveraged ESOP borrows money to acquire shares of the employer company (sponsor). The money may be borrowed from the plan sponsor or from an outside lender, with or without a guarantee from the plan sponsor. The debt usually is collateralized by the employer's shares. Debt obligations of an ESOP shall be reported as borrowed money by company sponsors, except when the ESOP has both the ability and intent to satisfy the debt from sources other than dividends on the company stock, contributions from the company or the sale or exchange of the company's securities.

4. The sponsor shall record the issuance of shares or the sale of treasury shares to an ESOP when it occurs. The consideration recorded for the stock issued is unearned compensation and the unearned ESOP shares shall be recorded as a separate reduction of unassigned funds (surplus).

5. The unearned shares initially held by the ESOP in a suspense account are called suspense or unallocated shares. As the debt is repaid (generally from employer contributions and dividends on the employer's stock), suspense shares are released and must be allocated to individual accounts as of the end of the ESOP's fiscal year. As ESOP shares are committed to be released, unearned ESOP shares shall be credited and, depending on the purpose for which the shares are released, either (a) compensation cost, (b) dividends payable, or (c) compensation liabilities shall be charged consistent with SOP 93-6.

6. Because employers control the use of dividends on unallocated shares, dividends on unallocated shares are not considered dividends for financial reporting purposes (although such dividends are generally subject to normal dividend requirements under state statutes or regulations). Dividends on unallocated shares used to pay debt service shall be reported as a reduction of debt or of accrued interest payable. Dividends on unallocated shares paid to participants or added to participant accounts shall be reported as compensation cost. Dividends on allocated shares shall be charged to unassigned funds (surplus).

7. If the ESOP sells the suspense shares and uses the proceeds to repay the debt, the employer shall report the release of the suspense shares as a credit to unearned ESOP shares based on the cost of the shares to the ESOP, charge debt and accrued interest payable, and recognize the difference in paid-in capital. However, if there is a difference between the amount paid to an outside lender and the net carrying amount of the debt, such difference shall be reported as a capital gain or loss on extinguishment of debt and, accordingly, shall be charged to operations and disclosed in the financial statements with other disclosures required by paragraph 17.

8. If an employer reacquires the suspense shares from the ESOP, the purchase of the shares shall be accounted for as a treasury stock transaction consistent with SOP 93-6.

Nonleveraged ESOPs

9. Employers with nonleveraged ESOPs shall report compensation cost equal to the contribution called for in the period under the plan.

10. Employers with nonleveraged ESOPs shall charge dividends on shares held by the ESOPs to unassigned funds (surplus), except that dividends on suspense account shares of pension reversion ESOPs shall be accounted for the same way as dividends on suspense account shares of leveraged ESOPs.

Pension Reversion ESOPs

11. Pension reversion ESOPs are created by transferring the assets of a defined benefit pension plan to existing or newly created ESOPs and may be leveraged or nonleveraged. Pension reversion ESOPs shall be accounted for consistent with SOP 93-6.

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Issues Related to Accounting for Income Taxes

Leveraged ESOPs

12. The amount of ESOP-related expense for a leveraged ESOP for a period may differ from the amount of the ESOP-related income tax deduction (prescribed by income tax rules and regulations) for that period. Differences shall be reported in accordance with SSAP No. 101 and result in either of the following situations:

a. The fair value of shares committed to be released differs from the cost of those shares to the employee stock ownership plan.

b. The timing of expense recognition is different for income tax and financial reporting purposes.

13. The tax effect of the difference, if any, between the cost of shares committed to be released and the fair value of the shares shall be recognized as income tax expense or benefit in the income statement.

14. The tax benefit of tax-deductible dividends on allocated and unallocated ESOP shares shall be recognized in the income statement.

Nonleveraged ESOPs

15. Reporting entities with nonleveraged ESOPs may accrue compensation cost for financial reporting purposes earlier than the cost is deductible for income tax purposes. Accruing the compensation cost earlier for financial reporting purposes creates a temporary difference that shall be accounted for in accordance with SSAP No. 101.

Other

16. Under federal income tax regulations, employer securities (such as convertible preferred stock) that are held by participants in an ESOP and are not readily tradable on an established market must include a put option. Securities subject to such repurchase obligations shall be reported as outstanding and as a component of capital stock and/or gross paid-in and contributed surplus in accordance with *SSAP No. 72—Surplus and Quasi-Reorganizations*.

Disclosures

17. An employer sponsoring an ESOP shall disclose the following information about the plan, if applicable:

a. A description of the plan, the basis for determining contributions, including the employee groups covered, and the nature and effect of significant matters affecting comparability of information for all periods presented. For leveraged ESOPs and pension reversion ESOPs, the description shall include the basis for releasing shares and how dividends on allocated and unallocated shares are used;

b. A description of the accounting policies followed for ESOP transactions, including the method of measuring compensation and the classification of dividends on ESOP shares;

c. The amount of compensation cost recognized during the period;

d. The number of allocated shares, committed-to-be-released shares, and suspense shares held by the ESOP at the balance sheet date;

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e. The fair value of unearned ESOP shares at the balance sheet date; and

f. The existence and nature of any repurchase obligation, including disclosure of the fair value of the shares allocated as of the balance sheet date, which are subject to a repurchase obligation.

18. Refer to the Preamble for further discussions regarding disclosure requirements. The disclosures in paragraph 17 shall be included in the annual audited statutory financial reports only.

Relevant Literature

19. This statement adopts SOP 93-6 with a modification to reject paragraphs 13 and 25 to the extent they require reporting all debt obligations of an ESOP as liabilities, paragraphs 28-34, 44 and 53.b. as they relate to earnings per share, and paragraph 37 as it relates to reporting gains and losses on extinguishment of debt.

20. This statement rejects *FASB Emerging Issues Task Force No. 89-11, Sponsor's Balance Sheet Classification of Capital Stock with a Put Option Held by an Employee Stock Ownership Plan*.

Effective Date and Transition

21. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 78—Employee Stock Ownership Plans*

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Statement of Statutory Accounting Principles No. 15

Debt and Holding Company Obligations

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 00-08, INT 00-10, INT 04-07, INT 04-15 and INT 08-08
Affected by	No other pronouncements
Interpreted by	INT 20-01
Relevant Appendix A Guidance	None

STATUS **1**

SUMMARY CONCLUSION **1**

Debt 1
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Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements 3
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Accounting for the Settlement of the Equity-Settled Portion of a Convertible Debt Instrument That Permits or Requires the Conversion Spread to Be Settled in Stock 3
Accounting for Federal Home Loan Banks 4
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Relevant Issue Papers 6

SCOPE OF STATEMENT

1. The purpose of this statement is to establish statutory accounting principles for recording debt and related disclosure requirements, including holding company obligations and any related guarantees in the financial statements of an insurance company subsidiary, and debt obligations of Employee Stock Ownership Plans (ESOPs).

SUMMARY CONCLUSION

Debt

2. Debt shall be reported as a liability unless (a) it is debt on real estate in accordance with *SSAP No. 40R—Real Estate Investments* (i.e., reported as a reduction in the carrying value of real estate), (b) it is offset against another asset in accordance with *SSAP No. 64—Offsetting and Netting of Assets and Liabilities*, or (c) other treatment is specified elsewhere within the *Accounting Practices and Procedures Manual*. Instruments that meet the requirements to be recorded as surplus as specified in *SSAP No. 72—*

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Surplus and Quasi-Reorganizations are not considered debt. *SSAP No. 25—Affiliates and Other Related Parties* also provides specific guidance for debt obligations owed to related parties.

3. Debt discount or premium, if any, shall be reported in the balance sheet as a direct deduction from or addition to the face amount of the note. Discount or premium shall be amortized over the life of the note using the interest method.

4. Interest on debt shall be accrued and charged to operations over the life of the debt, except when capitalized in accordance with *SSAP No. 44—Capitalization of Interest*. Interest payable shall include interest payable on all debt reported as a liability, approved interest on surplus notes, and interest payable on debt reported as a reduction in the carrying value of real estate.

5. Debt issuance costs (e.g., loan fees and legal fees) do not meet the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets*. Accordingly, these costs shall be charged to operations in the period incurred.

6. Debt obligations of ESOPs shall be reported as debt by company sponsors, except when the ESOP has both the ability and intent to satisfy the debt from sources other than dividends on the company stock, contributions from the company, or the sale or exchange of the company's securities. ESOPs are addressed in *SSAP No. 12—Employee Stock Ownership Plans*.

7. Debt which is subject to a troubled debt restructuring shall be accounted for in accordance with *SSAP No. 36—Troubled Debt Restructuring*.

8. Convertible debt securities that are convertible into common stock of the issuer or an affiliated company at a specified price at the option of the holder and which are sold at a price not significantly in excess of the face amount shall be accounted for solely as debt at the time of issuance. An expense shall be recognized, equal to the fair value of additional securities granted or other consideration issued to induce conversion subsequent to the issuance of convertible debt securities. This guidance applies regardless of who initiates the offer, the debt holder or the debtor, and whether the offer applies to all debt holders.

9. Proceeds from debt issued with detachable stock purchase warrants shall be allocated based on the relative fair value of the two securities at the time of issuance. The value attributable to the warrants shall be accounted for as paid-in capital.

10. Other types of debt securities, e.g., capital notes, shall be accounted for in accordance with the substance of the transaction.

11. A reporting entity shall derecognize a liability if, and only if, it has been extinguished. A liability has been extinguished if either of the following conditions is met:

a. The reporting entity pays the creditor and is relieved of its obligation for the liability. Paying the creditor includes delivery of cash, other financial assets, goods or services, or reacquisition by the debtor of its outstanding debt securities; or

b. The reporting entity is legally released from being the primary obligor under the liability, either judicially or by the creditor.

Convertible Debt Securities with Beneficial Conversion Features

12. Entities may issue convertible debt securities and convertible preferred stock with a nondetachable conversion feature that is in-the-money at the commitment date (a "beneficial conversion feature"). Those securities may be convertible into common stock at the lower of a conversion rate fixed at the commitment date or a fixed discount to the market price of the common stock at the date of

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conversion. Certain convertible securities may have a conversion price that is variable based on future events such as a subsequent round of financing at a price lower than the convertible securities' original conversion price, a liquidation or a change in control of the company, or an initial public offering at a share price lower than an agreed-upon amount.

13. Convertible debt securities and convertible preferred stock with beneficial conversion features are to be valued according to the appropriate statutory accounting statement; *SSAP No. 26R—Bonds* or *SSAP No. 32R—Preferred Stock.*

Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements

14. A line-of-credit or revolving-debt arrangement is an agreement that provides the borrower with the option to make multiple borrowings up to a specified maximum amount to repay portions of previous borrowings, and to then reborrow under the same contract. Line-of-credit and revolving-debt arrangements may include both amounts drawn by the debtor (a debt instrument) and a commitment by the creditor to make additional amounts available to the debtor under predefined terms (a loan commitment). In most situations, a debtor incurs costs to establish line-of-credit or revolving-debt arrangements, and some or all of the costs are deferred and amortized over the term of the arrangement.

15. Modifications to or exchanges of line-of-credit or revolving-debt arrangements, including the accounting for unamortized costs at the time of the change, fees paid to or received from the creditor and third-party costs incurred shall be expensed when incurred.

Holding Company Obligations

16. In situations where the reporting entity does not guarantee the obligation of the holding company, there is no legal obligation on the part of the reporting entity. Therefore, the reporting entity shall not record the obligation of its parent holding company unless the obligation relates to services or benefits incurred by a non-insurance parent company or holding company on its behalf. In these situations, the reporting entity shall recognize an expense for its share of the services or benefits provided to it during the period by the parent company or holding company based on an allocation from the parent or holding company. A liability shall be established for any such amounts due, but not yet paid. The amount of expense incurred and the allocation methodology utilized by the provider of such benefits shall also be disclosed. *SSAP No. 11—Postemployment Benefits and Compensated Absences*, *SSAP No. 92—Postretirement Benefits Other Than Pensions* and *SSAP No. 102—Pensions* address specific examples where the obligation relates to benefits provided to the subsidiary by a non-insurance parent company or holding company.

17. If the reporting entity guarantees an obligation of the holding company, the guidance in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* shall be followed for determining the recording and disclosure of the guarantee. SSAP Nos. 11, 92 and 102 provide specific accounting and disclosure guidelines for employee benefit plans when the reporting entity is directly liable for obligations under the plan.

Accounting for the Settlement of the Equity-Settled Portion of a Convertible Debt Instrument That Permits or Requires the Conversion Spread to Be Settled in Stock

18. Upon settlement of a security with the characteristics of Instrument C in *FASB Emerging Issues Task Force 90-19, Convertible Bonds with Issuer Option to Settle for Cash upon Conversion*, by payment of the accreted value of the obligation (recognized liability) in cash and settlement of the conversion spread (unrecognized equity instrument) with stock, only the cash payment should be considered in the computation of gain or loss on extinguishment of the recognized liability. That is, any shares transferred to settle the embedded equity instrument (referred to as the excess conversion spread in EITF 90-19) would not be considered in the settlement of the debt component.

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Accounting for Federal Home Loan Banks

19. Funding agreements issued to a federal home loan bank (FHLB) shall be evaluated on an individual basis, and shall be accounted for according to the substance of the individual arrangement and entity licensing. If the arrangement is in substance a funding agreement, including that the funds are used in an investment spread capacity, it shall be accounted for consistent with other funding agreements in accordance with *SSAP No. 52—Deposit-Type Contracts*. If the arrangement is in substance a borrowing agreement, it shall be accounted for in accordance with this statement, consistent with other borrowed money.

Disclosures

20. The financial statements shall disclose the following items related to debt, including FHLB borrowings accounted for under this SSAP:

a. Date issued;

b. Pertinent information concerning the kind of borrowing (e.g., debentures, commercial paper outstanding, bank loans, and lines of credit);

c. Face amount of the debt;

d. Carrying value of debt;

e. The rate at which interest accrues;

f. The effective interest rate;

g. Collateral requirements;

h. Interest paid in the current year;

i. A summary of significant debt terms and covenants and any violations;

j. The combined aggregate amount of maturities and sinking fund requirements for each of the five years following the latest balance sheet presented;

k. If debt was considered to be extinguished by in-substance defeasance prior to the effective date of this statement and any of the debt remains outstanding, a general description of the transaction and the amount of debt that is considered extinguished at the end of the period; and

l. If assets are set aside after the effective date of this statement solely for satisfying scheduled payments of a specific obligation, a description of the nature of restrictions placed on those assets.

21. FHLB borrowings accounted for under SSAP No. 15 should follow the disclosure requirements required in paragraph 20 as well as the disclosure requirements included in *SSAP No. 30R—Unaffiliated Common Stock*, paragraph ~~18~~19.

22. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

23. This statement adopts *Accounting Principles Board Opinion No. 14, Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants* and *FASB Statement No. 84, Induced Conversions of Convertible Debt*.

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24. This statement adopts *Accounting Principles Board Opinion No. 21, Interest on Receivables and Payables,* with a modification to require that debt issuance costs be charged to operations.

25. This statement adopts *Accounting Principles Board Opinion No. 26, Early Extinguishment of Debt* with modification to require that gains and losses from extinguishment of debt be reported as capital gains or losses and charged to operations unless the extinguishment reflects the forgiveness of a reporting entity's obligation to its parent or other stockholders. Forgiveness of a reporting entity's obligation to its parent or other stockholder shall be accounted for as contributed surplus under SSAP No. 72.

26. This statement adopts paragraphs 13 and 25 of AICPA *Statement of Position 93-6, Employers' Accounting for Employee Stock Ownership Plans* (SOP 93-6) with a modification to exclude debt obligations when the ESOP has both the ability and intent to satisfy the debt from sources other than dividends on the company's stock, contributions from the company, or the sale or exchange of the company's securities. This statement rejects paragraph 37 of SOP 93-6 as it relates to reporting gains and losses on extinguishment of debt which shall be accounted for consistent with *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items.*

27. This statement adopts *FASB Emerging Issues Task Force No. 90-19, Convertible Bonds with Issuer Option to Settle for Cash upon Conversion* with a modification to reject guidance related to earnings per share.

28. This statement adopts *FASB Technical Bulletin No. 80-1, Early Extinguishment of Debt through Exchange for Common or Preferred Stock,* with a modification to reject guidance related to classification of the loss as an extraordinary item.

29. This statement rejects *ASU 2015-0, Simplifying the Presentation of Debt Issuance Cost* and *ASU 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements* for statutory accounting.

30. This statement adopts the following pronouncements:

a. *Accounting Principles Board Opinion No. 12, paragraphs 16 and 17, Omnibus Opinion—1967*;

b. AICPA *Accounting Interpretations of APB 21, Interest on Receivables and Payables*;

c. AICPA *Accounting Interpretations of APB 26, Early Extinguishment of Debt*;

d. *FASB Emerging Issues Task Force No. 85-9, Revenue Recognition on Options to Purchase Stock of Another Entity;*

e. *FASB Emerging Issues Task Force No. 85-17, Accrued Interest upon Conversion of Convertible Debt*;

f. *FASB Emerging Issues Task Force No. 85-29, Convertible Bonds with a "Premium Put"*;

g. *FASB Emerging Issues Task Force No. 86-8, Sale of Bad-Debt Recovery Rights;*

h. *FASB Emerging Issues Task Force No. 86-15, Increasing-Rate Debt*;

i. *FASB Emerging Issues Task Force No. 86-18, Debtor's Accounting for a Modification of Debt Terms*;

j. *FASB Emerging Issues Task Force No. 86-28, Accounting Implications of Indexed Debt Instruments*;

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k. *FASB Emerging Issues Task Force No. 86-36, Invasion of a Defeasance Trust*;

l. *FASB Emerging Issues Task Force No. 95-15, Recognition of Gain or Loss When a Binding Contract Requires a Debt Extinguishment to Occur at a Future Date for a Specified Amount*;

m. *FASB Emerging Issues Task Force No. 02-15: Determining Whether Certain Conversions of Convertible Debt to Equity Securities Are Within the Scope of FASB Statement No. 84.*

31. This statement rejects *FASB Statement No. 4, Reporting Gains and Losses from Extinguishment of Debt* and *FASB Statement No. 64, Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements—an Amendment of FASB Statement No. 4*. This statement also rejects *FASB Emerging Issues Task Force No. 84-40, Long-Term Debt Repayable by a Capital Stock, FASB Emerging Issues Task Force No. 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios,* and *FASB Emerging Issues Task Force No. 98-14, Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements*.

Effective Date and Transition

32. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* The guidance in paragraph 8 related to who initiates an offer was previously included in *INT 04-07: EITF No. 02-15: Determining Whether Certain Conversions of Convertible Debt to Equity Securities Are Within the Scope of FASB Statement No. 84* and was effective September 12, 2004. The guidance in paragraphs 12 and 13 was originally contained within *INT 00-08: EITF 98-5: Accounting for Convertible Securities with Beneficial Conversion Features or Continently Adjustable Conversion Ratios* and was effective September 11, 2000. The guidance in paragraphs 14 and 15 was originally contained within *INT 00-10: EITF 98-14: Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements* and was effective June 12, 2000. The guidance in paragraph 18 was originally contained within *INT 04-15: EITF 03-7: Accounting for the Settlement of the Equity-Settled Portion of a Convertible Debt Instrument That Permits or Requires the Conversion Spread to be Settled in Stock (Instrument C of Issue No. 90-19)* and was effective December 5, 2004. Guidance in paragraph 19 was previously included within *INT 08-08: Balance Sheet Presentation of Funding Agreements Issued to a Federal Home Loan Bank* and was effective for periods beginning March 15, 2009. Guidance in paragraphs 20-21 related to FHLB agreements and borrowings was initially effective January 1, 2014.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 80—Debt*
- *Issue Paper No. 95—Holding Company Obligations*

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Statement of Statutory Accounting Principles No. 16 – Revised

Electronic Data Processing Equipment and Software

STATUS

Type of Issue	Common Area
Issued	Initial draft; Substantively revised October 18, 2010
Effective Date	January 1, 2001, January 1, 2002, and January 1, 2004
Affects	Supersedes SSAP No. 79, SSAP No. 81 and SSAP No. 82; Nullifies and incorporates INT 04-13
Affected by	No other pronouncements
Interpreted by	INT 01-18
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for electronic data processing (EDP) equipment and provisions for the accounting of other software.

SUMMARY CONCLUSION

EDP Equipment and Operating / Nonoperating System Software

2. EDP equipment and software generally meet the definition of assets established in *SSAP No. 4—Assets and Nonadmitted Assets*. EDP equipment and operating system software are admitted assets to the extent they conform to the requirements of this statement. Nonoperating system software are nonadmitted assets.

3. EDP equipment and operating system software shall be depreciated over the lesser of its useful life or three years. Nonoperating system software shall be depreciated over the lesser of its useful life or

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five years. In either case, the methods detailed in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* shall be used.

4. The aggregate amount of admitted EDP equipment and operating system software (net of accumulated depreciation) shall be limited to 3%~~three percent~~ of the reporting entity's capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for its most recently filed statement with the domiciliary state commissioner adjusted to exclude any EDP equipment and operating system software, net deferred tax assets and net positive goodwill.(INT 01-18)

5. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold shall be expensed when purchased, otherwise the EDP Equipment, operating and nonoperating system software assets shall be capitalized and depreciated in accordance with paragraph 3. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Research and Development Costs Incurred to Obtain or Develop Computer Software

6. Guidance on the accounting for research and development costs is provided in *SSAP No. 17—Preoperating and Research and Development Costs* and requires all research and development costs to be expensed when incurred. Pursuant to the guidance adopted within that SSAP:

a. To the extent that the acquisition, development, or improvement of a process by an enterprise for use in its selling or administrative activities includes costs for computer software, those costs are not research and development costs.

b. Costs incurred to purchase or lease computer software developed by others are not research and development costs unless the software is for use in research and development activities.

c. Costs incurred by an enterprise in developing computer software internally for use in its research and development activities are research and development costs. This includes costs incurred during all phases of software development because all of those costs are incurred in research and development activities.

7. Costs for computer software determined to be research and development costs shall be accounted for and disclosed in accordance with SSAP No. 17. Software costs not considered to be research and development costs shall be accounted for in accordance with this SSAP.

Accounting for the Costs of Computer Software to be Sold

8. This statement adopts with modification *FASB Codification 985-20, Software - Costs of Software to be Sold, Leased or Marketed* (ASC 985-20) to preclude the capitalization of software development costs and to reject guidance regarding the treatment of capitalized costs. Additionally, this statement rejects *FASB Codification 985-330, Software - Inventory* (ASC 985-330). Statutory modifications to ASC 985-20 and rejection of ASC 985-330 precludes capitalization of costs, and requires such costs to be expensed, for:

a. Costs of producing product masters incurred subsequent to establishing technological feasibility. Those costs include coding and testing performed subsequent to establishing technological feasibility.

b. Software production costs for computer software that is to be used as an integral part of a product or process.

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c. All indirect costs, including overhead related to programmers and the facilities they occupy.

d. Costs incurred for duplicating computer software, documentation and training materials from product masters and for physically packaging the product for distribution.

Software Revenue Recognition

9. This statement adopts with modification *FASB Codification 985-605, Software – Revenue Recognition – Provision for Losses* (ASC 985-605), as revised by *ASU 2009-14, Certain Revenue Arrangements That Include Software Elements* (ASU 2009-14), for statutory accounting terms and concepts:

a. References to GAAP guidance outside FASB Codification topic 985-605 shall be followed only to the extent in which that specific GAAP guidance has been adopted[1] for statutory accounting. The guidance within the applicable SSAP or statutory interpretation shall be considered the authoritative statutory guidance.

b. Any references to the accounting for capitalized development costs is rejected as all development costs are required to be expensed when incurred.

Costs of Computer Software Developed or Obtained for Internal Use and Web Site Development Costs

10. This statement adopts with modification *FASB Accounting Standards Codification (ASC) 350-40, Internal Use Software* (ASC 350-40) as described in this statement. (This adoption reflects adjustments to ASC 350-40 from *ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*.) This statement also adopts *FASB Accounting Standards Codification 350-50, Website Development Costs* (ASC 350-50) in its entirety.

11. This statement also adopts with modification the guidance reflected in ASC 350-40 for cloud computing arrangements as modified by *ASU 2018-15, Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract* and in this statement. Consistent with U.S. GAAP, the guidance in this statement for cloud computing hosting arrangements varies based on whether the cloud computing arrangement is a service contract:

a. An arrangement that is not a service contract applies to internal-use software if the 1) reporting entity has the contractual right to take possession of the software at any time during the hosting period without significant penalty; and 2) it is feasible for the reporting entity to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software.

b. If both conditions in paragraph 11.a. are not met, then the arrangement for internal-use software is considered a service contract.

12. For hosting arrangements that are not service contracts, reporting entities shall account for any internal-use software as follows:

a. The reporting entity shall recognize an operating or non-operating system software asset for the costs incurred for the software license in accordance with paragraph 3 of this statement. This is a modification from U.S. GAAP in which the asset is recognized as an

[1] If statutory accounting principles do not address the FASB Codification reference, consideration of whether the GAAP guidance is adopted for statutory accounting shall be determined in accordance with the respective pre-codification GAAP guidance.

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intangible asset. A liability shall also be recognized if payments for the software license are still required.

b. If the reporting entity has a hosting arrangement that includes both the acquisition of a software asset (pursuant to paragraph 11.a.) and an ongoing hosting arrangement, the reporting entity shall allocate the costs of the arrangement to the different elements. Costs for the ongoing hosting arrangement shall be accounted for in accordance with *SSAP No. 22R—Leases.*

13. For hosting arrangements that are service contracts, reporting entities shall account for the contract as follows:

a. The reporting entity shall capitalize implementation costs of the hosting arrangement (the costs incurred to implement the cloud hosting service contract), as nonoperating system software. The capitalized costs shall be consistent with the costs which are permitted to be capitalized for internal use software and shall be reported as a nonadmitted asset. These implementation costs shall be recognized as each module or component of the hosting arrangement is ready for its intended use.

b. The implementation costs shall be amortized over the lesser of the term of the hosting arrangement, or five years. (This statement adopts the provisions in ASC 350-40-35-13 through ASC 350-40-35-17 for determining the term of the hosting arrangement and for when amortization shall begin.) The amortization cost shall be recognized as depreciation of the nonoperating system software. (This is a modification from U.S. GAAP as the amortization is not recognized in the same expense line as the service contract lease.)

c. The capitalized implementation costs shall be recognized as impaired, with immediate write-off to income when the hosting arrangement (or separate modules or components of the hosting arrangement) ceases to be used, and when events or changes in circumstances occurs indicating that the carrying amount of the related implementation costs may not be recoverable. Example events include:

i. The hosting arrangement is not expected to provide substantive service potential.

ii. A significant change occurs in the extent or manner in which the hosting arrangement is used or is expected to be used.

iii. A significant change is made or will be made to the hosting arrangement.

d. The service contract hosting arrangement shall be accounted for in accordance with *SSAP No. 22R—Leases*. (The service contract hosting arrangement excludes implementation, set-up and other upfront costs (e.g., implementation costs) incurred in the hosting arrangement.)

14. The modifications to ASC 350-40 are as follows:

a. ASC 350-40-15-4 states that the accounting for costs of reengineering activities, which often are associated with new or upgraded software applications, is not included within scope. This guidance is expanded to require that such costs be expensed as incurred.

b. ASC 350-40-25-17 is amended to require software licenses acquired pursuant to paragraph 11.a. are captured within scope of this standard as software, and not as an intangible asset in scope of *SSAP No. 20—Nonadmitted Assets*.

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c. ASC 350-40-35-4 is amended to require entities to follow the amortization guidelines as established in paragraph 10 of *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

d. ASC 350-40-35-5 is amended to require that capitalized operating system software shall be depreciated for a period not to exceed three years. Capitalized nonoperating system software shall be depreciated for a period not to exceed five years. This is consistent with paragraph 3 of this statement.

e. ASC 350-40-35-9 is amended to require that if during the development of internal use software, an entity decided to market the software to others, the entity shall immediately expense any amounts previously capitalized.

f. ASC 350-40-50-1 is amended to require entities to follow the disclosure provisions provided in paragraph 17 of this statement and paragraph 5 of SSAP No. 17.

g. Any software costs capitalized in accordance with this statement shall be deemed either operating or nonoperating system software costs with amortization not to exceed the timeframes stipulated in paragraph 3. Unless this statement explicitly classifies a cost as nonoperating, entities shall make this determination in accordance with the definitions of operating and nonoperating system software contained in the Glossary. As noted in paragraph 2, nonoperating system software is a nonadmitted asset.

Non-Software Deliverables in Arrangements Containing More-Than-Incidental Software

15. In an arrangement that includes software that is more than incidental to the products or services as a whole, software and software-related elements are included within the scope of this guidance. Software-related elements include software products and services as well as any non-software deliverable(s) for which a software deliverable is essential to its functionality. For example, in an arrangement that includes software, computer hardware that will contain the software, and additional unrelated equipment, if the software is essential to the functionality of the hardware, the hardware would be considered software-related and, therefore, included within the scope of this guidance. However, because the software is not essential to the functionality of the unrelated equipment, the equipment would not be considered software-related and would, therefore, be excluded from the scope.

16. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of costs incurred within the scope of paragraphs 10 and 14 shall be expensed when incurred. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Disclosures

17. The disclosures in this paragraph are specific to EDP equipment and operating and nonoperating system software, but shall also be followed as directed under paragraph 14.e.

a. Depreciation and amortization expense for the period;

b. For EDP equipment and operating system software, balances of major classes of depreciable assets, by nature or function, at the balance sheet date;

c. For EDP equipment and operating system software, accumulated depreciation and amortization, either by major classes of depreciable assets or in total, at the balance sheet date; and

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d. A general description of the method or methods used in computing depreciation with respect to major classes of depreciable assets.

18. The financial statements shall disclose if the written capitalization policies and the resultant thresholds have changed from the prior period and the reason(s) for such change.

19. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures in paragraph 17 shall be included in the annual audited statutory financial reports only.

Relevant Literature

20. The revisions to this statement, adopted in October 2010, result from incorporating previously adopted statutory accounting guidance from SSAP No. 17, SSAP No. 79, SSAP No. 81, SSAP No. 82 and SSAP No. 87 into this statement. Revisions to incorporate the previously adopted statutory accounting guidance within this SSAP shall not be considered new statutory accounting guidance. This statement also adopts with modification ASU 2009-14, which revises the previous GAAP guidance adopted under SSAP No. 81. The GAAP revisions adopted within ASU 2009-14 are considered nonsubstantive and are effective immediately.

21. This statement references GAAP guidance in accordance with the current FASB Codification. The references to the FASB Codification are intended to reflect the previously adopted pre-codification GAAP guidance as communicated within SSAP No. 17, SSAP No. 81 and SSAP No. 82:

a. The pre-codification GAAP guidance reflected within SSAP No. 17 and incorporated within paragraph 8 through reference to the FASB ASC 985-20 includes:

i. *FASB Statement No. 86, Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed* was adopted with the exception of paragraphs 5 and 6 and paragraphs 8-11. Those paragraphs were rejected to preclude the capitalization of software development costs.

ii. *FASB Emerging Issues Task Force No. 96-14, Accounting for Costs Associated with Modifying Computer Software for the Year 2000* was adopted. This guidance was not included within the FASB Codification as it is considered no longer technologically helpful.

b. The pre-codification GAAP guidance reflected within SSAP No. 81 and incorporated within paragraph 9 through reference to the FASB ASC 985-605 includes:

i. *AICPA Statement of Position 97-2, Software Revenue Recognition* paragraphs 6-91 was adopted with certain modifications.

ii. *AICPA Statement of Position 98-9, Modification of SOP 97-2 Software Revenue Recognition, With Respect to Certain Transactions* paragraphs 6-8 was adopted. (Note: The adopted paragraphs reflect all of the changes to SOP 97-2.)

iii. *FASB Emerging Issues Task Force No. 00-3, Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware* was adopted in its entirety.

iv. *AICPA Statement of Position 98-4, Deferral of the Effective Date of a Provision of SOP 97-2, Software Revenue Recognition* was considered not applicable because the effective date was inconsistent with SSAP No. 81.

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c. The pre-codification GAAP guidance reflected within SSAP No. 82 and incorporated within paragraphs 10 and 11 through reference to the FASB ASC 350-40 includes:

i. *AICPA Statement of Position 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use* paragraphs 11-42 and paragraph 93 were adopted with modification.

ii. *FASB Emerging Issues Task Force No. 00-2, Accounting for Web Site Development Costs* was adopted in its entirety.

22. SSAP No. 16, SSAP No. 17 and SSAP No. 79 were effective for years beginning January 1, 2001. SSAP No. 81 and SSAP No. 82 were effective for years beginning January 1, 2002. SSAP No. 87 was effective for years beginning on and after January 1, 2004. Transition guidance from the initial adoption of these SSAPs has expired and is not duplicated within this statement.

Effective Date and Transition

23. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in paragraph 15 was originally contained within *INT 04-13: EITF No. 03-5: Applicability of AICPA Statement of Position 97-2 to Non-Software Deliverables in an Arrangement Containing More-Than-Incidental Software* and was effective December 5, 2004.

24. EDP equipment and operating system software capitalized prior to January 1, 2001, shall be depreciated over the lesser of its remaining useful life or three years. Nonoperating system software capitalized prior to January 1, 2001, shall be depreciated over the lesser of its remaining useful life or five years.

25. The adoption with modification of *ASU 2018-15, Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract,* is effective January 1, 2020, with early adoption permitted. The adoption shall occur either prospectively to all implementation costs incurred after the date of adoption, or as a change in accounting principle under *SSAP No. 3—Accounting Changes and Corrections of Errors.*

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 16—Electronic Data Processing Equipment and Software*
- *Issue Paper No. 17—Preoperating and Research and Development Costs*
- *Issue Paper No. 109—Depreciation of Non-Operating System Software – An Amendment to SSAP No. 16*
- *Issue Paper No. 111—Software Revenue Recognition*
- *Issue Paper No. 112—Accounting for the Costs of Computer Software Developed or Obtained for Internal Use and Web Site Development Costs*

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Statement of Statutory Accounting Principles No. 17

Preoperating and Research and Development Costs

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 99-18 and INT 08-04
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 2
Relevant Literature 2
Effective Date and Transition 2

REFERENCES **2**

Relevant Issue Papers 2
Preoperating and Research and Development Costs

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for organizational costs, research and development costs, and start-up costs for new and existing entities.

SUMMARY CONCLUSION

2. Preoperating, including organization and startup costs, and research and development costs shall be expensed as incurred. Preoperating and research and development costs are incurred for such new projects as: (a) arranging operations for a new entity (e.g., legal, actuarial and accounting costs associated with regulatory approval and licensing and issuance of stock), (b) establishing production, sales or service facilities at a new site, (c) changing operations or production significantly, or (d) developing and producing a new product, adopting a new process or offering a new service. Also included in research and development costs are all nonrefundable advance payments for goods or services that will be used or rendered for research and development activities. These nonrefundable advance payments shall be expensed when the advance payment is made.

3. Costs associated with business process reengineering activities, whether done internally or by third parties, shall be expensed when incurred. The total consulting contract price (or the sum of the linked contracts with the same vendor) in a business process reengineering project shall be allocated to each activity based on the relative fair values when a third party is used to complete such a project.

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4. Preoperating, including organization and start-up costs, and research and development costs specifically exclude tangible assets acquired in connection with such activities.

Disclosures

5. Disclosure shall be made in the financial statements of the total research and development costs charged to expense in each period for which an income statement is presented. The disclosure shall be included in the annual audited statutory financial report only.

6. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

7. This statement adopts *FASB Statement No. 2, Accounting for Research and Development Costs* and *FASB Interpretation No. 6, Applicability of FASB Statement No. 2 to Computer Software*. From January 1, 2001 through October 2010, this statement also adopted *FASB Statement No. 86*, *Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed* (FAS 86), with the exception of paragraphs 5 and 6 and paragraphs 8-11. These paragraphs have been rejected to preclude the capitalization of software development costs. *FASB Emerging Issues Task Force No. 96-14, Accounting for the Costs Associated with Modifying Computer Software for the Year 2000* (EITF 96-14) and *FASB Emerging Accounting Issues Task Force No. 97-13: Accounting for Costs Incurred in Connection with a Consulting Contract or an Internal Project that Combines Business Process Reengineering and Information Technical Transformation* (EITF 97-13) are adopted. Effective October 2010, FAS 86 and EITF 96-14 were rejected as FASB issued new GAAP guidance, which is reviewed in SSAP No. 16R.

8. This statement rejects *FASB Statement No. 7*, *Accounting and Reporting by Development Stage Enterprises, FASB Interpretation No. 7, Applying FASB Statement No. 7 in Financial Statements of Established Operating Enterprises, an interpretation of FASB Statement No. 7* and *FASB Emerging Issues Task Force No. 07-3, Accounting for Nonrefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities.*

Effective Date and Transition

9. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance reflected in paragraph 2 was previously included in *INT 08-04: FASB Emerging Issues Task Force No. 07-3, Accounting for Nonrefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities* and was originally effective May 31, 2008. Guidance reflected in paragraph 3 was originally included in *INT 99-18: EITF No. 97-13: Accounting for Costs Incurred in Connection with a Consulting Contract or an Internal Project That Combines Business Process Reengineering and Information Technology Transformation* and was effective October 4, 1999.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 17—Preoperating and Research and Development Costs*

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Statement of Statutory Accounting Principles No. 19

Furniture, Fixtures, Equipment and Leasehold Improvements

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 87 with guidance incorporated August 2011; Nullifies and incorporates INT 09-05
Affected by	No other pronouncements
Interpreted by	INT 01-18
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Furniture, Fixtures and Equipment 1
Leasehold Improvements Paid by the Reporting Entity as Lessee 2
Maintenance Costs Paid by Lessee 2
Depreciation and Amortization 2
Disclosures 3
Relevant Literature 3
Effective Date and Transition 4

REFERENCES **4**

Relevant Issue Papers 4

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for furniture, fixtures, and equipment (excluding electronic data processing equipment and software that is addressed in *SSAP No. 16R—Electronic Data Processing Equipment and Software*, leasehold improvements paid by the reporting entity as lessee, and depreciation of property and amortization of leasehold improvements. Concession service arrangements, as defined in *SSAP No. 22R—Leases*, are not leases, nor should they be recognized as property, plant or equipment. Therefore, these arrangements, and improvements to infrastructures within concession service arrangements, are outside of the scope of this standard.

SUMMARY CONCLUSION

Furniture, Fixtures and Equipment

2. Furniture, fixtures and equipment generally meet the definition of assets established in *SSAP No. 4—Assets and Nonadmitted Assets*. Such items also meet the criteria defining nonadmitted assets in SSAP No. 4. Accordingly, these assets shall be depreciated against net income as the estimated

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economic benefit expires and the undepreciated portion of these assets shall be reported as nonadmitted assets and charged against surplus.(INT 01-18)

3. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of such assets shall be expensed when purchased. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Leasehold Improvements Paid by the Reporting Entity as Lessee

4. Leasehold improvements shall be defined as lessee expenditures that are permanently attached to an asset that a reporting entity is leasing under an operating lease.

5. Leasehold improvements that increase the value and enhance the usefulness of the leased asset meet the definition of assets established in SSAP No. 4. Within that definition, such items also meet the criteria defining nonadmitted assets. Accordingly, such assets shall be reported as nonadmitted assets and charged against surplus. These nonadmitted assets shall be amortized against net income over the shorter of their estimated useful life or the remaining lease term as defined in SSAP No. 22R. Leasehold improvements that do not meet the definition of assets shall be charged to expense when acquired. The amortization of leasehold improvements (including property improvements and integral equipment) shall cease, with any remaining amount immediately expensed, in any event in which the lease is terminated in advance of the lease term. This includes situations in which leased real estate is acquired by the reporting entity lessee. Such improvements related to the functionality of health care delivery assets shall follow the accounting, reporting and impairment guidance in *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*, and an exception to the application of this guidance to leasehold improvements necessary for the functionality of health care delivery assets is included in SSAP No. 73. If leased real estate is acquired, recognition of the real estate shall follow the provisions in *SSAP No. 40R—Real Estate Investments*.

6. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of such assets shall be expensed when purchased. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Maintenance Costs Paid by Lessee

7. Maintenance costs incurred by the lessee for maintenance on the leased item that do not increase the value and enhance the usefulness of the leased asset shall be expensed when incurred. Reimbursable deposits shall be reflected as nonadmitted assets. Deposits paid to the lessor, reimbursable when the lessee incurs costs for lease maintenance activities, shall be recorded as nonadmitted assets. When the amount on deposit is less than probable of being returned, the deposit shall be recognized as an additional lease expense.

Depreciation and Amortization

8. Depreciable assets include all tangible capital assets classified as either admitted or nonadmitted in accordance with SSAP No. 4. Land shall not be considered a depreciable asset.

9. The acquisition cost of depreciable assets, net of salvage, shall be depreciated against net income over the estimated useful lives of the assets in a systematic and rational manner. The acquisition cost of a leasehold improvement shall be amortized against net income over the shorter of its estimated useful life or the lease term as defined in SSAP No. 22R. For leasehold improvements capitalized subsequent to inception of the lease, the cost shall be amortized over the shorter of its estimated useful life or the remaining lease term. Amounts capitalized for leasehold improvements in periods subsequent to the

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original lease term (i.e., during renewal periods), are amortized utilizing the shorter of the estimated useful life of the asset or the remaining lease term.

10. A variety of systematic depreciation and amortization methods is available such as the straight-line method, sum-of-the-years' digits method, and various declining balance methods. The depreciation or amortization method selected shall be that which most appropriately allocates the cost of the depreciable asset or leasehold improvement over its estimated useful life. The use of the sinking fund or constant yield methods of depreciation does not constitute acceptable statutory accounting practice.

11. Useful lives of depreciable assets and leasehold improvements can be obtained from contractors, appraisers, engineers, and manufacturers, or they may be based on prior experience. Estimates published by the Internal Revenue Service can be helpful in the selection of useful lives for specific assets.

12. Changes in the estimated useful lives of depreciable assets or leasehold improvements from one period to another shall be considered a change in accounting estimate and shall be accounted for in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

13. Changes in depreciation or amortization methods from one period to another shall be considered a change in accounting principle and shall be accounted for in accordance with SSAP No. 3.

14. Depreciation and amortization expense shall be recorded in the statement of income in accordance with *SSAP No. 70—Allocation of Expenses*.

Disclosures

15. The following disclosures shall be made in the financial statements:

a. Depreciation and amortization expense for the period;

b. A general description of the method or methods used in computing depreciation and amortization with respect to major classes of depreciable assets and leasehold improvements.

16. The financial statements shall disclose if the written capitalization policy and the resultant predefined thresholds changed from the prior period and the reason(s) for such change.

17. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures in paragraph 15 shall be included in the annual audited statutory financial reports only.

Relevant Literature

18. This statement adopts paragraphs 4 and 5 of *Accounting Principles Board Opinion No. 12, Omnibus* Opinion—*1967*. This statement also adopts *AICPA Practice Bulletin No. 1, Purpose and Scope of AcSEC Practice Bulletins and Procedures for Their Issuance, Exhibit A*.

19. This statement rejects *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins, "*Chapters 9A and 9C;" however, it is considered appropriate to use the concepts of depreciating assets discussed in the GAAP guidance, which requires that the acquisition cost less salvage value be recorded as an expense over the estimated useful life of the asset, as the basis for the statutory guidance in this statement. *FASB Emerging Issues Task Force No. 08-3: Accounting by Lessees for Maintenance Deposits* is adopted with modification to require reimbursable deposits to be reflected as nonadmitted assets.

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Effective Date and Transition

20. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. Guidance reflected in paragraphs 3, 6 and 16, incorporated from SSAP No. 87, was originally effective for years beginning on and after January 1, 2004. Guidance in paragraph 7 related to maintenance costs paid by lessee was previously included within *INT 09-05: FASB Emerging Issues Task Force No. 08-3: Accounting by Lessees for Maintenance Deposits* and was effective for periods beginning September 21, 2009.

21. The use of the sinking fund or constant yield method does not constitute acceptable statutory accounting practice and these methods shall not be applied to new properties acquired since December 3, 1990 (the date the Emerging Accounting Issues (E) Working Group reached its conclusion regarding this method) nor if the reporting entity changes its existing properties' method of depreciation. This conclusion would not impact those properties currently being depreciated using the constant yield method.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 19—Furniture, Fixtures, and Equipment*
- *Issue Paper No. 31—Leasehold Improvements Paid by the Reporting Entity as Lessee*
- *Issue Paper No. 67—Depreciation of Property and Amortization of Leasehold Improvements*
- *Issue Paper No. 119—Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29, 73, 79 and 82*

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Statement of Statutory Accounting Principles No. 20

Nonadmitted Assets

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 09-03
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Relevant Literature 3

Effective Date and Transition 3

REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for nonadmitted assets which are not specifically addressed in other statements.

SUMMARY CONCLUSION

2. The definition and accounting treatment for nonadmitted assets is outlined in *SSAP No. 4—Assets and Nonadmitted Assets* as follows:

> 3. As stated in the Statement of Concepts, "The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third-party interests should not be recognized on the balance sheet," and are, therefore, considered nonadmitted. For purposes of statutory accounting principles, a nonadmitted asset shall be defined as an asset meeting the criteria in paragraph 2, which is accorded limited or no value in statutory reporting, and is one which is:
>
> a. Specifically identified within the *Accounting Practices and Procedures Manual* as a nonadmitted asset; or
>
> b. Not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*.

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If an asset meets one of these criteria, the asset shall be reported as a nonadmitted asset and charged against surplus unless otherwise specifically addressed within the *Accounting Practices and Procedures Manual*. The asset shall be depreciated or amortized against net income as the estimated economic benefit expires. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of furniture, fixtures, equipment, or supplies, shall be expensed when purchased.

3. This statement shall not be considered an all-inclusive list of nonadmitted assets. Certain admitted assets and nonadmitted assets are addressed in other SSAPs.

4. Consistent with paragraph 2, the following assets shall be nonadmitted:

a. Deposits in Suspended Depositories—Amounts on deposit with suspended depositories may not be fully recoverable. Any amounts not reasonably expected to be recovered shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Amounts in excess of that written off shall be nonadmitted as they are not available to satisfy obligations to policyholders;

b. Bills Receivable Not for Premium and Loans Unsecured or Secured by Assets That Do Not Qualify As Admitted Investments—In accordance with SSAP No. 5R, amounts determined to be uncollectible or otherwise impaired shall be written off. Amounts in excess of that written off are not considered to be properly collateralized as there are no underlying assets which would otherwise be admitted invested assets. Such amounts shall be nonadmitted as they may be of questionable economic value if needed to fulfill policyholder obligations. Receivables arising from working capital finance programs designated by the Securities Valuation Office are subject to the guidance in *SSAP No. 105R—Working Capital Finance Investments*;

c. Loans on Personal Security, Cash Advances To, Or In The Hands Of, Officers Or Agents And Travel Advances—In accordance with SSAP No. 5R, amounts determined to be uncollectible or otherwise impaired shall be written off. Amounts in excess of that written off typically are unsecured and as such have no underlying assets which would otherwise be admitted assets. Such amounts shall be nonadmitted as they may be of questionable economic value if needed to fulfill policyholder obligations. Some of these items may also be considered prepaid expenses which, per *SSAP No. 29—Prepaid Expenses*, are nonadmitted;

d. All "Non-Bankable" Checks—Examples of "non-bankable" checks are NSF (non-sufficient funds) checks, post-dated checks, or checks for which payment has been stopped. Although these checks may still maintain probable future benefits (and thus meet the definition of assets), at the date on which they are non-bankable they are not available for policyholder obligations and shall be nonadmitted until the uncertainty related to the probable future benefit is resolved and the checks are converted to available funds;

e. Trade Names And Other Intangible Assets[1]—These assets, by their nature, are not readily marketable and available to satisfy policyholder obligations and shall be nonadmitted;

f. Automobiles, Airplanes and Other Vehicles—Automobiles, airplanes and other vehicles meet the definition of assets established in SSAP No. 4. However, they are not readily

[1] Defensible intangible assets are defined as an intangible asset acquired in a business combination or an asset acquisition that an entity does not intend to actively use but does intend to prevent others from using. These may also be referred to as a "locked-up asset" because while the asset is not being actively used, it is likely contributing to an increase in the value of other assets owned by the entity. These assets are not readily available to satisfy policyholder obligations and shall be nonadmitted.

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available to satisfy policyholder obligations and as a result the undepreciated portion shall be nonadmitted. The accounting for these assets shall be consistent with the accounting for equipment provided in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* or for commercial airplane leveraged leases, refer to the guidance in *SSAP No. 22R–Leases*;

g. Company's Stock as Collateral for Loan—When a reporting entity lends money and accepts its own stock as collateral for the loan, it shall report the amount of the loan receivable and any related accrued interest on the loan as a nonadmitted asset. The asset is nonadmitted as the collateral could not be used to satisfy the obligation in the event of default.

Relevant Literature

5. This statement adopts with modification *FASB Emerging Issues Task Force No. 08-7: Accounting for Defensive Intangible Assets* to nonadmit defensible intangible assets. This statement rejects Chapters 3A and 11 of *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins*.

Effective Date and Transition

6. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance reflected in footnote 1, incorporated from *INT 09-03: EITF 08-7: Accounting for Defensive Intangible Assets*, was effective June 13, 2009. With the adoption of SSAP No. 105R, revisions were incorporated into paragraph 4.b. These revisions from SSAP No. 105R are retained for historical purposes within *Issue Paper No. 147—Working Capital Finance Investments*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 90—Nonadmitted Assets*
- *Issue Paper No. 147—Working Capital Finance Investments*

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Statement of Statutory Accounting Principles No. 21 – Revised

Other Admitted Assets

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised November 15, 2018
Effective Date	January 1, 2001; December 31, 2018
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-001

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Collateral Loans 2
Structured Settlements – Reporting Entity Owner and Payee of Annuity 2
Structured Settlements – Reporting Entity Acquires Legal Right to Receive Payments 3
The Amount That Could Be Realized on Life Insurance Where the Reporting Entity is Owner and Beneficiary or Has Otherwise Obtained Rights to Control the Policy 4
Receivables for Securities 4
Other Amounts Receivable Under Reinsurance Contracts 5
Guaranteed Investment Contracts 5
State Guaranty Association Loan Agreements 5
Relevant Literature 6
Effective Date and Transition 6

REFERENCES **6**

Relevant Issue Papers 6

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for admitted assets which are not specifically addressed in other statements.

SUMMARY CONCLUSION

2. The definition and accounting treatment for admitted assets is outlined in paragraphs 2 and 3 of *SSAP No. 4—Assets and Nonadmitted Assets*.

3. Consistent with paragraph 2, the following assets shall be considered admitted and shall be reported in accordance with SSAP No. 4. These admitted assets are not addressed in other statements.

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Collateral Loans

4. Collateral loans are unconditional obligations[1] for the payment of money secured by the pledge of a~~n~~ qualifying investment[2] and meet the definition of assets as defined in SSAP No. 4, and are admitted assets to the extent they conform to the requirements of this statement. The outstanding principal balance on the loan and any related accrued interest shall be recorded as an admitted asset subject to the following limitations:

a. Loan Impairment—Determination as to the impairment of a collateral loan shall be based on current information and events. When it is considered probable that any portion of amounts due under the contractual terms of the loan will not be collected the loan is considered impaired. The impairment shall be measured based on the fair value of the collateral less estimated costs to obtain and sell the collateral. The difference between the net value of the collateral and the recorded asset shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*;

b. Nonadmitted Asset—In accordance with *SSAP No. 20—Nonadmitted Assets*, collateral loans secured by assets that do not qualify as investments, which would otherwise be admitted, shall be nonadmitted. Further, any amount of the loan outstanding which is in excess of the permitted relationship of fair value of the pledged investment to the collateral loan shall be treated as a nonadmitted asset. To support the admissibility of collateral loans, reporting entities shall maintain documentation sufficient to support the reasonableness of the fair value measurement of the underlying collateral, which shall be made available to the applicable domiciliary regulator and independent audit firm upon request.

Structured Settlements – Reporting Entity Owner and Payee of Annuity

5. The reporting of the present value of structured settlement annuities where the reporting entity is the owner and payee as described in SSAP No. 65, paragraph 17.a. shall account for the annuity an admitted asset at its net present realizable value. The annuity described is reported as an other-than-invested asset. Income from the annuities shall be recorded as miscellaneous income. The present value of the annuity and the related amortization schedule shall be obtained from the issuing life insurance company at the time the annuity is purchased. When the reporting entity is the owner and payee, no reduction shall be made to loss reserves.

[1] For purposes of determining a collateral loan in scope of this statement, a collateral loan does not include investments captured in scope of other statements. For example, *SSAP No. 26R—Bonds* includes securities (as defined in that statement) representing a creditor relationship whereby there is a fixed schedule for one or more future payments. Investments captured in SSAP No. 26R that are also secured with collateral shall continue to be captured within scope of SSAP No. 26R.

[2] A qualifying ~~I~~investment defined as those assets listed in Section 3 of *Appendix A-001—Investments of Reporting Entities*, which would, if held by the insurer, qualify for admittance. For example, if the collateral would not qualify for admittance under SSAP No. 4 due to encumbrances or other third-party interests, then it does not meet the definition of "qualifying" and the collateral loan, or any portion thereof which is not adequately collateralized, is not permitted to be admitted. In the cases where the collateral is an equity/unit investment in a joint venture, partnership, limited liability company, and/or SCA is pledged as collateral in a collateral loan, audited financial statements on a consistent annual basis are always required in accordance with *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* and/or *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

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Structured Settlements – Reporting Entity Acquires Legal Right to Receive Payments

6. A reporting entity that acquires (directly or indirectly) structured settlement payment rights[3] through a factoring company, excluding securitizations captured in SSAP No. 43R, shall report the acquisition as follows:

a. Period-certain (non-life contingent) structured settlement income streams shall be reported as other long-term invested assets[4], and are admitted assets if the rights to the future payments from a structured settlement have been legally acquired in accordance with all state and federal requirements. If the structured settlement has not met all legal requirements, including the court-approved transfer from the original recipient, then the reporting entity shall recognize the appropriate excise tax obligation and the structured settlement shall be nonadmitted.

b. Life-contingent structured settlement income streams shall be reported as other long-term invested assets on Schedule BA and shall be nonadmitted. (Nonadmittance is required regardless if the right to future payments has been legally transferred.)

7. Structured settlement income streams shall be initially reported at cost, including brokerage and other related fees. The cost generally reflects the net present value of the future payment streams with an embedded fixed-rate yield. Structured settlement income streams shall always be acquired at a discount, meaning the amount to be received shall be greater than the acquisition cost. As the structured settlement payments are earned, reporting entities shall reduce the book adjusted carrying value (BACV) to reflect the accrual of the income stream (proportionate payment of original cost on Schedule BA, Part 3) as well as corresponding investment income for the fixed rate spread. (For example, if a reporting entity acquires a structured settlement that equates to three payments, as each payment is received, the BACV would be decreased proportionately, with the pay-down recognized as a disposal.)

a. Impairment – Determination as to the impairment of a structured settlement income stream shall be based on current information and events. When a reporting entity does not expect to receive a structured settlement payment, the structured settlement shall be considered impaired. Once a structured settlement income stream is impaired, the entire amount of the reported structured settlement investment (including subsequent rights to cash flows related to the impaired structured settlement) shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. If the structured settlement payment is not expected to be received due to the credit quality of the issuer (e.g., the insurer/obligor making structured settlement payments), all structured settlement income streams expected from that obligor shall also be deemed impaired and written off in accordance with SSAP No. 5R. (For example, if a reporting entity acquired the rights to receive three structured settlement payments in a single brokerage transaction, when the first payment is not expected to be received, then all three structured settlement payments related to this acquisition shall be written off. If the reason for the impairment is due to the obligor, and the reporting entity had acquired other structured settlement income streams that are due from that obligor, all structured settlement income streams due from that obligor shall also be written off as impaired.)

[3] This guidance is specific to acquired structured settlement income streams (legal right to receive future payments from a structured settlement) and does not capture accounting and reporting guidance for the acquisition of any insurance product (e.g., life settlement, annuities, etc.).

[4] Reporting entities that hold qualifying structured settlement payment rights shall report the security on Schedule BA either as an "any other class of asset" or as a "fixed or variable interest rate investment with underlying characteristics of other fixed income instruments" if the structured settlement payment right qualifies for reporting within that reporting line (e.g., NAIC designation).

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b. Investment Income – The discount on acquired structured settlements shall be recognized as an adjustment of yield over the period of time until the cash payments under the structured settlements are received to produce a constant effective yield each year.

The Amount That Could Be Realized on Life Insurance Where the Reporting Entity is Owner and Beneficiary or Has Otherwise Obtained Rights to Control the Policy

8. The provisions in this paragraph are for life insurance policies, which are in compliance with Internal Revenue Code (IRC) §7702[5], in which the reporting entity is the owner and beneficiary[6]. For these owned products, the amount that could be realized on life insurance policies where the reporting entity is the owner and beneficiary, or has otherwise obtained the rights to control the policy, is similar to a cash deposit that is realizable on demand. As such, the amount that could be realized on a life insurance policy as of the date to which premiums have been paid shall be reported as an admitted asset. In determining the amount that could be realized, reporting entities shall consider the cash surrender value as well as other contractual terms which limit or provide for additional realizable amounts. If any of these contractual terms which limit or provide for additional realizable amounts allow the owner to pay variable premium (reducing or increasing the premium based on the increase or decrease of a variable investment vehicle of the policy), the life insurance policies must always remain compliant with IRC §7702 to be an admitted asset under this paragraph. Amounts recoverable by the reporting entity at the discretion of the issuing company shall not be included. Amounts realizable beyond one year from the surrender date shall be discounted. For group policies or a group of individual life policies, reporting entities shall assume surrender on a policy by policy or certificate by certificate basis, unless contractual terms only allow for surrender of all policies or certificates as a group, in which case the amount that could be realized shall be determined on a group basis. Disclosure is required of the amount of the cash surrender value that is within an investment vehicle by investment category (e.g., bonds, common stock, joint ventures, derivatives, etc.)

Receivables for Securities

9. Sales of securities are recorded as of the trade date. A receivable due from the broker is established in instances when a security has been sold, but the proceeds from the sale have not yet been received. Unless the receivable for securities meets the criteria set forth in paragraph 11, the receivable for securities is an admitted asset to the extent it conforms to the requirements of this statement. For receivables arising from the sale of a security which was acquired on a "To Be Announced" ("TBA") basis, or from the sale of securities that are received as stock distributions that may be restricted (unregistered) or in physical form, and which has yet to be actually received, admissibility shall be in accordance with paragraph 12.

10. An evaluation shall be made in accordance with SSAP No. 5R, to determine if there is impairment. If, in accordance with SSAP No. 5R, it is probable the balance or any portion thereof is uncollectible, any such deemed uncollectible receivable shall be written off and charged against income

[5] In order to be in compliance with IRC §7702:

1. The contract must be considered "life insurance" under applicable state insurance law. This is a contractual definition that includes:
    - The contract must be filed and approved as life insurance.
    - It must be regulated as life insurance under applicable laws and regulations (such as variable life insurance regulation and non-forfeiture laws).
    - There must be an insurable interest in the continued life of the insured (federal and state law also require the consent of the insured to the coverage).
    - There must be a significant transfer of mortality risk between the policyholder and the insurance company.
2. The contract must meet one of two actuarial tests of the policy's cash value relation to its death benefit to assure that, prior to death/maturity, the policy cash value does not exceed the net single premium required to fund the death benefit.

[6] These life insurance products shall be acquired with the primary consideration of the costs related to employee benefit obligations or the loss of a key person.

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in the period the determination is made. If it is reasonably possible, but not probable, the balance or any portion thereof is uncollectible and is therefore not written off, the disclosure requirements outlined in SSAP No. 5R shall be followed.

11. Receivables for securities not received within 15 days from the settlement date shall be nonadmitted and shall be classified as "other-than-invested assets."

12. Receivables arising from the secondary sale of securities acquired on a TBA basis, or from stock distributions that may be restricted (unregistered) or in physical form, which have not yet been received by the seller in the secondary sale transaction, may be admitted until the security is exchanged for payment. TBA securities are originally purchased well in advance of the actual date of security issuance (frequently 90 days or more). Accordingly, secondary sales of securities so acquired may occur before the date of issuance. Sales of securities so acquired always include a provision that requires simultaneous delivery of the security and receipt of consideration. Upon the secondary sale, and prior to the actual receipt, of a security acquired on a TBA basis, the seller in the secondary sale transaction records a liability for the book value of the security thus sold and a receivable for the consideration reflected in the secondary sale transaction. Profits or losses emanating from the secondary sale transaction are recorded in the same manner as profits and losses emanating from any other sale transaction involving an investment.

Other Amounts Receivable Under Reinsurance Contracts

13. Amounts receivable from Servicemen's Group Life Insurance (SGLI) or Federal Employees' Group Life Insurance (FEGLI) pools and Federal Crop Insurance programs shall be reported as admitted assets.

Guaranteed Investment Contracts

14. Guaranteed Investment Contracts (GICs) purchased for investment purposes meet the definition of assets as defined in SSAP No. 4, and are admitted assets to the extent they conform to the requirements of this statement.

15. Purchases for which all contractual rights and ownership of the GIC result in an investment similar to a corporate bond shall be accounted for in accordance with the guidance in *SSAP No. 26R—Bonds*.

16. An investment in a GIC payment stream is created when an intermediary purchases individual GICs, pools them, and sells the rights to the payment stream. These investments shall be reported as other long-term invested assets and shall be carried at amortized cost.

17. If, in accordance with SSAP No. 5R, it is probable that the carrying value of a GIC is not fully recoverable the investment shall be considered impaired. Accordingly, the cost basis of the investment shall be written down to the undiscounted estimated cash flows and the amount of the write down shall be accounted for as a capital loss. The new cost basis shall not be changed for subsequent recoveries in fair value.

State Guaranty Association Loan Agreements

18. State guaranty associations have the statutory authority to reinsure any or all of the policies of an impaired or insolvent insurer and borrow funds. When this is done in the case of reinsurance, the assuming carrier receives assets supporting the liabilities from the insolvent company's estate and/or the responsible state guaranty association. If available, the state guaranty association transfers cash at the closing of the transaction. Loan agreements may be utilized in the event a guaranty association does not have the funds on hand or is unable to raise the funds by the closing date. In the case of adverse cash flow situations, guaranty associations may enter into loan agreements with insurers to provide funds that will

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allow the association to perform its duties as required by statute. These loan agreements are essentially credit risk free because the notes are backed by all member insurers of an association.

19. Loan agreements issued by state guaranty associations taken by an insurance company in connection with funding an assumption reinsurance agreement or as interim financing meet the definition of assets as defined in SSAP No. 4, are admitted assets to the extent they conform to the requirements of this statement, and shall be reported as a note receivable—other-than-invested assets.

Relevant Literature

20. This statement is consistent with *FASB Statement No. 114, Accounting by Creditors for the Impairment of a Loan* which was adopted with modification in *SSAP No. 37—Mortgage Loans*. This statement is consistent with *Accounting Principles Board Opinion No. 21, Interest on Receivables and Payables* which was adopted in *SSAP No. 15—Debt and Holding Company Obligations.*

21. This statement adopts *FASB Emerging Issues Task Force No. 88-5, Recognition of Insurance Death Benefits* and *FASB Technical Bulletin 85-4, Accounting for Purchases of Life Insurance* with the modification that the entity must be the owner and the beneficiary. This statement also adopts with modification *FASB Emerging Issues Task Force No. 06-05, Accounting for Purchases of Life Insurance – Determining the Amount That Could be Realized in Accordance with FASB Technical Bulletin No. 85-4*. Guidance has been included within this SSAP to clarify how to determine the amount that could be realized on life insurance in situations where the reporting entity is the owner and beneficiary or has otherwise obtained rights to control the policy.

Effective Date and Transition

22. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* The guidance for structured settlements when the reporting entity acquires the legal right to receive payments is effective December 31, 2018. The clarification regarding audits of qualifying collateral pledged for collateral loans in the footnote 2 to paragraph 4 requires applicable audits to be obtained for the 2023 reporting period in the subsequent year. In periods after year-end 2023, the audits of equity collateral pledged for collateral loans are required to be obtained for the reporting year in which it was pledged and annually thereafter. The annual audit lag shall be consistent from period to period.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 87—Other Admitted Assets*
- *Issue Paper 160—Structured Settlements Acquired as Investments*

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Statement of Statutory Accounting Principles No. 22 – Revised

Leases

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised August 3, 2019
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper 161 effective January 1, 2020.
Affects	Nullifies and incorporates INT 00-02, INT 00-27, INT 04-20 and INT 09-05; Nullifies INT 02-15 and INT 04-18
Affected by	No other pronouncements
Interpreted by	INT 20-01
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. The purpose of this statement is to establish statutory accounting principles for leases. It addresses:

   a. Accounting and reporting by lessees;

   b. Accounting and reporting by lessors;

   c. Sale-leaseback transactions;

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d. Leveraged leases for lessors;

e. Related party leases; and

f. Disclosures.

SUMMARY CONCLUSION

2. A lease is defined as a contract or part of a contract conveying the right to control the use of property, plant or equipment (land and/or depreciable assets) for a stated period of time in exchange for consideration. This definition does not include contracts for services that do not transfer the right to use property, plant or equipment from one contracting party to the other (i.e., employee lease contracts) or service concession arrangements[1]. Agreements that do transfer the right to control the use of property, plant or equipment meet the definition of a lease even though substantial services by the contractor (lessor) may be called for in connection with the operation or maintenance of the assets.

3. Property, plant or equipment, (including computer software) as used in this SSAP, includes only land and/or depreciable assets. Therefore, inventory (including equipment parts inventory), other intangible assets, assets under construction, leases to explore for or use minerals, natural gas and similar nonregenerative resources, and leases of biological assets, such as timber cannot be the subject of a lease for accounting purposes. Additionally, non-depreciable assets, including investments and premium receivables do not meet the definition of property, plant or equipment and cannot be the subject of a lease for accounting purposes.

Determining Whether an Arrangement Contains a Lease

4. Determining whether an arrangement contains a lease that is within the scope of this SSAP should be based on the substance of the arrangement. At inception of a contract, an entity shall determine whether that contract is or contains a lease. A contract is or contains a lease if the contract conveys the right to control the use of identified property, plant or equipment (an identified asset) for a period of time in exchange for consideration. A period of time may be described in terms of the amount of use of an identified asset (for example, the number of production units that an item of equipment will be used to produce).

Identifying an Asset

5. An asset can be identified by being explicitly or implicitly specified within the contract. Although specific property, plant or equipment may be explicitly identified in an arrangement, it is not the subject of a lease if fulfillment of the arrangement is not dependent on the use of the specified property, plant or equipment. A warranty obligation that permits or requires the substitution of the same or similar property, plant or equipment when the specified property, plant or equipment is not operating properly does not preclude lease treatment. In addition, a contractual provision (contingent or otherwise) permitting or requiring the owner/seller to substitute other property, plant or equipment for any reason on or after a specified date does not preclude lease treatment prior to the date of substitution. Property, plant or equipment has been implicitly specified if, for example, the seller owns or leases only one asset with

[1] A service concession arrangement is an arrangement between a public sector entity grantor and an operating entity under which the operating entity operates the grantor's infrastructure (for example, airports, roads, bridges, tunnels, prisons and hospitals) for a specified period of time. A public-sector entity includes a governmental body or an entity to which the responsibility to provide public service has been delegated. In a service concession arrangement, both of the following conditions exist:

a. The grantor controls or has the ability to modify or approve the services that the operating entity must provide with the infrastructure, to whom it must provide them and at what price.

b. The grantor controls, through ownership, beneficial entitlement, or otherwise, any residual interest in the infrastructure at the end of the term of the arrangement.

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which to fulfill the obligation and it is not economically feasible or practicable for the owner/seller to perform its obligation through the use of alternative property, plant or equipment. Property, plant or equipment can also be implicitly specified at the time the asset is made available for use by the lessee.

6. Even if an asset is specified, the asset does not qualify as an identified asset if the lessor has the substantive right to substitute the asset throughout the period of use. A lessor's right to substitute an asset is substantive only if (1) the lessor has the practical ability to substitute alternative assets throughout the period of use (for example, the lessee cannot prevent the lessor from substituting an asset, and alternative assets are readily available to the lessor or could be sourced by the lessor within a reasonable period of time), and (2) the lessor would benefit economically from the exercise of its right to substitute the asset (that is, the economic benefits associated with substituting the asset is expected to exceed the costs associated with substituting the asset).

7. An entity's evaluation of whether a lessor's substitution right is substantive is based on facts and circumstances at inception of the contract and shall exclude consideration of future events that, at inception, are not considered likely to occur. Examples of future events that, at inception of the contract, would not be considered likely to occur and, thus, should be excluded from the evaluation include, but are not limited to, the following:

a. An agreement by a future lessee to pay an above-market rate for use of the asset;

b. The introduction of new technology that is not substantially developed at inception of the contract;

c. A substantial difference between the lessee's use of the asset, or the performance of the asset and the use or performance considered likely at inception of the contract;

d. A substantial difference between the market price of the asset during the period of use and the market price considered likely at inception of the contract.

8. If the asset is located at the lessee's premises or elsewhere, the costs associated with substitution are generally higher than when located at the lessor's premises and, therefore, are more likely to exceed the benefits associated with substituting the asset. If the lessor has a right or an obligation to substitute the asset only on or after either a particular date or the occurrence of a specified event, the lessor does not have the practical ability to substitute alternative assets throughout the period of use. The lessor's right or obligation to substitute an asset for repairs or maintenance, if the asset is not operating properly, or if a technical upgrade becomes available, does not preclude the lessee from having the right to use an identified asset. If the lessee cannot readily determine whether the lessor has a substantive substitution right, the lessee shall presume that any substitution right is not substantive.

9. A capacity portion of an asset is an identified asset if it is physically distinct (for example, a floor of a building or a segment of a pipeline that connects a single lessee to the larger pipeline). A capacity or other portion of an asset that is not physically distinct (for example, a capacity portion of a fiber optic cable) is not an identified asset, unless it represents substantially all of the capacity of the asset and thereby provides the lessee with the right to obtain substantially all of the economic benefits from use of the asset.

Right to Control the Use of the Identified Asset

10. To determine whether a contract conveys the right to control the use of an identified asset for a period of time, an entity shall assess whether, throughout the period of use, the lessee has both:

a. The right to obtain substantially all of the economic benefits from use of the identified asset.

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i. To control the use of an identified asset, a lessee is required to have the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use (for example, by having exclusive use of the asset throughout that period). A lessee can obtain economic benefits from use of an asset directly or indirectly in many ways, such as by using, holding, or subleasing the asset. The economic benefits from use of an asset include its primary output and byproducts (including potential cash flows derived from these items) and other economic benefits from using the asset that could be realized from a commercial transaction with a third party.

ii. When assessing the right to obtain substantially all of the economic benefits from use of an asset, an entity shall consider the economic benefits that result from use of the asset within the defined scope of a lessee's right to use the asset in the contract.

iii. If a contract requires a lessee to pay the lessor or another party a portion of the cash flows derived from use of an asset as consideration, those cash flows paid as consideration shall be considered to be part of the economic benefits that the lessee obtains from use of the asset. For example, if a lessee is required to pay the lessor a percentage of sales from use of retail space as consideration for that use, that requirement does not prevent the lessee from having the right to obtain substantially all of the economic benefits from use of the retail space. That is because the cash flows arising from those sales are considered to be economic benefits that the lessee obtains from use of the retail space, a portion of which it then pays to the lessor as consideration for the right to use that space.

b. The right to direct the use of the identified asset.

i. A lessee has the right to direct the use of an identified asset throughout the period of use in either of the following situations. Additionally, if the lessee in the contract is a joint operation or a joint arrangement, an entity shall consider whether the joint operation or joint arrangement has the right to control the use of an identified asset throughout the period of use.

(a) The lessee has the right to direct how and for what purpose the asset is used throughout the period of use. If the lessee has the right to control the use of an identified asset for only a portion of the term of the contract, the contract contains a lease for that portion of the term.

(b) The relevant decisions about how and for what purpose the asset is used are predetermined and at least one of the following conditions exists:

(1) The lessee has the right to operate the asset (or to direct others to operate the asset in a manner that it determines) throughout the period of use without the lessor having the right to change those operating instructions.

(2) The lessee designed the asset (or specific aspects of the asset) in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

ii. The relevant decisions about how and for what purpose an asset is used can be predetermined in a number of ways. For example, the relevant decisions can be

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predetermined by the design of the asset or by contractual restrictions on the use of the asset.

iii. In assessing whether a lessee has the right to direct the use of an asset, an entity shall consider only rights to make decisions about the use of the asset during the period of use unless the lessee designed the asset (or specific aspects of the asset) in accordance with paragraph 10.b.i.(b). Consequently, unless that condition exists, an entity shall not consider decisions that are predetermined before the period of use. For example, if a lessee is able only to specify the output of an asset before the period of use, the lessee does not have the right to direct the use of that asset. The ability to specify the output in a contract before the period of use, without any other decision-making rights relating to the use of the asset, gives a lessee the same rights as any lessee that purchases goods or services.

iv. A contract may include terms and conditions designed to protect the lessor's interest in the asset or other assets, to protect its personnel, or to ensure the lessor's compliance with laws or regulations. These are examples of protective rights. For example, a contract may specify the maximum amount of use of an asset or limit where or when the lessee can use the asset, may require a lessee to follow particular operating practices, or may require a lessee to inform the lessor of changes in how an asset will be used. Protective rights typically define the scope of the lessee's right of use but do not, in isolation, prevent the lessee from having the right to direct the use of an asset.

v. A lessee has the right to direct how and for what purpose an asset is used throughout the period of use if, within the scope of its right of use defined in the contract, it can change how and for what purpose the asset is used throughout that period. In making this assessment, an entity considers the decision-making rights that are most relevant to changing how and for what purpose an asset is used throughout the period of use. Decision-making rights are relevant when they affect the economic benefits to be derived from use. The decision-making rights that are most relevant are likely to be different for different contracts, depending on the nature of the asset and the terms and conditions of the contract.

11. An entity shall reassess whether a contract is or contains a lease only if the terms and conditions of the contract are changed.

Separating Components of a Contract

12. An entity shall identify the separate lease components within the contract. An entity shall consider the right to use an underlying asset to be a separate lease component (that is, separate from any other lease components of the contract) if both of the following criteria are met:

a. The lessee can benefit from the right of use either on its own or together with other resources that are readily available to the lessee. Readily available resources are goods or services that are sold or leased separately (by the lessor or other lessors) or resources that the lessee already has obtained (from the lessor or from other transactions or events).

b. The right of use is neither highly dependent on nor highly interrelated with the other right(s) to use underlying assets in the contract. A lessee's right to use an underlying asset is highly dependent on or highly interrelated with another right to use an underlying asset if each right of use significantly affects the other.

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13. The consideration in the contract shall be allocated to each separate lease component and nonlease component of the contract. Components of a contract include only those items or activities that transfer a good or service to the lessee.

14. An entity shall account for each separate lease component separately from the nonlease components of the contract. Nonlease components are not within the scope of this statement and shall be accounted for in accordance with the statutory accounting guidance applicable to the nonlease component.

15. An entity shall combine two or more contracts, at least one of which is or contains a lease, entered into at or near the same time with the same counterparty (or related parties) and consider the contracts as a single transaction if any of the following criteria are met:

a. The contracts are negotiated as a package with the same commercial objective(s).

b. The amount of consideration to be paid in one contract depends on the price or performance of the other contract.

c. The rights to use underlying assets conveyed in the contracts are a single lease component.

16. As a practical expedient, when nonlease components are an insignificant part of a lease agreement, a lessee and a lessor may, as an accounting policy election by class of underlying asset, choose not to separate nonlease components from lease components and instead to account for each separate lease component and the nonlease components associated with that lease component as a single lease component. The nonlease components must be closely related to the elements of the lease to be recognized as a single lease component. For lease agreements between related parties, lease and nonlease components must be separated.

Modification

17. An entity shall account for a modification to a contract as a separate contract (that is, separate from the original contract) when both of the following conditions are present:

a. The modification grants the lessee an additional right of use not included in the original lease (for example, the right to use an additional asset).

b. The lease payments increase commensurate with the standalone price for the additional right of use, adjusted for the circumstances of the particular contract. For example, the standalone price for the lease of one floor of an office building in which the lessee already leases other floors in that building may be different from the standalone price of a similar floor in a different office building, because it was not necessary for a lessor to incur costs that it would have incurred for a new lessee.

18. An entity shall account for initial direct costs, lease incentives and any other payments made to or by the entity in connection with a modification to a lease in the same manner as those items would be accounted for in connection with a new lease.

Accounting and Reporting by Lessees

19. All leases shall be considered operating leases, which means that rental expense is recognized over the lease term, without recognition of a right-to-use asset or lease liability. Rent on operating leases, reflecting all lease considerations in paragraph 20, shall be charged to expense on a straight-line basis over the lease term. Statutory accounting rejects the recognition of a right-to-use lease asset and the associated lease liabilities.

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20. The consideration in the contract for a lessee includes all of the following payments that will be made during the lease term:

a. Any fixed payments (for example, monthly service charges) or in substance fixed payments, less any incentives paid or payable to the lessee.

b. Any other variable payments that depend on an index or a rate, initially measured using the index or rate at the commencement date.

21. A lessee should recognize contingent rental expense (in annual periods as well as in interim periods) prior to the achievement of the specified target that triggers the contingent rental expense, provided that achievement of that target is considered probable. Previously recorded rental expense should be reversed into income at such time that it is probable that the specified target will not be met.

22. For the early termination or non-use of leased property, plant or equipment benefits, the lessee shall recognize liabilities, initially measured at fair value. Liabilities for costs to terminate a contract before the end of its term shall be recognized when the entity terminates the contract in accordance with the contract terms (i.e., gives written notice of termination or negotiated termination with the lessor).

23. Liabilities for costs that will continue to be incurred under a contract for its remaining term without economic benefit shall be recognized as the cease-date (the date the entity ceases using the right conveyed by the contract – i.e., the right to use a leased property). The fair value of the liability at the cease-use date shall be determined based on the remaining lease rentals, adjusted for the effects of any prepaid or deferred items recognized under the lease, and reduced by estimated sublease rentals that could be reasonably obtained for the property, even if the entity does not intend to enter into a sublease. Remaining lease rentals shall not be reduced to an amount less than zero.

24. An entity shall determine the lease term as the noncancellable period of the lease, together with all of the following:

a. Periods covered by an option to extend the lease if the lessee is reasonably certain to exercise that option.

b. Periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option.

c. Periods covered by an option to extend (or not to terminate) the lease in which exercise of the option is controlled by the lessor.

25. A lessee shall reassess the lease term or a lessee option to purchase the underlying asset only if and at the point in time that any of the following occurs:

a. There is a significant event or a significant change in circumstances that is within the control of the lessee that directly affects whether the lessee is reasonably certain to exercise or not to exercise an option to extend or terminate the lease or to purchase the underlying asset.

b. There is an event that is written into the contract that obliges the lessee to exercise (or not to exercise) an option to extend or terminate the lease.

c. The lessee elects to exercise an option even though the entity had previously determined that the lessee was not reasonably certain to do so.

d. The lessee elects not to exercise an option even though the entity had previously determined that the lessee was reasonably certain to do so.

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26. At the commencement date, an entity shall include the periods described in paragraph 24 in the lease term having considered all relevant factors that create an economic incentive for the lessee (that is, contract-based, asset-based, entity-based and market-based factors). Those factors shall be considered together, and the existence of any one factor does not necessarily signify that a lessee is reasonably certain to exercise or not to exercise an option.

27. Maintenance costs incurred by the lessee for maintenance on the leased item that do not increase the value and enhance the usefulness of the leased asset shall be expensed when incurred pursuant to *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*. Reimbursable deposits shall be reflected as nonadmitted assets. Deposits paid to the lessor, reimbursable when the lessee incurs costs for lease maintenance activities, shall be recorded as nonadmitted assets. When the amount on deposit is less than probable of being returned, the deposit shall be recognized as an additional lease expense.

Accounting and Reporting by Lessors

28. The definition of property, plant and equipment for lessors is defined in paragraph 3 and is the same as for lessees. All leases, except leveraged leases as defined in paragraph 42, shall be considered operating leases and accounted for by the lessor as follows:

a. The leased property, plant or equipment shall be included in the same balance sheet category it would be had the property, plant or equipment not been leased. The property, plant or equipment shall be depreciated following the lessor's normal depreciation policies for such assets;

b. Rental income shall be reported as investment income as it becomes receivable according to the provisions of the lease. Rentals may be recognized before they become due, if rentals vary from the straight-line basis. The guidance in *SSAP No. 34—Investment Income Due and Accrued* shall be applied to the receivable balance; and

c. Initial direct costs shall be charged to expense when incurred and shall not be deferred and allocated over the lease term. Initial direct costs are those incremental costs that the lessor has incurred in directly evaluating, negotiating, administering and closing a lease transaction.

29. If the terms of a variable payment amount other than those in paragraph 20.b. relate to a lease component, even partially, the lessor shall not recognize those payments before the changes in facts and circumstances on which the variable payment is based occur (for example, when the lessee's sales on which the amount of the variable payment depends occur). When the changes in facts and circumstances on which the variable payment is based occur, the lessor shall allocate those payments to the lease and nonlease components of the contract.

30. Contingent rental income shall be recognized as revenue when the changes in the factor(s) on which the contingent lease payments is (are) based actually occur.

Sale-Leaseback Transactions

31. Sale-leaseback transactions involve the sale of property, plant or equipment by the owner and a lease of the property, plant or equipment back to the seller. Sale-leaseback accounting is a method of accounting in which the seller-lessee records the sale and removes all property, plant or equipment and related liabilities from its balance sheet. The definition of property, plant and equipment eligible for sale-leaseback treatment is in paragraph 3. As noted in paragraph 3, non-depreciable assets, including investments and premium receivables, do not meet the definition of property, plant or equipment, are not allowed to be included in lease transactions, and therefore, are not allowed to be included in sale-leaseback transactions. Assets that do not meet the definition of property, plant and equipment in

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paragraph 3 may only be used in sale-leaseback transactions as permitted practices with regulatory approval.

32. A sale of property, plant or equipment that is accompanied by a leaseback of all or any part of the property, plant or equipment for all or part of its remaining economic life shall be accounted for by the buyer-lessor and seller-lessee as a purchase and operating lease and a sale and an operating lease, respectively, unless the sale-leaseback includes sale of nonadmitted assets to a related party. If the transaction involves a sale of nonadmitted assets to a related party, the transaction shall be accounted for by the deposit method detailed in paragraph 37.

33. Sale-leaseback accounting shall be used by a seller-lessee only if a sale-leaseback transaction includes all of the following:

a. A normal leaseback is a lessee-lessor relationship that involves active use of the property by the seller-lessee in consideration for payment of rent, including contingent rentals that are based on future operations of the seller-lessee. The phrase active use of the property by the seller-lessee refers to use of the property during the lease term in the seller-lessee's trade or business, provided that subleasing of the leased property is minor.

b. Admitted assets, if the buyer-lessor is a related party, or either admitted or nonadmitted assets if the buyer-lessor is not a related party. For purposes of this paragraph, related parties include those identified in SSAP No. 25 and entities created for the purpose of buying and leasing nonadmitted assets for the reporting entity and/or its affiliates.

34. Under sale-leaseback accounting, any profit on the sale shall be deferred and amortized in proportion to the related gross rental charged to expense over the lease term, with the exception of a sale of real estate settled entirely in cash.

35. A sale of real estate, settled entirely in cash, that is accompanied by a leaseback of all or any part of the property, plant or equipment for all or part of its remaining economic life shall be accounted for by the buyer-lessor and seller-lessee as a purchase and operating lease and a sale and an operating lease, respectively. The sale and gain shall be recognized directly to special surplus funds and subsequently amortized to unassigned funds (surplus) over the lease term.

Deposit Method and Financing Method

36. The deposit method is used when the transaction involves a sale-leaseback of nonadmitted assets to a related party. To the extent that leases between related parties are, in substance, arms-length transactions the guidance in this statement shall be applied. The determination of whether related party leases qualify as arms-length transactions is addressed in SSAP No. 25.

37. If a sale-leaseback transaction is accounted for by the deposit method, lease payments decrease and collections on the buyer-lessor's note, if any, increase the seller-lessee's deposit account. The sale-leaseback assets identified in paragraph 31 and any related debt continue to be included in the seller-lessee's balance sheet, and the seller-lessee continues to depreciate the sale-leaseback assets. A seller-lessee that is accounting for any transaction by the deposit method shall recognize a loss if at any time the net carrying amount of the sale-leaseback assets exceeds the sum of the balance in the deposit account, the fair value of the unrecorded note receivable and any debt assumed by the buyer.

38. If a sale-leaseback transaction is accounted for by the deposit method and then subsequently qualifies for sales recognition under paragraph 33, the transaction is accounted for using sale-leaseback accounting, and the gain or loss is recognized in accordance with the provisions of paragraph 34 of this statement. In addition, the leaseback is classified and accounted for in accordance with this statement as if the sale had been recognized at the inception of the lease. The change in the related lease accounts that would have been recorded from the inception of the lease had the transaction initially qualified for sale-

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leaseback accounting is included in computing the gain or loss recognized in accordance with paragraph 34 of this statement.

39. A sale-leaseback transaction that does not qualify for sale-leaseback accounting nor the deposit method shall be accounted for by the financing method. Under this method the seller-lessee shall not derecognize the transferred asset and shall account for any amounts received as a financial liability and the buyer-lessor shall not recognize the transferred asset and shall account for the amounts paid as a receivable.

40. If a sale-leaseback transaction is reported as under the financing method, lease payments, exclusive of an interest portion, decrease and collections on the buyer-lessor's note increase the seller-lessee's liability account with a portion of the lease payments being recognized under the interest method. The seller-lessee reports the sales proceeds as a liability, continues to report the sale-leaseback assets identified in paragraph 31 as an asset and continues to depreciate the sale-leaseback assets.

41. If a sale-leaseback transaction accounted for under the financing method subsequently qualifies under paragraph 33, the transaction is then recorded using sale-leaseback accounting, and the cumulative change in the related balance sheet accounts is included in the computation of the gain recognized in accordance with the provisions of paragraph 34 of this statement. In addition, the leaseback is classified and accounted for as an operating lease as if the sale had been recognized at the inception of the lease. The change in the related lease accounts from the inception of the lease to the date the sale is recognized is included in the gain recognized in accordance with paragraph 34 of this statement.

Leveraged Leases for Lessors

42. A lessor shall record its investment in a leveraged lease. Generally, leveraged leases are those in which the lessor acquires, through the incurrence of debt (such that the lessor is substantially “leveraged” in the transaction), property, plant or equipment with the intentions to lease the asset(s) to the lessee. The net of the balances of the following accounts as measured in accordance with this guidance shall represent the lessor’s initial and continuing investment in leveraged leases:

a. Rentals receivable

b. Investment-tax-credit receivable

c. Estimated residual value of the leased asset

d. Unearned and deferred income.

43. A lessor shall initially measure its investment in a leveraged lease net of the nonrecourse debt. The net of the balances of the following accounts shall represent the initial and continuing investment in leveraged leases:

a. Rentals receivable, net of that portion of the rental applicable to principal and interest on the nonrecourse debt.

b. A receivable for the amount of the investment tax credit to be realized on the transaction.

c. The estimated residual value of the leased asset. The estimated residual value shall not exceed the amount estimated at lease inception except if the lease agreement includes a provision to escalate minimum lease payments either for increases in construction or acquisition cost of the leased property, plant or equipment or for increases in some other measure of cost or value (such as general price levels) during the construction or preacquisition period. In that case, the effect of any increases that have occurred shall be

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considered in the determination of the estimated residual value of the underlying asset at lease inception.

d. Unearned and deferred income consisting of both of the following:

i. The estimated pretax lease income (or loss), after deducting initial direct costs, remaining to be allocated to income over the lease term.

ii. The investment tax credit remaining to be allocated to income over the lease term.

44. The investment in leveraged leases minus deferred taxes arising from differences between pretax accounting income and taxable income shall represent the lessor's net investment in leveraged leases for purposes of computing periodic net income from the leveraged lease. Given the original investment and using the projected cash receipts and disbursements over the term of the lease, the rate of return on the net investment in the years in which it is positive shall be computed. The rate is that rate that, when applied to the net investment in the years in which the net investment is positive, will distribute the net income to those years and is distinct from the interest rate implicit in the lease. In each year, whether positive or not, the difference between the net cash flow and the amount of income recognized, if any, shall serve to increase or reduce the net investment balance. The use of the term years is not intended to preclude application of the accounting prescribed in this paragraph to shorter accounting periods.

45. The pretax lease income (or loss) and investment tax credit elements shall be allocated in proportionate amounts from the unearned and deferred income included in the lessor's net investment. The tax effect of the pretax lease income (or loss) recognized shall be reflected in tax expense for the year. The tax effect of the difference between pretax accounting income (or loss) and taxable income (or loss) for the year shall be charged or credited to deferred taxes.

46. If, at any time during the lease term the application of the method prescribed in this section would result in a loss being allocated to future years, that loss shall be recognized immediately. This situation might arise in circumstances in which one of the important assumptions affecting net income is revised.

47. The projected timing of income tax cash flows generated by the leveraged lease is an important assumption and shall be reviewed annually, or more frequently, if events or changes in circumstances indicate that a change in timing has occurred or is projected to occur. The income effect of a change in the income tax rate shall be recognized in the first accounting period ending on or after the date on which the legislation effecting a rate change becomes law.

48. The lessor shall record its investment net of the nonrecourse debt. In cases where the asset being leased is a nonadmitted asset, any net leveraged lease asset shall be nonadmitted. However, leveraged leases involving commercial airplanes are admitted assets.

Disclosures

49. The following disclosures shall be made in the financial statements of lessees:

a. A general description of the lessee's leasing arrangements including, but not limited to, the following:

i. Rental expense for each period for which an income statement is presented, with separate amounts for minimum rentals, contingent rentals, and sublease rentals. Rental payments under leases with terms of a month or less that were not renewed need not be included;

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ii. The basis on which contingent rental payments are determined;

iii. The existence and terms of renewal or purchase options and escalation clauses; and

iv. Restrictions imposed by lease agreements, such as those concerning dividends, additional debt and further leasing;

v. Identification of lease agreements that have been terminated early or for which the lessee is no longer using the leased property, plant or equipment benefits, and the liability recognized in the financial statements under these agreements.

b. For leases having initial or remaining lease terms in excess of one year:

i. Future minimum rental payments required as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding years; and

ii. The total of minimum rentals to be received in the future under noncancelable subleases as of the date of the latest balance sheet presented.

c. For sale-leaseback transactions:

i. A description of the terms of the sale-leaseback transaction, including future commitments or obligations; and

ii. For those accounted for as deposits, (a) the obligation for future minimum lease payments as of the date of the latest balance sheet presented in the aggregate and for each of the five succeeding years and (b) the total of minimum sublease rentals, if any, to be received in the future under noncancelable subleases in the aggregate and for each of the five succeeding years.

iii. For those accounted for using the financing method, it is required to disclose the information in i. as well as the financing obligation and lease liabilities.

50. When leasing is a significant part of the lessor's business activities in terms of revenue, net income, or assets, the following information with respect to leases shall be disclosed in the financial statements:

a. For operating leases:

i. The cost and carrying amount, if different, of property, plant or equipment on lease or held for leasing by major classes of property, plant or equipment according to nature or function, and the amount of accumulated depreciation in total as of the date of the latest balance sheet presented;

ii. Minimum future rentals on noncancelable leases as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding years;

iii. Total contingent rentals included in income for each period for which an income statement is presented; and

iv. A general description of the lessor's leasing arrangements.

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b. For leveraged leases:

i. A description of the terms including the pretax income from the leveraged leases. For purposes of presenting the investment in a leveraged lease in the lessor's balance sheet, the amount of related deferred taxes shall be presented separately (from the remainder of the net investment);

ii. Separate presentation (from each other) shall be made of pretax income from the leveraged lease, the tax effect of pretax income, and the amount of investment tax credit recognized as income during the period; and

iii. When leveraged leasing is a significant part of the lessor's business activities in terms of revenue, net income, or assets, the components of the net investment balance in leveraged leases shall be disclosed.

51. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

52. This statement rejects *ASU 2016-02, Leases*. For statutory accounting, leases are treated as operating leases for lessees and rejects the treatment as financing leases specified in 842-10-25 and rejects the recognition of the right to use assets and related liabilities. For statutory accounting, specific guidance is adopted on sale leaseback transactions, specific guidance from lessors, leveraged leases from sections 842-40 and 842-50, respectively. The financing method is rejected for statutory accounting but adopted for instances where a sale-leaseback transaction fails sale accounting. The guidance within *INT 02-15: EITF 00-11: Lessors' Evaluation of Whether Leases of Certain Integral Equipment Meet the Ownership Transfer Requirements of FASB Statement 13* applied to leases with inception between January 1, 2003 and January 1, 2020. With adoption of substantive revisions to SSAP No. 22R this guidance is nullified.

a. Accounting Standards Codification (ASC) 420-10-25 paragraphs 11-13 and ASC 420-10-30 paragraph 8 regarding the recognition of costs to terminate an operating lease before the end of the term and costs that will continue to be incurred under the contract for its remaining term without economic benefit are adopted. Other provisions of ASC 420 are rejected in *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items*.

b. *ASU 2014-05, Service Concession Arrangements* (Adopted with modification to only exclude service concession arrangements from the lease definition.)

c. *ASU 2017-10, Determining the Customer of the Operation Services* (Adopted with modification to clarify the customer in the previously adopted service concession arrangement definition.)

d. *ASU 2018-01, Land Easement Practical Expedient for Transition to Topic 842* (Rejected in its entirety.)

e. *ASU 2018-10, Codification Improvements to Topic 842, Leases* (Rejected in its entirety.)

f. *ASU 2018-11, Leases (Topic 842), Targeted Improvements* (Rejected in its entirety.)

g. *ASU 2018-20, Leases (Topic 842), Narrow-Scope Improvements for Lessors* (Rejected for statutory accounting, except for paragraph 842-10-15-(40-42) as it was modified by ASU 2018-20.)

h. *ASU 2019-01, Leases (Topic 842), Codification Improvements* (Rejected in its entirety.)

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i. *ASU 2021-05, Leases (Topic 842), Lessors—Certain Leases with Variable Lease Payments* (Rejected in its entirety.)

j. *ASU 2021-09, Leases (Topic 842), Discount Rate for Lessees That Are Not Public Business Entities* (Rejected in its entirety.)

53. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~53.~~54. This statement is effective for years beginning January 1, 2001. The substantive revisions documented in *Issue Paper No. 161—Leases* are effective for all new leases entered into, and for existing leases reassessed due to a change in terms and conditions under paragraph 11, on or after January 1, 2020. Earlier adoption is permitted. The guidance in paragraph 34 regarding commercial airplanes was originally contained within *INT 00-02: Accounting for Leveraged Leases Involving Commercial Airplanes Under SSAP No. 22—Leases* and was effective March 13, 2000. The guidance in paragraph 5 was originally contained within *INT 04-20: EITF 01-8: Determining Whether an Arrangement Contains a Lease* and was effective March 13, 2005. Guidance in paragraph 27 related to maintenance costs incurred by lessee was previously included within *INT 09-05: EITF 08-3: Accounting by Lessees for Maintenance Deposits* and was effective for periods beginning September 21, 2009. The guidance in paragraphs 17 and 18 was originally contained within *INT 00-27: EITF 98-9: Accounting for Contingent Rent* and was effective September 11, 2000.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 22—Leases*
- *Issue Paper No. 161—Leases*

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Statement of Statutory Accounting Principles No. 23

Foreign Currency Transactions and Translations

STATUS

Type of Issue..... Common Area
Issued ..... Initial Draft
Effective Date ..... January 1, 2001
Affects..... No other pronouncements
Affected by..... No other pronouncements
Interpreted by..... No other pronouncements
Relevant Appendix A Guidance ..... None

STATUS **1**
SCOPE OF STATEMENT **1**
SUMMARY CONCLUSION **1**
Relevant Literature 3
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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for accounting for foreign currency transactions and translations.

SUMMARY CONCLUSION

2. A foreign currency transaction is a transaction denominated in a currency other than the reporting entity's functional currency. The reporting entity's functional currency is defined as the currency of the primary economic environment in which the reporting entity operates. Foreign currency translation is the translation of financial statements, denominated in the reporting entity's functional currency, into U.S. dollars prior to their incorporation into financial statements through consolidation or the equity method of accounting.

3. For the purposes of this statement, a U.S. domiciled reporting entity's reporting currency shall be defined as the U.S. dollar, regardless of the primary economic environment in which the reporting entity operates. In order to ensure consistency, all elements of statutory financial statements shall be reported in U.S. dollars.

4. Each foreign currency transaction shall be examined and a determination made if the foreign currency transaction was made in support of insurance operations denominated in the same foreign currency. For example, some reporting entities engage in insurance operations in foreign countries with the premiums collected and claims paid in local currency. As in any insurance operation there will at times be uncollected premiums, policy reserves, unpaid claims, and other incomplete transactions that

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must be recorded in the reporting entity's balance sheet. Premiums, reserves, and claims normally are recorded in U.S. dollars at the rate of exchange that is in effect at the time the policy is written, or when the claim is incurred. Changes in exchange rates, while not affecting the foreign policyholder, do affect the value of the foreign business as it is recorded in U.S. dollars.

5. Foreign currency transactions made in support of insurance operations denominated in the same foreign currency, such as foreign branches, shall be accounted for as follows:

a. Canadian Insurance Operations—Canadian insurance operations, resulting in less than 10% of the reporting entity's admitted assets, less than 10% of the reporting entity's liabilities and less than 10% of the reporting entity's net premium, can be translated to U.S. dollars by making an adjustment to the net assets of the foreign operation. The adjustment is calculated by summarizing the assets and liabilities in the foreign currency and in U.S. dollars. The net value is converted to U.S. dollars at the current rate of exchange and compared with the net value in U.S. dollars recorded by the reporting entity. Any difference in the net value to current exchange rates is recorded as a separate asset or liability and the change in the foreign exchange adjustment is recorded as an unrealized capital gain or loss. If a reporting entity does not meet the requirements of this paragraph or elects to translate each financial statement line item, the reporting entity shall follow the accounting in paragraph 5.b. of this statement;

b. All Other Foreign Insurance Operations—All other foreign insurance operations must be translated to U.S. dollars as follows: each financial statement line shall be translated to U.S. dollars by applying the following exchange rates: (i) for assets and liabilities, the exchange rate at the balance sheet date shall be used and (ii) for revenues, expenses, gains, losses and surplus adjustments, the exchange rate at the dates on which those elements are recognized shall be used. Because translation at the exchange rates at the dates the numerous revenues, expenses, gains, losses and surplus adjustments are recognized is generally impractical, an appropriately weighted average exchange rate for the period may be used to translate those elements. Gains or losses due to translating foreign operations to U.S. dollars shall be recorded as unrealized capital gains or losses.

6. All other foreign currency transactions shall be accounted for as follows:

a. Assets and liabilities denominated in foreign currencies shall be accounted for at their U.S. dollar equivalent values using exchange rates at the balance sheet date. Income and expenses recognized during an accounting period shall be recorded at an appropriately weighted average exchange rate;

b. Changes in balance sheet asset and liability values due to fluctuations in foreign currency exchange rates shall be recorded as unrealized capital gains and losses until the asset is sold or exchanged or the liability is settled. Additionally, in situations in which the reporting entity has an investment in a foreign entity (such as an investment in a joint venture under *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* or an investment in subsidiary under *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*), the parent reporting entity shall realize foreign currency translation changes when the parent loses control of the foreign entity, the parent entity derecognizes the entire equity method investment, or the parent entity acquires control in a foreign entity when the parent previously only held a noncontrolling interest (step acquisition). Upon partial sale or acquisition of control of a foreign entity, the parent reporting entity shall realize a pro-rata share of foreign currency translation changes. Upon settlement, or the situations previously described, all previously recorded unrealized capital gains and losses shall be reversed and the foreign exchange profit or loss for the entire holding period shall be recorded as a realized capital gain or loss.

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When a foreign entity investee is substantially liquidated, the entire unrealized foreign currency translation balance is to be realized;

c. Transactions involving settlement in cash, such as purchases, payment of expenses, sales, and receipt of income, shall be recorded at their U.S. dollar equivalent value based on the foreign currency exchange rate as of the transaction date. Any foreign currency exchange gains or losses on purchases, payment of expenses, sales, maturities or changes in income or expense accruals shall be recorded as a capital gain or loss realized on the purchase, sale or maturity.

7. Nominal information such as par value of investments may be expressed in the foreign currency or U.S. dollar equivalent (description of issue), but where the information is displayed comparatively (column of par values), U.S. dollar equivalent amount shall be used. The U.S. dollar equivalent amount is translated utilizing the exchange rate at the balance sheet date. Ratios and factors shall be based on data that is entirely consistent with respect to currency.

8. A currency in a highly inflationary environment (one that has cumulative inflation of approximately 100% or more over a three year period) is not considered stable enough to serve as a functional currency and the more stable currency of the reporting parent is to be used instead. If a reporting entity's books of record are not maintained in its functional currency, remeasurement into the functional currency is required. That remeasurement is required before translation into the reporting currency. The remeasurement process is intended to produce the same result as if the reporting entity's books of record had been maintained in the functional currency. The remeasurement of and subsequent accounting for transactions denominated in a currency other than the functional currency shall be recognized as a realized gain or loss in the statement of operations.

Relevant Literature

9. This statement adopts, with modification, *ASU 2013-05, Parents Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity.* Modifications within this statement reflect the statutory accounting definition of controlling interest, as specified in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* and *SSAP No. 25—Affiliates and Other Related Parties*, as well as the reporting specified in this statement.

10. This statement rejects *FASB Statement No. 52, Foreign Currency Translation*, *FASB Emerging Issues Task Force No. 87-12, Foreign Debt-for-Equity Swaps, FASB Emerging Issues Task Force No. 87-26, Hedging of Foreign Currency Exposure with a Tandem Currency, FASB Emerging Issues Task Force No. 92-4, Accounting for a Change in Functional Currency When an Economy Ceases to Be Considered Highly Inflationary, FASB Emerging Issues Task Force No. 95-2, Determination of What Constitutes a Firm Commitment for Foreign Currency Transactions Not Involving a Third Party, FASB Emerging Issues Task Force No. 96-15, Accounting for the Effects of Changes in Foreign Currency Exchange Rates on Foreign-Currency-Denominated Available-for-Sale Debt Securities* and *FASB Interpretation No. 37, Accounting for Translation Adjustments upon Sale of Part of an Investment in a Foreign Entity, an interpretation of FASB Statement No. 52*, and *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins*, Chapter 12.

Effective Date and Transition

11. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 81—Foreign Currency Transactions and Translations*

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Statement of Statutory Accounting Principles No. 24

Discontinued Operations and Unusual or Infrequent Items

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 02-17
Affected by	No other pronouncements
Interpreted by	INT 08-05
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles related to the accounting and reporting for discontinued operations and unusual or infrequently occurring items.

SUMMARY CONCLUSION

Identification of Discontinued Operations

2. A disposal of a component[1] shall be considered a discontinued operation if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results when any situation detailed in paragraphs 2.a. through 2.c. occurs. Examples of a strategic shift include a disposal of a major geographical area, major line of business, a major equity method investment or other major parts of the entity.

[1] A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. A component of an entity may be a reportable segment or an operating segment, a reporting unit, a subsidiary or an asset group. For purposes of this statement, reference to a component also includes "groups of components."

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a. The entity to be sold[2] meets all of the following criteria to be classified as held for sale:

i. Management, having the authority to approve the transaction, commits to a plan to sell;

ii. The entity to be sold is available for immediate sale in its present condition subject only to terms that are usual and customary;

iii. An active program to locate a buyer and other actions to complete the sale have been initiated;

iv. The sale and transfer is expected to qualify as a completed sale within one year unless the qualifying exceptions in paragraph 4 are noted;

v. The entity to be sold is being actively marketed for sale at a price that is reasonable in relation to its current fair value; and

vi. Actions required to complete the plan to sell indicate that it is unlikely that significant changes will be made to the plan or that the plan will be withdrawn.

b. The component is disposed of by sale.

c. The component is disposed of other than by sale (for example, by abandonment, in an exchange measured based on the recorded amount of the nonmonetary asset relinquished, or in a distribution to owners in a spinoff)(INT 08-05).

3. A business or nonprofit activity that, on acquisition, meets the criteria of paragraph 2.a. is a discontinued operation.

4. Events or circumstances beyond an entity's control may extend the period required to complete the sale of an entity to be sold beyond one year. An exception to the one-year requirement in paragraph 2.a.iv. shall apply in the following situations in which those events or circumstances arise:

a. If at the date that an entity commits to a plan to sell an entity to be sold, the entity reasonably expects that others (not a buyer) will impose conditions on the transfer of the entity to be sold that will extend the period required to complete the sale and both of the following conditions are met:

i. Actions necessary to respond to those conditions cannot be initiated until after a firm purchase commitment is obtained; and

ii. A firm purchase commitment is probable within one year.

b. If an entity obtains a firm purchase commitment and, as a result, a buyer or others unexpectedly impose conditions on the transfer of an entity to be sold previously classified as held for sale that will extend the period required to complete the sale and both of the following conditions are met:

i. Actions necessary to respond to the conditions have been or will be timely initiated; and

ii. A favorable resolution of the delaying factors is expected.

[2] A component, group of components or a business or nonprofit activity subject to this statement are collectively referred to as "the entity to be sold."

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c. If during the initial one-year period circumstances arise that previously were considered unlikely and, as a result, an entity to be sold previously classified as held for sale is not sold by the end of that period and all of the following conditions are met:

i. During the initial one-year period the entity initiated actions necessary to respond to the change in circumstances;

ii. The entity to be sold is being actively marketed at a price that is reasonable given the change in circumstances; and

iii. The criteria in paragraph 2.a. are met.

Measurement and Reporting of Discontinued Operations

5. Upon classification as held for sale[3] (paragraph 2.a.), the entity to be sold shall be measured and reported at the lower of its carrying value or fair value less costs to sell. Costs to sell are incremental direct costs to transact a sale. These costs include broker commissions, legal and title transfer fees and closing costs that must be incurred before legal title can be transferred. These costs exclude expected future losses associated with the operations of the entity to be sold while it is classified as held for sale. The calculation of fair value less costs to sell shall be updated each period until the disposal transaction occurs, but only additional losses shall be recognized. Entities are not permitted to recognize recoveries as a result of improvements in fair value or costs to sell. Depreciation or amortization shall no longer be recognized once an asset is classified as held for sale.

6. A realized loss shall be recognized for any initial or subsequent write-down to fair value less costs to sell. If a component is disposed of without being classified as held for sale, a realized loss shall be recognized in the period of the disposal. Regardless if an entity is classified as held for sale, a gain shall not be recognized until the disposal transaction is complete.

7. The results of a reporting entity's discontinued operations shall be reported consistently with the entity's reporting of continuing operations (i.e., no separate line item presentation in the balance sheet or statement of operations aggregating current and future losses from the measurement date).

8. If the entity decides not to sell the discontinued operation, the assets shall be reported at the lower of the carrying amount before the asset was classified as held for sale, adjusted for depreciation that would have been recognized if the asset had not been classified as held for sale, or fair value at the date of the decision not to sell.

Unusual or Infrequently Occurring Items

9. A material event or transaction that an entity considers to be of an unusual nature or of a type that indicates infrequency of occurrence or both shall be reported consistently with the reporting entity's reporting of continuing operations (i.e., no separate line item presentation in the balance sheet or statement of operations). Such items shall not be charged directly to surplus unless specifically addressed elsewhere within the *Accounting Practices and Procedures Manual*.

a. "Unusual Nature" shall be defined as the underlying event or transaction that should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity, taking into account the environment in which the entity operates.

[3] Pursuant to *SSAP No. 90—Impairment or Disposal of Real Estate Investments*, paragraph 21, real estate investments are classified as held for sale under the same criteria identified in paragraph 2.a. These real estate investments are not considered discontinued operations and shall follow the guidelines in SSAP No. 90.

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b. "Infrequency of Occurrence" is defined as the underlying event or transaction that would not reasonably be expected to recur in the foreseeable future, taking into account the environment in which the entity operates.

Business Interruption Insurance Recoveries

10. Business interruption (BI) insurance is designed to protect the prospective earnings or profits of the insured entity. That is, BI insurance provides coverage if business operations are suspended due to the loss of use of property and equipment resulting from a covered cause of loss. BI insurance coverage generally provides for reimbursement of certain costs and losses incurred during the reasonable period required to rebuild, repair, or replace the damaged property. The types of costs and losses covered typically include:

a. Gross margin that was "lost" or not earned due to the suspension of normal operations

b. A portion of fixed charges and expenses in relation to that lost gross margin

c. Other expenses incurred to reduce the loss from business interruption (for example, rent of temporary facilities and equipment, use of subcontractors, and so forth)

An entity may choose how to classify BI insurance recoveries in the statement of operations, as long as that classification is not contrary to existing statutory accounting principles.

Disclosures

Discontinued Operations

11. The following shall be disclosed in the notes to the financial statements that cover the period in which a discontinued operation either has been disposed of or is classified as held for sale under paragraph 2.a.:

a. Description of the facts and circumstances leading to the disposal or expected disposal and a description of the expected manner and timing of that disposal.

b. The loss recognized on the discontinued operation. The recognized loss shall be reported for the reporting period, and as a cumulative total since classified as held for sale.

c. The carrying amount immediately prior to the classification as held for sale, and the current fair value less costs to sell, including the balance sheet lines where the item is reported. Also report income received from the discontinued operation prior to the disposal transaction.

12. If the entity decides to change its plan of sale for the discontinued operation, disclose a description of the facts and circumstances leading to the decision to change the plan and the effect on the assets reported in the financial statements.

13. Adjustments to amounts reported related to discontinued operations as a result of:

a. The resolution of contingencies that arise pursuant to the terms of the disposal transaction, such as the resolution of purchase price contingencies and indemnification issues with the purchaser.

b. The resolution of contingencies that arise from and are directly related to the disposal of a discontinued operation of the component in a period prior to its disposal, such as environmental and product warranty obligations retained by the seller.

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c. The settlement of employee benefit plan obligations (pension, postemployment benefits other than pensions, and other postemployment benefits), provided the settlement is directly related to the disposal transaction. (A settlement is directly related to the disposal transaction if there is a demonstrated direct cause-and-effect relationship and the settlement occurs no later than one year following the disposal transaction, unless it is delayed by events or circumstances beyond an entity's control.)

14. If the entity will retain significant continuing involvement with a discontinued operation after the disposal transaction, the entity shall complete the disclosures in paragraphs 14.a. through 14.c. Examples of significant continuing involvement include a supply and distribution arrangement, a financial guarantee, an option to repurchase and an equity method investment in the discontinued operation.

a. Description of the activities that give rise to the continuing involvement.

b. The period of time the involvement is expected to continue.

c. The expected cash inflows/outflows as a result of continuing involvement.

15. If the entity will retain an equity interest in the discontinued operations after the disposal date, disclose the ownership interest before and after the disposal transaction and the entity's share of the income or loss of the investee as of the year-end reporting date after the disposal transaction.

Unusual/Infrequent Items

16. The nature, including a general description of the transactions, and financial effects of each unusual or infrequent event or transaction shall be disclosed in the notes to the financial statements. Gains or losses of a similar nature that are not individually material shall be aggregated. This disclosure shall include the line items which have been affected by the event or transaction considered to be unusual and/or infrequent. If the unusual or infrequent item is as the result of government assistance, ~~(as defined in *ASU 2021-10, Government Assistance, Disclosures by Business Entities about Government Assistance)*~~ disclosure shall additionally include the form in which the assistance has been received (for example, cash or other assets), and information regarding significant terms and conditions of the transaction, with items including, to the extent applicable, the duration or period of the agreement, and commitments made by the reporting entity, provisions for recapture, or other contingencies.

Business Interruption Insurance Recoveries

17. The following information should be disclosed in the notes to the financial statements in the period(s) in which BI insurance recoveries are recognized:

a. The nature of the event resulting in business interruption losses

b. The aggregate amount of BI insurance recoveries recognized during the period and the line item(s) in the statement of operations in which those recoveries are classified (including amounts defined as an extraordinary item pursuant to this SSAP).

18. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

19. This statement adopts with modification *ASU 2014-08, Presentation of Financial Statements and Property, Plant and Equipment— Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. Modifications from ASU 2014-08 include:

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a. This statement rejects guidance in ASU 2014-08 for separate reporting of discontinued operations. An entity's discontinued operations shall be reported consistently with the entity's reporting of continuing operations.

b. A gain from discontinued operations shall not be recognized until the disposal transaction is complete. Losses shall be recognized when discontinued operations are classified as held for sale, and are required in subsequent periods when the fair value less costs to sell is below the carrying value. Losses are not permitted to be adjusted for subsequent recoveries in fair value changes or improvements in the expected costs to sell.

c. This statement only adopts the ASU 2014-08 disclosures applicable for all types of discontinued operations, and only to the extent reflected in this statement. The detailed disclosures for discontinued operations for components or group of components and discontinued operations comprising an equity method investment are rejected and not required.

20. This statement adopts with modification *ASU 2015-01, Income Statement—Extraordinary and Unusual Items.* The statutory accounting modification to ASU 2015-01 requires reporting entities to report unusual or infrequent items consistently with other operations and prevents recognizing unusual or infrequent events or transactions as a separate component of operations. Additionally, disclosures of these transactions are required in the statutory financial statements. As ASU 2015-01 eliminated the concept of an "extraordinary item," the adoption of ASU 2015-01 nullifies the previous consideration of GAAP guidance related to this term.

21. This statement adopts with modification *Emerging Issues Task Force No. 01-13: Income Statement Display of Business Interruption Insurance Recoveries*, with changes of GAAP references to statutory terminology.

22. The following U.S. GAAP accounting principles were previously noted as adopted in this statement. However, upon the adoption with modification of ASU 2014-08 and ASU 2015-01, the following guidance is considered rejected for statutory accounting purposes:

a. *Accounting Principles Board Opinion No. 30*, *Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions,* (APB No. 30), paragraphs 13-18.

b. *AICPA Accounting Interpretations, Reporting the Results of Operations: Accounting Interpretations of APB Opinion No. 30*, relating to the definition of extraordinary items and terminology relevant to the disposal of a segment and the criteria for recording a related loss.

c. *FASB Emerging Issues Task Force No. 85-36, Discontinued Operations with Expected Gain and Interim Operating Losses.*

d. *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets* (FAS 144), paragraphs 44.a. – 44.c.

23. The following standards were rejected prior to the adoption with modification of ASU 2014-08 and ASU 2015-01 and are still noted as rejected for statutory accounting:

a. *FASB Statement No. 146, Accounting for Costs Associated with Exit or Disposal Activities*;

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b. *FASB Emerging Issues Task Force No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)*; and

c. *FASB Emerging Issues Task Force No. 95-18, Accounting and Reporting for a Discontinued Business Segment When the Measurement Date Occurs after the Balance Sheet Date but before the Issuance of Financial Statements.*

24. This statement ~~adopts~~rejects *ASU 2021-10, Government Assistance: Disclosure by Business Entities about Government Assistance*~~, with modification to require disclosure by all entity types~~. However, it does incorporate general disclosures about government assistance for all reporting entity types.

Effective Date and Transition

25. This statement was originally effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance in paragraphs 10 and 17 was originally contained in *INT 02-17: EITF 01-13: Income Statement Display of Business Interruption Insurance Recoveries* and was effective September 10, 2002.

26. Changes from the adoption with modification of ASU 2014-08 and ASU 2015-01 are not expected to change the measurement or reporting process for discontinued operations or unusual or infrequent items. As such, these changes are considered nonsubstantive and were effective immediately upon adoption on June 17, 2015.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 24—Discontinued Operations and Extraordinary Items*

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Statement of Statutory Accounting Principles No. 25

Affiliates and Other Related Parties

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 96 with guidance incorporated August 2011; Nullifies and incorporates INT 03-16
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-440

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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SCOPE OF STATEMENT

1. Related party transactions are subject to abuse because reporting entities may be induced to enter transactions that may not reflect economic realities or may not be fair and reasonable to the reporting entity or its policyholders. As such, related party transactions require specialized accounting rules and increased regulatory scrutiny. This statement establishes statutory accounting principles and disclosure requirements for related party transactions.

2. This statement shall be followed for all related party transactions, including transactions with parties that own 10% or more of the reporting entity, even if the transaction is also governed by other statutory accounting principles. Furthermore, this statement shall be followed in all transactions which involve unrelated parties as intermediaries between related parties. In determining whether a transaction is a related party transaction, consideration shall be given to the substance of the agreement and the parties whose actions or performance materially impact the insurance reporting entity under the transaction. For example, an investment acquired from a non-related intermediary in which the investment return is predominantly contingent on the performance of a related party shall be considered a related party investment. As a general principle, it is erroneous to conclude that the mere inclusion of a non-related intermediary eliminates the requirement to assess and properly identify the related party transaction in

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accordance with the provisions of this statement. It is also erroneous to conclude that the presence of non-related assets in a structure predominantly comprised of related party investments eliminates the requirement to assess and identify the investment transaction as a related party arrangement.

3. If a company receives the stock of an affiliated company as a capital contribution rather than through a purchase, the transaction shall be accounted for according to *SSAP No. 25—Affiliates and Other Related Parties, SSAP No. 95—Nonmonetary Transactions*, or *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*, based on the details of each transaction. The statutory purchase method within *SSAP No. 68—Business Combinations* is not applicable for stock received as a capital contribution.

SUMMARY CONCLUSION

4. Related parties are defined as entities that have common interests as a result of ownership, control, affiliation or by contract. Related parties shall include but are not limited to the following:

a. Affiliates of the reporting entity, as defined in paragraph 5;

b. Trusts for the benefit of employees, such as pension and profit-sharing trusts and Employee Stock Ownership Plans that are managed by or under the trusteeship of management of the reporting entity, its parent or affiliates;

c. The principal owners, directors, and officers of the reporting entity;

d. Any immediate family member of a principal owner, director or executive officer of the reporting entity, which means any child, stepchild, parent, stepparent, spouse, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, or individual related by blood or marriage whose close association is equivalent to a family relationship of such director, executive officer or nominee for director, or any person (other than a tenant or employee) sharing the household of such director, executive officer or nominee for director;

e. Companies and entities which share common control, such as principal owners, directors, or officers, including situations where principal owners, directors, or officers have a controlling stake in another reporting entity;

f. Any direct or indirect ownership greater than 10% of the reporting entity results in a related party classification regardless of any disclaimer of control or disclaimer of affiliation;

g. The management of the reporting entity, its parent or affiliates (including directors);

h. Members of the immediate families of principal owners and management of the reporting entity, its parent or affiliates and their management;

i. Parties with which the reporting entity may deal if either party directly or indirectly controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interest;

j. A party which can, directly or indirectly, significantly influence the management or operating policies of the reporting entity, which may include a provider who is contracting with the reporting entity. This is not intended to suggest that all provider contracts create related party relationships;

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k. A party which has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests;

l. Attorney-in-fact of a reciprocal reporting entity or any affiliate of the attorney-in-fact; and

m. A U.S. manager of a U.S. Branch or any affiliate of the U.S. manager of a U.S. Branch.

5. An affiliate is defined as an entity that is within the holding company system or a party that, directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with the reporting entity. An affiliate includes a parent or subsidiary and may also include partnerships, joint ventures, and limited liability companies as defined in *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*. Those entities are accounted for under the guidance provided in SSAP No. 48, which requires an equity method for all such investments. An affiliate is any person that is directly or indirectly, owned or controlled by the same person or by the same group of persons, that, directly or indirectly, own or control the reporting entity. Any invested asset held by a reporting entity which is issued by an affiliated entity, or which includes the obligations of an affiliated entity, is an affiliated investment.

6. Control is defined as the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of the investee, whether through the (a) ownership of voting securities, (b) by contract other than a commercial contract for goods or nonmanagement services, (c) by contract for goods or nonmanagement services where the volume of activity results in a reliance relationship (d) by common management, or (e) otherwise. Control shall be presumed to exist if a reporting entity and its affiliates directly or indirectly, own, control, hold with the power to vote, or hold proxies representing 10% or more of the voting interests of the entity.

7. Control as defined in paragraph 6 shall be measured at the holding company level. For example, if one member of an affiliated group has a 5% interest in an entity and a second member of the group has an 8% interest in the same entity, the total interest is 13%, and therefore, each member of the affiliated group shall be presumed to have control. This presumption will stand until rebutted by an evaluation of all the facts and circumstances relating to the investment. The insurer shall maintain documents substantiating its determination for review by the domiciliary commissioner. Examples of situations where the presumption of control may be in doubt include the following:

a. Any limited partner investment in a limited partnership, unless the limited partner is affiliated with the general partner.

b. An entity where the insurer owns less than 50% of an entity and there is an unaffiliated individual or group of investors who own a controlling interest.

c. An entity where the insurer has given up participation rights[1] as a shareholder to the investee.

[1] The term "participating rights" refers to the type of rights that allows an investor to effectively participate in significant decisions related to an investee's ordinary course of business and is distinguished from the more limited type of rights referred to as "protective rights". Refer to the sections entitled: "Protective Rights" and "Substantive Participating Rights" in EITF 96-16, *Investor's Accounting for an Investee When the Investor Owns a Majority of the Voting Stock but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights*. The term "participating rights" shall be used consistent with the discussion of substantive participating rights in this EITF.

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d. Agreements where direct or indirect non-controlling ownership interest is less than 10% where the parties have structured the arrangement in this structure to avoid the 10% threshold in paragraph 4.f. and paragraph 8.

8. Any direct or indirect ownership interest of the reporting entity greater than 10% results in a related party classification regardless of any disclaimer of control or disclaimer of affiliation. The *Insurance Holding Company System Regulatory Act* (#440) and the *Insurance Holding Company System Model Regulation With Reporting Forms and Instructions* (#450) include a provision that allows for the disclaimer of affiliation and/or the disclaimer of control for members of an insurance holding company system. The disclaimer must be filed with the state insurance commissioner. Entities whose relationship is subject to a disclaimer of affiliation or a disclaimer of control are related parties and are subject to the related party disclosures within this statement. Such a disclaimer does not eliminate a "related party" distinction or disclosure requirements for material transactions pursuant to SSAP No. 25.

9. For entities not controlled by voting interests, such as limited partnerships, trusts and other special purpose entities, control may be held by a general partner, servicer, or by other arrangements. The ability of the reporting entity or its affiliates to direct the management and policies of an entity through such arrangements shall constitute control as defined in paragraph 6. Additionally, a reporting entity or its affiliates may have indirect control of other entities through such arrangements. For example, if a limited partnership were to be controlled by an affiliated general partner, and that limited partnership held greater than 10% of the voting interests of another company[2], indirect control shall be presumed to exist unless the presumption of control can be overcome as detailed in paragraph 7. If direct or indirect control exists, whether through voting securities, contracts, common management or otherwise, the arrangement is considered affiliated under paragraph 5. Consistent with paragraph 8, a disclaimer of affiliation does not eliminate a "related party" distinction or disclosure requirements for material transactions pursuant to SSAP No. 25.

10. Transactions between related parties must be in the form of a written agreement. The written agreement must provide for timely settlement of amounts owed, with a specified due date. Amounts owed to the reporting entity over ninety days from the written agreement due date shall be nonadmitted, except to the extent this is specifically addressed by other statements of statutory accounting principles (SSAPs). If the due date is not addressed by the written agreement, any uncollected receivable is nonadmitted.

Related Party Loans

11. Loans or advances (including debt, public or private) made by a reporting entity to its parent or principal owner shall be admitted if approval for the transaction has been obtained from the domiciliary commissioner and the loan or advance is determined to be collectible based on the parent or principal owner's independent payment ability. An affiliate's ability to pay shall be determined after consideration of the liquid assets or revenues available from external sources (i.e., determination shall not include dividend paying ability of the subsidiary making the loan or advance) which are available to repay the balance and/or maintain its account on a current basis. Evaluation of the collectibility of loans or advances shall be made periodically. If, in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. Pursuant to *SSAP No. 72—Surplus and Quasi-Reorganization*, forgiveness by a reporting entity of any debt, surplus note or other obligation of its parent or other stockholder shall be accounted for as a dividend.

[2] Consistent with SSAP No. 97, footnote 1, investments in an exchange traded fund (ETF), a mutual fund (as defined by the SEC) or a foreign open-end investment fund governed and authorized in accordance with regulations established by the applicable foreign jurisdiction does not reflect ownership in an underlying entity, regardless of the ownership percentage the reporting entity (or the holding company group) has of the ETF, mutual fund or foreign open-end investment fund unless ownership of the fund actually results in "control" with the power to direct or cause the direction of management of an underlying company. ETFs, mutual funds and foreign open-end investment funds are comprised of portfolios of securities subject to the regulatory requirements of the federal securities laws or the applicable foreign jurisdictions laws.

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12. Loans or advances by a reporting entity to all other related parties shall be evaluated by management and nonadmitted if they do not constitute arm's-length transactions as defined in paragraph 15. Loans or advances made by a reporting entity to related parties (other than its parent or principal owner) that are economic transactions as defined in paragraph 15 shall be admitted. This includes financing arrangements with providers of health care services with whom the reporting entity contracts with from time to time. Such arrangements can include both loans and advances to these providers. Evaluation of the collectibility of loans or advances shall be made periodically. If, in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

13. Any advances under capitation arrangements made directly to providers, or to intermediaries that represent providers, that exceed one month's payment shall be nonadmitted assets.

14. Indirect loans are loans or extensions of credit to any person who is not an affiliate, where the reporting entity makes loans or extensions of credit with the agreement or understanding that the proceeds of the transactions, in whole or in substantial part, are to be used to make loans or extensions of credit to, to purchase assets of, or to make investments in, any affiliate of the reporting entity making the loans or extensions of credit. The admissibility of indirect loans made by a reporting entity for the benefit of its parent or principal owner shall be determined in accordance with the guidelines in paragraph 11. Indirect loans or advances made for the benefit of all other related parties shall be evaluated and accounted for consistent with loans or advances to related parties as described in paragraph 12 and paragraph 13.

Transactions Involving the Exchange of Assets or Liabilities

15. An arm's-length transaction is defined as a transaction in which willing parties, each being reasonably aware of all relevant facts and neither under compulsion to buy, sell, or loan, would be willing to participate. A transaction between related parties involving the exchange of assets or liabilities shall be designated as either an economic transaction or non-economic transaction. An economic transaction is defined as an arm's-length transaction which results in the transfer of the risks and rewards of ownership and represents a consummated act thereof, i.e., "permanence." The appearance of permanence is also an important criterion in assessing the economic substance of a transaction. In order for a transaction to have economic substance and thus warrant revenue (loss) recognition, it must appear unlikely to be reversed. If subsequent events or transactions reverse the effect of an earlier transaction prior to the issuance of the financial statements, the reversal shall be considered in determining whether economic substance existed in the case of the original transaction. Subsequent events are addressed in *SSAP No. 9—Subsequent Events*. An economic transaction must represent a bonafide business purpose demonstrable in measurable terms. A transaction which results in the mere inflation of surplus without any other demonstrable and measurable betterment is not an economic transaction. The statutory accounting shall follow the substance, not the form of the transaction.

16. In determining whether there has been a transfer of the risks and rewards of ownership in the transfer of assets or liabilities between related parties, the following—and any other relevant facts and circumstances related to the transaction—shall be considered:

a. Whether the seller has a continuing involvement in the transaction or in the financial interest transferred, such as through the exercise of managerial authority to a degree usually associated with ownership;

b. Whether there is an absence of significant financial investment by the buyer in the financial interest transferred, as evidenced, for example, by a token down payment or by a concurrent loan to the buyer;

c. Whether repayment of debt that constitutes the principal consideration in the transaction is dependent on the generation of sufficient funds from the asset transferred;

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d. Whether limitations or restrictions exist on the buyer's use of the financial interest transferred or on the profits arising from it;

e. Whether there is retention of effective control of the financial interest by the seller.

17. A transaction between related parties may meet the criteria for treatment as an economic transaction at one level of financial reporting, but may not meet such criteria at another level of financial reporting. An example of such a transaction is a reporting entity purchasing securities at fair value from an affiliated reporting entity that carried the securities at amortized cost. This transaction meets the criteria of an economic transaction at this level of financial reporting, and therefore, the selling reporting entity would record a gain and the acquiring reporting entity would record the securities at their cost (fair value on the transaction date). At the common parent level of reporting, this transaction has resulted in the mere inflation of surplus, and therefore, is a non-economic transaction. The parent reporting entity shall defer the net effects of any gain or increase in surplus resulting from such transactions by recording a deferred gain and an unrealized loss. The deferred gain shall not be recognized by the parent reporting entity unless and until arms-length transaction(s) with independent third parties give rise to appropriate recognition of the gain.

18. A non-economic transaction is defined as any transaction that does not meet the criteria of an economic transaction. Similar to the situation described in paragraph 17, transfers of assets from a parent reporting entity to a subsidiary, controlled or affiliated entity shall be treated as non-economic transactions at the parent reporting level because the parent has continuing indirect involvement in the assets.

19. When accounting for a specific transaction, reporting entities shall use the following valuation methods:

a. Economic transactions between related parties shall be recorded at fair value at the date of the transaction. To the extent that the related parties are affiliates under common control, the controlling reporting entity shall defer the effects of such transactions that result in gains or increases in surplus (see paragraph 17);

b. Non-economic transactions between reporting entities, which meet the definition of related parties above, shall be recorded at the lower of existing book values or fair values at the date of the transaction;

c. Non-economic transactions between a reporting entity and an entity that has no significant ongoing operations other than to hold assets that are primarily for the direct or indirect benefit or use of the reporting entity or its affiliates, shall be recorded at the fair value at the date of the transaction; however, to the extent that the transaction results in a gain, that gain shall be deferred until such time as permanence can be verified;

d. Transactions which are designed to avoid statutory accounting practices shall be reported as if the reporting entity continued to own the assets or to be obligated for a liability directly instead of through a subsidiary.

Examples of transactions deemed to be non-economic include security swaps of similar issues between or among affiliated companies, and swaps of dissimilar issues accompanied by exchanges of liabilities between or among affiliates.

Transactions Involving Services

20. Transactions involving services between related parties can take a variety of different forms. One of the significant factors as to whether these transactions will be deemed to be arm's length is the amount charged for such services. In general, amounts charged for services are based either on current market

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rates or on allocations of costs. Determining market rates for services is difficult because the circumstances surrounding each transaction are unique. Unlike transactions involving the exchange of assets and liabilities between related parties, transactions for services create income on one party's books and expense on the second party's books, and therefore, do not lend themselves to the mere inflation of surplus. These arrangements are generally subject to regulatory approval.

21. Transactions involving services provided between related parties shall be recorded at the amount charged[3]. Regulatory scrutiny of related party transactions where amounts charged for services do not meet the fair and reasonable standard established by Appendix A-440, may result in (a) amounts charged being recharacterized as dividends or capital contributions, (b) transactions being reversed, (c) receivable balances being nonadmitted, or (d) other regulatory action. Expenses that result from cost allocations shall be allocated subject to the same fair and reasonable standards, and the books and records of each party shall disclose clearly and accurately the precise nature and details of the transaction. See *SSAP No 70—Allocation of Expenses* for additional discussion regarding the allocation of expenses.

Disclosures

22. The financial statements shall include disclosures of all material related party transactions, including transactions with the ownership interests identified in paragraph 23. In some cases, aggregation of similar transactions, that on a stand-alone basis are not material, may be appropriate. Sometimes, the effect of the relationship between the parties may be so pervasive that disclosure of the relationship alone will be sufficient. If necessary to the understanding of the relationship, the name of the related party should be disclosed. Transactions shall not be purported to be arm's-length transactions unless there is demonstrable evidence to support such statement. The disclosures shall include:

a. The nature of the relationships involved;

b. A description of the transactions for each of the periods for which financial statements are presented, and such other information considered necessary to obtain an understanding of the effects of the transactions on the financial statements. Exclude reinsurance transactions, any non-insurance transactions which involve less than ½ of 1% of the total admitted assets of the reporting entity, and cost allocation transactions. The following information shall be provided if applicable:

   i. Date of transaction;

   ii. Explanation of transaction;

   iii. Name of reporting entity;

   iv. Name of affiliate;

   v. Description of assets received by reporting entity;

   vi. Statement value of assets received by reporting entity;

   vii. Description of assets transferred by reporting entity; and

[3] The amount charged shall be reviewed when there are any modifications or waivers subsequent to the establishment of the contract terms. If waivers or modifications to amounts charged occur, the related party transaction shall be reassessed to determine whether the contract continues to reflect fair and reasonable standards. If the transaction was with a parent or other stockholder and the charge for services has been fully waived, then the guidance in SSAP No. 72 for recognition as contributed capital (forgiveness of reporting entity obligation) or as a dividend (forgiveness of amount owed to the reporting entity) shall apply.

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viii. Statement value of assets transferred by reporting entity.

c. The dollar amounts of transactions for each of the periods for which financial statements are presented and the effects of any change in the method of establishing the terms from that used in the preceding period;

d. Amounts due from or to related parties as of the date of each balance sheet presented and, if not otherwise apparent, the terms and manner of settlement;

e. Any guarantees or undertakings, written or otherwise, shall be disclosed in accordance with the requirements of SSAP No. 5R. In addition, the nature of the relationship to the beneficiary of the guarantee or undertaking (affiliated or unaffiliated) shall also be disclosed;

f. A description of material management or service contracts and cost-sharing arrangements involving the reporting entity and any related party. This shall include, but is not limited to, sale lease-back arrangements, computer or fixed asset leasing arrangements, and agency contracts, which remove assets otherwise recordable (and potentially nonadmitted) on the reporting entity's financial statements;

g. The nature of the control relationship whereby the reporting entity and one or more other enterprises are under common ownership or control and the existence of that control could result in operating results or financial position of the reporting entity significantly different from those that would have been obtained if the enterprises were autonomous. The relationship shall be disclosed even though there are no transactions between the enterprises; and

h. The amount deducted from the value of an upstream intermediate entity or ultimate parent owned, either directly or indirectly, via a downstream subsidiary, controlled, or affiliated entity, in accordance with SSAP No. 97. ~~the *Purposes and Procedure Manual of the NAIC Investment Analysis Office*, "Procedures for Valuing Common Stocks and Stock Warrants."~~

23. The disclosures of ownership interests in the reporting entity shall be provided outside of the financial statements (Schedule Y). The intent of this disclosure is to capture information related to active ownership and is not intended for passive fund owners to be reported.

a. Disclosure is required for all owners with greater than 10% ownership of the reporting entity.

b. Reporting entity must disclose each owner's ultimate controlling party and must provide a listing of other U.S. insurance groups or entities under that ultimate controlling party's control.

24. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

25. This statement adopts *FASB Statement No. 57, Related Party Disclosures* with a modification to paragraph 4 to require disclosure of compensation arrangements, expense allowances, and other similar items in the ordinary course of business.

26. This statement rejects *ASU 2009-17, Consolidations (Topic 810)—Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities, ASU 2010-02, Consolidation (Topic 810)—Accounting and Reporting for Decreases in Ownership of a Subsidiary—a Scope Clarification,*

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ASU 2010-10, Consolidations (Topic 810)—Amendments for Certain Investment Funds, ASU 2013-06, Not-For-Profit Entities, Services Received from Personnel of an Affiliate, ASU 2014-07, Consolidation (Topic 810)—Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements, ASU 2015-02, Consolidation (Topic 810)—Amendments to the Consolidation Analysis, ASU 2016-17, Consolidation (Topic 810)—Interests Held through Related Parties That Are under Common Control, ASU 2018-17, Consolidation (Topic 810)—Targeted Improvements to Related Party Guidance for Variable Interest Entities and AICPA *Accounting Interpretations, Business Combinations: Accounting Interpretations of APB Opinion No. 16, No. 39*, "Transfers and Exchanges between Companies under Common Control."

27. Guidance in paragraph 10 was incorporated from SSAP No. 96 as discussed in *Issue Paper No. 128—Settlement Requirements for Intercompany Transactions, An Amendment to SSAP No. 25—Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties*. SSAP No. 96 was nullified in 2011 with the guidance from that SSAP retained within this SSAP.

Effective Date and Transition

28. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

29. Guidance reflected in paragraph 10, incorporated from SSAP No. 96, is effective for reporting periods ending December 31, 2007. Early adoption is permitted. A change resulting from the application of this paragraph shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance reflected in paragraph 3, incorporated from *INT 03-16: Contribution of Stock*, was originally effective December 7, 2003.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*

Relevant Issue Papers

- *Issue Paper No. 25—Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties*
- *Issue Paper No. 128—Settlement Requirements for Intercompany Transactions, An Amendment to SSAP No. 25—Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties*

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Statement of Statutory Accounting Principles No. 26 – Revised

Bonds

STATUS

Type of Issue	Common Area
Issued	Initial draft; Substantively revised April 2017
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 156 effective December 31, 2017
Affects	Supersedes SSAP No. 99 with guidance incorporated November 2010; Nullifies and incorporates INT 02-05
Affected by	No other pronouncements
Interpreted by	INT 01-25; INT 06-02; INT 06-07; INT 07-01
Relevant Appendix A Guidance	None

STATUS **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for bonds, specific fixed-income investments, and particular funds identified by the Securities Valuation Office (SVO) as qualifying for bond treatment as identified in this statement.

2. This statement excludes:

a. Loan-backed and structured securities addressed in *SSAP No. 43R—Loan-Backed and Structured Securities.*

b. Securities that meet the definition in paragraph 3 with a maturity date of one year or less from date of acquisition, which qualify as cash equivalents or short-term investments. These investments are addressed in *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments*.

c. Securities that meet the definition in paragraph 3, but for which the contractual amount of the instrument to be paid at maturity (or the original investment) is at risk for other than failure of the borrower to pay the contractual amount due. These investments, although in the form of a debt instrument, incorporate risk of an underlying variable in the terms of the agreement, and the issuer obligation to return the full principal is contingent on the performance of the underlying variable. These investments are addressed in *SSAP No. 86—Derivatives*, unless the investment is a mortgage-referenced security addressed in *SSAP No. 43R—Loan-Backed and Structured Securities*. This exclusion is specific to instruments in which the terms of the agreement make it possible that the reporting entity could lose all or a portion of its principal amount due/original investment amount (for other than failure of the issuer to pay the contractual amounts due). These instruments incorporate both the credit risk of the issuer, as well as the risk of an underlying variable (such as the performance of an equity index or the performance of an unrelated security). Securities that are labeled "principal-protected notes" are captured within this exclusion if the "principal protection" involves only a portion of the principal/original investment amount and/or if the protection requires the reporting entity to meet qualifying conditions in order to be safeguarded from the risk of loss from the underlying linked variable. Securities that may have changing positive interest rates in response to a linked underlying variable or the passage of time, or that have the potential for increased principal repayments in response to a linked variable (such as U.S. Treasury Inflation-Indexed Securities) that do not incorporate risk of original investment/principal loss (outside of default risk) are not captured in this exclusion. Securities within the scope of SSAP No. 43R, foreign denominated bonds (if only by virtue of their denomination in a foreign currency) and securities comprising elements of risk consistent with replication (synthetic assets) transactions (RSATs) as defined in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, are also not captured in this exclusion. This exclusion does not impact RSATs as defined in SSAP No. 86.

d. Mortgage loans and other real estate lending activities made in the ordinary course of business. These investments are addressed in *SSAP No. 37—Mortgage Loans* and *SSAP No. 39—Reverse Mortgages*.

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SUMMARY CONCLUSION

3. Bonds shall be defined as any securities[1] representing a creditor relationship, whereby there is a fixed schedule for one or more future payments. This definition includes:

a. U.S. Treasury securities;(INT 01-25)

b. U.S. government agency securities;

c. Municipal securities;

d. Corporate bonds, including Yankee bonds and zero-coupon bonds;

e. Convertible bonds, including mandatory convertible bonds as defined in paragraph 11.b;

f. Fixed-income instruments specifically identified:

i. Certifications of deposit that have a fixed schedule of payments and a maturity date in excess of one year from the date of acquisition;

ii. Bank loans issued directly by a reporting entity or acquired through a participation, syndication or assignment;

iii. Hybrid securities, excluding: surplus notes, subordinated debt issues which have no coupon deferral features, and traditional preferred stocks.

iv. Debt instruments in a certified capital company (CAPCO) (INT 06-02)

4. The definition of a bond, per paragraph 3, does not include equity/fund investments, such as mutual funds or exchange-traded funds. However, the following types of SVO-identified investments are provided special statutory accounting treatment and are included within the scope of this statement. These investments shall follow the guidance within this statement, as if they were bonds, unless different treatment is specifically identified in paragraphs 23-29.

a. Exchange traded funds (ETFs), which qualify for bond treatment, as identified in ~~Part Three of~~ the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and published on the SVO web page ~~at *https://content.naic.org/industry/securities-valuation-office*~~. (SVO-identified ETFs are reported on Schedule D – Part 1.)

5. Investments within the scope of this statement issued by a related party, or acquired through a related party transaction, are also subject to the provisions and disclosure requirements of *SSAP No. 25—Affiliates and Other Related Parties.* Investments within the scope of this statement meet the definition of

[1] This statement adopts the GAAP definition of a security as it is used in FASB Codification Topic 320 and 860.

Security: A share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:

a. It is either represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.

b. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.

c. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests or obligations.

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assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement and SSAP No. 25.

Acquisitions, Disposals and Changes in Unrealized Gains and Losses

6. A bond acquisition or disposal shall be recorded on the trade date (not the settlement date) except for the acquisition of private placement bonds which shall be recorded on the funding date. At acquisition, bonds shall be reported at their cost, including brokerage and other related fees. The reported cost of a bond received as a property dividend or capital contribution shall be the initial recognized value. SSAP No. 25 shall be used to determine whether a transfer is economic or noneconomic for initial recognition.

7. For reporting entities required to maintain an interest maintenance reserve (IMR), the accounting for realized capital gains and losses on sales of bonds shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities required to maintain an asset valuation reserve (AVR), the accounting for unrealized gains and losses shall be in accordance with SSAP No. 7.

8. For reporting entities not required to maintain an IMR, realized gains and losses on sales of bonds shall be reported as net realized capital gains or losses in the statement of income. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

Amortized Cost

9. Amortization of bond premium or discount shall be calculated using the scientific (constant yield) interest method taking into consideration specified interest and principal provisions over the life of the bond.[2] (INT 07-01) Bonds containing call provisions (where the issue can be called away from the reporting entity at the issuer's discretion), except "make-whole" call provisions, shall be amortized to the call or maturity value/date which produces the lowest asset value (yield-to-worst). Although the concept for yield-to-worst shall be followed for all callable bonds, make-whole call provisions, which allow the bond to be callable at any time, shall not be considered in determining the timeframe for amortizing bond premium or discount unless information is known by the reporting entity indicating that the issuer is expected to invoke the make-whole call provision.

Application of Yield-to-Worst

10. For callable bonds[3], the first call date after the lockout period (or the date of acquisition if no lockout period exists) shall be used as the "effective date of maturity" for reporting in Schedule D, Part 1. Depending on the characteristics of the callable bonds, the yield-to-worst concept in paragraph 9 shall be applied as follows:

[2] For perpetual bonds with an effective call option, any applicable premium shall be amortized utilizing the yield-to-worst method.

[3] Callable bonds within the scope of paragraph 10 excludes bonds with make-whole call provisions unless information is known by the reporting entity indicating that the issuer is expected to invoke the make-whole call provision.

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a. For callable bonds with a lockout period, premium in excess of the next call price[4] (subsequent to acquisition[5] and lockout period) shall be amortized proportionally over the length of the lockout period. After each lockout period (if more than one), remaining premium shall be amortized to the call or maturity value/date which produces the lowest asset value.

b. For callable bonds without a lockout period, the book adjusted carrying value (at the time of acquisition) of the callable bonds shall equal the lesser of the next call price (subsequent to acquisition) or cost. Remaining premium shall then be amortized to the call or maturity value/date which produces the lowest asset value.

c. For callable bonds that do not have a stated call price, all premiums over par shall be immediately expensed. For callable bonds with a call price at par in advance of the maturity date, all premiums shall be amortized to the call date.

Balance Sheet Amount

11. Bonds, as defined in paragraph 3, shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and the designation assigned in the NAIC *Valuations of Securities* product prepared by the NAIC Securities Valuation Office (SVO).

a. Bonds, except for mandatory convertible bonds: For reporting entities that maintain an asset valuation reserve (AVR), the bonds shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value. For reporting entities that do not maintain an AVR, bonds that are designated highest-quality and high-quality (NAIC designations 1 and 2, respectively) shall be reported at amortized cost; all other bonds (NAIC designations 3 to 6) shall be reported at the lower of amortized cost or fair value. For perpetual bonds which do not possess or no longer possess an effective call option, the bond shall be reported at fair value regardless of NAIC designation.

b. Mandatory convertible bonds: Mandatory convertible bonds are subject to special reporting instructions and are not assigned NAIC designations or unit prices by the SVO. The balance sheet amount for mandatory convertible bonds shall be reported at the lower of amortized cost or fair value during the period prior to conversion. This reporting method is not impacted by NAIC designation or information received from credit rating providers (CRPs). Upon conversion, these securities will be subject to the accounting guidance of the statement that reflects their revised characteristics. (For example, if converted to common stock, the security will be in scope of *SSAP No. 30R—Unaffiliated Common Stock*, if converted to preferred stock, the security will be in scope of *SSAP No. 32R—Preferred Stocks*.)

12. The premium paid on a zero coupon convertible bond that produces a negative yield as a result of the value of a warrant exceeding the bond discount shall be written off immediately so that a negative yield is not produced. The full amount of the premium should be recorded as amortization within investment income on the date of purchase.

[4] Reference to the "next call price" indicates that the reporting entity shall continuously review the call dates/prices to ensure that the amortization (and resulting BACV) follows the yield-to-worst concept throughout the time the reporting entity holds the bond.

[5] The reporting entity shall only consider call dates/prices that occur after the reporting entity acquires the bond. If all of the call dates had expired prior to the reporting entity acquiring the bond, the reporting entity would consider the bond continuously callable without a lockout period.

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Impairment

13. An other-than-temporary(INT 06-07) impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of a debt security in effect at the date of acquisition.[6] A decline in fair value which is other-than-temporary includes situations where a reporting entity has made a decision to sell a security prior to its maturity at an amount below its carrying value. If it is determined that a decline in the fair value of a bond is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the entire difference between the bond's carrying value and its fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of the impairment loss shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR/IMR, the accounting for the entire amount of the realized capital loss shall be in accordance with SSAP No. 7. The other-than-temporary impairment loss shall be recorded entirely to either AVR or IMR (and not bifurcated between credit and non-credit components) in accordance with the annual statement instructions.

14. In periods subsequent to the recognition of an other-than-temporary impairment loss for a bond, the reporting entity shall account for the other-than-temporarily impaired security as if the security had been purchased on the measurement date of the other-than-temporary impairment. The fair value of the bond on the measurement date shall become the new cost basis of the bond and the new cost basis shall not be adjusted for subsequent recoveries in fair value. The discount or reduced premium recorded for the security, based on the new cost basis, shall be amortized over the remaining life of the security in the prospective manner based on the amount and timing of future estimated cash flows. The security shall continue to be subject to impairment analysis for each subsequent reporting period. Future declines in fair value which are determined to be other-than temporary shall be recorded as realized losses.

Income

15. Interest income for any period consists of interest collected during the period, the change in the due and accrued interest between the beginning and end of the period as well as reductions for premium amortization and interest paid on acquisition of bonds, and the addition of discount accrual. In accordance with *SSAP No. 34—Investment Income Due and Accrued*, investment income shall be reduced for amounts which have been determined to be uncollectible. Contingent interest may be accrued if the applicable provisions of the underlying contract and the prerequisite conditions have been met.

16. A bond may provide for a prepayment penalty or acceleration fee in the event the bond is liquidated prior to its scheduled termination date. Such fees shall be reported as investment income when received.

17. The amount of prepayment penalty and/or acceleration fees to be reported as investment income or loss shall be calculated as follows:

a. For called or tendered bonds in which the total proceeds (consideration) received exceeds par:

i. The amount of investment income reported is equal to the consideration received less the par value of the investment; and

[6] If a bond has been modified from original acquisition, the guidance in *SSAP No. 36—Troubled Debt Restructuring* and paragraph 22 of *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* shall be followed, as applicable. After modification of original terms, future assessments to determine other-than-temporary impairment shall be based on the modified contractual terms of the debt instrument.

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ii. Any difference between the book adjusted carrying value (BACV) and the par value at the time of disposal shall be reported as realized capital gains and losses, subject to the authoritative literature in SSAP No. 7.

b. For called or tendered bonds in which the consideration received is less than par[7]:

i. To the extent an entity has in place a process to identify explicit prepayment penalty or acceleration fees, these should be reported as investment income. (An entity shall consistently apply their process. Once a process is in place, an entity is required to maintain a process to identify prepayment penalties for called bonds in which consideration received is less than par.)

ii. After determining any explicit prepayment penalty or acceleration fees, the reporting entity shall calculate the resulting realized gain as the difference between the remaining consideration and the BACV, which shall be reported as realized capital gain, subject to the authoritative literature in SSAP No. 7.

Origination Fees

18. Origination fees represent fees charged to the borrower in connection with the process of originating or restructuring a transaction such as the private placement of bonds. The fees include, but are not limited to, points, management, arrangement, placement, application, underwriting and other fees pursuant to such a transaction. Origination fees shall not be recorded until received in cash. Origination fees intended to compensate the reporting entity for interest rate risks (e.g., points) shall be amortized into income over the term of the bond consistent with paragraph 9 of this statement. Other origination fees shall be recorded as income upon receipt.

Origination, Acquisition and Commitment Costs

19. Costs related to origination when paid in the form of brokerage and other related fees shall be capitalized as part of the cost of the bond, consistent with paragraph 6 of this statement. All other costs, including internal costs or costs paid to an affiliated entity related to origination, purchase or commitment to purchase bonds shall be charged to expense when incurred.

Commitment Fees

20. Commitment fees are fees paid to the reporting entity that obligate the reporting entity to make available funds for future borrowing under a specified condition. A fee paid to the reporting entity to obtain a commitment to make funds available at some time in the future, generally, is refundable only if the bond is issued. If the bond is not issued, then the fees shall be recorded as investment income by the reporting entity when the commitment expires.

21. A fee paid to the reporting entity to obtain a commitment to be able to borrow funds at a specified rate and with specified terms quoted in the commitment agreement, generally, is not refundable unless the commitment is refused by the reporting entity. This type of fee shall be deferred, and amortization shall depend on whether or not the commitment is exercised. If the commitment is exercised, then the fee shall be amortized in accordance with paragraph 9 of this statement over the life of the bond as an adjustment to the investment income on the bond. If the commitment expires unexercised, the commitment fee shall be recognized in income on the commitment expiration date.

[7] This guidance applies to situations in which consideration received is less than par but greater than the book adjusted carrying value (BACV). Pursuant to the yield-to-worst concept, bonds shall be amortized to the call or maturity date that produces the lowest asset value. In the event a bond has not been amortized to the lowest value prior to the call, or in cases of an accepted tender bond offer (BACV is greater than the consideration received), the entire difference between consideration received and the BACV shall be reported to investment income.

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Exchanges and Conversions

22. If a bond is exchanged or converted into other securities (including conversions of mandatory convertible securities addressed in paragraph 11.b.), the fair value of the bond surrendered at the date of the exchange or conversion shall become the cost basis for the new securities with any gain or loss realized at the time of the exchange or conversion. However, if the fair value of the securities received in an exchange or conversion is more clearly evident than the fair value of the bond surrendered, then it shall become the cost basis for the new securities.

SVO-Identified Investments

23. SVO-identified investments, as discussed in paragraph 4, are captured within the scope of this statement for accounting and reporting[8] purposes only. The inclusion of these investments within this statement is not intended to contradict state law regarding the classification of these investments and does not intend to provide exceptions to state investment limitations involving types of financial instruments (e.g., equity/fund interests), or with regards to concentration risk (e.g., issuer).

24. SVO-identified investments shall be initially reported at cost, including brokerage and other related fees. Subsequently, SVO-identified investments shall be reported at fair value,[9] with changes in fair value recorded as unrealized gains or losses, unless the reporting entity has elected use[10] of a documented systematic approach to amortize or accrete the investment in a manner that represents the expected cash flows from the underlying bond holdings. This special measurement approach is referred to as the "systematic value" measurement method and shall only be used for the SVO-identified investments within the scope of this statement.

25. Use of the systematic value for SVO-identified investments is limited as follows:

a. Systematic value is only permitted to be designated as the measurement method for AVR filers acquiring qualifying investments that have an NAIC designation of 1 to 5, and for non-AVR filers acquiring qualifying investments with an NAIC designation of 1 or 2. SVO-identified investments that have an NAIC designation of 6 for AVR filers or 3-6 for non AVR filers shall be measured at fair value.

b. Designated use of a systematic value is an irrevocable election per qualifying investment (by CUSIP) at the time investment is originally acquired[11]. Investments owned prior to being identified by the SVO as a qualifying SSAP No. 26R investment are permitted to be subsequently designated to the systematic value measurement method. This designation shall be applied as a change in accounting principle pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors*, which requires the reporting entity to recognize a cumulative effect to adjust capital and surplus as if the systematic value measurement method had been applied retroactively for all prior periods in which the investment was held. The election to use systematic value for investments shall be made

[8] With the inclusion of these SVO-identified investments in Schedule D, Part 1 or Schedule DA, specific guidelines are detailed in the annual statement instructions for reporting purposes.

[9] For these investments, net asset value (NAV) is allowed as a practical expedient to fair value.

[10] The election to use systematic value is not a permitted or prescribed practice as it is an accounting provision allowed within this SSAP. Similarly, this election does not override state statutes, and if a state does not permit reporting entities the election to use systematic value as the measurement method, this is also not considered a permitted or prescribed practice. SVO-identified investments reported at fair value (NAV) or systematic value, if in accordance with the provisions of this standard, are considered in line with SSAP No. 26R and do not require permitted or prescribed disclosures under *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures*.

[11] This guidance requires investments purchased in lots to follow the measurement method established at the time the investment was first acquired.

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before the year-end reporting of the investment in the year in which the SVO first identifies the investment as a qualifying SSAP No. 26R investment.

c. Once designated for a particular investment, the systematic value measurement method must be retained as long as the qualifying investment is held by the reporting entity and the investment remains within the scope of this statement with an allowable NAIC designation per paragraph 25.a. Upon a full sale/disposal of an SVO-identified investment (elimination of the entire CUSIP investment), after 90 days the reporting entity can reacquire the SVO-identified investment and designate a different measurement method. If the reporting entity was to reacquire the same investment within 90 days after it was sold/disposed, the reporting entity must utilize the measurement method previously designated for the investment. Subsequent/additional purchases of the same SVO-identified investment (same CUSIP) already held by a reporting entity must follow the election previously made by the reporting entity. If an investment no longer qualifies for a systematic value measurement because the NAIC designation has declined, then the security must be subsequently reported at the lower of "systematic value" or fair value. If the security has been removed from the SVO-identified listings, and is no longer in scope of this statement, then the security shall be measured and reported in accordance with the applicable SSAP.

d. Determination of the designated systematic value must follow the established[12] approach, which is consistently applied for all equity/fund SVO-identified investments designated for a systematic value. In all situations, an approach that continuously reflects "original" or "historical cost" is not an acceptable measurement method. The designated approach shall result with systematic amortization or accretion of the equity/fund investment in a manner that represents the expected cash flows from the underlying bond holdings.

26. Income distributions received from SVO-identified investments (cash or shares) shall be reported as interest income in the period in which it is earned. For those SVO-identified investments where the systematic value method is applied, interest income shall be recognized based on the book yield applied to the carrying value each period, similar to bonds.

27. For reporting entities required to hold an IMR and AVR reserve, realized and unrealized gains and losses for the SVO-identified investments shall be consistent with bonds within the scope of this standard. With this guidance, recognition of gains/losses (and corresponding AVR/IMR impacts) will be based on the ETF, and not activity that occurs within the ETF (e.g., such as changes in the underlying bonds held within the ETF). Also consistent with the guidance for bonds, recognized losses from other-than-temporary impairments shall be recorded entirely to either AVR or IMR (and not bifurcated between credit and non-credit components) in accordance with the annual statement instructions.

28. SVO-identified investments reported at systematic value shall recognize other-than-temporary impairments in accordance with the following guidance:

a. A decision to sell an SVO-identified investment that has a fair value less than systematic value results in an other-than-temporary impairment that shall be recognized.

b. In situations in which an SVO-identified investment has a fair value that is less than systematic value, the reporting entity must assess for other-than-temporary impairment. For these investments, a key determinant, along with other impairment indicators in *INT 06-07: Definition of Phrase "Other Than Temporary*," shall be whether the net present value of the projected cash flows for the underlying bonds in the SVO-identified

[12] Exhibit B details the established systematic value approach.

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investment have materially[13] declined from the prior reporting period (most recent issued financial statements) or from the date of acquisition. In calculating the net present value of the projected cash flows for each reporting period, entities shall discount cash flows using a constant purchase yield, which is the initial book yield at acquisition[14]. Consistent with INT 06-07, a predefined threshold to determine whether the decline in projected cash flows (e.g., percentage change) shall result in an other than temporary impairment has not been set, as exclusive reliance on such thresholds removes the ability of management to apply its judgement.

c. Upon identification of an SVO-identified investment as OTTI, the reporting entity shall recognize a realized loss equal to the difference between systematic value and the current fair value. (Although the determination of OTTI is likely based on projected cash flows, the realized loss recognized for the OTTI is based on the difference between systematic value and fair value.) The fair value of the SVO-identified investment on the date of the OTTI shall become the new cost basis of the investment.

d. Subsequent to recognition of an OTTI, the SVO-identified investment is required to be reported at the lower of the then-current period systematic value or fair value. As the underlying bonds can be replaced within an ETF, it is possible for a subsequent period systematic value and fair value to recover above the fair value that existed at the time an OTTI was recognized. As such, the requirement for subsequent reporting at the lower of systematic value or fair value is intended to be a current period assessment. For example, in reporting periods after an OTTI, the systematic value for an SVO-identified investment may exceed the fair value at the time of the OTTI, but in no event shall the reported systematic value exceed the then-current period fair value. If current calculated systematic value is lower than the current fair value, systematic value is required.

29. Impairment guidance for SVO-identified investments reported at fair value is consistent with impairment guidance for investments captured under SSAP No. 30R. Pursuant to this guidance, realized losses are required to be recognized when a decline in fair value is considered to be other-than-temporary. Subsequent fluctuations in fair value shall be recorded as unrealized gains or losses. Future declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses. A decision to sell an impaired security results with an other-than-temporary impairment that shall be recognized.

Disclosures

30. The financial statements shall include the following disclosures:

a. Fair value in accordance with *SSAP No. 100R—Fair Value*;

b. Concentrations of credit risk in accordance with *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures*;

c. The basis at which the bonds, mandatory convertible securities, and SVO-identified investments identified in paragraph 4, are stated;

[13] The net present value of cash flows will decline in a declining interest rate environment. Reporting entities shall use judgment when assessing whether the decline in cash flows is related to a decline in interest rates or the result of a non-interest related decline, and determine whether the decline represents an OTTI pursuant to INT 06-07.

[14] Transition guidance in paragraph 35 shall be followed for initial application and for investments that are designated as SVO-identified investments eligible for systematic value.

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d. Amortization method for bonds and mandatory convertible securities, and if elected by the reporting entity, the approach for determining the systematic value for SVO-identified securities per paragraph 24. If utilizing systematic value measurement method approach for SVO-identified investments, the reporting entity must include the following information:

i. Whether the reporting entity consistently utilizes the same measurement method for all SVO-identified investments[15] (e.g., fair value or systematic value). If different measurement methods are used[16], information on why the reporting entity has elected to use fair value for some SVO-identified investments and systematic value for others.

ii. Whether SVO-identified investments are being reported at a different measurement method from what was used in an earlier current-year interim and/or in a prior annual statement. (For example, if reported at systematic value prior to the sale, and then reacquired and reported at fair value.) This disclosure is required in all interim reporting periods and in the year-end financial statements for the year in which an SVO-identified investment has been reacquired and reported using a different measurement method from what was previously used for the investment. (This disclosure is required regardless of the length of time between the sale/reacquisition of the investments, but is only required in the year in which the investment is reacquired.)

iii. Identification of securities still held that no longer qualify for the systematic value method. This should separately identify those securities that are still within the scope of SSAP No. 26R and those that are being reported under a different SSAP.

e. For each balance sheet presented, the book/adjusted carrying values, fair values, excess of book/carrying value over fair value or fair value over book/adjusted carrying values for each pertinent bond or assets receiving bond treatment, category reported in Annual Statement Schedule D – Bonds issued by:

i. U.S. Governments;

ii. All Other Governments;

iii. States, Territories and Possessions (Direct and Guaranteed);

iv. U.S. Political Subdivisions of States, Territories and Possessions (Direct and Guaranteed);

v. U.S. Special Revenue & Special Assessment Obligations and all Non-Guaranteed Obligations of Agencies and Authorities of Governments and Their Political Subdivisions;

vi. Industrial & Miscellaneous (Unaffiliated);

vii. Hybrid Securities;

[15] As identified in paragraph 25.d., a consistent approach must be followed for all investments designated to use the systematic value method. As such, this disclosure is limited to situations in which a reporting entity uses both fair value and systematic value for reported SVO-identified investments.

[16] The guidance in this statement allows different measurement methods by qualifying investment (CUSIP), but it is anticipated that companies will generally utilize a consistent approach for all qualifying investments.

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viii. Parent, Subsidiaries and Affiliates;

f. For the most recent balance sheet, the book/adjusted carrying values and the fair values of bonds and assets receiving bond treatment, reported in statutory Annual Statement Schedule D – Part 1A due:

i. In one year or less (including items without a maturity date which are payable on demand and in good standing);

ii. After one year through five years;

iii. After five years through ten years;

iv. After ten years (including items without a maturity date which are either not payable on demand or not in good standing).

g. For each period for which results of operations are presented, the proceeds from sales of bonds and assets receiving bond treatment, reported in Annual Statement Schedule D – Bonds and gross realized gains and gross realized losses on such sales.

h. For each balance sheet presented, all bonds in an unrealized loss position for which other-than-temporary declines in value have not been recognized:

i. The aggregate amount of unrealized losses (that is, the amount by which cost or amortized cost exceeds fair value) and

ii. The aggregate related fair value of bonds with unrealized losses.

i. The disclosures in paragraphs 30.h.i. and 30.h.ii. should be segregated by those bonds that have been in a continuous unrealized loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 months or longer using fair values determined in accordance with SSAP No. 100R.

j. As of the most recent balance sheet date presented, additional information should be included describing the general categories of information that the investor considered in reaching the conclusion that the impairments are not other-than-temporary.

k. When it is not practicable to estimate fair value in accordance with SSAP No. 100R, the investor should disclose the following additional information, if applicable, as of each date for which a statement of financial position is presented in its annual financial statements:

i. The aggregate carrying value of the investments not evaluated for impairment, and

ii. The circumstances that may have a significant adverse effect on the fair value.

l. For securities sold, redeemed or otherwise disposed as a result of a call or tender offer feature (including make-whole call provisions), disclose the number of CUSIPs sold, disposed or otherwise redeemed and the aggregate amount of investment income generated as a result of a prepayment penalty and/or acceleration fee.

31. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures in paragraphs 30.b., 30.e., 30.f., 30.g., 30.h., 30.i., 30.j. and 30.k. shall be included in the annual audited statutory financial reports only.

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Relevant Literature

32. This statement adopts *AICPA Statement of Position 90-11, Disclosure of Certain Information by Financial Institutions About Debt Securities Held as Assets,* and *AICPA Practice Bulletin No. 4, Accounting for Foreign Debt/Equity Swaps*. This statement also adopts *FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. This statement adopts the GAAP definition of "security" as it is used in FASB Codification Topic 320 and 860.

33. This statement rejects the GAAP guidance for debt securities, which is contained in *ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs*, *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, ASU 2017-08, Premium Amortization on Purchased Callable Debt* Securities, ASU *2016-01, Financial Instruments – Overall*, *FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases, FASB Emerging Issues Task Force No. 89-18, Divestitures of Certain Investment Securities to an Unregulated Commonly Controlled Entity under FIRREA,* and *FASB Emerging Issues Task Force No. 96-10, Impact of Certain Transactions on Held-to-Maturity Classifications Under FASB Statement No. 115.* Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

34. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance in paragraphs 13 and 14 was previously included within *SSAP No. 99—Accounting for Securities Subsequent to an Other-Than-Temporary Impairment* and was effective for reporting periods beginning on January 1, 2009, and thereafter, with early adoption permitted. In 2010, the guidance from SSAP No. 99 was incorporated within the impacted standards, with SSAP No. 99 superseded. The original impairment guidance included in this standard, and the substantive revisions reflected in SSAP No. 99 are retained for historical purposes in Issue Paper No. 131. Guidance reflected in paragraph 12, incorporated from *INT 02-05: Accounting for Zero Coupon Convertible Bonds*, was originally effective December 8, 2002. Guidance adopted in December 2013 clarifying the 'yield-to-worst' concept for bonds with make-whole call provisions is a nonsubstantive change initially effective January 1, 2014, unless the company has previously been following the guidance. (Companies that have previously been following the original intent, as clarified in the revisions, should not be impacted by these changes.) The guidance in paragraph 17 with respect to the calculation of investment income for prepayment penalty and/or acceleration fees is effective January 1, 2017, on a prospective basis and is required for interim and annual reporting periods thereafter. Early application is permitted.

35. In April 2017, substantive revisions, as detailed in Issue Paper No. 156, were adopted. These revisions, effective December 31, 2017, clarify the definition of a bond and what is in scope of the bond definition, as well as incorporate new guidance for SVO-identified investments identified as in scope of SSAP No. 26R, but that are not considered bonds. As of the effective date, reporting entities shall modify the measurement method for SVO-identified investments to reflect the guidance in the substantive revisions as follows:

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a. For SVO-identified investments captured within SSAP No. 26R and held by the reporting entity at the time of transition that will be reported at fair value (or NAV), the reporting entity shall reflect an unrealized gain or unrealized loss for the difference between the prior book/adjusted carrying value and fair value (NAV). Subsequently the investment shall continue to be reported at fair value (or NAV) with fair value fluctuations recorded as unrealized gains or losses, until the time of sale or recognition of an other-than-temporary impairment.

b. For SVO-identified investments captured within SSAP No. 26R and held by the reporting entity at the time of transition for which the reporting entity elects use of the systematic value measurement method, as of December 31, 2017, the reporting entity shall identify the SVO-identified investment with a code in the Annual Statement Schedule D - Part 1 and continue reporting the investment using the measurement method utilized throughout 2017. As the revisions move the prior measurement method (fair value/original cost) to systematic value, which is a new measurement concept, the reporting entity shall begin calculating systematic value using the SVO-identified investments portfolio's aggregated cash flows (ACF) on January. 1, 2018, and use the December 31, 2017, book/adjusted carrying value to calculate the initial book yield. This new measurement approach is a change in accounting principle pursuant to SSAP No. 3, and shall be disclosed under SSAP No. 3. However, a cumulative effect adjustment to capital and surplus is not anticipated as reporting entities will be applying the book/adjusted carrying value as of December 31, 2017, to the aggregated cash flows on January 1, 2018, to calculate initial book yield.

   i. In accordance with the systematic value methodology, at the next reporting period date, the reporting entity shall amortize or accrete the carrying value by the difference between the effective interest using the initial book yield, and the distributions received, and shall recalculate the new effective book yield using the new carrying value and ACF as of the last day of the reporting period.

   ii. For situations in which there is an interval of time between when a company purchases an investment and when the investment is designated as an SVO-identified investment eligible for systematic value, the book yield should be calculated by equating the book/adjusted carrying value at that time to the ACF.

c. As the necessary historical ACF data is not available for calculating the initial book yield at acquisition for the net present value constant purchase yield (NPV-CPY) method for impairment recognition, reporting entities shall use recently published yield-to-maturity (YTM) as their constant purchase yield to be applied for NPV-CPY impairment recognition. For December 31, 2017, reporting, in addition to identifying the SVO-identified investments designated for systematic value, reporting entities shall disclose the CPY for each SVO-identified investment for NPV-CPY impairment recognition going forward.

d. For SSAP No. 26R Scope Revisions: If the revisions reflected in SSAP No. 26R (e.g., definitions) result with an investment no longer qualifying (or qualifying) within the scope of SSAP No. 26R, this change shall be reflected prospectively from the effective date. As such, investments previously included within SSAP No. 26, that will move within the scope of another SSAP and reporting schedule shall be shown as dispositions on Schedule D – Part 4, and shown as an acquisition on the schedule for which it will be subsequently reported. (If the revisions move the investment into the scope of SSAP No. 26R, the investment shall be reported as a disposition on the prior investment schedule and as an acquisition on the Schedule D – Part 3.)

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36. Revisions adopted April 2019, to explicitly exclude securities for which the contract amount of the instrument to be paid at maturity (or the original investment) is at risk for other than failure of the borrower to pay the contractual amount due, are effective December 31, 2019.

37. On July 30, 2020, nonsubstantive revisions were adopted to clarify existing guidance that all prepayment penalty and acceleration fees for when a bond is liquidated prior to its scheduled maturity date, including those from tendered bonds, shall follow the guidance in SSAP No. 26R. Reporting entities that have historically applied this guidance shall not change historical practices, but an effective date of January 1, 2021, with early application permitted, is allowed for reporting entities to make systems changes to capture tendered bonds in scope of this guidance.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*
- NAIC Valuation of Securities product prepared by the Securities Valuation Office

Relevant Issue Papers

- *Issue Paper No. 26—Bonds, Excluding Loan-Backed and Structured Securities*
- *Issue Paper No. 131—Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment*
- *Issue Paper No. 156—Bonds*

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EXHIBIT A – GLOSSARY

Bank Loan – Fixed-income instruments, representing indebtedness of a borrower, made by a financial institution. Bank loans can be issued directly by a reporting entity or acquired through an assignment, participation or syndication:

- **Assignment** – A bank loan assignment is defined as a fixed-income instrument in which there is the sale and transfer of the rights and obligations of a lender (as assignor) under an existing loan agreement to a new lender (and as assignee) pursuant to an Assignment and Acceptance Agreement (or similar agreement) which effects a novation under contract law, so the new lender becomes the direct creditor of and is in contractual privity with the borrower having the sole right to enforce rights under the loan agreement.

- **Participation –** A bank loan participation is defined as a fixed-income investment in which a single lender makes a large loan to a borrower and subsequently transfers (sells) undivided interests in the loan to other entities. Transfers by the originating lender may take the legal form of either assignments or participations. The transfers are usually on a nonrecourse basis, and the originating lender continues to service the loan. The participating entity may or may not have the right to sell or transfer its participation during the term of the loan, depending on the terms of the participation agreement. Loan Participations can be made on a parri-passu basis (where each participant shares equally) or a senior subordinated basis (senior lenders get paid first and the subordinated participant gets paid if there are sufficient funds left to make a payment).

- **Syndication –** A bank loan syndication is defined as a fixed-income investment in which several lenders share in lending to a single borrower. Each lender loans a specific amount to the borrower and has the right to repayment from the borrower. Separate debt instruments exist between the debtor and the individual creditors participating in the syndication. Each lender in a syndication shall account for the amounts it is owed by the borrower. Repayments by the borrower may be made to a lead lender that then distributes the collections to the other lenders of the syndicate. In those circumstances, the lead lender is simply functioning as a servicer and shall not recognize the aggregate loan as an asset. A loan syndication arrangement may result in multiple loans to the same borrower by different lenders. Each of those loans is considered a separate instrument.

Bond – Securities representing a creditor relationship, whereby there is a fixed schedule for one or more future payments.

Convertible Bond – A bond that can be converted into a different security, typically shares of common stock.

Hybrids – Securities whose proceeds are accorded some degree of equity treatment by one or more of the nationally recognized statistical rating organizations (NRSRO) and/or which are recognized as regulatory capital by the issuer's primary regulatory authority. Hybrid securities are designed with characteristics of debt and equity and are intended to provide protection to the issuer's senior note holders. Hybrid securities are sometimes referred to as capital securities. An example of a hybrid is a trust-preferred security. Excluded from bond classification are surplus notes, which are reported on BA; subordinated debt issues, which have no coupon deferral features; and "Traditional" preferred stocks, which should be captured under SSAP No. 32R. Traditional preferred stocks include, but are not limited to a) U.S. issuers that do not allow tax deductibility for dividends; and b) those issued as preferred stock of the entity of an operating subsidiary, not through a trust or a special purpose trust.

Trust Preferred Securities – Security possessing characteristics of both equity and debt. A company creates trust-preferred securities by creating a trust, issuing debt to it, and then having it issue preferred securities to investors. Trust-preferred securities are generally issued by bank holding companies. The

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preferred securities issued by the trust are what are referred to as trust-preferred securities. The security is a hybrid security with characteristics of both subordinated debt and preferred stock in that it is generally very long term (30 years or more), allows early redemption by the issuer, makes periodic fixed or variable interest payments, and matures at face value. In addition, trust preferred securities issued by bank holding companies will usually allow the deferral of interest payments for up to 5 years.

Mandatory Convertible Bonds - A type of convertible bond that has a required conversion or redemption feature. Either on or before a contractual conversion date, the holder must convert the mandatory convertible bond into the underlying common stock.

Security – Adopts the GAAP definition of a security as it is used in FASB Codification Topic 320 and 860: A share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:

a. It is either represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.

b. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.

c. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

Yankee Bonds – A bond denominated in U.S. dollars that is publicly issued in the U.S. by foreign banks and corporations. According to the Securities Act of 1933, these bonds must first be registered with the Securities and Exchange Commission (SEC) before they can be sold. Yankee bonds are often issued in tranches. Yankee bonds, or bonds issued by foreign entities denominated in U.S. dollars are not considered hybrid securities unless they have equity-like features.

Zero Coupon Bond – A bond that does not pay interest during the life of the bond. Instead, investors buy zero coupon bonds at a deep discount from their face value, which is the amount a bond will be worth when it "matures" or comes due. When a zero coupon bond matures, the investor will receive one lump sum equal to the initial investment plus the imputed interest, which is discussed below. The maturity dates on zero coupon bonds are usually long-term. Because zero coupon bonds pay no interest until maturity, their prices fluctuate more than other types of bonds in the secondary market. In addition, although no payments are made on zero coupon bonds until they mature, investors may still have to pay federal, state, and local income tax on the imputed or "phantom" interest that accrues each year.

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EXHIBIT B – SYSTEMATIC VALUE CALCULATION

The established systematic value method is considered an "aggregated cash flow" (ACF) method in which the cash flow streams from the individual bond holdings are aggregated into a single cash flow stream. These cash flows are scaled such that, when equated with the market price at which the ETF was purchased or sold, an internal rate of return is calculated, representing the investor's initial book yield for the ETF. Although the initial book yield is utilized to determine the current period effective yield, and the resulting adjustments to the ETF's reported (systematic) value, the book yield is recalculated at least quarterly in order to adjust the investor's book yield to reflect current cash flow projections of the current bond holdings within the ETF.

The following calculation shall be followed by reporting entities electing systematic value:

1. Download **cash flows** file from ETF provider website.

NAV:	$115.07	(Official end-of-day NAV found on ETF provider website)
Maturity:	12/8/2027	= SUMPRODUCT (CASHFLOW_DATE column, PRINCIPAL column)/SUM (PRINCIPAL column)
When Paid:	Monthly	
Par Value:	2,500	# shares purchased
Monthly Effective Interest:	$0.40	= (Recalculated Effective Book Yield from prior month x Prior Month Ending Book Value /12)
Distribution:	$0.34	Found on provider website
Net Amortization/Accretion:	$0.06	= (Monthly Effective Interest) – (Distribution)
Prior Month Ending Book Value:	$115.35	
NPV Constant Yield Method:	$117.10	= XNPV (Initial Book Yield, CASHFLOW column, CASHFLOW_DATE column) / 1000000
Initial Book Yield:	4.15%	
Book (Systematic) Value:	$115.41	= (Prior Period Ending Book Value) + (Net "amortization/ accretion")
Expense Ratio:	0.1500%	
Recalulated Effective Book Yield:	4.1639%	=XIRR(CASHFLOW column, CASHFLOW_DATE column, 0.05)

All formulas on the left are at a per share level (excepting "Par Value" which represents the number of shares purchased for this lot).

The resulting values calculated on the left are aggregated to reflect the total number of shares held on the previous tabs reflecting how one might populate Schedule D Part 1 with these values.

Additionally, the cash flows in the data file are based on 1 million shares. This was done in order to make the cash flows easier to observe and work wih (i.e., at a single share level, cash flows would be at fractional dollar levels). Therefore, in order to calculate the yield, investors must multiply the price of the ETF by 1 million shares and then use that value as a cash outflow against the positive cash inflows from the bond portfolio in order to calculate the IRR.

CUSIP	ASOF_DATE	CALL_TYPE	CASHFLOW_DATE	INTEREST	PRINCIPAL	CASHFLOW
2. Insert a row in between the column headings and the cash flow data.		3. Filter for "Call Type" is WORST. (Click "Data" at the top of Excel sheet, then click "Filter" and click the new dropdown box in the "Call Type" cell and select only "WORST.")	4. Enter the date of the cash flow data file underneath cash flow date. **8/31/20X1**			5. Under the column "CASHFLOW" enter the following formula in Excel: =(-Ending Book Value)*1000000 **(115,414,059.56)**
"Ticker"	8/31/20X1	WORST	9/8/20X1	136,538.564	81,472.372	218,010.937
"Ticker"	8/31/20X1	WORST	9/9/20X1	5,990.106	0	5,990.106
"Ticker"	8/31/20X1	WORST	9/10/20X1	9,706.324	0	9,706.324

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EXHIBIT C – AMORTIZATION TREATMENT FOR CALLABLE BONDS

Example 1: Call Price Less Than BACV Throughout the Life of the Bond

12/31/2008 – Issuance of Bond. Par = 100/10-Year Bond (Matures 12/31/2018)
01/01/2009 – Call Date/Call Price 107
12/15/2010 – Reporting Entity Acquires Bond. Cost = 106
01/01/2012 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 104
01/01/2014 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 103
01/01/2016 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 102

General Note for Examples: The reporting entity purchased the bond at a premium (cost was greater than par). The 1/1/2009 call date and price is ignored as it occurred prior to the reporting entity acquiring the bond. The bolded numbers represent the lowest asset value at each reporting period. The bond is amortized to the lowest asset value, which in this scenario is amortizing to the call dates and prices. (The standard amortization to the maturity date is shown as it should be compared to the amortization to the call date/price to verify that the BACV at any given reporting date reflects the lowest asset value.)

Date	Action	Cost	Call Price	BACV (Under Call Date/Price)	Amortization to the Lowest Value	BACV Under Standard Amortization
12/15/2010	Acquired	106		106		106
12/31/2011	Lockout Period			**104**	2	105.25
01/01/2012	Call Date		104	**104**		
12/31/2012	Year-End Reporting			**103.5**	0.5	104.50
12/31/2013	Year-End Reporting			**103**	0.5	103.75
01/01/2014	Call Date		103	**103**		
12/31/2014	Year-End Reporting			**102.5**	0.5	103
12/31/2015	Year-End Reporting			**102**	0.5	102.25
01/01/2016	Call Date Exercised		102	**102**		

Standard Amortization
This table shows the amortization with a purchase date of 12/15/2010 at $106 through the maturity date of 12/31/2018.

12/15/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Amortization	.75	.75	.75	.75	.75	.75	.75	.75
BACV	105.25	104.50	103.75	103	102.25	101.50	100.75	100

	Consideration	Par Value	BACV at Disposal Date	Realized Gain/Loss*
01/01/2016 Call Exercised	102	100	102	(2)

* Per paragraph 15, the entity would recognize a $(2) loss (BACV less par), and investment income of $2 (consideration less par).

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Example 2: Call Price Could be Greater Than BACV

12/31/2008 – Issuance of Bond. Par = 100/10-Year Bond (Matures 12/31/2018)
01/01/2009 – Call Date/Call Price 107
12/15/2010 – Reporting Entity Acquires Bond. Cost = 104
01/01/2012 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 106
01/01/2014 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 103
01/01/2016 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 102

The bolded numbers represent the lowest asset value:

Date	Action	Cost	Call Price	BACV (Under Call Date / Price)	Amortization To the Lowest Asset Value	BACV Under Standard Amortization
12/15/2010	Acquired	104		104		104
12/31/2011	Lockout Period		106	104	0.5	**103.50**
01/01/2012	Call Date		106	104		**103.50**
12/31/2012	Year-End Reporting			103.5	0.5	**103**
12/31/2013	Year-End Reporting			103	0.5	**102.50**
01/01/2014	Call Date		103	103		**102.50**
12/31/2014	Year-End Reporting			102.5	0.5	**102**
12/31/2015	Year-End Reporting			102	0.5	**101.50**
01/01/2016	Call Date Exercised		102	102		**101.50**

Standard Amortization
This table shows the amortization with a purchase date of 12/15/2010 at $104 through the maturity date of 12/31/2018.

12/15/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Amortization	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
BACV	103.50	103	102.50	102	101.50	101	100.50	100

	Consideration	Par Value	BACV at Disposal Date	Realized Gain/Loss*
01/01/2016 Call Exercised	102	100	101.50	(1.50)

* Per paragraph 15, the entity would recognize a $(1.50) loss (BACV less par), and investment income of $2 (consideration less par).

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Example 3: Call Price Could be Greater Than BACV

12/31/2008 – Issuance of Bond. Par = 100/10-Year Bond (Matures 12/31/2018)
01/01/2009 – Call Date/Call Price 107
12/15/2010 – Reporting Entity Acquires Bond. Cost = 104
01/01/2012 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 106
01/01/2014 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 102
01/01/2016 – Scheduled Call Date Subsequent to Reporting Entity Acquisition. Call Price 101

Note – This illustration shows that the evaluation of whether standard amortization (to the maturity date) or the call date price may change over the time. The bolded numbers represent the lowest asset value:

Date	Action	Cost	Call Price	BACV (Under Call Date / Price)	Amortization To the Lowest Asset Value	BACV Under Standard Amortization
12/15/2010	Acquired	104		104		
12/31/2011	Lockout Period		106	104	0.5	**103.50**
01/01/2012	Call Date		106	104		**103.50**
12/31/2012	Year-End Reporting			103	0.5	**103**
12/31/2013	Year-End Reporting			**102**	1	102.50
01/01/2014	Call Date		102	**102**		102.50
12/31/2014	Year-End Reporting			**101.5**	0.5	102
12/31/2015	Year-End Reporting			**101**	0.5	101.50
01/01/2016	Call Date Exercised		101	**101**		101.50

Standard Amortization
This table shows the amortization with a purchase date of 12/15/2010 at $104 through the maturity date of 12/31/2018.

12/15/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Amortization	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
BACV	103.50	103	102.50	102	101.50	101	100.50	100

	Consideration	Par Value	BACV at Disposal Date	Realized Gain/Loss*
01/01/2016 Call Exercised	101	100	101	(1)

* Per paragraph 15, the entity would recognize a $(1) loss (BACV less par), and investment income of $1 (consideration less par).

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Example 4: Continuously Callable Bond – Callable at Par After Initial Lockout Period

12/31/2008 – Issuance of Bond. Par = 100/10-Year Bond (Matures 12/31/2018)
01/01/2009 – Call Date / Call Price 107 – Continuously Callable Thereafter at Par
12/15/2010 – Reporting Entity Acquires Bond. Cost = 104

The bolded numbers represent the lowest asset value:

Date	Action	Cost	Call Price	BACV (Under Call Date/Price)	Amortization To the Lowest Asset Value	BACV Under Standard Amortization
12/15/2010	Acquired	104		100	4	
12/31/2010	Year-End Reporting		100	**100**	There is no subsequent amortization as the premium was fully expensed at acquisition.	104
12/31/2011	Year-End Reporting		100	**100**		103.50
12/31/2012	Year-End Reporting		100	**100**		103
12/31/2013	Year-End Reporting		100	**100**		102.50
12/31/2014	Year-End Reporting		100	**100**		102
12/31/2015	Year-End Reporting		100	**100**		101.50
01/01/2016	Year-End Reporting		100	**100**		101.50

Standard Amortization
This table shows the amortization with a purchase date of 12/15/2010 at $104 through the maturity date of 12/31/2018.

12/15/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Amortization	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
BACV	103.50	103	102.50	102	101.50	101	100.50	100

	Consideration	Par Value	BACV at Disposal Date	Realized Gain/Loss*
01/01/2016 Call Exercised	100	100	100	0

* Since the call price is par and could occur immediately after acquisition, the premium is immediately expensed. When the bond is called, there is no gain or loss as the consideration received equals the BACV.

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Example 5: Determination of Prepayment Penalty When Call Price is Less Than Par

Call Price Less than Par					
Entity 1				**Entity 2**	
Par	100			Par	100
BACV	24			BACV	25
Consideration	26			Consideration	26
Explicit fee	1			Explicit fee	1
Remaining consideration	25			Remaining consideration	25
Gain	2			Gain	0
Income*	0			Income**	1

*Entity 1 does not have in place a process to identify explicit prepayment penalty or acceleration fees.

**Entity 2 has in place a process to identify explicit prepayment penalty or acceleration fees.

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Statement of Statutory Accounting Principles No. 27

Off-Balance-Sheet and Credit Risk Disclosures

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for disclosure of information about financial instruments with off-balance-sheet risk and financial instruments with concentration of credit risk.

SUMMARY CONCLUSION

2. A financial instrument shall be defined as cash, evidence of an ownership interest in an entity, or a contract that both:

   a. Imposes on one entity a contractual obligation (i) to deliver cash or another financial instrument to a second entity or (ii) to exchange other financial instruments on potentially unfavorable terms with the second entity; and

   b. Conveys to that second entity a contractual right (i) to receive cash or another financial instrument from the first entity or (ii) to exchange other financial instruments on potentially favorable terms with the first entity.

3. Examples of the financial instruments, which encompass both assets and liabilities recognized and not recognized in the financial statement, to which this statement applies include, but are not limited

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to, short-term investments, bonds, common stocks, preferred stocks, mortgage loans, derivatives[1], financial guarantees written, standby letters of credit, notes payable and deposit-type contracts.

Disclosure of Extent, Nature, and Terms of Financial Instruments with Off-Balance-Sheet Risk

4. For financial instruments[1] with off-balance-sheet risk, except as noted in paragraphs 14 and 15 of *FASB Statement No. 105, Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk* (FAS 105), a reporting entity shall disclose in the financial statements the following information by class of financial instrument:

a. The face or contract amount (or notional principal amount if there is no face or contract amount); and

b. The nature and terms including, at a minimum, a discussion of (i) the credit and market risk of those instruments, (ii) the cash requirements of those instruments, and (iii) the related accounting policy pursuant to the requirements of *APB Opinion No. 22, Disclosure of Accounting Policies*.

5. Additional disclosures related to derivatives and embedded credit derivatives are addressed in *SSAP No. 86—Derivatives*.

Disclosure of Credit Risk of Financial Instruments with Off-Balance-Sheet Credit Risk

6. For financial instruments[1] with off-balance-sheet credit risk, except as noted in paragraphs 14 and 15 of FAS 105, an entity shall disclose in the financial statements the following information by class of financial instrument:

a. The amount of accounting loss the entity would incur if any party to the financial instrument failed completely to perform according to the terms of the contract and the collateral or other security, if any, for the amount due proved to be of no value to the entity; and

b. The entity's policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity's access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

Disclosure of Concentrations of Credit Risk of All Financial Instruments

7. Except as noted in paragraph 14 of FAS 105, a reporting entity shall disclose all significant concentrations of credit risk arising from all financial instruments[1] whether from an individual or group. Group concentrations of credit risk exist if a number of individuals or groups are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The following shall be disclosed in the financial statements about each significant concentration:

a. Information about the (shared) activity, region, or economic characteristic that identifies the concentration;

b. The amount of the accounting loss due to credit risk the entity would incur if parties to the financial instruments that make up the concentration failed completely to perform

[1] The financial instruments captured within this statement shall include financial instruments that contain embedded derivatives that are not separately recognized as financial instruments with derivatives under SSAP No. 86, and that expose the holder to the possibility (however remote) of making future payments.

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according to the terms of the contracts and the collateral or other security, if any, for the amount due proved to be of no value to the entity; and

c. The entity's policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity's access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

Annual and Quarterly Disclosure Requirements

8. Refer to the Preamble for further information regarding disclosure requirements. The disclosures in paragraph 7 shall be included in the annual audited statutory financial reports only.

Relevant Literature

9. This statement adopts the provisions of FAS 105 with the following modifications:

a. The disclosures required in paragraph 17 of FAS 105 shall distinguish between derivatives entered into for hedging purposes and for other-than-hedging purposes.

b. Paragraph 19 of FAS 105 is rejected. It addresses voluntary disclosures not required by this statement.

Effective Date and Transition

10. This statement is effective for years beginning January 1, 2001.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 27—Disclosure of Information about Financial Instruments with Concentration of Credit Risk*
- *Issue Paper No. 33—Disclosures about Fair Value of Financial Instruments*
- *Issue Paper No. 85—Derivative Instruments (as it relates to disclosure about financial instruments with off-balance-sheet risk)*

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Statement of Statutory Accounting Principles No. 29

Prepaid Expenses

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 87 with guidance incorporated August 2011; Nullifies and incorporates INT 08-04
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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REFERENCES **2**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the accounting for prepaid expenses. This statement does not address accounting for deferred policy acquisition costs and other underwriting expenses, income taxes, and guaranty fund assessments. This statement does not address nonrefundable advance payments for goods or services received for use in future research and development activities, which are addressed in *SSAP No. 17—Preoperating and Research and Development Costs.*

SUMMARY CONCLUSION

2. A prepaid expense is an amount which has been paid in advance of receiving future economic benefits anticipated by the payment. Prepaid expenses generally meet the definition of assets in *SSAP No. 4—Assets and Nonadmitted Assets*. Such expenditures also meet the criteria defining nonadmitted assets as specified in SSAP No. 4, (i.e., the assets are not readily available to satisfy policyholder obligations). Prepaid expenses shall be reported as nonadmitted assets and charged against unassigned funds (surplus). They shall be amortized against net income as the estimated economic benefit expires.

3. In accordance with the reporting entity's written capitalization policy, prepaid expenses less than a predefined threshold shall be expensed when purchased. The reporting entity shall maintain a

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capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Disclosures

4. The financial statements shall disclose if the written capitalization policy and the resultant predefined thresholds changed from the prior period and the reason(s) for such change.

Relevant Literature

5. This statement rejects *AICPA Practice Bulletin No. 13, Direct-Response Advertising and Probable Future Benefits, AICPA Statement of Position 93-7, Reporting on Advertising Costs* and *FASB Emerging Issues Task Force No. 88-23, Lump-Sum Payments under Union Contracts*.

Effective Date and Transition

6. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance reflected in paragraphs 3 and 4, incorporated from SSAP No. 87, was originally effective for years beginning on and after January 1, 2004.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 29—Prepaid Expenses (excluding deferred policy acquisition costs and other underwriting expenses, income taxes and guaranty fund assessments)*
- *Issue Paper No. 119—Capitalization Policy, An Amendment to SSAP Nos. 4, 19,29, 73, 79 and 82*

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Statement of Statutory Accounting Principles No. 30 – Revised

Unaffiliated Common Stock

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised November 15, 2018
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 158 effective January 1, 2019
Affects	Nullifies INT 02-07
Affected by	No other pronouncements
Interpreted by	INT 06-02; INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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REFERENCES **6**

Other 6
Relevant Issue Papers 6

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for common stocks.

2. Investments in common stock of subsidiaries, controlled or affiliated entities (investments in affiliates) are not within the scope of this statement. They are addressed in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

3. Investments in the form of common stock that are in substance residual interests or a residual security tranche, as defined in *SSAP No. 43R—Loan-Backed and Structured Securities* or *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, shall be reported on Schedule BA: Other Long-Term Assets in the dedicated reporting lines for residuals.

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SUMMARY CONCLUSION

~~3.~~4. Common stocks (excluding investments in affiliates) are securities which represent a residual/subordinate ownership in a corporation. This definition includes:

a. Publicly traded common stocks;

b. Common stocks that are not publicly traded; and

c. Common stocks restricted as to transfer of ownership[1]

~~4.~~5. In addition, the following equity[2] investments are captured within scope of this statement:

a. Master limited partnerships trading as common stock and American deposit receipts only if the security is traded on the New York or NASDAQ exchange;

b. Publicly traded common stock warrants;

c. Shares of SEC registered Investment Companies[3] captured under the Investment Company Act of 1940 (open-end investment companies (mutual funds), closed-end funds and unit investment trusts), regardless of the types or mix of securities owned by the fund (e.g., bonds or stocks[4]), including shares of funds referenced in the "NAIC Fixed Income-Like SEC Registered Funds List" as identified in ~~Part Three of~~ the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and published on the SVO web page;

d. Exchange Traded Funds, except for those identified for bond or preferred stock treatment, as identified in ~~Part Three of~~ the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and published on the SVO web page ~~at *https://content.naic.org/industry/securities-valuation-office*~~;

e. Foreign open-end investment funds governed and authorized in accordance with regulations established by the applicable foreign jurisdiction. Other foreign funds are excluded from the scope of this statement; and

f. Equity interests in certified capital companies in accordance with *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)*.

~~5.~~6. Investments within scope of this statement meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted* Assets and are admitted assets to the extent they conform to the requirements of this statement.

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[1] Restricted stock shall be defined as a security for which sale is restricted by governmental or contractual requirement (other than in connection with being pledged as collateral), except where that requirement terminates within one year or if the holder has the power by contract or otherwise to cause the requirement to be met within one year. Any portion of the security that can be reasonably expected to qualify for sale within one year is not considered restricted. Regardless of redemption timeframe, FHLB capital stock is considered restricted stock until actual redemption by the FHLB.

[2] Unless as specifically noted, the equity investments identified within scope are subject to the provisions of this standard as if they were common stock investments.

[3] Non-SEC registered investment companies (e.g., private investment companies or hedge funds) are excluded from the scope of this statement.

[4] Money market mutual funds are considered cash equivalents under SSAP No. 2R.

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Acquisitions and Sales

~~6.~~7. At acquisition, common stocks shall be reported at their cost, including brokerage and other related fees. Common stock acquisitions and dispositions shall be recorded on the trade date. Private placement stock transactions shall be recorded on the funding date. A reporting entity may become qualified for use of equity method accounting by an increase in the level of ownership. In this situation, the reporting entity shall add the cost of acquiring additional interest in the investee to the current basis of the previously held interest and shall apply the equity method, as prescribed in SSAP No. 97, prospectively, as of the date the investment becomes qualified for equity method accounting.

~~7.~~8. A reporting entity can subscribe for the purchase of stock, but not be required to make payment until a later time. Transactions of this nature are common in the formation of corporations. Common stock acquired under a subscription represents a conditional transaction in a security authorized for issuance but not yet actually issued. Such transactions are settled if and when the actual security is issued and the exchange or National Association of Securities Dealers (NASD) rules that the transactions are to be settled. Common stock acquired under a subscription shall be recorded as an admitted asset when the reporting entity or its designated custodian or transfer agent takes delivery of the security and the security is recorded in the name of the reporting entity or its nominee (i.e., the accounting for such common stock acquisitions shall be on the settlement date).

Balance Sheet Amount

~~8.~~9. Investments in scope of this standard shall be reported at fair value. For FHLB capital stock, which is only redeemable at par, the fair value shall be presumed to be par, unless considered other-than-temporarily impaired. Mutual funds, unit-invested funds, and exchange traded funds without a readily determinable fair value are permitted to be reported at net asset value if permitted as a practical expedient pursuant to the guidance in SSAP No. 100R. Closed-end funds are not permitted to be reported at net asset value and shall be reported at fair value. Changes in fair value (or net asset value, as permitted) shall be recorded as unrealized gains or losses.

~~9.~~10. For reporting entities required to maintain an Asset Valuation Reserve (AVR), the accounting for unrealized capital gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities not required to maintain an AVR, unrealized capital gains and losses shall be recorded as a direct credit or charge to surplus.

Impairment

~~10.~~11. For any decline in the fair value of a common stock which is determined to be other than temporary (INT 06-07) the common stock shall be written down to fair value as the new cost basis and the amount of the write down shall be accounted for as a realized loss. For those reporting entities required to maintain an AVR, realized losses shall be accounted for in accordance with SSAP No. 7. Subsequent fluctuations in fair value shall be recorded as unrealized gains or losses. Future declines in fair value which are determined to be other than temporary shall be recorded as realized losses. A decline in fair value which is other than temporary includes situations where a reporting entity has made a decision to sell a security at an amount below its carrying value.

Income

~~11.~~12. Dividends on common stock shall be recorded as investment income on the ex-dividend date with a corresponding receivable to be extinguished upon receipt of cash (i.e., dividend income shall be recorded on stocks declared to be ex-dividends on or prior to the statement date).

~~12.~~13. For reporting entities required to maintain an AVR, the accounting for realized capital gains and losses on sales of common stock shall be in accordance with SSAP No. 7. For reporting entities not required

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to maintain an AVR, realized gains and losses on sales of common stock shall be reported as realized gains/losses in the statement of operations.

Stock Splits, Stock Dividends, Payment in Kind Dividends, and Stock Exchanges

~~13.~~14. Stock splits, stock dividends, payment in kind dividends, and stock exchanges shall be accounted for in accordance with *SSAP No. 95—Nonmonetary Transactions*.

FHLB Capital Stock

~~14.~~15. FHLB capital stock is held by reporting entities that are members of an FHLB. Each reporting entity must acquire FHLB capital stock for membership and maintain capital stock holding sufficient to support its business activity (borrowings[5]) in accordance with the respective FHLB's capital plan. The price of FHLB capital stock cannot fluctuate, and all FHLB capital stock must be purchased, repurchased or transferred at its par value. FHLB capital stock is restricted for redemption in accordance with the FHLB capital plan and shall be coded as restricted within the financial statements (e.g., investment schedules and general interrogatories).

~~15.~~16. Acquisition of FHLB capital stock allows members to conduct business activity (borrowings) from an FHLB. The amount of capital stock acquired determines the reporting entity's eligible borrowing amount. At a minimum, all borrowings from an FHLB (regardless of structure) must also be fully collateralized in accordance with the FHLB capital plan, which determines the amount of collateral required by type of pledged instrument. Collateral pledged to an FHLB shall be coded as restricted within the financial statements (e.g., investments schedules and general interrogatories). Collateral pledged to an FHLB by a reporting entity FHLB member is considered an admitted asset if all of the conditions in paragraphs ~~15~~16.a. through ~~15~~16.d. are met:

a. The asset would have been admitted under SSAP No. 4[6];

b. The pledging insurer continues to receive the income on the pledged collateral;

c. The pledging insurer can remove and substitute other securities with little or advance notice to the FHLB as long as the insurer complies with related investment quality and market value provisions; and

d. There has been no uncured default or event to indicate an impairment or loss contingency for the pledged assets.

~~16.~~17. The guidance in paragraph ~~14~~15 and paragraph ~~15~~16 is specific for reporting entities that are FHLB members. A reporting entity that engages with an FHLB through an "affiliate arrangement" (meaning an affiliate of the reporting entity is the FHLB member), is not considered an FHLB member. In those situations, any FHLB capital stock held by the non-FHLB member reporting entity or collateral pledged to an FHLB on behalf of an affiliate shall be nonadmitted. Detail of the affiliate FHLB arrangement, including any collateral pledged or funds received, shall be captured as a related party transaction (as if the activity occurred directly with the affiliate) under the provisions of *SSAP No. 25—Affiliates and Other Related Parties*.

[5] Membership in an FHLB allows reporting entities to take advances / borrow from the FHLB. These borrowings can be structured in a variety of ways, for example: debt, funding agreements, repurchase agreements, securities lending, etc. Borrowings from an FHLB shall be reflected in the financial statements in accordance with the SSAP that addresses the substance of the agreement.

[6] As detailed in SSAP No. 4, if assets are pledged or otherwise restricted by the action of a related party, the assets are not permitted to be admitted in the statutory financial statements. As such, a reporting entity pledging assets to an FHLB on behalf of an affiliate shall nonadmit the pledged assets.

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Disclosures

~~17.~~18. The following disclosures regarding common stocks shall be made in the financial statements:

a. Basis at which the common stocks are stated; and

b. A description, as well as the amount, of common stock that is restricted outside of FHLB agreements and the nature of the restriction. (Disclosures of FHLB capital stock are captured in paragraph ~~18~~19.)

c. For each balance sheet presented, all common stocks in an unrealized loss position for which other-than-temporary declines in value have not been recognized,

i. The aggregate amount of unrealized losses (that is, the amount by which cost or amortized cost exceeds fair value) and

ii. The aggregate related fair value of common stocks with unrealized losses.

d. The disclosures in (i) and (ii) above should be segregated by those common stocks that have been in a continuous unrealized loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 months or longer using fair values determined in accordance with *SSAP No. 100R—Fair Value*.

e. As of the most recent balance sheet presented, additional information should be included describing the general categories of information that the investor considered in reaching the conclusion that the impairments are not other-than-temporary.

f. When it is not practicable to estimate fair value, the investor should disclose the following additional information, if applicable, as of each date for which a statement of financial position is presented in its annual financial statements:

i. The aggregate carrying value of the investments not evaluated for impairment, and

ii. The circumstances that may have a significant adverse effect on the fair value.

FHLB Disclosures

~~18.~~19. For reporting entity FHLB members, the following information shall be disclosed in the financial statements for current and prior year and between general account and separate account activity. The information in the disclosures shall be presented gross even if a right to offset exists per *SSAP No. 64—Offsetting and Netting of Assets and Liabilities*.

a. General description of FHLB agreements, with information on the nature of the agreement, type of borrowing (advances, lines of credit, borrowed money, etc.) and use of the funding.

b. Amount of FHLB capital stock held, in aggregate, and classified as follows: i) membership stock (separated by Class A and Class B); ii) Activity Stock; and iii) Excess Stock. For membership stock, report the amount of FHLB capital stock eligible for redemption[7] and the anticipated timeframe for redemption: i) less than 6 months, ii) 6 months to 1 year, iii) 1 year to 3 years, and iv) 3 to 5 years.

[7] For FHLB membership stock to be eligible for redemption, written notification must have been provided to the FHLB prior to the reporting date.

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c. Amount (fair value and carrying value) of collateral pledged to the FHLB as of the reporting date. In addition, report the maximum amount of collateral pledged to the FHLB at any time during the current reporting period. (Maximum shall be determined on the basis of carrying value, but with fair value also reported.)

d. Aggregate amount of borrowings at the reporting date from the FHLB, reflecting compilation of all advances, loans, funding agreements, repurchase agreements, securities lending, etc., outstanding with the FHLB, and classify whether the borrowing is in substance: i) debt (*SSAP No. 15—Debt and Holding Company Obligations*), ii) a funding agreement (*SSAP No. 52—Deposit-Type Contracts*), or iii) Other. For funding agreements, report the total reserves established. Report the maximum amount of aggregate borrowings from an FHLB at any time during the current reporting period, the actual or estimated maximum borrowing capacity as determined by the insurer, with a description of how the borrowing capacity was determined, and whether current borrowings are subject to prepayment penalties.

~~19.~~20. The disclosures in paragraphs ~~17~~18.c. through ~~17~~18.f. shall be included in the annual audited statutory financial reports only. The FHLB disclosures in paragraph ~~18~~19 are required in all interim and annual financial statements regardless if the activity is materially different from the activity reported during the prior reporting period. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

~~20.~~21. This statement adopts *ASU 2016-07, Investments - Equity Method and Joint Ventures,* modified to reflect statutory terms including the definition of control and statutory reporting concepts. This statement rejects *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities*, and *ASU 2016-01, Financial Instruments – Overall and FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities*.

Effective Date and Transition

~~21.~~22. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Revisions adopted to this statement in October 2013 amending SSAP No. 15 and SSAP No. 52 to incorporate FHLB disclosure information are initially effective for interim and annual reporting periods after January 1, 2014. Revisions adopted to this statement in November 2018, incorporating closed-end funds and unit-investment trusts within scope, are initially effective January 1, 2019. Revisions adopted in April 2019 to explicitly include foreign registered open-end investment funds in scope are effective January 1, 2019.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*
- NAIC Valuation of Securities product prepared by the Securities Valuation Office

Relevant Issue Papers

- *Issue Paper No. 30—Investments in Common Stock (excluding investments in common stock of subsidiary, controlled, or affiliated entities)*
- *Issue Paper No. 158—Unaffiliated Common Stock*

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Statement of Statutory Accounting Principles No. 32 – Revised

Preferred Stock

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised July 30, 2020
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 164 effective January 1, 2021
Affects	Supersedes SSAP No. 99 with guidance incorporated November 2010; Nullifies and incorporates INT 99-29
Affected by	No other pronouncements
Interpreted by	INT 06-02; INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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EXHIBIT A – GLOSSARY **8**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for preferred stock.

2. Investments in preferred stock of entities captured in *SSAP No. 97—Investments in Subsidiaries, Controlled or Affiliated Entities* or *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability*

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Companies[1] as well as preferred stock interests of certified capital companies per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)* are included within the scope of this statement. The requirement to file investments in preferred stock of certain subsidiaries, controlled or affiliated entities with the NAIC pursuant to SSAP No. 97 does not affect the application of the accounting, valuation or admissibility under this statement. In addition to the provisions of this statement, preferred stock investments in SCAs are also subject to the provisions of *SSAP No. 25—Affiliates and Other Related Parties* and *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

3. Investments in the form of preferred stock that are in substance residual interests or a residual security tranche, as defined in *SSAP No. 43R—Loan-Backed and Structured Securities* or *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, shall be reported on Schedule BA: Other Long-Term Assets in the dedicated reporting lines for residuals.

SUMMARY CONCLUSION

~~3.~~4. Preferred stock which may or may not be publicly traded is a security that represents ownership of a corporation and gives the holder a claim prior to the claim of common stockholders on earnings and also generally on assets in the event of liquidation. Most preferred stock pays a fixed dividend that is paid prior to the common stock dividend, stated in a dollar amount or as a percentage of par value. Preferred stock does not usually carry voting rights. Preferred stock has characteristics of both common stock and debt. Preferred stock shall include:

a. Redeemable preferred stock, which is preferred stock subject to mandatory redemption requirements or whose redemption is at the option of the holders. Redeemable preferred stock is any stock which 1) the issuer undertakes to redeem at a fixed or determinable price on the fixed or determinable date or dates, whether by operation of a sinking fund or otherwise; or 2) is redeemable at the option of the holders. Preferred stock which meet one or more of these criteria would be classified as redeemable preferred stock,[2] regardless of other attributes such as voting rights or dividend rights.

b. Perpetual preferred stock, which is preferred stocks which are not redeemable or for which redemption is not at the option of the holder (non-redeemable preferred stock). Perpetual preferred stock is any preferred stock which does not meet the criteria to be classified as redeemable preferred stock pursuant to paragraph ~~3~~4.a.

c. Publicly traded preferred stock warrants.

~~4.~~5. The definition of preferred stock, as defined in paragraph ~~3~~4, does not include fund investments. However, the following types of SVO-identified investments are captured within scope of this statement.

a. Exchange Traded Funds, which qualify for preferred stock treatment, as identified in ~~Part Three of~~ the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and published on the SVO web page ~~at *https://content.naic.org/industry/securities-valuation-office*~~. SVO-identified preferred stock ETFs shall follow the accounting provisions for perpetual preferred stock.

[1] Certain legal entities captured in SSAP No. 48, such as LLCs that are corporate-like, do not issue preferred stock in legal form, but instead issue identical instruments labeled preferred units, interests, or shares. These instruments shall be captured in this statement provided they meet the structural characteristics as defined in paragraph ~~3~~4. Additionally, these instruments shall not be in-substance common stock in which the holder has risk and reward characteristics that are substantially similar to common stock.

[2] Preferred stock shall be classified by its characteristics. For example, a preferred stock that is named "redeemable perpetual preferred stock" shall be reported as either "redeemable" or "perpetual" preferred stock based on whether the characteristics of paragraph ~~3~~4.a. are met.

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~~5.~~6. Restricted preferred stock is defined[3] as either redeemable or perpetual preferred stock that must be traded in compliance with special Securities Exchange Commission (SEC) regulations concerning its purchase and resale. These restrictions generally result from affiliate ownership, merger and acquisition (M&A) activity and underwriting activity. Pursuant to the SEC, restricted securities are securities acquired in an unregistered, private sale from the issuing company or from an affiliate of the issuer. They typically bear a "restrictive" legend clearly stating that the holding may not resell the stock in the public marketplace unless the sale is exempt from the SEC's registration requirements. Restricted preferred stock is generally considered an admitted asset; however, admittance may be limited based on the degree of restriction in accordance with *SSAP No. 4—Assets and Nonadmitted Assets*. Restricted preferred stock shall be coded as restricted in the investment schedule and disclosed pursuant to *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures.*

~~6.~~7. Preferred stocks meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement, SSAP No. 25 and SSAP No. 97.

Acquisitions and Sales

~~7.~~8. At acquisition, preferred stock shall be reported at cost, including brokerage and other related fees. Preferred stock received as dividends shall be recorded at fair value. Acquisitions and dispositions shall be recorded on the trade date. Private placement stock transactions shall be recorded on the funding date.

~~8.~~9. A reporting entity can subscribe for the purchase of stock, but not be required to make payment until a later time. Transactions of this nature are common in the formation of corporations. Preferred stock acquired under a subscription represents a conditional transaction in which preferred stock is authorized for issuance but not yet actually issued. Such transactions are settled if and when the actual preferred stock is issued and the exchange or National Association of Securities Dealers (NASD) rules that the transactions are to be settled. Preferred stock acquired under a subscription shall be recorded as an admitted asset when the reporting entity or its designated custodian or transfer agent takes delivery of the preferred stock and the preferred stock is recorded in the name of the reporting entity or its nominee, (i.e., the accounting for such preferred stock acquisitions shall be on the settlement date).

Amortization

~~9.~~10. Redeemable preferred stock purchased at a premium shall be amortized to reduce the carrying value to the call or redemption value over the period to the call or earliest redemption date, whichever produces the lowest asset value (yield to worst). Redeemable preferred stock purchased at a discount shall be accreted to increase the carrying value to the redemption price over the period to maturity or the latest redemption date.

~~10.~~11. Amortization (and accretion) of the premium and discount arising at acquisition shall be calculated using the interest method and shall be reported through investment income.

[3] This definition of restricted stock does not preclude a "restricted asset" classification for any preferred stock that is restricted (e.g., not under the exclusive control of the entity) by actions of the reporting entity or others. For example, if a reporting entity has pledged preferred stock, or used preferred stock in securities lending / repo transactions, the preferred stock shall be coded and disclosed as restricted stock pursuant to *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures.*

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Balance Sheet Amount

~~11.~~12. Preferred stock shall be valued based on (a) the underlying characteristics (redeemable, perpetual or mandatory convertible), (b) the quality rating expressed as an NAIC designation, and (c) whether an asset valuation reserve (AVR) is maintained by the reporting entity[4]:

a. For reporting entities that do not maintain an AVR:

i. Highest-quality or high-quality redeemable preferred stocks (NAIC designations 1 and 2) shall be valued at amortized cost. All other redeemable preferred stocks (NAIC designations 3 to 6) shall be reported at the lower of amortized cost or fair value.

ii. Perpetual preferred stock and publicly traded preferred stock warrants shall be reported at fair value, not to exceed any currently effective call price.

iii. Mandatory convertible preferred stocks (regardless if the preferred stock is redeemable or perpetual) shall be reported at fair value, not to exceed any currently effective call price, in the periods prior to conversion. Upon conversion to common stock, these securities shall be in scope of SSAP No. 30R.

iv. For preferred stocks reported at fair value, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

b. For reporting entities that maintain an AVR:

i. Highest-quality, high-quality or medium quality redeemable preferred stocks (NAIC designations 1 to 3) shall be valued at amortized cost. All other redeemable preferred stocks (NAIC designations 4 to 6) shall be reported at the lower of amortized cost or fair value.

ii. Perpetual preferred stock and publicly preferred stock warrants shall be valued at fair value, not to exceed any currently effective call price.

iii. Mandatory convertible preferred stocks (regardless if the preferred stock is redeemable or perpetual) shall be reported at fair value, not to exceed any currently effective call price, in the periods prior to conversion. Upon conversion to common stock, these securities shall be in scope of SSAP No. 30R.

iv. For preferred stocks reported at fair value, the accounting for unrealized gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve.*

Impairment of Redeemable Preferred Stock

~~12.~~13. An other-than-temporary(INT 06-07) impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of the preferred stock in effect at the date of acquisition. An assessment of other-than-temporary impairment shall occur whenever mandatory redemption rights or sinking fund requirements do not occur. A decline in fair value which is other-than-temporary includes situations where the reporting entity has made a decision to sell the preferred stock prior to its maturity at an amount below its carrying value (i.e., amortized cost). If

[4] In all situations noted in this statement in which the fair value is limited to the currently effective call price, this limitation only applies when the call is 1) currently exercisable by the issuer, or 2) the issuer has announced that the instruments will be redeemed/called.

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it is determined that a decline in the fair value of a redeemable preferred stock is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the entire difference between the redeemable preferred stock's carrying value and its fair value, not to exceed any currently effective call price, at the balance sheet date of the reporting period for which the assessment is made. The measurement of the impairment loss shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR, realized losses shall be accounted for in accordance with SSAP No. 7.

~~13.~~14. In periods subsequent to the recognition of other-than-temporary impairment loss for a redeemable preferred stock, the reporting entity shall account for the other-than-temporarily impaired preferred stock as if the preferred stock had been purchased on the measurement date of the other-than-temporary impairment. The fair value of the redeemable preferred stock on the other-than-temporary impairment measurement date shall become the new cost basis of the redeemable preferred stock and the new cost basis shall not be adjusted for subsequent recoveries in fair value. The discount or reduced premium recorded for the preferred stock, based on the new cost basis, shall be amortized over the remaining life of the preferred stock in the prospective manner based on the amount and timing of future estimated cash flows. The preferred stock shall continue to be subject to impairment analysis for each subsequent reporting period. Future declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses.

Impairment of Perpetual Preferred Stock

~~14.~~15. For any decline in the fair value of perpetual preferred stock or publicly traded preferred stock warrants, which is determined to be other-than-temporary (INT 06-07), the perpetual preferred stock or warrant shall be written down to fair value as the new cost basis and the amount of the write down shall be accounted for as a realized loss. For reporting entities required to maintain an AVR, realized losses shall be accounted for in accordance with SSAP No. 7. Subsequent fluctuations in fair value shall be recorded as unrealized gains or losses. Future declines, which are determined to be other-than-temporary, shall be recognized as realized losses. A decline in fair value which is other-than-temporary includes situations where the reporting entity has made a decision to sell a preferred stock at an amount below its carrying value.

Income

~~15.~~16. Dividends on preferred stock shall be recorded as investment income for dividend-eligible preferred stock on the ex-dividend date with a corresponding receivable to be extinguished upon dividend settlement. Dividends received shall be recognized in the form received (e.g., cash, preferred stock, common stock) at fair value with differences between fair value and the dividend receivable recognized as gains or losses. Subsequent treatment shall follow the statement that addresses the type of asset received. For example, dividends received in the form of common stock shall be accounted for and reported in accordance with SSAP No. 30R.

Redemption of Preferred Stock

~~16.~~17. A reporting entity that sells or redeems preferred stock back to the issuer shall recognize consideration received in excess of the book/adjusted carrying value as a realized gain or loss. This recognition shall occur regardless of whether the issuer repurchases the preferred shares at market value, or if the shares are redeemed by the issuer at a predetermined set call price.

Exchanges and Conversions

~~17.~~18. If preferred stock is exchanged or converted into other securities, the fair value of the preferred stock surrendered at the date of the exchange or conversion shall become the cost basis for the new securities with any gain or loss realized at the time of the exchange or conversion. However, if the fair value of the

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securities received in an exchange or conversion is more clearly evident than the fair value of the preferred stock surrendered, then it shall become the cost basis for the new securities.

Disclosures

~~18.~~19. The following disclosures regarding preferred stocks shall be made in the financial statements:

a. Fair values in accordance with *SSAP No. 100R—Fair Value*;

b. Concentrations of credit risk in accordance with SSAP No. 27;

c. Basis at which the preferred stocks are stated, and

d. A description as well as the amount of preferred stock that is restricted and the nature of the restriction.

e. For each balance sheet presented, all preferred stocks in an unrealized loss position for which other-than-temporary declines in value have not been recognized:

i. The aggregate amount of unrealized losses (that is, the amount by which cost or amortized cost exceeds fair value), and

ii. The aggregate related fair value of preferred stocks with unrealized losses.

f. The disclosures in (i) and (ii) above should be segregated by those preferred stocks that have been in a continuous unrealized loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 months or longer using fair values determined in accordance with SSAP No. 100R.

g. As of the date of the most recent balance sheet presented, additional information should be included describing the general categories of information that the investor considered in reaching the conclusion that the impairments are not other-than-temporary.

h. When it is not practicable to estimate fair value, the investor should disclose the following additional information, if applicable, as of each date for which a statement of financial position is presented in its annual financial statements:

i. The aggregate carrying value of the investments not evaluated for impairment, and

ii. The circumstances that may have a significant adverse effect on the fair value.

~~19.~~20. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosure requirements of paragraphs ~~18~~19.b., ~~18~~19.e., ~~18~~19.f., ~~18~~19.g. and ~~18~~19.h. shall be included in the annual audited statutory financial reports only.

Relevant Literature

~~20.~~21. This statement rejects *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial* Liabilities*, ASU 2016-01, Financial Instruments – Overall, FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities* and *FASB Emerging Issues Task Force No. 86-32, Early Extinguishment of a Subsidiary's Mandatorily Redeemable Preferred Stock*. This statement adopts *FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,* paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. Effective December 31, 2023, this statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial

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Instruments, *ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~21.~~22. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* The guidance in paragraphs ~~23~~24-~~26~~27 was previously included within *SSAP No. 99—Accounting for Securities Subsequent to an Other-Than-Temporary Impairment* and was effective for reporting periods beginning on January 1, 2009, and thereafter, with early adoption permitted. In 2010, the guidance from SSAP No. 99 was incorporated within the impacted standards, with SSAP No. 99 superseded. The original impairment guidance included in this standard, and the substantive revisions reflected in SSAP No. 99 are retained for historical purposes within Issue Paper No. 131. The guidance in paragraphs 2 and ~~3~~4 to SSAP No. 32 was originally superseded January 1, 2005, by guidance included in *SSAP No. 88—Investments in Subsidiaries, Controlled and Affiliated Entities, A replacement of SSAP No. 46*, and then subsequently reflected in SSAP No. 97. In 2011, the guidance related to preferred stock of SCAs from SSAP No. 97 was incorporated into this statement and revised to reflect a definition of preferred stock. The original guidance included in this statement, and the substantive revisions reflected in SSAP No. 88 and SSAP No. 97 (including the title change already reflected in SSAP No. 32) are retained for historical purposes within Issue Paper Nos. 32 and 118. Guidance in paragraph ~~17~~18 was originally contained in *INT 99-29: Classification of Step-Up Preferred Stock* and was effective December 6, 1999.

~~22.~~23. On July 30, 2020, substantive revisions, as detailed in *Issue Paper No. 164—Preferred Stock* were adopted. These revisions update definitions of preferred stock and reporting values based on characteristics of the preferred stock and are effective January 1, 2021, with early adoption permitted.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*
- NAIC Valuation of Securities product prepared by the Securities Valuation Office

Relevant Issue Papers

- *Issue Paper No. 32—Investments in Preferred Stock (excluding investments in preferred stock of subsidiary, controlled, or affiliated companies)*
- *Issue Paper No. 131—Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment*
- *Issue Paper No. 164—Preferred Stock*

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EXHIBIT A – GLOSSARY

Callable Preferred Stock – A preferred stock in which the issuer has the right to call or redeem the stock at a preset price after a defined date. Callable preferred stock can be either redeemable preferred stock or perpetual preferred stock depending on other characteristics of the preferred stock. For example, callable preferred stock with a maturity or a specific buyback date would be redeemable preferred stock, whereas callable preferred stock electable at the discretion of the issuer is perpetual preferred stock.

Convertible Preferred Stock – A preferred stock that is convertible into another security based on a conversion rate. For example, convertible preferred stock that is convertible into common stock on a two-for-one basis (two shares of common for each share of preferred).

Cumulative Preferred Stock – A preferred stock with a provision that missed dividend payments must be paid to cumulative preferred shareholders before other classes of preferred stock shareholders and common shareholders can receive dividend payments. Cumulative preferred stock may have different levels, with a "first" or "senior" cumulative preferred, "regular" cumulative preferred and "subordinate" cumulative preferred that determines the priority in which accumulated unpaid dividends or asset liquidation occurs. (Under SSAP No. 32R, holders of cumulative preferred stock are not permitted to recognize a receivable for unpaid cumulative dividends until declared and the reporting entity is entitled to the divided.)

Dividend Declaration Date – The date a corporation declares a dividend payment to its shareholders.

Dividend Record Date – The date that identifies the shareholders that are entitled to a declared dividend.

Dividend Payment Date – The date the declared dividend will be paid.

Ex-Dividend Date – The cut-off date of holding stock to be captured as a shareholder on record entitled to the dividend. (A shareholder that sells their stock on the ex-dividend date would continue to be identified as a shareholder on record entitled to a declared dividend. Anyone who acquires a stock on the ex-dividend date would not be a shareholder on record entitled to a declared dividend.)

Mandatory Redeemable Preferred Stock – A preferred stock that embodies an unconditional obligation requiring the issuer to redeem the instrument by transferring its assets at a specified or determinable date (or dates) or upon an event that is certain to occur. (The existence of a mandatory redemption right does not convert the holder of a preferred stock into a creditor, and an issuer may be prohibited from redeeming shares when redemption would cause an impairment of capital.)

Noncumulative Preferred Stock – A preferred stock that does not entitle the stockholder to accumulated unpaid dividends. After missing dividend payments, a corporation only has to be make current dividend payments to preferred stock holders before providing dividends to common stock holders.

Participating Preferred Stock – A preferred stock that gives the holder participation in the additional earnings of a business or liquidation rights in addition to the normal preferred stock dividend. Pursuant to the terms of the preferred stock, the participation rights may only be activated when income or operations of the issuer exceeds a certain threshold level.

Payment-in-kind (PIK) – A term of the preferred stock prospectus that identifies that dividends may take the form of securities (e.g., common stock) rather than cash.

Perpetual Preferred Stock - Preferred stocks which are not redeemable or are redeemable solely at the option of the issuer. Perpetual preferred stock is any preferred stock which does not meet the criteria to be classified as redeemable preferred stock.

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Preferred stock - A security, which may or may not be publicly traded, that shows ownership of a corporation and gives the holder a claim, prior to the claim of common stockholders on earnings and also generally on assets in the event of liquidation.

Redeemable Preferred Stock - Preferred stock subject to mandatory redemption requirements or whose redemption is outside the control of the issuer. Redeemable preferred stock is any stock which 1) the issuer undertakes to redeem at a fixed or determinable price on the fixed or determinable date or dates, whether by operation of a sinking fund or otherwise; 2) is redeemable at the option of the holders; or 3) has conditions for redemption which are not solely within the control of the issuer, such as stock which must be redeemed out of future earnings. Preferred stock which meet one or more of these three criteria is redeemable preferred stock regardless of other attributes such as voting rights or dividend rights.

Restricted Preferred Stock - Redeemable or perpetual preferred stock that must be traded in compliance with special SEC regulations concerning its purchase and resale. These restrictions generally result from affiliate ownership, M&A activity and underwriting activity. Pursuant to the SEC, restricted securities are securities acquired in an unregistered, private sale from the issuing company or from an affiliate of the issuer. They typically bear a "restrictive" legend clearly stating that the holding may not resell the stock in the public marketplace unless the sale is exempt from the SEC's registration requirements.

Sinking Fund – A potential component of a preferred stock charter that requires the issuer to regularly set funds aside in a separate custodial account for the exclusive purpose of redeeming preferred stock shares. Failure of an issuer to provide to the sinking fund does not create an act of default. Rather, the stock charter may implement provisions for failing to provide to the sinking fund, which could include penalties, restrictions of providing common stock dividends or the repurchase of the preferred stock.

Step-Up Preferred Stock – A potential component of a preferred stock charter that identifies whether specific terms will increase over time or with stated provisions. For example, a "step-up dividend" is a feature that increases the dividend rate. A "step-up call" is a feature that increases the call price. A "step-up conversion" increases the conversion price.

Term Preferred Stock – Preferred stock with a mandatory redemption requirement (maturity date) captured in the definition of redeemable preferred stock.

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Statement of Statutory Accounting Principles No. 34

Investment Income Due and Accrued

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 99 with guidance incorporated November 2010
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 2

Effective Date and Transition 2

REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investment income due and accrued.

SUMMARY CONCLUSION

2. Investment income due shall be defined as investment income earned and legally due to be paid to the reporting entity (i.e., receivable) as of the reporting date. Investment income accrued shall be defined as investment income earned as of the reporting date but not legally due to be paid to the reporting entity until subsequent to the reporting date.

3. In general, gross investment income shall be recorded as earned and shall include investment income collected during the period, the change in investment income due and accrued, the change in unearned investment income plus any amortization (e.g., discounts or premiums on bonds, origination fees on mortgage loans, etc.) Immediate amortization of premium which occurs upon recognition of an other-than-temporary impairment loss for a debt security with a recorded premium shall be reported as a realized loss and shall not be included in investment income.

4. Investment income due and accrued shall be recorded as an asset in accordance with *SSAP No. 4—Assets and Nonadmitted Assets*. An evaluation shall be made of such assets in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, to determine whether an impairment exists. Amounts determined to be uncollectible shall be written off through the statement of operations. Then an evaluation shall be made to determine nonadmitted amounts.

5. This two-step process is set forth below.

a. Investment income due and accrued shall be assessed for collectibility. If, in accordance with SSAP No. 5R, it is probable the investment income due and accrued balance is uncollectible, the amount shall be written off and shall be charged against investment income in the period such determination is made;

b. Any remaining investment income due and accrued (i.e., amounts considered probable of collection) representing either (1) amounts that are over 90 days past due (generated by any invested asset except mortgage loans in default), or (2) amounts designated elsewhere in the *Accounting Practices and Procedures Manual* as nonadmitted shall be considered nonadmitted assets and recognized through a direct charge to surplus in accordance with SSAP No. 4. These nonadmitted amounts shall be subject to continuing assessments of collectibility and, if determined to be uncollectible, a write-off shall be recorded in the period such determination is made in accordance with paragraph 5.a.

6. Accrued interest on mortgage loans that are in default (as defined in *SSAP No. 37—Mortgage Loans*) shall be recorded as Investment Income Due and Accrued when such interest is deemed collectible. Interest can be accrued on mortgage loans in default if deemed collectible; if interest is deemed uncollectible, it shall not be accrued and any previously accrued amounts are to be written off in accordance with the guidelines in paragraph 5.a. If a mortgage loan in default has interest 180 days past due which has been assessed as collectible, all interest shall be considered a nonadmitted asset and recognized through a direct charge to surplus as outlined in paragraph 5.b.

Disclosures

7. The following disclosures shall be made for investment income due and accrued in the financial statements. (SSAP No. 37 captures disclosures for mortgage loans on nonaccrual status pursuant to paragraph 6.)

a. The bases by category of investment income for excluding (nonadmitting) any investment income due and accrued;

b. Disclose total amount excluded;

c. Disclose the gross, nonadmitted and admitted amounts for interest income due and accrued;

d. Disclose aggregate deferred interest;

e. Disclose cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance/par value.[1]

8. Refer to the Preamble for further discussion regarding disclosure requirements.

Effective Date and Transition

9. This statement adopts *FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,* paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. Effective December 31, 2023,

[1] In disclosing the cumulative amount of PIK interest, identify the specific amounts of PIK interest by lot and aggregate the amounts by CUSIP/PPN that have a net increase to the original par value. The net increase includes PIK interest added to the par value less disposals (i.e., repayments; sales) that are first applied to any PIK interest outstanding. As a practical expedient, an insurer may calculate the cumulative amount of PIK interest on a bond by subtracting the original principal/par value from the current principal/par value, but not less than $0.

this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

10. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* The guidance in paragraph 3 was previously included within *SSAP No. 99—Accounting for Securities Subsequent to an Other-Than-Temporary Impairment* and was effective for reporting periods beginning on January 1, 2009, and thereafter, with early adoption permitted. In 2010, the guidance from SSAP No. 99 was incorporated within the impacted standards, with SSAP No. 99 superseded. The original paragraph 3 guidance from this standard, and the substantive revisions reflected in SSAP No. 99 are retained for historical purposes within Issue Paper No. 131.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 34—Investment Income Due and Accrued*
- *Issue Paper No. 131—Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment*

Statement of Statutory Accounting Principles No. 35 – Revised

Guaranty Fund and Other Assessments

STATUS

Type of Issue	Common Area
Issued	Finalized March 13, 2000; Substantively revised October 18, 2010, December 15, 2013, June 12, 2014, and December 10, 2016
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 143R effective January 1, 2011, with additional revisions effective January 1, 2017
Affects	Nullifies INT 03-01; Nullifies and incorporates INT 07-03
Affected by	No other pronouncements
Interpreted by	INT 02-22
Relevant Appendix A Guidance	A-010; A-820

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

Reporting Assets for Premium Tax Offsets and Policy Surcharges 3
Discounting of Liabilities and Assets Related to Long-Term Care Assessments 4
Acting as an Agent for Collection and Remittance of Fees and Assessments 5
Applying the Recognition Criteria 6
Disclosures 7
Relevant Literature 8
Effective Date and Transition 9

REFERENCES **9**

Relevant Issue Papers 9

EXHIBIT A – PRIMARY METHODS OF GUARANTY FUND ASSESSMENTS **10**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for guaranty fund and other assessments.

2. Guaranty fund assessments represent a funding mechanism employed by states to provide funds to cover policyholder obligations of insolvent reporting entities. Most states have enacted legislation establishing guaranty funds for both life and health insurance and for property and casualty insurance to provide for covered claims or to meet other insurance obligations of insolvent reporting entities in the state.

3. This statement addresses other assessments including but not limited to workers' compensation second injury funds and for funds that pay operating costs of an insurance department, a state guaranty

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fund, and/or the workers' compensation board. This statement also addresses health related assessments including but not limited to state health insurance high-risk pools, health insurance small group and individual reinsurance pools, state health demographic and risk adjustment assessments. Guidance regarding the Affordable Care Act Section 9010 assessment is provided in *SSAP No. 106—Affordable Care Act Section 9010 Assessment*.

SUMMARY CONCLUSION

4. This statement adopts with modification guidance from *Accounting Standard Codification 405-30,* Insurance-*Related Assessments* (ASC 405-30) as reflected within this SSAP. Consistent with ASC 405-30-25-1, entities subject to assessments shall recognize liabilities for insurance-related assessments when all of the following conditions are met (paragraph 17 provides guidance on applying the recognition criteria):

a. An assessment has been imposed or information available prior to issuance of the statutory financial statements indicates that it is probable that an assessment will be imposed.

b. The event obligating an entity to pay an imposed or probable assessment has occurred on or before the date of the financial statements.

c. The amount of the assessment can be reasonably estimated.

Guaranty fund and other assessments shall be charged to expense (Taxes, Licenses and Fees) and a liability shall be accrued when the above criteria are met except for certain health related assessments which shall be reported as a part of claims. Health related assessments that are reported as a part of claims instead of taxes, licenses and fees are those assessments that are designed for the purpose of spreading the risk of severe claims or adverse enrollment selection among all participating entities, and where the funds collected via the assessment are re-distributed back to the participating entities based upon the cost of specific claims, enrollment demographics, or other criteria affecting health care expenses. This standard does not permit liabilities for guaranty funds or other assessments to be discounted, except for liabilities for guaranty funds and the related assets recognized from accrued and paid liability assessments from insolvencies of entities that wrote long-term care contracts (see paragraphs 12-14).

5. For refunded guaranty or other fund assessments and assessments used to fund state operating expenses, reporting entities shall credit the refund or charge the assessment to expense when notification of the refund or assessment is made.

6. For premium-based guaranty fund assessments, except those that are prefunded, paragraph 4.a. is met when the insolvency has occurred. For purposes of applying this guidance, the insolvency shall be considered to have occurred when a reporting entity meets a state's (ordinarily the state of domicile of the insolvent reporting entity) statutory definition of an insolvent reporting entity. In most states, the reporting entity must be declared to be financially insolvent by a court of competent jurisdiction. In some states, there must also be a final order of liquidation. Prefunded guaranty-fund assessments and premium-based administrative type assessment are presumed probable when the premiums on which the assessments are expected to be based are written. Loss-based administrative-type and second injury fund assessments are presumed probable when the losses on which the assessments are expected to be based are incurred.

7. Paragraph 4.b. requires that the event obligating an entity to pay an imposed or probable assessment has occurred on or before the date of the financial statements. Based on the fundamental differences in how assessment mechanisms operate, the event that makes an assessment probable (for example, an insolvency) may not be the event that obligates an entity. The following defines the event that obligates an entity to pay an assessment:

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a. For premium-based assessments, the event that obligates the entity is generally writing the premiums or becoming obligated to write or renew (such as multiple-year, noncancelable policies) the premiums on which the assessments are expected to be based. Some states, through law or regulatory practice, provide that an insurance entity cannot avoid paying a particular assessment even if that insurance entity reduces its premium writing in the future. In such circumstances, the event that obligates the entity is a formal determination of insolvency or similar triggering event. For example, in certain states, an insurance entity may remain liable for assessments even though the insurance entity discontinues the writing of premiums. In this circumstance, the underlying cause of the liability is not the writing of the premium, but the insolvency. Regulatory practice would be determined based on the stated intentions or prior history of the insurance regulators.

b. For loss-based assessments, the event that obligates an entity is an entity's incurring the losses on which the assessments are expected to be based.

8. Paragraph 4.c. requires that the amounts can be reasonably estimated. For retrospective-premium-based guaranty fund assessments, a reporting entity's estimate of the liability shall reflect an estimate of its share of the ultimate loss expected from the insolvency. The reporting entity shall also estimate any applicable premium tax credits and policy surcharges. An entity need not be able to compute the exact amounts of the assessments or be formally notified of such assessments by a guaranty fund to make a reasonable estimate of its liability. Entities subject to assessments may have to make assumptions about future events, such as when the fund making the assessment will incur costs and pay claims to determine the amounts and the timing of assessments. The best available information about market share or premiums by state and premiums by line of business generally should be used to estimate the amount of future assessments. Estimates of loss-based assessments should be consistent with estimates of the underlying incurred losses and should be developed based upon enacted laws or regulations and expected assessment rates. Premium tax credits or policy surcharges may only be considered in the estimate if it is probable they will be realized. Because of the uncertainties surrounding some insurance-related assessments, the range of assessment liability may have to be re-evaluated regularly during the assessment process. Changes in the amount of the liability (or asset) as information becomes available over time and revisions to estimates in the amount or timing of the payments shall be recorded in taxes, licenses and fees.

9. In accordance with SSAP No. 5R, when the reasonable estimate of the loss is a range, the amount in the range that is considered the best estimate shall be accrued. When, in management's opinion, no amount within management's estimate of the range is a better estimate than any other amount, however, the midpoint (mean) of management's estimate in the range shall be accrued. For purposes of this statement, it is assumed that management can quantify the high end of the range. If management determines that the high end of the range cannot be quantified, then a range does not exist, and management's best estimate shall be accrued.

Reporting Assets for Premium Tax Offsets and Policy Surcharges

10. The liability for accrued assessments shall be established gross of any probable and estimable recoveries from premium tax credits and premium surcharges. When it is probable that a paid or accrued assessment will result in an amount that is recoverable from premium tax offsets or policy surcharges, an asset shall be recognized for that recovery in an amount that is determined based on current laws, projections of future premium collections or policy surcharges from in-force policies, and as permitted in accordance with paragraphs 10.a., 10.b. and 10.c. Assets recognized from paid and accrued guaranty fund (or other) liability assessments from insolvencies of entities that primarily wrote long-term care are also subject to the discounting requirements in paragraphs 12-14. Any recognized asset from premium tax credits or policy surcharges shall be re-evaluated regularly to ensure recoverability. Upon expiration, tax credits no longer meet the definition of an asset and shall be written off.

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a. For assessments paid before premium tax credits are realized or policy surcharges are collected, an asset results, which represents a receivable for premium tax credits that will be taken and policy surcharges which will be collected in the future. These receivables, to the extent it is probable they will be realized, meet the definition of assets, as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement. The asset shall be established and reported independent from the liability (not reported net).

b. Assets recognized from accrued liability assessments shall be determined in accordance with the type of guaranty fund assessment as detailed in the following subparagraphs. Assets recognized from accrued liability assessments meet the definition of an asset under SSAP No. 4, and are admitted assets to the extent they conform to the requirements of this statement.

i. For retrospective-premium-based and loss-based assessments, to the extent that it is probable that accrued liability assessments will result in a recoverable amount in a future period from business currently in-force considering appropriate persistency rates for long-duration contracts, an asset shall be recognized at the time the liability is recorded. In-force policies do not include expected renewals of short-term contracts except in cases when retrospective-premium-based assessments are imposed on short-term health contracts for the insolvencies of insurers that wrote long-term care contracts. In which case, to the extent that it is probable that premium tax credits from accrued liability assessments will result in a recoverable amount in a future period from business currently in force, appropriate renewal rates of short-term health contracts shall be taken into consideration when recognizing the asset.

ii. For prospective-premium-based assessments, the recognition of assets from accrued liability assessments is limited to the amount of premium an entity has written or is obligated to write and to the amounts recoverable over the life of the in-force policies. This SSAP requires reporting entities to recognize prospective-based-premium assessments as the premium is written or obligated to be written by the reporting entity. Accordingly, the expected premium tax offset or policy surcharge asset related to the accrual of prospective-premium-based assessments shall be based on and limited to the amount recoverable as a result of premiums the insurer has written or is obligated to write.

c. An asset shall not be established for paid or accrued assessments that are recoverable through future premium rate structures.

11. An evaluation of assets recognized under paragraph 10 shall be made in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* to determine if there is any impairment. If, in accordance with SSAP No. 5R, it is probable that the asset is no longer realizable, the asset shall be written off to the extent it is not realizable and charged to income in the period the determination is made. Considering expected future premiums other than on in-force policies for long duration contracts in evaluating recoverability of premium tax offsets or policy surcharges is not permitted. For short-term health contracts subject to long-term care assessments, appropriate renewal rates may be considered in evaluating recoverability of premium tax offsets or policy surcharges.

Discounting of Liabilities and Assets Related to Long-Term Care Assessments

12. Liabilities – Liabilities from guaranty funds or other assessments from the insolvencies of entities that wrote long-term care contracts that extend in excess of one year to payment shall be discounted as

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prescribed in paragraph 14. If the liability amount is prefunded in full in the year of the insolvency, it is not to be discounted. Because requirements for payments vary by jurisdiction, the discount period, based on the expected dates for payment, shall be determined on the basis of jurisdiction.

13. Assets – Discounting of premium tax credit assets recognized from accrued and paid long-term care assessments is required for assets as prescribed in paragraph 14 when the time to forecasted recoverability is in excess of one year. Discounting premium tax credit assets is required if recoverability exceeds one year, even in instances when the related liability is not discounted. Because of variations in the recoverability of tax credits, determination of the time to recoverability for application of the discount period shall be on the basis of jurisdiction.

14. Discount Rate – The following discount rate shall be applied to the assets and liabilities that are to be discounted pursuant to paragraphs 12 and 13:

a. The discount rate to be applied is the maximum valuation interest rate for whole life policies that is detailed in Appendix A-820, paragraphs 7.a., 8.a. and 9.a. This discount rate is the rate referenced by Appendix A-010, Exhibit I, paragraph 3, as the maximum allowed interest rate for contract reserves.

b. Appendix A-820 applies a rate that is determined at the date of policy issuance. For purposes of discounting the long-term care guaranty fund assessments and related assets, the discount rate applied to balances expected to be settled in excess of one year (paid or recovered), shall be the maximum valuation interest rate for whole life policies (specified in Appendix A-820) in effect for the reporting date. With this guidance, the discount rate is updated annually as the specified whole-life discount rate is updated and the same rate is applied to all discounted insolvencies.

Acting as an Agent for Collection and Remittance of Fees and Assessments

15. In certain circumstances, a reporting entity acts as an agent for certain state or federal agencies in the collection and remittance of fees or assessments. In these circumstances, the liability for the fees and assessments rests with the policyholder rather than with the reporting entity. The reporting entity's obligation is to collect and subsequently remit the fee or assessment.(INT 02-22) When both the following conditions are met, an assessment shall not be reported in the statement of operations of a reporting entity:

a. The assessment is reflected as a separately identifiable item on the billing to the policyholder; and

b. Remittance of the assessment by the reporting entity to the state or federal agency is contingent upon collection from the insured.

16. The impact to the statement of operations depends on the nature of the charge:

a. For charges which are the ultimate responsibility of the policyholder, follow existing guidance in paragraph 15, and pass these charges and recoveries through the balance sheet with no impact to the statement of operations.

b. For charges which are the ultimate responsibility of the reporting entity and may be recovered all or in part, apply gross or net reporting in the statement of operations as appropriate based on the nature of the charge and recovery. For example, charges which are considered in rate development or for which the recovery is classified as premium should be reported gross, charges for which recovery is considered a reduction of the expense should be reported net.

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c. For collection or administrative fees, report such fees as revenue in the statement of operations as "Finance and Service Charges Not Included in Premiums" or "Aggregate Write-Ins for Miscellaneous Income".

Applying the Recognition Criteria

17. Application of the recognition criteria in paragraph 4:

a. *Retrospective-premium-based guaranty-fund assessments* - An assessment is probable of being imposed when a formal determination of insolvency occurs[1]. At that time, the premium that obligates the entity for the assessment liability has already been written. Accordingly, an entity that has the ability to reasonably estimate the amount of the assessment shall recognize a liability for the entire amount of future assessments related to a particular insolvency when a formal determination of insolvency is rendered.

b. *Prospective-premium-based guaranty-fund assessments* - The event that obligates the entity for the assessment liability generally is the writing of, or becoming obligated to write or renew, the premiums on which the expected future assessments are to be based (for example, multiple-year contracts under which an insurance entity has no discretion to avoid writing future premiums). Therefore, the event that obligates the entity generally will not have occurred at the time of the insolvency. Law or regulatory practice affects the event that obligates the entity in either of the following ways:

i. In states that, through law or regulatory practice, provide that an entity cannot avoid paying a particular assessment in the future (even if the entity reduces premium writings in the future), the event that obligates the entity is a formal determination of insolvency or a similar event. An entity that has the ability to reasonably estimate the amount of the assessment shall recognize a liability for the entire amount of future assessments that cannot be avoided related to a particular insolvency when a formal determination of insolvency occurs.

ii. In states without such a law or regulatory practice, the event that obligates the entity is the writing of, or becoming obligated to write, the premiums on which the expected future assessments are to be based. An entity that has the ability to reasonably estimate the amount of the assessments shall recognize a liability when the related premiums are written or when the entity becomes obligated to write the premiums.

c. *Prefunded-premium-based guaranty-fund assessments* - A liability for an assessment arises when premiums are written. Accordingly, an entity that has the ability to reasonably estimate the amount of the assessment shall recognize a liability as the related premiums are written.

d. *Other premium-based assessments* - Other premium-based assessments shall be accounted for in the same manner as prefunded premium-based guaranty-fund assessments.

[1] As detailed within paragraph 6 for premium-based guaranty-fund assessments, an insolvency shall be considered to have occurred when a reporting entity meets a state's (ordinarily the state of domicile of the insolvent reporting entity) statutory definition of an insolvent reporting entity. In most states, the reporting entity must be declared to be financially insolvent by a court of competent jurisdiction. In some states, there must also be a final order of liquidation.

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e. *Loss-based assessments* - An assessment is probable of being asserted when the loss occurs. The obligating event of the assessment also has occurred when the loss occurs. Accordingly, an entity that has the ability to reasonably estimate the amount of the assessment shall recognize a liability as the related loss is incurred.

f. *Administrative-type assessments* – As this assessment is typically an annual amount per entity assessed to fund operations of the guaranty association, regardless of the existence of an insolvency, such assessments are generally expensed in the period assessed.

Disclosures

18. A reporting entity shall disclose the following:

a. Describe the nature of any assessments that could have a material financial effect, by type of assessment, and state the estimate of the liability, identifying whether the corresponding liability has been recognized under paragraph 4, a liability has not been recognized as the obligating event has not yet occurred, or that an estimate cannot be made.

b. For assessments with liabilities recognized under paragraph 4, disclose the amount of the recognized liabilities, any related asset for premium tax credits or policy surcharges, the periods over which the assessments are expected to be paid, and the period over which the recorded premium tax offsets or policy surcharges are expected to be realized.

c. Disclose assets recognized from paid and accrued premium tax offsets or policy surcharges, and include a reconciliation of assets recognized within the previous year's annual statement to the assets recognized in the current year's annual statement. The reconciliation shall reflect, in aggregate, each component of the increase and decrease in paid and accrued premium tax offsets and policy surcharges, including the amount charged off.

d. Disclosures shall be made in accordance with paragraph 31 of SSAP No. 5R when there is at least a reasonable possibility that the impairment of an asset from premium tax offsets or policy surcharges may have been incurred.

e. The financial statements shall disclose the following related to guaranty fund liabilities and assets related to assessments from insolvencies of entities that wrote long-term care contracts. The disclosures shall be by insolvency except for paragraph 18.e.ii., which is the same rate for all discounted insolvencies:

i. The undiscounted and discounted amount of the guaranty fund assessments and related assets;

ii. The discount rate applied as of the current reporting date (determined in accordance with paragraphs 12-14);

iii. The number of jurisdictions for which the long-term care guaranty fund assessments payables were discounted and the number of jurisdictions for which asset recoverables were discounted;

iv. Identify the ranges of years used to discount the assets and the range of years used to discount the liabilities;

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v. The weighted average numbers of years of the discounting time period for long-term care guaranty fund assessment liabilities; and

vi. The weighted average number of years of the discounting time period for the asset recoverables.

Illustration of paragraph 18.e.iii. through paragraph 18.e.vi. disclosures:

	Payables			Recoverables		
Name of the Insolvency	Number of Jurisdictions	Range of Years	Weighted Average Number of Years	Number of Jurisdictions	Range of Years	Weighted Average Number of Years
ABC Estate	10	2-10	8	8	5-20	10

19. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

20. This statement adopts GAAP guidance for recording guaranty fund and other assessments, which is contained in *Accounting Standards Codification 405-30, Insurance Related Assessments* (ASC 405-30) to the extent reflected in this SSAP. Statutory accounting modifications from ASC 405-30 are as follows:

a. The option to discount accrued liabilities (and reflect the time value of money in anticipated recoverables) is rejected for statutory accounting. Liabilities and assets related to assessments from insolvencies of entities that wrote long-term care contracts are required to be discounted as described in paragraphs 12-14; however, other liabilities for guaranty funds or other assessments shall not be discounted.

b. The use of a valuation allowance for premium tax offsets and policy surcharges no longer probable for realization has been rejected for statutory accounting. Evaluation of assets shall be made in accordance with SSAP No. 5R, and if it is probable that the asset is no longer realizable, the asset shall be written off and charged to income in the period the determination is made.

c. Guidance within ASC 405-30 pertaining to noninsurance entities has been rejected as not applicable for statutory accounting.

d. Guidance within ASC 405-30 pertaining to accrual of an asset based on future renewals of premium is modified to allow accrual of the asset based on in-force short-term health contract renewals in instances when retrospective-premium-based assessments are imposed on short-term health contracts for the insolvencies of insurers that wrote long-term care contracts.

21. This statement also adopts with modification *Emerging Issues Task Force No. 06-3: How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation)* (EITF 06-3), now included in *Accounting Standards Codification 605-45, Revenue Recognition, Principal Agent Considerations* to the extent reflected in paragraph 16 of this statement.

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Effective Date and Transition

22. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Substantive revisions to paragraphs 4, 6, 7, 8, 10, 11, 17 and 18 as documented in *Issue Paper No. 143R—Guaranty Fund Assessments* are initially effective for the reporting period beginning January 1, 2011. The result of applying this revised statement shall be considered a change in accounting principle in accordance with SSAP No. 3. Pursuant to SSAP No. 3, the cumulative effect of changes in accounting principles shall be reported as an adjustment to unassigned funds (surplus) in the period of the change in accounting principle. The cumulative effect recognized through surplus from initial application of this statement shall reflect the removal of liabilities established under SSAP No. 35, and the re-establishment of liabilities required under SSAP No. 35R. If there is no change in the liabilities recognized (for example, retrospective-premium based assessments), no cumulative effect adjustment shall occur. With regards to assets, the entity shall complete an assessment of the SSAP No. 35 asset reported as of the transition date. If it is determined that the reported asset exceeds what is allowed under SSAP No. 35R, then the excess asset shall be written-off, through unassigned funds, so the ultimate asset reflected corresponds with what is permitted under SSAP No. 35R. Although it is possible that the excess asset will be reinstated once the liability assessment is recognized (prospective-premium based assessments), it is inappropriate to continue to reflect an asset for assessments that are not reflected within the financial statements. The guidance in paragraph 16 adopted with modification *Emerging Issues Task Force No. 06-3: How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation)* and was incorporated from INT 07-03 and effective September 29, 2007. The Section 9010 ACA fee has specific guidance (adopted December 2013) that was effective for annual reporting periods beginning January 1, 2014, and was moved to SSAP No. 106 in June 2014. Consistent with the federal repeal of the Section 9010 ACA fee, SSAP No. 106 was superseded effective January 1, 2021. As documented in Issue Paper No. 143R, modification of the adoption of ASC 405-30 to allow accrual of the asset based on in-force short-term health contract renewals in instances when retrospective-premium-based assessments are imposed on short-term health contracts for the insolvencies of insurers that wrote long-term care contracts as described in paragraph 10.b.i., paragraph 11 and paragraph 20.d. is initially effective January 1, 2017. Although the ASC 405-30 option to discount liabilities is still rejected, effective for reporting periods after January 1, 2017, reporting entities are required to discount guaranty fund assessments, and related assets, resulting from the insolvencies of insurers that wrote long-term care contracts, in accordance with the provisions of paragraphs 12-14 of this statement, as documented in Issue Paper No. 143R.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 35—Accounting for Guaranty Fund and Other Assessments*
- *Issue Paper No. 143R—Guaranty Fund Assessments*
- *Issue Paper No. 148—Affordable Care Act Section 9010 Assessment*

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EXHIBIT A – PRIMARY METHODS OF GUARANTY FUND ASSESSMENTS

a. *Retrospective-premium-based assessments* - Guaranty funds covering benefit payments of insolvent life, annuity, and health insurance entities typically assess entities based on premiums written or received in one or more years before the year of insolvency. Assessments in any year are generally limited to an established percentage of an entity's average premiums for the three years preceding the insolvency. Assessments for a given insolvency may take place over several years.

b. *Prospective-premium-based assessments* - Guaranty funds covering claims of insolvent property and casualty insurance entities typically assess entities based on premiums written in one or more years after the insolvency. Assessments in any year are generally limited to an established percentage of an entity's premiums written or received for the year preceding the assessment. Assessments for a given insolvency may take place over several years.

c. *Prefunded-premium-based assessments* - This kind of assessment is intended to prefund the costs of future insolvencies. Assessments are imposed before any particular insolvency and are based on the current level of written premiums. Rates to be applied to future premiums are adjusted as necessary.

d. *Administrative-type assessments* - These assessments are typically a flat (annual) amount per entity to fund operations of the guaranty association, regardless of the existence of an insolvency.

e. *Other premium-based assessments* - Entities are subject to a variety of other insurance-related assessments. Many states and a number of local governmental units have established other funds supported by assessments. The most prevalent uses for such assessments are (*a*) to fund operating expenses of state insurance regulatory bodies (for example, the state insurance department or workers' compensation board) and (*b*) to fund second-injury funds.

    i. *Premium-based* - The assessing organization imposes the assessment based on the entity's written premiums. The base year of premiums is generally either the current year or the year preceding the assessment.

    ii. *Loss-based* - The assessing organization imposes the assessment based on the entity's incurred losses or paid losses in relation to that amount for all entities subject to that assessment in the particular jurisdiction.

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Statement of Statutory Accounting Principles No. 36

Troubled Debt Restructuring

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 03-12
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for troubled debt restructuring.

SUMMARY CONCLUSION

2. A troubled debt restructuring is defined as a debt restructuring whereby the creditor, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise grant. That concession either stems from an agreement between the creditor and the debtor or is imposed by law or a court. Many troubled debt restructurings involve modifying terms to reduce or defer cash payments required of the debtor in the near future to help the debtor attempt to improve its financial condition and eventually be able to pay the creditor. The creditor, for example, may accept cash, other assets, or an equity interest in the debtor in satisfaction of the debt though the value received is less than the amount of the debt, because the creditor concludes the concession will maximize recovery of its investment. A debtor in a troubled debt restructuring can obtain funds from sources other than the existing creditor, if at all, only at effective interest rates (based on market prices) so high that it cannot afford to

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pay them. A troubled debt restructuring shall include debt that is fully satisfied by foreclosure, repossession, or other transfer of assets or by grant of equity securities by the debtor that is, in a technical sense, not restructured.

3. The determination of whether a debt restructuring is considered a troubled debt restructuring, as defined above, shall be made independently for the debtor and the creditor.

4. A debt restructuring shall not necessarily be considered a troubled debt restructuring for purposes of this statement even if the debtor is experiencing some financial difficulties. In general, a debtor that can obtain funds from sources other than the existing creditor at market interest rates at or near those for nontroubled debt is not involved in a troubled debt restructuring. For example, a troubled debt restructuring is not involved if:

a. The fair value of cash, other assets, or an equity interest accepted by a creditor from a debtor in full satisfaction of its receivable at least equals the creditor's recorded investment in the receivable;

b. The fair value of cash, other assets, or an equity interest transferred by a debtor to a creditor in full settlement of its payable at least equals the debtor's carrying amount of the payable;

c. The creditor reduces the effective interest rate on the debt primarily to reflect a decrease in market interest rates in general or a decrease in the risk so as to maintain a relationship with a debtor that can readily obtain funds from other sources at the current market interest rate;

d. The debtor issues, in exchange for its debt, new marketable debt having an effective interest rate based on its market price that is at or near the current market interest rates of debt with similar maturity dates and stated interest rates issued by nontroubled debtors; or

e. The debtor, in connection with bankruptcy proceedings, enters into debt restructuring that results in a general restatement of most of the debtor's liabilities.

Determining Whether a Creditor Has Granted a Concession

5. A creditor has granted a concession when, as a result of the restructuring, it does not expect to collect all amounts due, including interest accrued at the original contract rate. In that situation, and if the payment of principal at original maturity is primarily dependent on the value of collateral, an entity shall consider the current value of that collateral in determining whether the principal will be paid.

6. A creditor may restructure a debt in exchange for additional collateral or guarantees from the debtor. In that situation, a creditor has granted a concession when the nature and amount of that additional collateral or guarantees received as part of a restructuring do not serve as adequate compensation for other terms of the restructuring. When additional guarantees are received in a restructuring, an entity shall evaluate both a guarantor's ability and its willingness to pay the balance owed.

7. If a debtor does not otherwise have access to funds at a market rate for debt with similar risk characteristics as the restructured debt, the restructuring would be considered to be at a below-market rate, which may indicate that the creditor has granted a concession. In that situation, a creditor shall consider all aspects of the restructuring in determining whether it has granted a concession.

8. A temporary or permanent increase in the contractual interest rate as a result of a restructuring does not preclude the restructuring from being considered a concession because the new contractual interest rate on the restructured debt could still be below market interest rates for new debt with similar

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risk characteristics. In that situation, a creditor shall consider all aspects of the restructuring in determining whether it has granted a concession.

Determining Whether a Debtor Is Experiencing Financial Difficulties

9. In evaluating whether a receivable is a troubled debt restructuring, a creditor must determine whether the debtor is experiencing financial difficulties. In making this determination, a creditor shall consider the following indicators:

a. The debtor is currently in payment default on any of its debt. In addition, a creditor shall evaluate whether it is probable that the debtor would be in payment default on any of its debt in the foreseeable future without the modification. That is, a creditor may conclude that a debtor is experiencing financial difficulties, even though the debtor is not currently in payment default.

b. The debtor has declared or is in the process of declaring bankruptcy.

c. There is substantial doubt as to whether the debtor will continue to be a going concern.

d. The debtor has securities that have been delisted, are in the process of being delisted, or are under threat of being delisted from an exchange.

e. On the basis of estimates and projections that only encompass the debtor's current capabilities, the creditor forecasts that the debtor's entity-specific cash flows will be insufficient to service any of its debt (both interest and principal) in accordance with the contractual terms of the existing agreement for the foreseeable future.

f. Without the current modification, the debtor cannot obtain funds from sources other than the existing creditors at an effective interest rate equal to the current market interest rate for similar debt for a nontroubled debtor.

The above list of indicators is not intended to include all indicators of a debtor's financial difficulties.

Evaluating Whether a Restructuring Results in a Delay in Payment That is Insignificant

10. A restructuring that results in only a delay in payment that is insignificant is not a concession. The following factors, when considered together, may indicate that a restructuring results in a delay in payment that is insignificant:

a. The amount of the restructured payments subject to the delay is insignificant relative to the unpaid principal or collateral value of the debt and will result in an insignificant shortfall in the contractual amount due.

b. The delay in timing of the restructured payment period is insignificant relative to any one of the following:

i. The frequency of payments due under the debt

ii. The debt's original contractual maturity

iii. The debt's original expected duration

11. If the debt has been previously restructured, an entity shall consider the cumulative effect of the past restructurings when determining whether a delay in payment resulting from the most recent restructuring is insignificant.

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Accounting by Debtors

12. A debtor shall account for a troubled debt restructuring according to the type of the restructuring (transfer of assets in full settlement, grant of equity interest in full settlement, modification of terms or combination of types). Generally, troubled debt restructuring involving the transfer of assets or the grant of an equity interest shall be accounted for at the fair value of the assets transferred or the equity interest granted.

13. A debtor in a troubled debt restructuring involving only modification of terms of a payable—that is, not involving a transfer of assets or grant of an equity interest—shall account for the effects of the restructuring prospectively from the time of restructuring, and shall not change the carrying amount of the payable at the time of the restructuring unless the carrying amount exceeds the total future cash payments specified by the new terms. That is, the effects of changes in the amounts or timing (or both) of future cash payments designated as either interest or face amount shall be reflected in future periods. Interest expense shall be computed in a way that a constant effective interest rate is applied to the carrying amount of the payable at the beginning of each period between restructuring and maturity. The new effective interest rate shall be the discount rate that equates the present value of the future cash payments specified by the new terms (excluding amounts contingently payable) with the carrying amount of the payable.

14. If the total future cash payments specified by the new terms of a payable, including both payments designated as interest and those designated as face amount, are less than the carrying amount of the payable, the debtor shall reduce the carrying amount to an amount equal to the total future cash payments specified by the new terms and shall recognize a gain on restructuring of payables equal to the amount of the reduction. Thereafter, all cash payments under the terms of the payable shall be accounted for as reductions of the carrying amount of the payable, and no interest expense shall be recognized on the payable for any period between the restructuring and maturity of the payable.

15. A debtor shall not recognize a gain on a restructured payable involving indeterminate future cash payments as long as the maximum total future cash payments may exceed the carrying amount of the payable. Amounts designated either as interest or as face amount by the new terms may be payable contingent on a specified event or circumstance (e.g., the debtor may be required to pay specified amounts if its financial condition improves to a specified degree within a specified period). To determine whether the debtor shall recognize a gain according to the provisions of paragraphs 13 and 14, those contingent amounts shall be included in the "total future cash payments specified by the new terms" to the extent necessary to prevent recognizing a gain at the time of restructuring that may be offset by future interest expense. Thus, the debtor shall apply *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* in which probability of occurrence of a gain contingency is not a factor and shall assume that contingent future payments will have to be paid. The same principle applies to amounts of future cash payments that must sometimes be estimated to apply the provisions of paragraphs 13 and 14. For example, if the number of future interest payments is flexible because the face amount and accrued interest is payable on demand or becomes payable on demand, estimates of total future cash payments shall be based on the maximum number of periods possible under the restructured terms.

16. If a troubled debt restructuring involves amounts contingently payable, those contingent amounts shall be recognized as a payable and as interest expense in future periods in accordance SSAP No. 5R. Thus, in general, interest expense for contingent payments shall be recognized in each period in which (a) it is probable that a liability has been incurred and (b) the amount of that liability can be reasonably estimated. Before recognizing a payable and interest expense for amounts contingently payable, however, accrual or payment of those amounts shall be deducted from the carrying amount of the restructured payable to the extent that contingent payments included in "total future cash payments specified by the new terms" prevented recognition of a gain at the time of restructuring (paragraph 15).

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Accounting by Creditors

17. A creditor shall account for a troubled debt restructuring according to the type of the restructuring (receipt of assets in full satisfaction, modification of terms, combination of types). Generally, troubled debt restructuring involving the transfer of assets shall be accounted for at the fair value of the assets received. Troubled debt restructuring involving modification of terms shall be accounted for at fair value (as determined by acceptable appraisal methodologies) in accordance with *SSAP No. 100R—Fair Value*. If the restructured loan is collateral dependent, fair value shall be the fair value of the collateral. If the restructured loan is not collateral dependent, fair value shall be determined in accordance with SSAP No. 100R. If the determined fair value of the loan is less than the recorded investment in the loan (including accrued interest, net deferred loan fees or costs, and unamortized premium or discount), a new cost basis shall be established at the fair value with the difference being recorded as a realized loss in the statement of operations. After the troubled debt restructuring, a creditor shall account for the assets consistent with the statutory guidance for such assets.

18. A creditor shall account for assets, including foreclosed property and equity interests in corporations, joint ventures, or partnerships, received in satisfaction of the loan at their fair value (as determined by acceptable appraisal methodologies) at the time of restructuring or at the book value of the loan if lower. If the fair value is less than the book value, the required writedown shall be recognized as a realized capital loss. The creditor shall reclassify the asset from loans to the appropriate asset account, such as real estate or other invested assets, at the time that the creditor obtains clear title to the asset except for mortgage loans which shall follow the guidance in paragraph 18 of SSAP No. 37. After the troubled debt restructuring, a creditor shall account for the assets received in satisfaction of the loan consistent with the statutory guidance for similar assets.

19. Any fees received in connection with a modification of terms of a troubled debt restructuring shall be applied as a reduction of the recorded investment in the loan. All costs associated with the restructuring, including direct loan origination costs, shall be charged to expense as incurred.

Disclosure by Debtors

20. A debtor in a troubled debt restructuring shall disclose in the financial statements the following information about troubled debt restructurings that have occurred during a period for which financial statements are presented:

a. For each restructuring or separate restructuring within a fiscal period for the same category of payables, (e.g., accounts payable or subordinated debentures), a description of the principal changes in terms, the major features of settlement, or both;

b. Aggregate gain on restructuring of payables and the related income tax effect; and

c. Aggregate net gain or loss on transfers of assets recognized during the period.

21. A debtor shall disclose in financial statements for periods after a troubled debt restructuring the extent to which amounts contingently payable are included in the carrying amount of restructured payables. A debtor shall also disclose total amounts that are contingently payable on restructured payables and the conditions under which those amounts would become payable or would be forgiven.

22. Refer to the Preamble for further discussion regarding disclosure requirements.

Disclosure by Creditors

23. A creditor shall disclose in the financial statements the information captured in paragraphs 23.a., 23.b. and 23.c. about troubled debt restructuring as of the date of each balance sheet presented.

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Disclosures captured from paragraphs 23.d. and 23.e. are required in the statutory audited financial statements only:

a. As of the date of each statement of financial position presented, the recorded investment in the loans for which impairment has been recognized in accordance with this statement and the related realized capital loss. (For mortgage loans, the disclosures in SSAP No. 37 shall also be completed.)

b. The amount of commitments, if any, to lend additional funds to debtors owing receivables whose terms have been modified in troubled debt restructuring

c. The creditor's income recognition policy for interest income on an impaired loan

d. For troubled debt restructurings that occurred during the annual reporting period, aggregated by type of instrument, qualitative and quantitative information on (1) how the items were modified and (2) the financial effects of the modifications

e. If restructured within the previous 12 months and there has been a payment default during that period, disclose qualitative and quantitative information about the defaulted instruments, aggregated by type of instrument, including: (1) type of instruments that defaulted and (2) the amount of recorded investments for which default occurred

24. Refer to the Preamble for further discussion regarding disclosure requirements.

25. This statement is not intended to modify the requirement for life and health insurers to complete the annual statement exhibit disclosing long-term mortgage loans in good standing with restructured terms.

Relevant Literature

26. This statement rejects *ASU 2022-02, Troubled Debt Restructurings and Vintage Disclosures* and the U.S. GAAP guidance within the Accounting Standards Codification for troubled debt restructurings for creditors. This ASU is rejected as the U.S. GAAP guidance for troubled debt restructuring by creditors has been significantly modified to eliminate the separate recognition of losses from restructurings as losses are captured within the allowance for credit losses valuation account established pursuant to *ASU 2016-13, Financial Instruments – Credit Losses*. As statutory accounting has not adopted ASU 2016-13, the prior troubled debt restructuring adopted from U.S GAAP in effect prior to ASU 2016-13 and ASU 2022-02 has been retained. With the rejection of ASU 2022-02, reporting entities shall continue to apply the prior concepts within SSAP No. 36 when assessing and classifying modifications as troubled debt restructurings. These retained concepts do not permit entities to consider troubled debt restructurings as new loans and therefore do not permit immediate recognition of unamortized fees, costs, or prepayment penalties as interest income at the time of restructuring. Additionally, fees received by a reporting entity from a restructuring shall continue to reduce the recorded investment and all costs incurred by a reporting entity with the restructuring shall continue to be charged to expense as incurred.

27. Although the statutory accounting guidance for troubled debt restructurings for creditors no longer reflects authoritative guidance from U.S. GAAP, the guidance in SSAP No. 36 reflects the following superseded U.S. GAAP guidance as follows:

a. Adopted with modification *FASB Statement No. 15*, *Accounting by Debtors and Creditors for Troubled Debt Restructurings* (FAS 15) to specify that creditors shall reclassify assets obtained in a troubled debt restructuring from loans to the appropriate asset account at the time the creditor obtains clear title to the asset, except for mortgage loans which shall be reclassified at the beginning of the redemption period unless it is probable that the mortgage loan will be redeemed and with modification to require that

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gains and losses from extinguishment of debt be reported as capital gains or losses, and charged to operations.

b. Adopted paragraphs 310-40-15-13 through 310-40-15-18 and 310-40-15-20 of the FASB Codification incorporated through *FASB ASU 2011-02, A Creditors Determination of Whether a Restructuring Is a Troubled Debt Restructuring*.

c. Adopted with modification the disclosure requirements included in paragraphs 310-10-50-33 through 310-10-50-34 of the FASB Codification originally incorporated from *ASU 2010-20, Receivables (Topic 310), Disclosures About the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, deferred by *ASU 2011-01, Receivables (Topic 310), Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20* and reinstated through ASU 2011-02. These disclosure requirements were modified to be applicable for all troubled debt restructurings within the scope of SSAP No. 36, rather than limited to troubled debt restructurings of "financing receivables."

d. Adopted paragraphs 9, 22, and 25 of *FASB Statement No. 114*, *Accounting by Creditors for Impairment of a Loan* (FAS 114). Adopted *FASB Statement No. 118*, *Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures* as it relates to troubled debt restructuring.

e. Adopts *FASB Technical Bulletin 81-6, Applicability of Statement 15 to Debtors in Bankruptcy Situations* and *FASB Technical Bulletin 80-2, Classification of Debt Restructuring by Debtors and Creditors*, *FASB Emerging Issue Task Force No. 87-18, Use of Zero Coupon Bonds in a Troubled Debt Restructuring*, *FASB Emerging Issue Task Force No. 87-19, Substituted Debtors in a Troubled Debt Restructuring*, *FASB Emerging Issue Task Force No. 89-15*, *Accounting for a Modification of Debt Terms When the Debtor is Experiencing Financial Difficulties* consistent with the modifications to FAS 15, *FASB Emerging Issues Task Force No. 96-22, Applicability of the Disclosures Required by FASB Statement No. 114 When a Loan Is Restructured in a Troubled Debt Restructuring into Two (or More) Loans* and *FASB EITF 02-4: Determining Whether a Debtor's Modification or Exchange of Debt Instruments is Within the Scope of FASB Statement No. 15*.

f. This statement is consistent with paragraph 14 of *FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases* (FAS 91), but FAS 91 was rejected in *SSAP No. 26R—Bonds.*

28. For historical reference purposes, the following superseded U.S. GAAP guidance was previously rejected within this statement:

a. Paragraphs 6.d., 13 and 21 of FAS 114.

b. FASB Emerging Issues Task Force No. 94-8, Accounting for Conversion of a Loan into a Security in a Troubled Debt Restructuring and FASB Technical Bulletin 94-1, Application of Statement 115 to Debt Securities Restructured in a Troubled Debt Restructuring.

Effective Date and Transition

29. This statement is effective for years beginning January 1, 2001. The provisions of this statement shall be applied to all troubled debt restructurings entered into on or after January 1, 2001. The adoption of *FASB EITF 02-4: Determining Whether a Debtor's Modification or Exchange of Debt Instruments is*

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within the Scope of FASB Statement No. 15 was incorporated from INT 03-12 and effective December 7, 2003. The revisions adopted in August 2012 from ASU 2011-02 and ASU 2010-20 are effective January 1, 2013, with early application permitted.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*

Relevant Issue Papers

- *Issue Paper No. 36—Troubled Debt Restructurings*

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Statement of Statutory Accounting Principles No. 37

Mortgage Loans

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 99-04
Affected by	No other pronouncements
Interpreted by	INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the accounting and reporting of mortgage loans and related fees.

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SUMMARY CONCLUSION

2. A mortgage loan is defined as a debt obligation that is not a security, which is secured by a mortgage on real estate. In addition to mortgage loans directly originated, a mortgage loan also includes mortgage loans acquired or obtained through assignment, syndication or participation[1]. Investments that reflect "participating mortgages," "mortgage loan fund," "bundled mortgage loans[2]" or the "securitization of assets" are not considered mortgage loans within scope of this SSAP.

a. A security is a share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:

i. It is either represented by an instrument issued in bearer or registered form, or if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.

ii. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.

iii. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

3. Mortgage loans meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

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[1] Examples of agreements intended to be captured within this statement:

a. Reporting entity is a "co-lender" in a single mortgage loan agreement that identifies more than one lender (which includes the reporting entity) with the real estate collateral securing all lenders identified in the agreement. For these single-mortgage loan agreements, each lender is incorporated directly into the loan documents. The key differentiating characteristic of a mortgage loan provided under a group "mortgage loan co-lending agreement" rather than a solely owned mortgage loan is that no one lender of the lending group may unilaterally foreclose on the mortgage. With these agreements, the lenders must foreclose on the mortgage loan as a group.

b. Reporting entity has a "participation agreement" to invest in a single-mortgage loan. The reporting entity is not the lender of record named as a payee on the mortgage loan, but the lender of record sells a portion of the mortgage loan to the reporting entity through an assignment or participation interest under the participation agreement. Under a participation agreement, the reporting entity acquires an undivided interest in the single mortgage loan proceeds to be received by the lender of record. Under a participation agreement, single mortgage loan proceeds include the periodic mortgage loan principal and interest payments received by the lender of record, and all rights and proceeds received in the foreclosure of a mortgage, deed of trust, deed in lieu of foreclosure, or other similar proceeding by the lender of record. The amount of the proceeds to be received by the reporting entity is based on the ratio of its participation interest to the then-outstanding single mortgage loan balance. To qualify as a mortgage loan under the scope of this statement, the reporting entity must have a signed participation agreement with the lender of record named in the mortgage loan, the financial rights and obligations of the reporting entity under the participation agreement are the same as the lender of record, the reporting entity's participation interest in the single mortgage loan proceeds must be pari-passu with the lender of record named on the mortgage loan agreement, and the participation agreement must be properly and promptly recorded on the lender or record's books and records. For the purposes of this footnote, "financial rights" may include the right to take legal action against the borrower, or participate with the other lenders in determining whether legal action should be taken, but typically does not include the right to solely initiate legal action, foreclosure, or under normal circumstances, communicate directly with the borrower.

[2] The scope of this SSAP is limited to single mortgage loan agreements. Although single mortgage loan agreements can potentially have more than one lender (e.g., co-lenders/participations) and more than one borrower (such as in a tenancy-in-common arrangement), the concept of a "single mortgage loan" does not include arrangements in which a reporting entity acquires more than one mortgage loan in a sole transaction. (For example, if a reporting entity was to acquire an interest in a "bundle" of mortgage loans with various unrelated borrowers and collateral, this agreement would be outside of the scope of this SSAP. However, a bundle of mortgage loans does not include a "bulk purchase" where the reporting entity's interest in each mortgage loan is legally separate and divisible and the purchase just facilitates the acquisitions of multiple single mortgage loan agreements.)

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Commitment Fees

4. Commitment (or commitment standby) fees are fees paid to the reporting entity that obligate the reporting entity to make or acquire a loan or to satisfy an obligation of another party under a specified condition. A fee paid to the reporting entity to obtain a commitment to make funds available at some time in the future, generally, is refundable only if the loan is granted. If the loan is not granted, then the fees shall be recorded as investment income by the reporting entity when the commitment is no longer available.

5. A fee paid to the reporting entity to obtain a commitment to be able to borrow funds at a specified rate and with specified terms quoted in the commitment agreement, generally, is not refundable unless the commitment is refused by the reporting entity. This type of fee shall be deferred, and amortization shall depend on whether or not the commitment is exercised. If the commitment is exercised, then the fee shall be amortized in accordance with paragraph 9 over the life of the loan as an adjustment to the investment income on the loan. If the commitment expires unexercised, the commitment fee shall be recognized in income on the commitment expiration date.

Loan Origination Fees

6. Loan origination fees are defined as fees charged to the borrower in connection with the process of originating, refinancing, or restructuring a loan. The term includes, but is not limited to, points, management, arrangement, placement, application, underwriting, and other fees pursuant to a lending transaction. Nonrefundable loan origination fees shall not be recorded until received in cash. Nonrefundable fees representing points shall be deferred as part of the loan balance and amortized over the life of the loan in accordance with paragraph 9. Nonrefundable fees other than points shall be recorded in income upon receipt.

Loan Origination, Acquisition, and Commitment Costs

7. All costs incurred in connection with originating a loan, acquiring purchased loans or committing to purchase loans shall be charged to expense as incurred.

Initial Investment

8. For mortgage loans originated by the reporting entity, the initial investment in mortgage loans shall be recorded at the principal amount of the loan net of any amounts deferred under the provisions of paragraphs 5 and 6. For mortgage loans purchased by a reporting entity, the initial investment shall be recorded as the amount paid to the seller. Accordingly, there may be a premium or discount on such loans resulting from a difference between the amount paid and the principal amount.

Amortization

9. Premiums and discounts on acquired loans, and mortgage interest points and commitment fees (if such qualify for amortization as described in paragraphs 5 and 6) shall be recognized as an adjustment of yield over the life of the loan (i.e., the period of time until total principal proceeds of the loan are received in cash) to produce a constant effective yield each year to maturity. If the reporting entity holds a large number of similar loans for which the prepayments of principal are probable, (probable is used in the same context as in paragraph 6 in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, which defines probable as the future event or events are likely to occur), and the timing and amount can be reasonably estimated, the reporting entity shall include estimates of future principal prepayments in the calculation of the constant effective yield necessary to apply the interest method. The amount recognized as an adjustment of yield shall be credited or charged to interest income in the calculation of net investment income.

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Prepayments

10. Payments received in advance of due dates may produce prepaid interest which shall be recorded as a liability, Unearned Investment Income, on the reporting entity's balance sheet. The portion of the payments received in advance of due dates that represents prepayments of principal shall be recorded as a reduction in the mortgage loan balance.

11. A mortgage loan may provide for a prepayment penalty or acceleration fee in the event the loan is liquidated prior to its scheduled termination date. Such fees shall be reported as investment income when received.

Interest Income

12. Interest income shall be recorded as earned and shall be included in investment income in the Summary of Operations. Interest income shall include interest collected, the change in interest income due and accrued, and the change in unearned interest income as well as amortization of premiums, discounts, and deferred fees as specified in paragraph 9.

Accrued Interest

13. Reporting entities that use servicing agents for their mortgage loans shall report the Interest Due and Accrued asset on the balance sheet consistently with the income statement treatment of the charge for servicing costs. If interest income is reported net of servicing costs, which is usual when the servicing agent fee is based on a percentage retention of each interest payment, then the interest receivable in the balance sheet shall be net of the related servicing costs. If interest is reported gross, with the servicing costs reported as an expense item, then interest due and accrued shall be reflected as an asset at the gross amount, with an appropriate liability to reflect the related servicing cost accrual.

14. When a loan is determined to be in default (per the contractual terms of the loan), the accrued interest on the loan shall be recorded as investment income due and accrued if deemed collectible. If a loan in default has any investment income due and accrued which is 180 days past due and collectible, the investment income shall continue to accrue, but all interest related to the loan is to be reported as a nonadmitted asset. If accrued interest on a mortgage loan in default is not collectible, the accrued interest shall be written off immediately and no further interest accrued.

15. Contingent interest represents income generated through the occurrence of specific economic events in relation to the borrower. For example, contingent interest may become payable upon the attainment of a given level of cash flow or income. Contingent interest may be reported as income when received or accrued. The proper accrual of such income does, however, require an analysis of the applicable provisions in the underlying agreement and the verification that the prerequisite conditions have been met.

Impairments

16. A mortgage loan shall be considered to be impaired when, based on current information and events, it is probable that a reporting entity will be unable to collect all amounts due according to the contractual terms of the mortgage agreement. According to the contractual terms means that both the contractual principal payments and contractual interest payments of the mortgage loan will be collected as scheduled in the mortgage agreement. A reporting entity shall measure impairment based on the fair value (as determined by acceptable appraisal methodologies) of the collateral less estimated costs to obtain and sell. The difference between the net value of the collateral[3] and the recorded investment in the mortgage

[3] If the mortgage loan is subject to a mortgage loan participation or co-lending agreement, collateral valuations conducted for impairment assessment, and the reporting of the appraisal value of land and buildings, shall only reflect the reporting entity's pro-rata share of the collateral/appraised value as it relates to the reporting entity's interest in the mortgage loan.

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loan shall be recognized as an impairment by creating a valuation allowance with a corresponding charge to unrealized loss or by adjusting an existing valuation allowance for the impaired loan with a corresponding charge or credit to unrealized gain or loss. Subsequent to the initial measurement of impairment, if there is a significant change (increase or decrease) in the net value of the collateral, the reporting entity shall adjust the valuation allowance; however, the net carrying amount of the loan shall at no time exceed the recorded investment in the loan. For reporting entities required to maintain an asset valuation reserve (AVR), the unrealized gain or loss on impairments shall be included in the calculation of the AVR. If the impairment is other than temporary (INT 06-07), a direct write down shall be recognized as a realized loss, and a new cost basis is established. This new cost basis shall not be changed for subsequent recoveries in value. Mortgage loans for which foreclosure is probable shall be considered permanently impaired.

17. For loans that are in default, being voluntarily conveyed, or being foreclosed, additional expenses, such as insurance, taxes, and legal fees that have been incurred to protect the investment or to obtain clear title to the property shall not be added to the carrying value, but shall be expensed when incurred.

18. Reporting entities shall derecognize mortgage loans and recognize real estate (subject to SSAP No. 40R) when receiving physical possession (resulting in a in substance repossession or foreclosure) of real estate property collateralizing a mortgage loan only when the following occurs:

a. The reporting entity obtains legal title to the real estate property upon completion of a foreclosure. This includes situations in which the reporting entity receives legal title to the real estate property even if the borrower has redemption rights that provide the borrower with the legal right for a period of time after a foreclosure to reclaim the real estate property by paying certain amounts specified by law.

b. The borrower conveys all interest in the real estate property to the reporting entity to satisfy the loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. The deed in lieu of foreclosure or similar legal agreement is completed when agreed-upon terms and conditions have been satisfied by both the borrower and the reporting entity.

19. Real estate recognized pursuant to paragraph 18 shall be initially recognized at the lower of the recorded investment in the mortgage loan or fair value less costs to sell. If the real estate is recognized at fair value less costs to sell, then a realized loss shall be recognized for the difference between that amount and the recorded investment in the mortgage loan. (A gain shall not be recognized as a result of foreclosure.)

20. Reporting entities that hold mortgage loans that are government-guaranteed shall derecognize the mortgage loans and recognize a separate other receivable (as an aggregate write-in for an other-than-invested asset) upon foreclosure (that is the reporting entity receives physical possession of the assets regardless of whether formal foreclosure proceedings take place, or in which the reporting entity otherwise obtains one or more of the debtor's assets in place of all or part of the receivable) if the following conditions are met:

a. The loan has a government guarantee that is not separable from the loan before foreclosure.

b. At the time of foreclosure, the reporting entity has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the reporting entity has the ability to recover under that claim. A reporting entity would be considered to have the ability to recover under the guarantee at the time of foreclosure if the reporting entity

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determines that it has maintained compliance with the conditions and procedures required by the guarantee program.

c. At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed.

21. The separate other receivable recognized under paragraph 20 shall reflect the amount of the mortgage loan balance (principal and interest) expected to be recovered from the guarantor. A realized loss shall be recognized for any amount of the recorded investment in the mortgage loan that is not expected to be recovered. If the conditions in paragraph 20 are not met, upon foreclosure, the real estate collateralizing the mortgage loan (if any) shall be recognized pursuant to paragraph 19.

22. The separate other receivable recognized under paragraph 20, even if over ninety days past due, is an admitted asset similar to other receivables guaranteed by the government. If, in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

Escrow Payments

23. Amounts paid to the reporting entity by the mortgagor to cover future tax payments, insurance premiums, and other costs related to the property requires the creation of escrow accounts in the general ledger to record these liabilities. If these amounts are held by the servicing agents, they shall be reported on the reporting entity's balance sheet both as an asset and as a liability when they produce income for the reporting entity. This may occur if the servicing agent invests the escrow funds and is required to remit the income (or portion thereof) to the reporting entity.

Construction Loans

24. A construction loan is defined as a mortgage loan of less than three years in term, made for financing the cost of construction of a building or other improvement to real estate, which is secured by the real estate. The principal amount of a construction loan shall be the amount of funds disbursed to the borrower. If, in accordance with the terms of the contract, interest is deferred until the maturity of the loan, the accrued interest shall be included in the balance of the loan outstanding. The impairment test in paragraph 16 shall be applied to all construction loans, regardless of whether there are any defaults. Accordingly, construction loans shall not be reported at an amount greater than the fair value of the property. The percentage of completion of the property shall be considered in determining fair values of property securing construction loans.

Disclosures

25. The following disclosures shall be made in the financial statements:

a. Fair values in accordance with *SSAP No. 100R—Fair Value;*

b. Concentrations of credit risk in accordance with SSAP No. 27 as well as 1) information as to how and to what extent management monitors the credit quality of its mortgage loans in an ongoing manner, and 2) to assess the quantitative and qualitative risks arising from the credit quality of its mortgage loans. To meet these objectives reporting entities shall provide information, aggregated by type, about the credit quality of mortgage loans including the following;

i. A description of the credit quality indicator

ii. The recorded investment in mortgage loans by credit quality indicator

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iii. For each credit quality indicator, the date or range of dates in which the information was updated for that credit quality indicator

c. Description of the valuation basis of the mortgage loans;

d. Information on the minimum and maximum rates of interest received for new loans made by category;

e. Maximum percentage of any one loan to the value of security at the time of the loan;

f. An age analysis of mortgage loans, aggregated by type, with identification of mortgage loans in which the insurer is a participant or co-lender in a mortgage loan agreement, capturing: 1) recorded investment of current mortgage loans, 2) recorded investment of mortgage loans past due classified as 30-59 days past due, 60-89 days past due, 90-179 days past due, and greater than 180 days past due; 3) recorded investment of mortgage loans 90 days and 180 days past due still accruing interest; 4) interest accrued for mortgage loans 90 days and 180 days past due; and 5) recorded investment and number of mortgage loans where interest has been reduced, by percent reduced; and

g. Taxes, assessments, and amounts advanced not included in the mortgage loan total.

26. The following additional disclosures shall be made for impaired loans:

a. The total recorded investment in impaired loans, aggregated by type, at the end of each period with (i) the amount for which there is a related allowance for credit losses determined in accordance with this statement and the amount of that allowance, (ii) the amount for which there is no related allowance for credit losses determined in accordance with this statement, and (iii) the total recorded investment in impaired loans subject to a participant or co-lending mortgage loan agreement for which the reporting entity is restricted from unilaterally foreclosing on the mortgage loan;

b. The policy for recognizing interest income on impaired loans, including how cash receipts are recorded;

c. For each period for which results of operations are presented, the average recorded investment, aggregated by type, in the impaired loans during each period, the related amount of interest income recognized during the time within that period that the loans were impaired, the recorded investments on nonaccrual status pursuant to SSAP No. 34, paragraph 6 and, unless not practicable, the amount of interest income recognized using a cash-basis method of accounting during the time within that period that the loans were impaired; and

d. For each period for which results of operations are presented, the activity in the allowance for credit losses account, including the balance in the allowance for credit losses account at the beginning and end of each period, additions charged to operations, direct write-downs charged against the allowance, and recoveries of amounts previously charged off.

e. The aggregate amount of mortgage loans derecognized as a result of foreclosure and the corresponding amounts of:

i. Real estate collateral recognized.

ii. Other collateral recognized.

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iii. Receivables recognized from a government guarantee of the foreclosed mortgage loan.

27. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosure requirements of paragraph 25.b. shall be included in the annual audited statutory financial reports only.

Relevant Literature

28. This statement adopts *FASB Statement No. 114, Accounting by Creditors for Impairment of a Loan* (FAS 114), and *FASB Statement No. 118, Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures, an amendment of FASB Statement No. 114*, for collateral dependent loans with the following modifications:

a. Impairment shall be measured based on the fair value of the collateral less costs to obtain and sell, whereas that is just one option under FAS 114; and

b. The reporting entity is required to record any other than temporary impairment as a realized loss and shall not record subsequent recoveries in fair value.

29. This statement adopts disclosure requirements in paragraphs 310-10-50-7, 310-10-50-7A, 310-10-50-15, and 310-10-50-29(b) of *ASU 2010-20, Disclosures about the Credit Quality of Financing Receivables and the Allowance For Credit Losses* (ASU 2010-20) for mortgage loans only. Other disclosure requirements of ASU 2010-20, and the application of the adopted disclosures to other investments or receivables are rejected as not applicable for statutory accounting. This statement also adopts *ASU 2014-14, Receivable – Troubled Debt Restructuring by Creditors, Classification of Certain Government-Guaranteed Mortgage Loans Upon Foreclosure* and *FASB Emerging Issues Task Force Issue No. 84-19, Mortgage Loan Payment Modifications*.

30. This statement adopts with modification *ASU 2014-04, Troubled Debt Restructuring by Creditors – Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure*. The ASU 2014-04 guidance has been modified to remove the restrictions limiting it to residential real estate with a consumer mortgage loan. The guidance reflected in this statement shall encompass all foreclosed mortgage loans collateralized by real estate. Additionally, ASU 2014-04 guidance has been modified to require a "lower-of" valuation method for the real estate collateral recognized from a foreclosure. This guidance will result in a deferral of any gain as a result of a mortgage loan foreclosure. Recognition of any gain shall be deferred until the real estate property is sold and the excess proceeds over the mortgage loan balance are attributable to the reporting entity and not required to be remitted back to the mortgage loan debtor.

31. This statement rejects *FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*, *FASB Emerging Issues Task Force No. 88-17, Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations,* and *AICPA Practice Bulletin 6, Amortization of Discounts on Certain Acquired Loans*. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments*, *ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, *ASU 2019-04 Codification Improvements to Topics 326, 815, 825*, *ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*, *ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

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Effective Date and Transition

32. This statement is effective for years beginning January 1, 2001. Initial recognition of the impairment losses resulting from the application of this statement shall apply to mortgage loans held at January 1, 2001, and be based on management's best estimates as of that date. Insurers shall release all unamortized amounts included in IMR related to prepayment penalties upon adoption of Codification and recognize such change in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance in this paragraph related to unamortized amounts included in IMR was originally contained within *INT 99-04: Recognition of Prepayment Penalties Upon Adoption of Codification* and was effective March 8, 1999.

33. The adoption of ASU 2014-14 and the adoption with modification of ASU 2014-04 (detailed in paragraphs 18-22 and 26.e.) shall be applied prospectively from the date of adoption (March 28, 2015). With this prospective application, guidance adopted from ASU 2014-14 applies to all foreclosures that occur after the date of adoption, and guidance from ASU 2014-04 applies to all instances of the reporting entity receiving physical possession of real estate property collateralized by mortgage loans that occur after the date of adoption.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 37—Mortgage Loans*

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Statement of Statutory Accounting Principles No. 38

Acquisition, Development and Construction Arrangements

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Relevant Literature 2
Effective Date and Transition 2

REFERENCES **2**

Relevant Issue Papers 2

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for real estate acquisition, development and construction (ADC) arrangements and provides guidance on when to account for ADC arrangements as mortgage loans and when to account for ADC arrangements as investments in real estate or real estate joint ventures.

SUMMARY CONCLUSION

2. ADC arrangements shall be defined as lending agreements that are made to the owner of property to finance the acquisition, development and construction of real estate projects on the property in which the lender participates in the expected residual profits. Expected residual profit is the amount of profit, whether called interest or another name (e.g., equity kicker) above a reasonable amount of interest and fees expected to be earned by the lender. ADC arrangements shall include participations in loans and purchased loans that meet that definition of ADC arrangements.

3. If the lender is expected to receive over 50% of the expected residual profits of the project, the ADC arrangement shall be classified and accounted for as an investment in real estate in accordance with *SSAP No. 40R—Real Estate Investments*. If the lender is expected to receive 50% or less of the expected residual profits, the ADC arrangement shall be classified and accounted for as a loan or as a real estate joint venture, depending on the circumstances.

4. If any of the characteristics in paragraph 9.b. through 9.e. of *AcSEC Practice Bulletin 1*, "Exhibit I, ADC Arrangements" (PB1), or if a qualifying personal guarantee (as defined in PB1) is

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present, the ADC arrangement shall be classified and accounted for as a construction loan in accordance with *SSAP No. 37—Mortgage Loans*. Otherwise, the ADC arrangement shall be classified and accounted for as a real estate joint venture in accordance with *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*.

5. The factors that are evaluated in determining the accounting treatment at inception may subsequently change for some ADC arrangements, for example, as a result of a renegotiation of the terms. Consequently, the accounting treatment for an ADC arrangement shall be periodically reassessed, as described in paragraph 20 of PB1. Any changes in classification shall result in a reclassification of the asset at the amount the asset should be reported at under its new classification with the net effect, if any, charged to income in the period that the change in classification is made.

6. Regardless of whether an ADC arrangement is accounted for as an investment in real estate, a joint venture, or a mortgage loan, the ADC arrangement meets the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and is an admitted asset to the extent it conforms to the requirements of this statement.

7. ADC arrangements may involve related parties, in which case, *SSAP No. 25—Affiliates and Other Related Parties* shall also be followed.

Relevant Literature

8. This statement adopts PB1, "Exhibit I, ADC Arrangements" and *FASB Emerging Issues Task Force No. 86-21, Application of the AICPA Notice to Practitioners regarding Acquisition, Development, and Construction Arrangements to Acquisition of an Operating Property.*

Effective Date and Transition

9. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 38—Acquisition, Development and Construction Arrangements*

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Statement of Statutory Accounting Principles No. 39

Reverse Mortgages

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Valuation and Impairment 2
Disclosures 3
Relevant Literature 4
Effective Date and Transition 4

REFERENCES **4**

Relevant Issue Papers 4

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for reverse mortgages.

SUMMARY CONCLUSION

2. A reverse mortgage loan is defined as a non-recourse loan with the following characteristics:

   a. It is secured by a mortgage against the primary residence of the borrower;

   b. It guarantees a stream of cash disbursements to the borrower, either for the life of the borrower with no limit or up to a set percentage of the value of the residence or as a line of credit which the borrower can draw upon as needed; and

   c. It has no maturity date and requires no repayment until one of the following events occur:

      i. The borrower dies;

      ii. The borrower sells the residence;

      iii. The residence ceases to be the borrower's primary residence; or

      iv. The borrower terminates the loan by paying back the outstanding balance.

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3. A reverse mortgage meets the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and is an admitted asset to the extent it conforms to the requirements of this statement. Reverse mortgages shall be recorded as an other invested asset on the reporting entity's statement of financial position and Schedule BA, Other Long-Term Invested Assets, of the annual statement.

4. To be considered admitted assets, investments in reverse mortgages are limited to first lien mortgages only.

5. All expenses associated with acquiring reverse mortgages shall be recognized immediately as investment expense.

6. Revenue associated with originating or otherwise acquiring reverse mortgages, including non-refundable fees, shall be amortized to investment income on a straight line basis over the period from inception to the expected maturity date.

7. Generally, fees are not paid by the borrower at the time of closing but become payable when the outstanding balance of the reverse mortgage becomes due. In these situations, no accounting entries are recorded at the time of closing. Investment income shall be recognized and the outstanding balance of the loan shall increase as the fees are amortized.

8. If fees are paid by the borrower at the time of closing, a liability shall be established. Investment income shall be recognized and the liability shall decrease as the fees are amortized.

9. Interest is payable by the borrower when the outstanding balance of the reverse mortgage becomes due. Accrued interest shall be calculated on the outstanding balance of the loan on a monthly basis. As it is earned, accrued interest shall be recorded to investment income and added to the outstanding balance of the loan.

10. The outstanding balance of the reverse mortgage shall include the accumulation of amounts disbursed, accrued interest, and amortized origination fees (i.e., origination fees not paid by the borrower at the time of closing). Neither the fair value of the underlying collateral nor the obligation for future cash payments guaranteed by the lender are recorded.

11. The lender's equity in the appreciation of the property, if any, is not recorded until realized upon the sale of the home.

Valuation and Impairment

12. The major categories of risk affecting reverse mortgages are:

a. Mortality risk—risk of loan payments extending beyond the borrower's original projected life expectancy. Since most reverse mortgages guarantee a continuing monthly payment to the borrower, there is the possibility that the borrower will collect cash payments and accrue interest exceeding the ultimate disposal value of the collateral. In situations where loan payments extend beyond the borrower's original projected life expectancy, the reporting entity will experience a diminished yield, and may experience a loss. Reverse mortgage contracts shall be combined into groups which are of sufficient size to provide an actuarially and statistically credible basis for estimating life expectancy to project future cash flows;

b. Collateral risk—risk of deterioration in the value of the collateral such that it is insufficient to cover the loan balance. This risk shall be evaluated loan-by-loan and is based on information obtained from periodic real estate appraisals and other pertinent information;

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c. Interest rate risk—risk of interest rates rising on adjustable rate reverse mortgages to the extent that accrued interest creates a collateral risk.

13. Reverse mortgages subject to the risks addressed in paragraph 12 shall be reported net of an appropriate actuarially calculated valuation reserve. Assumptions shall be applied consistently to similar loans. The assumptions, cash flow projections, and evaluation of risk shall be reviewed and updated at least annually. The fair value of the underlying collateral and the obligation for future cash payments guaranteed by the lender shall be considered in cash flow projections. Future appreciation in property value beyond the valuation date shall not be included in the projection of cash receipts.

14. If the impairment is temporary, any resulting adjustment shall be made to the valuation reserve (contra-asset) and unrealized gains and losses. Subsequent to the initial measurement of impairment, if there is a significant change (increase or decrease) in the risk factors affecting the value of the mortgage, the reporting entity shall adjust the valuation allowance in accordance with paragraph 13; however, the net carrying amount of the loan shall at no time exceed the recorded investment in the loan. The term recorded investment in the loan is distinguished from net carrying amount of the loan because the latter term is net of the valuation allowance, while the former term is not. The recorded investment (including accrued interest, net deferred loan fees, and unamortized premium or discount) in the loan does, however, reflect any direct write down of the investment. If the impairment is other than temporary (INT 06-07), the investment shall be written down to fair value as the new cost basis and the amount of the write down shall be accounted for as a realized loss. The new basis shall not be changed for subsequent recoveries in fair value. A reverse mortgage shall be considered to be impaired when, based on current information and events, it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of the reverse mortgage. "According to the contractual terms" means that both the contractual principal payments and contractual interest payments of the loan will be collected as specified in the reverse mortgage agreement.

Disclosures

15. The following disclosures shall be made for reverse mortgages in the financial statements:

a. A description of the reporting entity's accounting policies and methods, including the statistical methods and assumptions used in calculating the reserve;

b. General information regarding the reporting entity's commitment under the agreement;

c. The reserve amount which is netted against the asset value;

d. Investment income or loss recognized in the period as a result of the re-estimated cash flows.

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16. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

17. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~17.~~18. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 39—Reverse Mortgages*

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Statement of Statutory Accounting Principles No. 40 – Revised

Real Estate Investments

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised December 12, 2014
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 149 effective January 1, 2015
Affects	Supersedes SSAP No. 77 with guidance incorporated August 2012; Nullifies INT 04-18; Nullifies and incorporates INT 99-16, INT 99-22, INT 99-25, INT 08-02 and INT 08-07
Affected by	Paragraphs 11, 12 and 25 superseded by SSAP No. 90
Interpreted by	INT 06-13
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Income, Expenses, and Capital Improvements 5
Sale of Real Estate 5
Real Estate Projects Under Development 6
Participating Mortgage Loans 6
Disclosures 6
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REFERENCES **9**

Relevant Issue Papers 9

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for real estate investments.

SUMMARY CONCLUSION

2. Real estate investments are defined as directly-owned real estate properties and single real estate property investments that are directly and wholly-owned through a limited liability company (LLC) that meet all of the criteria in paragraph 4. Real estate investments may be acquired in exchange for consideration (including but not limited to cash, a contract for deed or mortgage, or other non-cash consideration) obtained through foreclosure or voluntary conveyance in satisfaction of a mortgage loan, or received as contributed surplus. Real estate investments meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

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3. Real estate investments include certain acquisition, development and construction arrangements (ADC) as defined in *SSAP No. 38—Acquisition, Development and Construction Arrangements*.

4. A single real estate property investment that is wholly-owned by an LLC that is directly[1] and wholly-owned by the reporting entity shall be captured within this statement and reported on Schedule A – Real Estate if all of the following criteria are met. Real estate owned through an LLC that meets the stated criteria shall follow all statutory requirements within this statement[2]. Real estate owned through an LLC that does not meet the criteria shall be reported on Schedule BA – Other Long-Term Invested Assets. Regardless if reported on Schedule A or Schedule BA, all LLC's owned by the reporting entity shall be detailed in Schedule Y.

a. The real estate LLC has no transactions of its own other than transactions associated with an ownership structure utilized only for the ownership and management of a single real estate investment exclusively for the reporting entity (e.g., real estate taxes). A reporting entity may have more than one LLC that wholly-owns a single real estate property investment, but each LLC must separately comply with the paragraph 4 conditions, and be separately reported on Schedule A. All transactions of the LLC shall be reported as transactions of the reporting entity pursuant to the guidance in paragraphs 15-17.

b. The LLC only owns a single real estate property supported by an appraisal pursuant to paragraphs 13-14. A single real estate property can include multiple parcels of land and more than one structure; however, to be considered a single real estate property, the multiple of parcels of land and structure(s) must be contiguously located and managed together as a single asset (with reasonable allowances for public access routes). Criteria that may assist with determining a single real estate property would include the legal definition of the property, real estate tax assessments, postal address, the appraisal and the management and use of the property.

c. The reporting entity solely controls the real estate property in a manner similar to directly-owned real estate. As such, the reporting entity controls others' access to the real estate, and the real estate must be able to be sold exactly as, and as promptly as, directly-owned real estate.

d. The reporting entity solely and distinctly possesses all risks (other than the limitation of potential liability afforded by the LLC structure itself) and rewards of ownership of the real estate investment, without any constraints imposed by the LLC. A standard mortgage or encumbrance by an unrelated party is not considered a sharing of risks or rewards and is permitted within this guidance. However, a participating mortgage loan (paragraph 22) with related or unrelated parties, or loans or other encumbrances from related parties, would result with the reporting entity not solely and distinctly possessing all risks and rewards of the real estate investment.

e. The reporting entity is the only member of the LLC. The LLC is not comprised of any other members, including: groups, competing interests, mutual beneficial interests, or co-venturers. The single-member ownership is required even if other members in the LLC are affiliates. An LLC comprised of affiliated parties is not within scope of this statement.

[1] For example, qualifying LLCs that are owned by a downstream holding company are not within scope of this statement regardless if the downstream holding company is wholly-owned by the reporting entity.

[2] The inclusion in this statement of real estate owned by a single member LLC is not an election by the reporting entity. All real estate owned in an LLC meeting the criteria in paragraph 4 are required to be captured within this statement, and are subject to this statement's requirements for valuation and admittance. Departures from the requirements within this SSAP, or continuing to follow SSAP No. 48 for these investments would be considered a departure from NAIC statutory accounting principles subject to permitted or prescribed practice disclosure requirements.

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f. There shall be no apportionment by the LLC or the reporting entity of the appraised value, expenses or income from the single real estate property to any other entity or between the general or separate account.

5. Real estate investments shall be reported in accordance with the following balance sheet categories, with parenthetical disclosure of the amount of related encumbrances:

a. Properties occupied by the company – depreciated cost, less encumbrances;

b. Properties held for the production of income – depreciated cost, less encumbrances; and

c. Properties held for sale – lower of depreciated cost or fair value, less encumbrances and estimated costs to sell the property. (Paragraph 21 of *SSAP No. 90—Impairment or Disposal of Real Estate Investments* provides criteria that must be met for this real estate classification.)

6. Any real estate which is owned by and is more than 50% occupied by the reporting entity and its affiliates shall be considered property occupied by the company. "More than 50% occupied" shall mean that the square footage occupied by the reporting entity and its affiliates totals more than 50% of the rentable square footage of the property, including common areas. This shall include property occupied by the company which is not necessarily home office (e.g., claims processing, data processing and branch centers). Property which does not meet this 50% requirement shall be classified as property held for the production of income or property held for sale, consistent with SSAP No. 90.

7. Encumbrances represent outstanding mortgages or other debt related to the real estate investment and any unpaid accrued acquisition or construction costs. Participating mortgage loan liabilities are addressed in paragraphs 22-24. Interest expense shall be included in investment expenses.

8. The cost of real estate represents the fair value of the consideration exchanged plus any costs incurred to place the real estate asset in usable condition, including but not limited to, brokerage fees, legal fees, demolition, clearing and grading, fees of architects and engineers, any additional expenditures made for equipment and fixtures that are made a permanent part of the structure and certain interest costs as provided for in *SSAP No. 44—Capitalization of Interest*. Where cost includes both land and building, the cost shall be allocated among the assets purchased based on the relative values determined using appraisals, as described in paragraph 13. The cost shall be reduced by any amounts received for sales of rights or privileges in connection with the property or by any cash recoveries received after acquiring title to the property. The cost of real estate which has been foreclosed upon shall be initially established in accordance with *SSAP No. 36—Troubled Debt Restructuring* and *SSAP No. 37—Mortgage Loans*. The cost of contributed real estate shall be initially established in accordance with *SSAP No. 95—Nonmonetary Transactions* as a nonreciprocal transfer.

9. Internal preacquisition costs classified as nonoperating at the date of a property acquisition (that otherwise meet the requirements of paragraph 4 of FAS 67) shall be capitalized. If the entity subsequently determines that the property should have been classified as operating at the date of acquisition, such costs should be charged to expense and any additional costs shall be expensed as incurred. If internal preacquisition costs classified as operating at the date of acquisition were expensed as incurred, and the entity subsequently determines that the property should have been classified as nonoperating, the expensed costs shall remain as originally reported and shall not be reclassified to capitalized costs.

10. The cost of property included in real estate investments, other than land, shall be depreciated over the estimated useful life, not to exceed fifty years. Depreciation expense shall be included in investment expenses.

11. Properties occupied by the company and properties held for the production of income shall be carried at depreciated cost less encumbrances unless events or circumstances indicate the carrying amount

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of the asset (amount prior to reduction for encumbrances) may not be recoverable. Paragraph 5 of *FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* (FAS 121), provides examples of events or changes in circumstances which indicate that the recoverability of the carrying amount of properties occupied by the company or properties held for the production of income should be assessed. If the events or changes in circumstances set forth in paragraph 5 of FAS 121 are present or if other events or changes in circumstances indicate that the carrying amount of properties occupied by the company or properties held for the production of income may not be recoverable, the entity shall determine whether an impairment loss must be recognized in accordance with paragraph 6 of FAS 121. Property occupied by the company shall be evaluated using the asset grouping approach of paragraph 8 of FAS 121. An impairment loss is measured as the amount by which the individual carrying amounts exceed the fair value of properties occupied by the company or properties held for the production of income. Fair value is determined in accordance with paragraph 13 of this statement. If the fair value of the asset is less than the carrying value, the asset shall be written down to the fair value thereby establishing a new cost basis. The new cost basis shall not be changed for subsequent recoveries in fair value. The adjustment shall be recorded in the statement of operations as a realized loss.

12. Properties that the reporting entity has the intent to sell or is required to sell shall be classified as properties held for sale and carried at the lower of depreciated cost or fair value less encumbrances and estimated costs to sell the property consistent with paragraph 16 of FAS 121. The intent to sell a property exists when management, having the authority to approve the action, has committed to a plan to dispose of the asset, either by sale or abandonment. Fair value of the asset shall be determined in accordance with paragraph 13 of this statement. Subsequent revisions to the fair value of the asset shall be accounted for in accordance with paragraph 17 of FAS 121.

13. The current fair value of real estate shall be determined on a property by property basis (i.e., increases in the fair value of one property shall not be used to offset declines in fair value of another). If market quotes are unavailable, estimates of fair value shall be determined by an appraisal (internal or third party), which is based upon an evaluation of all relevant data about the market, considering the following:

a. A physical inspection of the premises;

b. The present value of future cash flows generated by the property (Discounted Cash Flows), or capitalization of stabilized net operating income (Direct Capitalization);

c. Current sales prices of similar properties with adjustments for differences in the properties (Sales Comparison Approach);

d. Costs to sell the property if the reporting entity does not have the intent or ability to hold the real estate as an investment; and

e. Replacement costs of the improvements, less depreciation, plus the value of the land (Cost Approach).

14. For all properties held for the production of income, the reporting entity must maintain an appraisal that is no more than five years old as of the reporting date. For all properties held for sale, an appraisal shall be obtained at the time such property is classified as held for sale, and subsequently an appraisal shall be maintained that is no more than five years old as of the reporting date. However, if conditions indicate there has been a significant decrease in the fair value of a property, a current appraisal shall be obtained. Additionally, appraisals shall be obtained for real estate investments at the time of foreclosure or contribution. Contributed real estate shall be supported by an independent third party appraisal at the date of contribution. If any of the previous conditions exist but an appraisal has not been

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obtained, the related property shall be considered a nonadmitted asset until the required appraisals are obtained.

Income, Expenses, and Capital Improvements

15. Rental income on real estate leased is addressed in *SSAP No. 22R—Leases*, which requires that rental income be included in investment income. Expenses incurred in operating the real estate investment, including but not limited to, real estate taxes, utilities, and ordinary repair and maintenance, shall be charged to expense as incurred and included in investment expenses.

16. Expenditures that are necessary to put the asset back into good operating condition or to keep it in good operating condition, shall be charged to expense as incurred. Expenditures that add to or prolong the life of the property shall be added to the cost of the real estate (capitalized) and depreciated over the remaining estimated useful life of the property. If the property was fully depreciated at the time capital improvements are incurred, the capital improvements shall be capitalized and depreciated over the remaining extended useful life of the asset.

17. A reporting entity shall include in both its income and expenses an amount for rent relating to its occupancy of its own buildings. The amount recorded shall be at a rate comparable to rent received from others and/or rental rates of like property in the same area. If this is unavailable, it shall be derived from consideration of the repairs, expenses, taxes, and depreciation incurred, plus interest added at an average fair rate on the carrying value of the reporting entity's investment in its home office building.

Sale of Real Estate

18. Recognition of profit on sales of real estate investments shall be accounted for in accordance with *FASB Statement No. 66, Accounting for Sales of Real Estate* (FAS 66), except as modified in paragraph 20 of this statement, *FASB Emerging Issues Task Force No. 87-9*, *Profit Recognition on Sales of Real Estate with Insured Mortgages or Surety Bonds, FASB Emerging Issues Task Force No. 87-29, Exchange of Real Estate Involving Boot, FASB Interpretation No. 43, Real Estate Sales an interpretation of FASB Statement No. 66* (FIN 43) and *FASB Emerging Issues Task Force No. 00-13, Determining Whether Equipment is "Integral Equipment" Subject to FASB Statements No. 66 and No. 98*(INT 06-13). This statement applies to all sales of real estate including real estate with property improvements or integral equipment. The terms "property improvements" and "integral equipment" refer to any physical structure or equipment attached to the real estate that cannot be removed and used separately without incurring significant costs, such as an office building. Additionally, this guidance applies to all transfers of financial assets that are in substance real estate.

19. Profit shall be recognized in full when real estate is sold, provided (a) the profit is determinable, that is, the collectibility of the sales price is reasonably assured or the amount that will not be collectible can be estimated, and (b) the earnings process is virtually complete, that is, the seller is not obliged to perform significant activities after the sale to earn the profit. Unless both conditions exist, recognition of all or part of the profit shall be postponed. Profit shall not be recognized by the full accrual method until all of the following criteria are met:

a. A sale is consummated;

b. The buyer's initial and continuing investments are adequate to demonstrate a commitment to pay for the property;

c. The seller's receivable is not subject to future subordination; and

d. The seller has transferred to the buyer the usual risks and rewards of ownership in a transaction that is in substance a sale and does not have a substantial continuing involvement with the property after the sale.

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20. The calculation of the buyer's initial investment specified in paragraph 9 of FAS 66 shall be modified to reflect that buyer's notes must be supported by letters of credit from institutions that are listed by the Securities Valuation Office of the National Association of Insurance Commissioners as meeting credit standards to be included in determining the buyer's initial investment. Any profit or loss is considered a realized gain or loss in the year of the sale in accordance with FAS 66.

Real Estate Projects Under Development

21. Costs and initial rental operations of real estate projects under development, which include ADC arrangements accounted for as real estate under the provisions of SSAP No. 38, shall be accounted for in accordance with *FASB Statement No. 67, Accounting for Costs and Initial Rental Operations of Real Estate* Projects (FAS 67). Costs incurred in connection with real estate projects shall be expensed as incurred unless the criteria established in FAS 67 are met. The statement value of a real estate project, or parts thereof, held for sale or development and sale shall not exceed the estimated selling price in the ordinary course of business less estimated costs of completion (to stage of completion assumed in determining the selling price), holding, and disposal (net realizable value). If costs exceed net realizable value, capitalization of eligible costs shall continue, however, an allowance shall be provided to reduce the admitted value to estimated net realizable value.

Participating Mortgage Loans

22. A participating mortgage loan is established when the lender is entitled to participate in appreciation of the fair value of mortgaged real estate, the results of operations of the mortgaged real estate project, or in both. Mortgage loan participation features should be recorded at fair value at inception of the loan. The borrower should recognize a participation liability for the determined fair valued amount, with a corresponding debit to a debt discount account. The debt discount should be amortized by the interest method, using the effective interest rate. After inception, adjustment of the participation liability should occur at each reporting date to current fair value. The corresponding debit or credit should be to the related debt discount account. The revised debt discount should be amortized prospectively, using the effective interest rate method.

23. The real estate investment with the participating mortgage loan should be reported in accordance with paragraph 5, with no adjustment for appreciation of fair value.

24. Extinguishment of participating mortgage loans prior to the due date should be determined in accordance with *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. Gains or losses from early extinguishment should be determined in considering the difference between the recorded amount of debt (including unamortized debt discount and the participation liability) and the amount exchanged to extinguish the debt.

Disclosures

25. An entity that recognizes an impairment loss shall disclose all of the following in financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment;

b. The amount of the impairment loss and how fair value was determined; and

c. The caption in the statement of operations in which the impairment loss is aggregated.

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26. An entity that engages in retail land sales operations shall disclose:

a. Maturities of accounts receivable for each of the five years following the date of the financial statements;

b. Delinquent accounts receivable and the method(s) for determining delinquency;

c. The weighted average and range of stated interest rates of receivables;

d. Estimated total costs and estimated dates of expenditures for improvements for major areas from which sales are being made over each of the five years following the date of the financial statements; and

e. Recorded obligations for improvements.

27. An entity that holds real estate investments through an LLC, which qualifies for inclusion in this statement because all the criteria in paragraph 4 are met, shall separately report each investment on Schedule A, and code the real estate as wholly-owned through an LLC.

28. An entity that holds real estate investments with participating mortgage loan features should disclose:

a. Aggregate amount of participating mortgage obligations at the balance-sheet date, with separate disclosure of the aggregate participation liabilities and related debt discounts.

b. Terms of participations by the lender in either the appreciation in the fair value of the mortgaged real estate project or the results of operations of the mortgaged real estate project, or both.

29. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

30. This statement adopts FAS 66, with modification to paragraph 10 to indicate that only letters of credit from institutions listed by the Securities Valuation Office of the National Association of Insurance Commissioners shall be included in determining the buyer's initial investment. Additionally, as they relate to FAS 66, the following are adopted: *FASB Emerging* Issues *Task Force Issue No. 86-6, Antispeculation Clauses in Real Estate Sales Contracts*, *FASB Emerging Issues Task Force No* 87-9*, Profit Recognition on Sales of Real Estate with Insured Mortgages or Surety Bonds, FASB Emerging Issues Task Force No* 87-29*, Exchange of Real Estate Involving Boot, FASB Emerging Issues Task Force No. 88-12, Transfer of Ownership Interest as Part of Down Payment under FASB Statement No. 66*, *FASB Emerging Issues Task Force No. 88-24, Effect of Various Forms of Financing under FASB Statement No. 66, FASB Emerging Issues Task Force No. 06-8: Applicability of the Assessment of a Buyer's Continuing Investment under FASB Statement No. 66 for Sales of Condominiums,* with modification consistent to paragraph 9 of FAS 66, in which continuing investment payments made in the form of buyer's notes must be supported by letters of credit from institutions that are listed by the Securities Valuation Office of the National Association of Insurance Commissioners as meeting credit standards to be included in determining the buyer's initial investment, and *FASB Emerging Issues Task Force No. 07-6: Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66, When the Arrangements Includes a Buy Sale Clause*.

31. This statement adopts *FASB Interpretation No. 43, Real Estate Sales, an Interpretation of FASB Statement No. 66* (FIN 43), which clarifies that the phrase "all real estate sales" includes sales of real estate with property improvements or integral equipment that cannot be removed and used separately from the real estate without incurring significant costs. This statement adopts *FASB Emerging Issues Task*

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Force No. 84-17, Profit Recognition on Sales of Real Estate with Graduated Payment Mortgages or Insured Mortgages, FASB Emerging Issues Task Force No. 89-13, Accounting for the Cost of Asbestos Removal, FASB Emerging Issues Task Force No. 89-14, Valuation of Repossessed Real Estate, FASB Emerging Issues Task Force No. 90-8, Capitalization of Costs to Treat Environmental Contamination, FASB Emerging Issues Task Force No. 95-23, The Treatment of Certain Site Restoration/Environmental Exit Costs When Testing a Long-Lived Asset for Impairment, FASB Emerging Issues Task Force 97-11: Accounting for Internal Costs Relating to Real Estate Property Acquisitions, FASB Emerging Issues Task Force No. 98-8: Accounting for Transfers of Investments That Are in Substance Real Estate and *FASB Emerging Issues Task Force No. 00-13, Determining Whether Equipment is "Integral Equipment" Subject to FASB Statements No. 66 and No. 98,* which clarifies the term "integral equipment" as used in this statement.

32. This statement adopts FAS 121 for real estate investments except for paragraphs 13, 14.c. and 14.d. which are rejected in *SSAP No. 68—Business Combinations and Goodwill*. This statement adopts FAS 67, AICPA *Statement of Position 92-1, Accounting for Real Estate Syndication Income,* and AICPA *Statement of Position 92-3*, *Accounting for Foreclosed Assets*. This statement also adopts *FAS 152: Accounting for Real Estate Time-Sharing Transactions, an amendment to FASB Statements No. 66 and 67*. FAS 152 is adopted as it modifies previously adopted GAAP guidance in FAS 66 and FAS 67 to identify the guidance that should/should not be applied to real estate time-sharing transactions. This guidance is adopted as it impacts the scope of previous adopted GAAP guidance to prevent an unnecessary GAAP to SAP difference. However, real estate time-sharing transactions are considered not applicable for statutory accounting, and the GAAP guidance in SOP 04-2 is rejected in Issue Paper No. 99.

33. This statement adopts *AICPA Statement of Position 97-1: Accounting by Participating Mortgage Loan* Borrowers (SOP 97-1) regarding the borrower's accounting for a participating mortgage loan.

34. This statement rejects paragraph 52 of *FASB Statement No. 60, Accounting and Reporting by Insurance* Enterprises and *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins*, "Chapter 10, Taxes, Section A—Real Estate and Personal Property Taxes."

Effective Date and Transition

35. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Correction of Errors*. Guidance in paragraph 8 was originally contained in *INT 99-16: EITF No. 97-11: Accounting for Internal Costs Relating to Real Estate Property Acquisitions* and was effective October 4, 1999. Guidance in paragraph 15 was originally contained in *INT 99-25: Accounting for Capital Improvements* and was effective December 6, 1999. Guidance in paragraphs 18-20 was previously included within *SSAP No. 77—Real Estate Sales* and was effective for years beginning January 1, 2002. The original guidance included in this standard from SSAP No. 77 is retained for historical purposes in Issue Paper No. 106. Guidance related to EITF 06-8 referenced in paragraph 30 was incorporated from *INT 08-02: EITF 06-8: Applicability of the Assessment of a Buyer's Continuing Investment under FASB Statement No. 66 for Sales of Condominiums* and was effective for periods beginning May 31, 2008. The guidance reflected in paragraph 30 adopting *EITF 07-6: Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66, When the Agreement Includes a Buy-Sell Clause* was incorporated from *INT 08-07: EITF 07-6, Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66 When the Agreement Includes a Buy-Sell Clause,* and was effective September 22, 2008.

36. The substantive revisions to incorporate real estate property investments that are wholly-owned by an LLC that is directly and wholly-owned by the reporting entity in accordance with the criteria detailed in paragraph 4 are effective as of January 1, 2015. For these investments previously reported within SSAP No. 48 and owned as of the effective date, the reporting entity shall recognize a cumulative

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effect of a change in accounting principle as if the entity had followed this statement since acquisition of the property. The change from applying these substantive revisions shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

37. To determine statement value for real estate owned through an LLC as of the paragraph 36 effective date, the reporting entity shall:

a. Allocate the original cost of the real estate investment to land and property other-than-land pursuant to paragraph 8.

b. To arrive at the current depreciated cost for property (excluding land), the entity shall apply the depreciation that would have occurred if this statement had been applied since acquisition, in accordance with the original expected useful life, adjusted for subsequent capital improvements pursuant to paragraph 16.

c. The depreciated cost calculated under paragraph 37.b. shall be compared to a current appraisal to determine if an impairment assessment is required under SSAP No. 90. Recognition of impairment shall result in a new cost basis for the property, with recalculation of the depreciation based on the property's remaining useful life, as limited by the terms of this statement.

d. The depreciated cost, reflecting any impairment from paragraph 37.c., less encumbrances, shall be recognized as the real estate investment as of the effective date.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 23—Property Occupied by the Company*
- *Issue Paper No. 40—Real Estate Investments*
- *Issue Paper No. 106—Real Estate Sales – An Amendment to SSAP No. 40—Real Estate Investments*
- *Issue Paper No. 149—Wholly-Owned Single Real Estate Property in an LLC*

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Statement of Statutory Accounting Principles No. 41 – Revised

Surplus Notes

STATUS

Type of Issue	Common Area
Issued	Initial draft; Substantively revised April 3, 2016
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 151 effective January 1, 2017
Affects	Nullifies and incorporates INT 04-02
Affected by	No other pronouncements
Interpreted by	INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for issuers and holders of surplus notes, and for holders of capital notes. Statutory accounting principles for issuers of capital notes are provided in *SSAP No. 15—Debt and Holding Company Obligations*.

SUMMARY CONCLUSION

Issuers of Surplus Notes

2. Reporting entities sometimes issue instruments that have the characteristics of both debt and equity. These instruments are commonly referred to as surplus notes, the term used herein, but are also referred to as surplus debentures or contribution certificates. These instruments are used for various reasons, including but not limited to:

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a. Providing regulators with flexibility in dealing with problem situations to attract capital to reporting entities whose surplus levels are deemed inadequate to support their operations;

b. Providing a source of capital to mutual and other types of non-stock reporting entities who do not have access to traditional equity markets for capital needs;

c. Providing an alternative source of capital to stock reporting entities, although not for the purpose of initially capitalizing the reporting entity.

3. Surplus notes issued by a reporting entity that are subject to strict control by the commissioner of the reporting entity's state of domicile and have been approved as to form and content shall be reported as surplus and not as debt only if the surplus note contains the following provisions:

a. Subordination to policyholders;

b. Subordination to claimant and beneficiary claims;

c. Subordination to all other classes of creditors other than surplus note holders; and

d. Interest payments and principal repayments require prior approval of the commissioner of the state of domicile.

4. Proceeds received by the issuer must be in the form of cash or other admitted assets having readily determinable values and liquidity satisfactory to the commissioner of the state of domicile.

5. Interest shall not be recorded as a liability nor an expense until approval for payment of such interest has been granted by the commissioner of the state of domicile. All interest, including interest in arrears, shall be expensed in the statement of operations when approved for payment. Unapproved interest shall not be reported through operations, shall not be represented as an addition to the principal or notional amount of the instrument, and shall not accrue further interest, i.e., interest on interest.

6. As of the date of approval of principal repayment by the commissioner of the state of domicile, the issuer shall reclassify such approved payments from surplus to liabilities.

7. Costs of issuing surplus notes (e.g., loan fees and legal fees) shall be charged to operations when incurred.

8. Discount or premium, if any, shall be reported in the balance sheet as a direct deduction from or addition to the face amount of the note. Such discount or premium shall be charged or credited to the statement of operations concurrent with approved interest payments on the surplus note and in the same proportion or percentage as the approved interest payment is to the total estimated interest to be paid on the surplus note.

Holders of Capital or Surplus Notes

9. Investments in capital or surplus notes meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement. Additionally, the amount admitted is specifically limited to the following two provisions:

a. The admitted asset value of a capital or surplus note shall not exceed the amount that would be admitted if the instrument was considered an equity instrument and added to any other equity instruments in the issuer held directly or indirectly by the holder of the capital or surplus note.

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b. The surplus note shall be nonadmitted if issued by an entity that is subject to any order of liquidation, conservation, rehabilitation or any company action level event based on its risk-based capital. Subsequent to this nonadmittance, if any of the conditions described ceased to exist, the holder may admit the surplus note at the value determined under paragraph 11. If a surplus note was nonadmitted pursuant to this paragraph, and the surplus note was ultimately determined to be other-than-temporarily impaired, the reporting entity shall recognize a realized loss for the portion of the surplus note determined to be other-than-temporarily impaired, with elimination of a corresponding amount of the previously nonadmitted assets.

10. Capital or surplus notes shall be valued in accordance with paragraph 11. Pursuant to that paragraph, the value is determined by NAIC credit rating provider (CRP) ratings. Part One – Capital and Surplus Debentures of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* provides guidance in determining the NAIC designation for these investments.

11. If the capital or surplus note has been rated by an NAIC CRP and has a designation equivalent of NAIC 1 or NAIC 2, then it shall be reported at amortized cost. If the capital or surplus note is not CRP rated or has an NAIC designation equivalent of NAIC 3 through 6, then the balance sheet amount shall be reported at the lesser of amortized cost or fair value, with fluctuations in value reflected as unrealized valuation changes.

12. For reporting entities required to maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

13. For surplus notes issued and held (directly or indirectly) between insurance reporting entities and subsidiary, controlled and affiliated entities, the guidance in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* requires adjustment to prevent double-counting of surplus notes. For example, an insurance reporting entity is not permitted to report the issuance of a surplus note as an increase in surplus and have an asset representing an investment in the SCA that includes the issued surplus note (held by an SCA). Pursuant to SSAP No. 97, the "investment in the SCA" shall be adjusted to eliminate the surplus note issued by the direct or indirect parent insurance reporting entity. This treatment shall also apply for instances in which the SCA acquires any portion of outstanding surplus notes issued by the direct or indirect parent through any means (e.g., directly acquired from the parent, acquired through a third-party broker, or via the market).

Income

14. Only interest that has been approved by the issuer's domiciliary commissioner shall be accrued as income by a holder of surplus notes. Interest income for any period consists of interest collected during the period and the change in the due and accrued interest between the beginning and end of the period approved by the issuer's domiciliary commissioner.

15. Except for the specific limitations on recognizing interest income in paragraph 14, investment income, and the recognition of uncollectible accrued interest, shall follow the guidance in *SSAP No. 34—Investment Income Due and Accrued.*

Impairment

16. An other-than-temporary impairment(INT 06-07) shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of the surplus note. Pursuant to the terms of a surplus note, payments of principal and interest may be delayed if the issuer's domiciliary commissioner does not approve payment. Extended delays of either principal or

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interest shall trigger an evaluation for an other-than-temporary impairment. An other-than-temporary impairment shall be recognized in situations when the reporting entity has made a decision to sell a surplus note prior to its maturity at an amount below its carrying value. If it is determined that a decline in fair value is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the difference between the surplus note's carrying value and the fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of impairment shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR, realized losses shall be accounted for in accordance with SSAP No. 7.

17. In periods subsequent to the recognition of an other-than-temporary impairment loss for a surplus note, the holder of the surplus note shall account for the other-than-temporarily impaired surplus note as if the surplus note had been purchased on the measurement date of the other-than-temporary impairment. The fair value of the surplus note on the measurement date shall become the new cost basis of the surplus note and the new cost basis shall not be adjusted for subsequent recoveries in fair value. The discount or reduced premium recorded for the surplus note, based on the new cost basis, shall be amortized over the remaining life of the surplus note in the prospective manner based on the amount and timing of future estimated cash flows. The surplus note shall continue to be subject to impairment analysis for each subsequent reporting period. Future declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses.

Disclosures

18. The notes to the financial statements of a reporting entity that issues surplus notes shall disclose the following as long as the surplus notes are outstanding:

a. Date issued;

b. Description and fair value of the assets received;

c. Holder of the note or, if public, the names of the underwriter and trustee, with identification on whether the holder of the surplus note is a related party per *SSAP No. 25—Affiliates and Other Related Parties*;

d. Original issue amount of note;

e. Carrying value of note;

f. The rate at which interest accrues;

g. Maturity dates or repayment schedules, if stated;

h. Unapproved interest and/or principal;

i. Life-to-date and current year approved interest and principal recognized;

    i. Percentage interest payments offset through 'administrative offsetting' (not inclusive of amounts paid to a third-party liquidity provider). For example, if $100 in interest was recognized through the year, $10 of which was remitted to a third-party liquidity provider and the reminder $90 was offset, the reporting entity shall report 100% as offset.

j. Disclosure of whether the surplus note was issued as part of a transaction with any of the following attributes:

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i. Do surplus note/associated asset terms negate or reduce cash flow exchanges, and/or are amounts payable under surplus note and amounts receivable under other agreements contractually linked? (For example, the asset provides interest payments only when the surplus note provides interest payments.)

ii. Are any amounts due under surplus notes and associated assets netted or offset (partially or in full) thus eliminating or reducing the exchange of cash or assets that would normally occur throughout the duration, or at maturity, of the agreement? (This may be referred to as administrative offsetting.)

iii. Were the proceeds from the issuance of a surplus note used to purchase an asset directly or indirectly from the holder of the surplus note?

k. Principle amount and fair value of assets received upon surplus note issuance, if applicable;

l. Subordination terms;

m. Liquidation preference to the reporting entity's common and preferred shareholders;

n. The repayment conditions and restrictions;

o. Information about any guarantees, support agreements or related party transactions associated with the surplus note issuance, and whether payments have been made under such agreements.

19. If a reporting entity has ceded business to a surplus note issuer that is a related party as part of a reinsurance transaction in which the surplus note meets any of the criteria in paragraph 18.j., the ceding entity shall provide a description of the transaction, including whether the criteria in paragraph 18.j. were met with respect to the surplus note issuance, as long as the reinsurance agreement remains in force. The ceding entity should provide a description of the risks reinsured, the related party reinsurer, any guarantees or support agreements, and the amount of notes outstanding.

20. If the proceeds from the issuance of a surplus note used to purchase an asset directly or indirectly from the holder of the surplus note, the following information shall be disclosed regarding the assets received:

a. Identification of asset, including the investment schedule where the asset is reported and reported NAIC designation.

b. Book/adjusted carrying value of asset as of the current reporting date.

c. A description of terms under which liquidity would be provided should a triggering event occur.

21. In addition to the above, a reporting entity shall identify all affiliates that hold any portion of a surplus debenture or similar obligation (including an offering registered under the Securities Act of 1933 or distributed pursuant to rule 144A under the Securities Act of 1933), and any holder of 10% or more of the outstanding amount of any surplus note registered under the Securities Act of 1933 or distributed pursuant to Rule 144A under the Securities Act of 1933.

Relevant Literature

22. This statement rejects *AICPA Practice Bulletin No. 15, Accounting by the Issuer of Surplus Notes*, which requires surplus notes to be accounted for as debt and that interest be accrued over the life of

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the surplus note, irrespective of the approval of interest and principal payments by the insurance commissioner. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

23. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3*—Accounting *Changes and Corrections of Errors*. The provisions of paragraph 3, which are required for an instrument to qualify as a surplus note, apply to all surplus notes issued or amended after December 12, 1991. Surplus notes issued on or before December 12, 1991, shall not be required to meet the provisions of paragraph 3 in order to be accounted for as a surplus note. Guidance reflected in paragraph 9.b., incorporated from *INT 04-02: Surplus Notes Issued by Entities Under Regulatory Action*, was originally effective June 13, 2004.

24. In April 2016 substantive revisions were adopted to change the valuation method for holders of surplus notes. With the adopted substantive revisions, surplus notes with a designation equivalent to NAIC 1 or NAIC 2 shall be reported at amortized cost. All other surplus notes are required to be reported at the lesser of amortized cost or fair value. The substantive revisions also incorporated guidance to clarify when surplus notes shall be nonadmitted, have an unrealized loss and undergo an other-than-temporary impairment assessment. The substantive revisions, detailed for historical purposes in Issue Paper No. 151, are effective January 1, 2017, and shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office, "Procedures for Valuing Surplus Debentures"*

Relevant Issue Papers

- *Issue Paper No. 41—Surplus Notes*
- *Issue Paper No. 151—Valuation for Holders of Surplus Notes*

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Statement of Statutory Accounting Principles No. 42

Sale of Premium Receivables

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 2
Relevant Literature 2
Effective Date and Transition 2

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the sale or factoring of premium receivables.

SUMMARY CONCLUSION

2. For purposes of this statement, receivables shall only include amounts due to the reporting entity for premium receivables (i.e., uncollected premium, agent's balances, and bills receivable).

3. A transfer of receivables can take the form of a transfer with recourse or a transfer without recourse:

a. Recourse means that the transferee has the right to receive payment from the transferor of those receivables for (i) failure of the debtors to pay when due, (ii) the effects of prepayments, or (iii) adjustments resulting from defects in the eligibility of the transferred receivables, for example defects in the legal title of the transferred receivables. When the transferor has the right to repurchase (a call) or the transferee has the right to require the transferor to repurchase (a put) the transferred receivables, the transfer shall be considered to have recourse;

b. Without recourse means that the transferor has surrendered all of the future economic implications of the risks and rewards embodied in the transferred receivables.

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4. A transfer of receivables with recourse shall not be recognized as a sale. A transfer of receivables without recourse shall only be recognized if the transferor receives cash for the receivables. The sale shall be recognized when cash is received.

5. If a transfer qualifies to be recognized as a sale, the difference between (a) the sales price and (b) the receivables transferred shall be recognized as a gain or loss. If receivables are sold with servicing retained and the stated servicing fee is less than a current (normal) servicing fee rate (a servicing fee rate that is representative of servicing fee rates most commonly used in comparable servicing agreements covering similar types of receivables) or no servicing fee is specified, the gain or loss recognized by the sale of receivables shall be adjusted to recognize the deviation of the stated servicing fee rate from the commonly used servicing fee rate and a liability shall be established to provide for a normal servicing fee in each subsequent servicing period, which shall not be less than the estimated servicing costs. When the stated servicing fee is greater than a normal servicing fee the gain or loss shall not be adjusted and the excess servicing fee revenues shall not be recorded currently but shall be recorded when realized.

6. If the conditions of paragraph 3.b. are not met, or the transfer is for other than cash, the receivables shall remain on the transferor's financial statements. A liability shall be established in an amount equal to the greater of the carrying amount of the receivables transferred or the amount of the proceeds received. To the extent that the proceeds received are less than the carrying amount of receivables transferred, a loss shall be recorded. The carrying amount of the receivable balance shall be evaluated at each reporting period and adjusted for any uncollectible amounts. The liability shall be derecognized as the transferee receives cash. When the proceeds received are greater than the receivables transferred, the liability shall be derecognized on a pro rata basis as the receivables are collected.

Disclosures

7. For transfers of receivables reported as sales, the transferor's financial statements shall disclose:

   a. The proceeds to the transferor; and

   b. The gain or loss recorded on the sale.

8. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

9. This statement rejects paragraph 83 of *FASB Statement No. 125*, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (FAS 125) to the extent that it permits sales recognition for sales of receivables with recourse provisions. FAS 125 is addressed in its entirety in *SSAP No. 18—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, which was superseded by *SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* adopts with modification *FAS 166, Accounting for Transfers of Financial Assets—An Amendment of FASB Statement No. 104* and supersedes SSAP No. 91R.

Effective Date and Transition

10. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 42—Sale of Premium Receivables*

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Statement of Statutory Accounting Principles No. 43 – Revised

Loan-Backed and Structured Securities

STATUS

Type of Issue	Common Area
Issued	Initial Draft; Substantively revised September 2009
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 140 effective September 30, 2009; December 2009 revisions to paragraph 27 effective December 31, 2009; Revisions to paragraphs 2, 3 and 4 adopted October 2010 effective January 1, 2011
Affects	Supersedes SSAP No. 98 and paragraph 13 of SSAP No. 99; Nullifies and incorporates INT 00-11
Affected by	No other pronouncements
Interpreted by	INT 06-07; INT 07-01; INT 22-01
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **2**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investments in loan-backed securities, structured securities and mortgage-referenced securities. In accordance with *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, retained beneficial interests from the sale of loan-backed securities and structured securities are accounted for in accordance with this statement. In addition, mortgage loans in scope of *SSAP No. 37—Mortgage Loans* that qualify under an SVO structural assessment are in scope of this statement as credit tenant loans (CTLs). Items captured in scope of this statement are collectively referred to as loan-backed securities.

SUMMARY CONCLUSION

2. Loan-backed securities are defined as securitized assets not included in structured securities, as defined below, for which the payment of interest and/or principal is directly proportional to the payments received by the issuer from the underlying assets, including but not limited to pass-through securities, lease-backed securities, and equipment trust certificates.

3. Structured securities are defined as loan-backed securities which have been divided into two or more classes for which the payment of interest and/or principal of any class of securities has been allocated in a manner which is not proportional to payments received by the issuer from the underlying assets.

4. Loan-backed securities are issued by special-purpose corporations or trusts (issuer) established by a sponsoring organization. The assets securing the loan-backed obligation are acquired by the issuer and pledged to an independent trustee until the issuer's obligation has been fully satisfied. The investor only has direct recourse to the issuer's assets, but may have secondary recourse to third parties through insurance or guarantee for repayment of the obligation. As a result, the sponsor and its other affiliates may have no financial obligation under the instrument, although one of those entities may retain the responsibility for servicing the underlying assets. Some sponsors do guarantee the performance of the underlying assets.

5. Mortgage-referenced securities do not meet the definition of a loan-backed or structured security but are explicitly captured in scope of this statement. In order to qualify as a mortgage-referenced security, the security must be issued by a government sponsored enterprise[1] or by a special purpose trust in a transaction sponsored by a government sponsored enterprise in the form of a "credit risk transfer" in which the issued security is tied to a referenced pool of mortgages and the payments received are linked to the credit and principal payment risk of the underlying mortgage loan borrowers captured in the referenced pool of mortgages. For these instruments, reporting entity holders may not receive a return of their full principal as principal repayment is contingent on repayment by the mortgage loan borrowers in the referenced pool of mortgages. Unless specifically noted, the provisions for loan-backed securities within this standard apply to mortgage-referenced securities.

6. Investments within the scope of this statement issued by a related party or acquired through a related party transaction or arrangement are also subject to the provisions, admittance assessments and disclosure requirements of *SSAP No. 25—Affiliates and Other Related Parties*. In determining whether a security is a related party investment, consideration should be given to the substance of the transaction, and the parties whose action or performance materially impacts the insurance reporting entity holding the security. Loan-backed and structured securities meet the definition of assets as defined in *SSAP No. 4—*

[1] Currently, only Fannie Mae and Freddie Mac are the government sponsored entities that either directly issue qualifying mortgage-referenced securities or sponsor transactions in which a special purpose trust issues qualifying mortgage-reference securities. However, this guidance would apply to mortgage-referenced securities issued by any other government sponsored entity that subsequently engages in the transfer of mortgage credit risk.

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Assets and Nonadmitted Assets and are admitted assets to the extent they conform to the requirements of this statement and SSAP No. 25.

a. Although a loan-backed or structured security may be acquired from a non-related issuer, if the assets held in trust predominantly[2] reflect assets issued by affiliates of the insurance reporting entity, and the insurance reporting entity only has direct recourse to the assets held in trust, the transaction shall be considered an affiliated investment. In such situations where the underlying collateral assets are issued by related parties that do not qualify as affiliates, these securities shall be identified as related party investments in the investment schedules.

b. A loan-backed or structured security may involve a relationship with a related party but not be considered an affiliated investment. This may be because the relationship does not result in direct or indirect control of the issuer or because there is an approved disclaimer of control or affiliation. Regardless of whether investments involving a related party relationship are captured in the affiliated investment reporting lines, these securities shall be identified as related party investments in the investment schedules. Examples of related party relationships would include involvement of a related party in sponsoring or originating the loan-backed or structured security or any type of underlying servicing arrangement. For the avoidance of doubt, investments from any arrangement that results in direct or indirect control, which include but are not limited to control through a servicer or other controlling arrangement, shall be reported as affiliated in accordance with SSAP No. 25.

7. The scope of this statement encompasses all types of loan-backed and structured securities, including, but not limited to, the following:

a. Loan-backed and structured securities acquired at origination,

b. Loan-backed and structured securities acquired subsequent to origination for which it is probable, at acquisition, that the reporting entity will be able to collect all contractually required payments receivable, and are accounted for at acquisition under SSAP No. 103R,

c. Loan-backed and structured securities for which it is probable, either known at acquisition or identified during the holding period[3], that the reporting entity will be unable to collect all contractually required payments receivable, and

d. Transferor's beneficial interests in securitization transactions that are accounted for as sales under SSAP No. 103R and purchased beneficial interests in securitized financial assets[4].

[2] In applying this guidance, a reporting entity is not required to complete a detailed review of the assets held in trust to determine the extent, if any, the assets were issued by related parties. Rather, this guidance is a principle concept intended to prevent situations in which related party transactions (particularly those involving affiliates) is knowingly captured in a SSAP No. 43R structure and not identified as a related party transaction (or not reported as an affiliated investment on the investment schedule) because of the involvement of a non-related trustee or SSAP No. 43R security issuer. As identified in SSAP No. 25, it is erroneous to conclude that the inclusion of a non-related intermediary, or the presence of non-related assets in a structure predominantly comprised of related party investments, eliminates the requirement to identify and assess the investment transaction as a related party arrangement.

[3] Securities classified within the type of paragraph 7.a. or 7.b. may be required to change classification to type 6.c. when it becomes probable that the reporting entity will be unable to collect all contractually required payments receivable.

[4] The accounting requirements related to these types of securities included in paragraphs 22-25 shall be determined at acquisition or initial transfer.

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8. At acquisition, loan-backed and structured securities, except for loan-backed or structured securities that are beneficial interests that are not of high credit quality or can contractually be prepaid or otherwise settled in such a way that the reporting entity would not recover substantially all of its recorded amount[5] (see paragraphs 22-25), shall be reported at cost, including brokerage and related fees. Acquisitions and dispositions shall be recorded on the trade date, not the settlement date, except for the acquisition of private placement loan-backed and structured securities which shall be recorded on the funding date. For securities where all information is not known as of the trade date (e.g., actual payment factors and specific pools), a reporting entity shall make its best estimate based on known facts.

9. Amortization of premium or discount shall be calculated using the scientific (constant yield) interest method and shall be recorded as an adjustment to investment income.(INT 07-01) The interest method results in a constant effective yield equal to the prevailing rate at the time of purchase or at the time of subsequent adjustments to book value. The amortization period shall reflect estimates of the period over which repayment of principal of the loan-backed and structured securities is expected to occur, not the stated maturity period.

10. Interest shall be accrued using the effective-yield method using the redemption prices and redemption dates used for amortizing premiums and discounts. Interest income consists of interest collected during the period, the change in the due and accrued interest between the beginning and end of the period as well as reductions for premium amortization and interest paid on acquisition of loan-backed and structured securities, and the addition of discount accrual. Contingent interest may be accrued if the applicable provisions of the underlying contract and the prerequisite conditions have been met.

11. For reporting entities required to maintain an IMR, the accounting for realized capital gains and losses on sales of loan-backed and structured securities shall be in accordance with paragraph ~~38~~40 of this statement. For reporting entities not required to maintain an IMR, realized gains and losses on sales of loan-backed and structured securities shall be recorded on the trade date and shall be reported as net realized capital gains or losses in the Statement of Income.

12. A loan-backed or structured security may provide for a prepayment penalty or acceleration fee in the event the investment is liquidated prior to its scheduled termination date. These fees shall be reported as investment income when received.

13. The amount of prepayment penalty and/or acceleration fees to be reported as investment income shall be calculated as follows:

a. The amount of investment income reported is equal to the total proceeds (consideration) received less the par value of the investment; and

b. Any difference between the book adjusted carrying value (BACV) and the par value at the time of disposal shall be reported as realized capital gains and losses subject to the authoritative literature in SSAP No. 7.

Collection of All Contractual Cashflows is Probable

14. The following guidance applies to loan-backed and structured securities for which it is probable that the investor will be able to collect all contractually required payments receivable. (Paragraphs 19-21 provide guidance for securities in which collection of all contractual cash flows is not probable and paragraphs 22-25 provide guidance for beneficial interests.) Prepayments are a significant variable element in the cash flow of loan-backed and structured securities because they affect the yield and determine the expected maturity against which the yield is evaluated. Falling interest rates generate faster

[5] As referenced in the Relevant Literature section, this statement adopts EITF 99-20, including the scope requirements of that guidance.

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prepayment of the mortgages underlying the security, shortening its duration. This causes the reporting entity to reinvest assets sooner than expected at potentially less advantageous rates. This is called prepayment risk. Extension risk is created by rising interest rates which slow repayment and can significantly lengthen the duration of the security. Differences in cash flows can also result from other changes in the cash flows from the underlying assets. If assets are delinquent or otherwise not generating cash flow, which should be reflected in the cash flow analysis through diminishing security cash flows, even if assets have not been liquidated and gain/losses have not been booked.

15. Changes in currently estimated cash flows, including the effect of prepayment assumptions, on loan-backed and structured securities shall be reviewed periodically, at least quarterly. The prepayment rates of the underlying loans shall be used to determine prepayment assumptions. Prepayment assumptions shall be applied consistently across portfolios to all securities backed by similar collateral (similar with respect to coupon, issuer, and age of collateral). Reporting entities shall use consistent assumptions across portfolios for similar collateral within controlled affiliated groups. Since each reporting entity may have a unique method for determining the prepayment assumptions, it is impractical to set standard assumptions for the industry. Relevant sources and rationale used to determine each prepayment assumption shall be documented by the reporting entity.

16. Loan-backed and structured securities shall be revalued using the currently estimated cash flows, including new prepayment assumptions, using either the prospective or retrospective adjustment methodologies, consistently applied by type of securities. However, if at anytime during the holding period, the reporting entity determines it is no longer probable that they will collect all contractual cashflows, the reporting entity shall apply the accounting requirements in paragraphs 19-21.

17. The prospective approach recognizes, through the recalculation of the effective yield to be applied to future periods, the effects of all cash flows whose amounts differ from those estimated earlier and the effects and changes in projected cash flows. Under the prospective method, the recalculated effective yield will equate the carrying amount of the investment to the present value of the anticipated future cash flows. The recalculated yield is then used to accrue income on the investment balance for subsequent accounting periods. There are no accounting changes in the current period unless the security is determined to be other than temporarily impaired.

18. The retrospective methodology changes both the yield and the asset balance so that expected future cash flows produce a return on the investment equal to the return now expected over the life of the investment as measured from the date of acquisition. Under the retrospective method, the recalculated effective yield will equate the present value of the actual and anticipated cash flows with the original cost of the investment. The current balance is then increased or decreased to the amount that would have resulted had the revised yield been applied since inception, and investment income is correspondingly decreased or increased.

Collection of All Contractual Cashflows is Not Probable

19. The following guidance applies to loan-backed and structured securities with evidence of deterioration of credit quality since origination for which it is probable, either known at acquisition or identified during the holding period, that the investor will be unable to collect all contractually required payments receivable, except for those beneficial interests that are not of high credit quality or can contractually be prepaid or otherwise settled in such a way that the reporting entity would not recover substantially all of its recorded amount determined at acquisition (see paragraphs 22-25).

20. The reporting entity shall recognize the excess of all cash flows expected at acquisition over the investor's initial investment in the loan-backed or structured security as interest income on an effective-

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yield basis over the life of the loan-backed or structured security (accretable yield).[6] Any excess of contractually required cash flows over the cash flows expected to be collected is the nonaccretable difference. Expected prepayments shall be treated consistently for determining cash flows expected to be collected and projections of contractual cash flows such that the nonaccretable difference is not affected. Similarly, the difference between actual prepayments and expected prepayments shall not affect the nonaccretable difference.

21. An investor shall continue to estimate cash flows expected to be collected over the life of the loan-backed or structured security. If, upon subsequent evaluation:

a. The fair value of the loan-backed or structured security has declined below its amortized cost basis, an entity shall determine whether the decline is other than temporary(INT 06-07). For example, if, based on current information and events, there is a decrease in cash flows expected to be collected (that is, the investor is unable to collect all cash flows expected at acquisition plus any additional cash flows expected to be collected arising from changes in estimate after acquisition (in accordance with paragraph 21.b.), an other-than-temporary impairment shall be considered to have occurred. The investor shall consider both the timing and amount of cash flows expected to be collected in making a determination about whether there has been a decrease in cash flows expected to be collected.

b. Based on current information and events, if there is a significant increase in cash flows previously expected to be collected or if actual cash flows are significantly greater than cash flows previously expected, the investor shall recalculate the amount of accretable yield for the loan-backed or structured security as the excess of the revised cash flows expected to be collected over the sum of (1) the initial investment less (2) cash collected less (3) other-than-temporary impairments plus (4) amount of yield accreted to date. The investor shall adjust the amount of accretable yield by reclassification from nonaccretable difference. The adjustment shall be accounted for as a change in estimate in conformity with *SSAP No. 3—Accounting Changes and Corrections of Errors*, with the amount of periodic accretion adjusted over the remaining life of the loan-backed or structured security (prospective method).

Beneficial Interests

22. The following paragraphs provide statutory accounting guidance for interest income and impairment for a reporting entity that continues to hold an interest in securitized financial assets accounted for as sales under SSAP No. 103R, or that purchases a beneficial interest in securitized financial assets that are not of high credit quality or can contractually be prepaid or otherwise settled in such a way that the reporting entity would not recover substantially all of its recorded amount, determined at acquisition or the date of transfer[7]. Beneficial interests that are of high credit quality and cannot contractually be prepaid or otherwise settled in such a way that the reporting entity would not recover substantially all of its recorded investment, shall be accounted for in accordance with paragraphs 14-18.

[6] A loan-backed or structured security may be acquired at a discount because of a change in credit quality or rate or both. When a loan-backed or structured security is acquired at a discount that relates, at least in part, to the security's credit quality, the effective interest rate is the discount rate that equates the present value of the investor's estimate of the security's future cash flows with the purchase price of the loan-backed or structured security.

[7] The accounting requirements related to these types of securities included in paragraphs 22-25 shall be determined at acquisition or initial transfer. As referenced in the Relevant Literature section, this statement adopts EITF 99-20 (as amended by FAS 166), including the scope requirements of that guidance.

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23. The reporting entity shall recognize the excess of all cash flows attributable to the beneficial interest estimated at the acquisition/transaction date (referred to herein as the transaction date) over the initial investment (the accretable yield) as interest income over the life of the beneficial interest using the effective yield method. If the holder of the beneficial interest is the reporting entity that transferred the financial assets for securitization, the initial investment would be the fair value of the beneficial interest as of the date of transfer, as required by SSAP No. 103R. The amount of accretable yield shall not be displayed in the balance sheet.

24. The reporting entity that holds a beneficial interest shall continue to update the estimate of cash flows over the life of the beneficial interest. If upon evaluation:

a. Based on current information and events it is probable that there is a favorable (or an adverse) change in estimated cash flows from the cash flows previously projected, then the investor shall recalculate the amount of accretable yield for the beneficial interest on the date of evaluation as the excess of estimated cash flows over the beneficial interest's reference amount (the reference amount is equal to (1) the initial investment less (2) cash received to date less (3) other-than-temporary impairments recognized to date [as described in paragraph 24.b.] plus (4) the yield accreted to date. The adjustment shall be accounted for prospectively as a change in estimate in conformity with SSAP No. 3, with the amount of periodic accretion adjusted over the remaining life of the beneficial interest. Based on estimated cash flows, interest income may be recognized on a beneficial interest even if the net investment in the beneficial interest is accreted to an amount greater than the amount at which the beneficial interest could be settled if prepaid immediately in its entirety.

b. The fair value of the beneficial interest has declined below its reference amount; a reporting entity shall determine whether the decline is other-than-temporary. If, based on current information and events it is probable that there has been an adverse change in estimated cash flows (in accordance with paragraph 24.a.), then (1) an other-than-temporary impairment shall be considered to have occurred and (2) the beneficial interest shall be written down to the current estimate of cash flows at the financial reporting date discounted at a rate equal to the current yield used to accrete the beneficial interest with the resulting change being recognized as a realized loss. Determining whether there has been a favorable (or an adverse) change in estimated cash flows from the cash flows previously projected (taking into consideration both the timing and amount of the estimated cash flows) involves comparing the present value of the remaining cash flows as estimated at the initial transaction date (or at the last date previously revised) against the present value of the cash flows estimated at the current financial reporting date. The cash flows shall be discounted at a rate equal to the current yield used to accrete the beneficial interest. If the present value of the original cash flows estimated at the initial transaction date (or the last date previously revised) is less than the present value of the current estimate of cash flows expected to be collected, the change is considered favorable (that is, an other-than-temporary impairment shall be considered to have not occurred). If the present value of the original cash flows estimated at the initial transaction date (or the last date previously revised) is greater than the present value of the current estimated cash flows, the change is considered adverse (that is, an other-than-temporary impairment shall be considered to have occurred). However, absent any other factors that indicate an other-than-temporary impairment has occurred, changes in the interest rate of a "plain-vanilla," variable-rate beneficial interest generally shall not result

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in the recognition of an other-than-temporary impairment[8] (a plain-vanilla, variable-rate beneficial interest does not include those variable-rate beneficial interests with interest rate reset formulas that involve either leverage or an inverse floater).

25. All cash flows estimated at the transaction date are defined as the holder's estimate of the amount and timing of estimated future principal and interest cash flows used in determining the purchase price or the holder's fair value determination for purposes of determining a gain or loss under SSAP No. 103R. Subsequent to the transaction date, estimated cash flows are defined as the holder's estimate of the amount and timing of estimated principal and interest cash flows based on the holder's best estimate of current information and events. A change in estimated cash flows is considered in the context of both timing and amount of the estimated cash flows.

Reporting Guidance for All Loan-Backed and Structured Securities

26. Loan-backed and structured securities shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual), and the designation assigned in the *NAIC Valuations of Securities* product prepared by the NAIC Securities Valuation Office or equivalent specified procedure. The carrying value method shall be determined as follows:

a. For reporting entities that maintain an Asset Valuation Reserve (AVR), loan-backed and structured securities, excluding residual tranches or interests, shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value.

b. For reporting entities that do not maintain an AVR, loan-backed and structured securities designated highest-quality and high-quality (NAIC designations 1 and 2, respectively), excluding residual tranches or interests, shall be reported at amortized cost; loan-backed and structured securities that are designated medium quality, low quality, lowest quality and in or near default (NAIC designations 3 to 6, respectively) shall be reported at the lower of amortized cost or fair value.

c. For residual tranches or interests[9] captured in scope of this statement, all reporting entities shall report the item on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value. Changes in the reported value from the prior period shall be recorded as unrealized gains or losses. For reporting entities that maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*.

[8] Changes in the interest rate of a "plain-vanilla," variable-rate beneficial interest (a plain-vanilla, variable-rate beneficial interest does not include those variable-rate beneficial interests with interest rate reset formulas that involve either leverage or an inverse floater) generally should not result in the recognition of an other-than-temporary impairment. For plain-vanilla, variable-rate beneficial interests, the yield is changed to reflect the revised interest rate based on the contractual interest rate reset formula. For example, if a beneficial interest pays interest quarterly at a rate equal to LIBOR plus 2% ~~percent~~, the yield of that beneficial interest is changed prospectively to reflect changes in LIBOR. However, changes in the fair value of a plain-vanilla, variable-rate beneficial interest due to credit events should be considered when evaluating whether there has been an other-than-temporary impairment.

[9] Reference to "residual tranches or interests" intends to capture securitization tranches and beneficial interests as well as other structures captured in scope of this statement that reflect loss layers without any contractual payments, whether principal or interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment's duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

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Residual Tranches or Interests

27. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.

28. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a residual should be based on the substance of the investment and how cash flows to the holder are determined.

a. Residuals often do not have contractual principal or interest.

b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance, and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.

c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.

d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.

e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.

Designation Guidance

~~27.~~29. For Residential Mortgage-Backed Securities (RMBS), Commercial Mortgage-Backed Securities (CMBS), and Collateralized Loan Obligations (CLOs) ~~RMBS/CMBS~~ securities within the scope of this statement, the initial NAIC designation used to determine the carrying value method and the final NAIC designation for reporting purposes is determined using a multi-step process or the NAIC designation assigned by the NAIC Securities Valuation Office. The P&P Manual provides detailed guidance. A general description of the processes is as follows:

a. Financial Modeling: Pursuant to the P&P Manual, the NAIC identifies select securities where financial modeling must be used to determine the NAIC designation. For a

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modeled RMBS/CMBS legacy security, meaning one which closed prior to January 1, 2013, the NAIC designation is based on financial modeling incorporating the insurers' carrying value. For ~~–~~a modeled RMBS/CMBS non-legacy security, meaning one which closed after December 31, 2012, or modeled CLO, the NAIC designation and NAIC designation category assigned by the NAIC Securities Valuation Office must be used. For those RMBS/CMBS legacy securities that are financially modeled, the insurer must use NAIC CUSIP specific modeled breakpoints provided by the modelers in determining initial and final designation for these identified securities. As specified in the P&P Manual, a modeled legacy security RMBS or CMBS tranche that has no expected loss, as compiled and published by the NAIC Securities Valuation Office, under any of the selected modeling scenarios would be assigned an NAIC 1 designation and NAIC 1.A designation category regardless of the insurer's book/adjusted carrying value. The three-step process for modeled RMBS/CMBS legacy securities is as follows:

i. Step 1: Determine Initial Designation – The current amortized cost (divided by remaining par amount) of a loan-backed or structured security is compared to the modeled breakpoint values assigned to each NAIC designation and NAIC designation category for each CUSIP to establish the initial NAIC designation.

ii. Step 2: Determine Carrying Value Method – The carrying value method, either the amortized cost method or the lower of amortized cost or fair value method, is then determined as described in paragraph 26 based upon the initial NAIC designation from Step 1.

iii. Step 3: Determine Final Designation – The final NAIC designation is determined by comparing the carrying value (divided by remaining par amount) of a security (based on paragraph ~~27~~29.a.ii.) to the NAIC CUSIP specific modeled breakpoint values assigned to the NAIC designation and NAIC designation category for each CUSIP or is mapped to an NAIC designation category, according to the instructions in the P&P Manual. This final NAIC designation shall be applicable for statutory accounting and reporting purposes and the NAIC designation category will be used for investment schedule reporting and establishing RBC and AVR charges. The final NAIC designation is not used for establishing the appropriate carrying value method in Step 2 (paragraph ~~27~~29.a.ii.).

b. All Other Loan-Backed and Structured Securities: For securities not subject to paragraph 27.a. (financial modeling) follow the established designation procedures according to the appropriate section of the P&P Manual. The NAIC designation shall be applicable for statutory accounting and reporting purposes (including determining the carrying value method and establishing the AVR charges). The carrying value method is established as described in paragraph 26.

Specific Interim Reporting Guidance Financially Modeled Securities

~~28.~~30. For securities that will be financially modeled under paragraph ~~27~~29, the guidance in this paragraph shall be applied in determining the reporting method for such securities acquired in the current year for quarterly financial statements. Securities reported as of the prior-year end shall continue to be reported under the prior-year end methodology for the current-year quarterly financial statements. For year-end reporting, securities shall be reported in accordance with paragraph ~~27~~29, regardless of the quarterly methodology used.

a. Reporting entities that acquired the entire financial modeling database for the prior-year end are required to follow the financial modeling methodology (paragraph ~~27~~29.a.) for all

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securities acquired in the subsequent year that were included in the financial modeling data acquired for the prior year-end.

b. Reporting entities that acquired identical securities (identical CUSIP) to those held and financially modeled for the prior year-end are required to follow the prior year-end financial modeling methodology (paragraph ~~27~~29.a.) for these securities acquired subsequent to year-end.

c. Reporting entities that do not acquire the prior-year financial modeling information for current-year acquired individual CUSIPS, and are not captured within paragraphs ~~28~~30.a. or 28.b., are required to follow the analytical procedures for non-financially modeled securities (paragraph ~~27~~29.b. as appropriate) until the current year financial modeling information becomes available and then follow the procedures for financially modeled securities (paragraph 29.a. as appropriate). Reporting entities that do acquire the individual CUSIP information from the prior-year financial modeling database shall use that information for interim reporting.

d. Reporting entities that acquire securities not previously modeled at the prior year-end are required to follow the analytical procedures for non-financially modeled securities (paragraph ~~27~~29.b. as appropriate) until the current year financial modeling information becomes available and then follow the procedures for financially modeled securities (paragraph 29.a. as appropriate).

Unrealized Gains and Losses and Impairment Guidance

~~29.~~31. For reporting entities required to maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with paragraph ~~38~~40 of this statement. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

~~30.~~32. The application of this reporting requirement resulting from NAIC designation (i.e., lower of cost or fair value) is not a substitute for other-than-temporary impairment recognition (paragraphs ~~35-39~~37-41). For securities reported at fair value where an other-than-temporary impairment has been determined to have occurred, the realized loss recognized from the other-than-temporary impairment shall first be applied towards the realization of any unrealized losses previously recorded as a result of fluctuations in the security's fair value due to the reporting requirements. After the recognition of the other-than-temporary impairment, the security shall continue to report unrealized gains and losses as a result of fluctuations in fair value.

~~31.~~33. If the fair value of a loan-backed or structured security is less than its amortized cost basis at the balance sheet date, an entity shall assess whether the impairment is other than temporary. Amortized cost basis includes adjustments made to the cost of an investment for accretion, amortization, collection of cash, previous other-than-temporary impairments recognized as a realized loss.

~~32.~~34. If an entity intends to sell the loan-backed or structured security (that is, it has decided to sell the security), an other-than-temporary impairment shall be considered to have occurred.

~~33.~~35. If an entity does not intend to sell the loan-backed or structured security, the entity shall assess whether it has the intent and ability[10] to retain the investment in the security for a period of time sufficient to recover the amortized cost basis. If the entity does not have the intent and ability to retain the

[10] This assessment shall be considered a high standard due to the accounting measurement method established for the securities within the scope of this statement (amortized cost).

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investment for the time sufficient to recover the amortized cost basis, an other-than-temporary impairment shall be considered to have occurred.

~~34.~~36. If the entity does not expect to recover the entire amortized cost basis of the security, the entity would be unable to assert that it will recover its amortized cost basis even if it does not intend to sell the security and the entity has the intent and ability to hold. Therefore, in those situations, an other-than temporary impairment shall be considered to have occurred. (For mortgage-referenced securities, an OTTI is considered to have occurred when there has been a delinquency or other credit event in the referenced pool of mortgages such that the entity does not expect to recover the entire amortized cost basis of the security.) In assessing whether the entire amortized cost basis of the security will be recovered, an entity shall compare the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If present value of cash flows expected to be collected is less than the amortized cost basis of the security, the entire amortized cost basis of the security will not be recovered (that is, a non-interest related decline[11] exists), and an other-than-temporary impairment shall be considered to have occurred. A decrease in cashflows expected to be collected on a loaned-backed or structured security that results from an increase in prepayments on the underlying assets shall be considered in the estimate of the present value of cashflows expected to be collected.

~~35.~~37. In determining whether a non-interest related decline exists, an entity shall calculate the present value of cash flows expected to be collected based on an estimate of the expected future cash flows of the impaired loan-backed or structured security, discounted at the security's effective interest rate.

a. For securities accounted for under paragraphs 14-18 – the effective interest rate of the loan-backed or structured security is the rate of return implicit in the security (that is, the contractual interest rate adjusted for any net deferred fees or costs, premium, or discount existing at the origination or acquisition of the security).

b. For securities accounted for under paragraphs 19-21 – the effective interest rate is the rate implicit immediately prior to the recognition of the other-than-temporary impairment.

c. For securities accounted for under paragraphs 22-25 – the reporting entity shall apply the guidance in paragraph 24.b.

~~36.~~38. When an other-than-temporary impairment has occurred because the entity intends to sell the security or has assessed that that they do not have the intent and ability to retain the investments in the security for a period of time sufficient to recover the amortized cost basis, the amount of the other-than-temporary impairment recognized in earnings as a realized loss shall equal the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. (This guidance includes loan-backed and structured securities previously held at lower of cost or market. For these securities, upon recognition of an other-than-temporary impairment, unrealized losses would be considered realized.)

~~37.~~39. When an other-than-temporary impairment has occurred because the entity does not expect to recover the entire amortized cost basis of the security even if the entity has no intent to sell and the entity has the intent and ability to hold, the amount of the other-than-temporary impairment recognized as a realized loss shall equal the difference between the investment's amortized cost basis and the present value of cash flows expected to be collected, discounted at the loan-backed or structured security's effective interest rate in accordance with paragraph ~~35~~37. (This guidance includes loan-backed and structured securities previously held at lower of cost or market. For these securities, upon recognition of

[11] A non-interest related decline is a decline in value due to fundamental credit problems of the issuer. Fundamental credit problems exist with the issuer when there is evidence of financial difficulty that may result in the issuer being unable to pay principal or interest when due. An interest related decline in value may be due to both increases in the risk-free interest rate and general credit spread widening.

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an other-than-temporary impairment, unrealized losses would be considered realized for the non-interest related decline. Hence, unrealized losses could continue to be reflected for these securities due to the reporting requirements.)

~~38.~~40. For reporting entities required to maintain an AVR or IMR, the accounting for unrealized gains and losses shall be in accordance with paragraph ~~38~~40.a. For realized gains and losses, the AVR and IMR analysis required and provision to allocate gains and losses between AVR and IMR is the same regardless whether the realized loss results from an impairment write-down or whether there was a gain or loss upon sale. Guidance on specific scenarios resulting in realized gains and losses are addressed in paragraphs ~~38~~40.b. through ~~38~~40.f.:

a. Unrealized Gains and Losses – Record all unrealized gains and losses through AVR. At the time an unrealized gain or loss is realized, the accounting shall follow the premise in paragraph ~~38~~40, as detailed in paragraphs ~~38~~40.b. through ~~38~~40.f. for specific transactions. Unrealized gains or losses that are realized shall be reversed from AVR before the recognition of the realized gain or loss within AVR and IMR. Gains and losses shall only be reflected in IMR when realized and as appropriate based on the analysis of interest and non-interest factors.

b. Other-Than-Temporary Impairment – Non-interest related other-than-temporary impairment losses shall be recorded through the AVR. If the reporting entity wrote the security down to fair value due to the intent to sell or does not have the intent and ability to retain the investment for a period of time sufficient to recover the amortized cost basis, the non-interest related portion of the other-than-temporary impairment losses shall be recorded through the AVR; the interest related other-than-temporary impairment losses shall be recorded through the IMR. The analysis for bifurcating impairment losses between AVR and IMR shall be completed as of the date when the other-than-temporary impairment is determined.

c. Security Sold at a Loss Without Prior OTTI – An entity shall bifurcate the loss into AVR and IMR portions depending on interest and non-interest related declines in accordance with the analysis performed as of the date of sale. As such, an entity shall report the loss in separate AVR and IMR components as appropriate.

d. Security Sold at a Loss With Prior OTTI – An entity shall bifurcate the current realized loss into AVR and IMR portions depending on interest and non-interest related declines in accordance with the analysis performed as of the date of sale. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

e. Security Sold at a Gain With Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale. The bifurcation between AVR and IMR that occurs as of the date of sale may be different from the AVR and IMR allocation that occurred at the time of previous other-than-temporary impairments. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

f. Security Sold at a Gain Without Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale.

~~39.~~41. For situations where an other-than-temporary impairment is recognized pursuant to paragraphs ~~36~~38 and ~~37~~39 of this statement, the previous amortized cost basis less the other-than-temporary

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impairment recognized as a realized loss shall become the new amortized cost basis of the investment. That new amortized cost basis shall not be adjusted for subsequent recoveries in fair value. Therefore, the prospective adjustment method shall be used for periods subsequent to loss recognition.

~~40.~~42. In periods subsequent to the recognition of an other than temporary impairment loss for a loan-backed or structured security, the reporting entity shall account for the other-than-temporarily impaired security as if the security had been purchased on the measurement date of the other-than-temporary impairment at an amortized cost basis equal to the previous amortized cost basis less the other-than-temporary impairment recognized as a realized loss. The difference between the new amortized cost basis and the cash flows expected to be collected shall be accreted as interest income. A reporting entity shall continue to estimate the present value of cash flows expected to be collected over the life of the loan-backed or structured security.

a. For securities accounted for under paragraphs 14-21, if upon subsequent evaluation, there is a significant increase in the cash flows expected to be collected or if actual cash flows are significantly greater than cash flows previously expected, such changes shall be accounted for as a prospective adjustment to the accretable yield in accordance with paragraphs 19-21. The security shall continue to be subject to impairment analysis for each subsequent reporting period. The new amortized cost basis shall not be changed for subsequent recoveries in fair value. Future declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses.

b. For beneficial interests accounted for under paragraphs 22-25, a reporting entity shall apply the guidance in paragraphs 23-24 to account for changes in cash flows expected to be collected.

~~41.~~43. It is inappropriate to automatically conclude that a security is not other-than-temporarily impaired because all of the scheduled payments to date have been received. However, it also is inappropriate to automatically conclude that every decline in fair value represents an other-than-temporary impairment. Further analysis and judgment are required to assess whether a decline in fair value indicates that it is probable that the holder will not collect all of the contractual or estimated cash flows from the security. In addition, the length of time and extent to which the fair value has been less than cost can indicate a decline is other than temporary. The longer and/or the more severe the decline in fair value, the more persuasive the evidence that is needed to overcome the premise that it is probable that the holder will not collect all of the contractual or estimated cash flows from the issuer of the security.

~~42.~~44. In making its other-than-temporary impairment assessment, the holder shall consider all available information relevant to the collectibility of the security, including information about past events, current conditions, and reasonable and supportable forecasts, when developing the estimate of future cash flows. Such information generally shall include the remaining payment terms of the security, prepayment speeds, the financial condition of the issuer(s), expected defaults, and the value of any underlying collateral. To achieve that objective, the holder shall consider, for example, industry analyst reports and forecasts, sector credit ratings, and other market data that are relevant to the collectibility of the security. The holder also shall consider how other credit enhancements affect the expected performance of the security, including consideration of the current financial condition of the guarantor of a security (if the guarantee is not a separate contract) and/or whether any subordinated interests are capable of absorbing estimated losses on the loans underlying the security. The remaining payment terms of the security could be significantly different from the payment terms in prior periods (such as for some securities backed by

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"nontraditional loans"[12]). Thus, the holder shall consider whether a security backed by currently performing loans will continue to perform when required payments increase in the future (including "balloon" payments). The holder also shall consider how the value of any collateral would affect the expected performance of the security. If the fair value of the collateral has declined, the holder needs to assess the effect of that decline on the ability of the holder to collect the balloon payment.

Origination Fees

~~43.~~45. Origination fees represent fees charged to the borrower in connection with the process of originating or restructuring a transaction. The fees include, but are not limited to, points, management, arrangement, placement, application, underwriting, and other fees pursuant to such a transaction. Origination fees shall not be recorded until received in cash. Origination fees intended to compensate the reporting entity for interest rate risks (e.g., points), shall be amortized into income over the term of the loan-backed or structured security consistent with paragraph 9 of this statement. Other origination fees shall be recorded as income upon receipt.

Origination, Acquisition, and Commitment Costs

~~44.~~46. Costs related to origination when paid in the form of brokerage and other related fees shall be capitalized as part of the cost of the loan-backed or structured security, consistent with paragraph 8 of this statement. All other costs, including internal costs or costs paid to an affiliated entity related to origination, purchase, or commitment to purchase loan-backed and structured securities, shall be charged to expense when incurred.

Commitment Fees

~~45.~~47. Commitment fees are fees paid to the reporting entity that obligate the reporting entity to make available funds for future borrowing under a specified condition. A fee paid to the reporting entity to obtain a commitment to make funds available at some time in the future, generally, is refundable only if the loan-backed or structured security is issued. If the loan-backed or structured security is not issued, then the fees shall be recorded as investment income by the reporting entity when the commitment expires.

~~46.~~48. A fee paid to the reporting entity to obtain a commitment to borrow funds at a specified rate and with specified terms quoted in the commitment agreement, generally, is not refundable unless the commitment is refused by the reporting entity. This type of fee shall be deferred, and amortization shall depend on whether or not the commitment is exercised. If the commitment is exercised, then the fee shall be amortized in accordance with paragraph 9 of this statement over the life of the loan-backed or structured security as an adjustment to the investment income on the loan-backed or structured security. If the commitment expires unexercised, the commitment fee shall be recognized in income on the commitment expiration date.

Giantization/Megatization of FHLMC or FNMA Mortgage-Backed Securities

~~47.~~49. Giantization/megatization of mortgage-backed securities is defined as existing pools of FHLMC or FNMA mortgage-backed securities (MBS) with like coupon and prefix which are repooled together by the issuing agency creating a new larger security. The new Fannie Mae "Mega" or Freddie Mac "Giant" is a guaranteed MBS pass-through representing an undivided interest in the underlying pools of loans.

[12] A nontraditional loan may have features such as (a) terms that permit principal payment deferral or payments smaller than interest accruals (negative amortization), (b) a high loan-to-value ratio, (c) multiple loans on the same collateral that when combined result in a high loan-to value ratio, (d) option adjustable-rate mortgages (option ARMs) or similar products that may expose the borrower to future increases in repayments in excess of increases that result solely from increases in the market interest rate (for example, once negative amortization results in the loan reaching a maximum principal accrual limit), (e) an initial interest rate that is below the market interest rate for the initial period of the loan term and that may increase significantly when that period ends, and (f) interest-only loans that should be considered in developing an estimate of future cash flows.

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~~48.~~50. Repooled FHLMC and FNMA securities meet the definition of substantially the same as defined in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. The transaction shall not be considered a sale/purchase and no gain or loss shall be recognized. To properly document the repooling, the transaction shall be reported through Schedule D of the annual statement as a disposition and an acquisition.

~~49.~~51. Transaction fees charged by the issuing agencies shall be capitalized and amortized over the life of the repooled security.

Structured Securities Acquired for a Specified Investment Strategy

~~50.~~52. To achieve certain strategic investment results, structured securities may be issued in combination with other structured securities as a unit or a pair. One strategy involves the purchase of two structured securities with opposite interest rate reset provisions. Under that strategy, the fixed coupon rate or maturity date for each structured security would be determined shortly after issuance depending on movements in market interest rates. Following that reset date, the resulting yields on each of the structured securities will move in opposite directions; however, the average yield of the two securities will generally reflect the market yield of the combined instruments in effect on the issuance date. In situations when structured securities are issued in combination with other structured securities as a unit or a pair, each structured security shall be accounted for separately in accordance with the appropriate SSAP. The guidance in paragraph 8 of SSAP No. 103R on the accounting for transfers of entire financial assets or group of entire financial assets that qualify as sales shall be applied to each structured security upon transfer.

Disclosures

~~51.~~53. In addition to the disclosures required for invested assets in general, the following disclosures regarding loan-backed and structured securities shall be made in the financial statements. Regardless of the allowances within paragraph 63 of the Preamble, the disclosures in paragraph ~~51~~53.f., ~~51~~53.g. and ~~51~~53.h. of this statement are required in separate, distinct notes to the financial statements:

a. Fair values in accordance with *SSAP No. 100R—Fair Value*.

b. Concentrations of credit risk in accordance with SSAP No. 27;

c. Basis at which the loan-backed and structured securities are stated;

d. The adjustment methodology used for each type of security (prospective or retrospective);

e. Descriptions of sources used to determine prepayment assumptions.

f. All securities within the scope of this statement with a recognized other-than-temporary impairment, disclosed in the aggregate, classified on the basis for the other-than-temporary impairment: (1) intent to sell, (2) inability or lack of intent to retain the investment in the security for a period of time sufficient to recover the amortized cost basis, or (3) present value of cash flows expected to be collected is less than the amortized cost basis of the security.

g. For each security with an other-than-temporary impairment, recognized in the current reporting period by the reporting entity, as the present value of cash flows expected to be collected is less than the amortized cost basis of the securities:

   i. The amortized cost basis, prior to any current-period other-than-temporary impairment.

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ii. The other-than-temporary impairment recognized in earnings as a realized loss.

iii. The fair value of the security.

iv. The amortized cost basis after the current-period other-than-temporary impairment.

h. All impaired securities (fair value is less than cost or amortized cost) for which an other-than-temporary impairment has not been recognized in earnings as a realized loss (including securities with a recognized other-than-temporary impairment for non-interest related declines when a non-recognized interest related impairment remains):

i. The aggregate amount of unrealized losses (that is, the amount by which cost or amortized cost exceeds fair value) and

ii. The aggregate related fair value of securities with unrealized losses.

i. The disclosures in (i) and (ii) above should be segregated by those securities that have been in a continuous unrealized loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 months or longer using fair values determined in accordance with SSAP No. 100R.

j. Additional information should be included describing the general categories of information that the investor considered in reaching the conclusion that the impairments are not other-than-temporary.

k. When it is not practicable to estimate fair value, the investor should disclose the following additional information, if applicable:

i. The aggregate carrying value of the investments not evaluated for impairment, and

ii. The circumstances that may have a significant adverse effect on the fair value.

l. For securities sold, redeemed or otherwise disposed as a result of a callable feature (including make whole call provisions), disclose the number of CUSIPs sold, disposed or otherwise redeemed and the aggregate amount of investment income generated as a result of a prepayment penalty and/or acceleration fee.

m. The items in the scope of this statement are also subject to the annual audited disclosures in *SSAP No. 26R—Bonds*, paragraphs 30.e., 30.f. and 30.g.

~~52.~~54. Refer to the Preamble for further discussion regarding disclosure requirements. All disclosures within this statement, except disclosures included in paragraphs ~~51~~53.b., ~~51~~53.k. and ~~51~~53.m., shall be included within the interim and annual statutory financial statements. Disclosure requirements in paragraphs ~~51~~53.b., ~~51~~53.k. and ~~51~~53.m. are required in the annual audited statutory financial statements only.

Relevant Literature

~~53.~~55. This statement adopts *FASB Emerging Issues Task Force No. 99-20*, *Exchange of Interest-Only and Principal-Only Securities for a Mortgage-Backed Security,* as amended by *FAS 166, Accounting for Transfers of Financial Assets, An Amendment of FAS 140,* and *FASB Staff Position EITF 99-20-1, Amendments to the Impairment Guidance of EITF Issue No. 99-20.* This statement adopts paragraphs 5, 7 and 9 of AICPA *Statement of Position 03-03, Accounting for Certain Loans or Debt Securities Acquired*

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in a Transfer (SOP 03-03) for loan-backed and structured securities only. With the exception of this specific adoption, consideration of SOP 03-03 is still pending consideration for statutory accounting.

~~54.~~56. This statement rejects *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, ASU 2016-01, Financial Instruments – Overall, FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities* and *FASB Statement No. 91,* Accounting *for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*.

~~55.~~57. This statement also rejects *FASB Emerging Issues Task Force No. 89-4, Accounting for a Purchased Investment in a Collateralized Mortgage Obligation Instrument or in a Mortgage-Backed Interest-Only Certificate, FASB Emerging Issues Task Force No. 90-2, Exchange of Interest-Only and Principal-Only Securities for a Mortgage-Backed Security, FASB Emerging Issues Task Force No. 93-18, Recognition of Impairment for an Investment in a Collateralized Mortgage Obligation Instrument or in a Mortgage-Backed Interest-Only Certificate*, *FASB Emerging Issues Task Force No. 96-12, Recognition of Interest Income and Balance Sheet Classification of Structured Notes,* and *FASB Emerging Issues Task Force* No. *98-15, Structured Notes Acquired for a Specified Investment Strategy*.

58. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~56.~~59. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Subsequent revisions to this statement include:

a. Substantive revisions pertaining to valuation and impairment based on expected cash flows, as detailed in *Issue Paper No. 140—Substantive Revisions to SSAP No. 43—Loan-Backed and Structured Securities*, were effective September 30, 2009. (Transition guidance previously included in SSAP No. 43R was removed from the SSAP in the *As of March 2018 Accounting Practices and Procedures Manual* but is retained for historical purposes in the issue paper.)

b. Substantive revisions to incorporate a new method to determine the final NAIC designation were effective, on a prospective basis, for reporting periods ending on or after December 31, 2009. In 2011, revisions were incorporated to this process to be consistent with the P&P Manual. These revisions expanded the guidance to explicitly detail the process for "financial modeling" and "modified filing exempt" securities.

c. Nonsubstantive revisions to clarify the accounting for gains and losses between AVR and IMR securities were adopted in June 2010 with a January 1, 2011, effective date with early application allowed. Reporting entities that had previously bifurcated gains and losses between AVR and IMR for sale transactions were restricted from reversing prior bifurcations and were prohibited from reverting to a process that did not bifurcate gains and losses in the period between adoption and the effective date.

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d. Nonsubstantive revisions, reflected in paragraph ~~50~~52, to incorporate guidance from *INT 00-11: EITF 98-15: Structured Notes Acquired for a Specified Investment Strategy* were effective September 11, 2000.

e. Nonsubstantive revisions pertaining to the calculation of investment income for prepayment penalty and/or acceleration fees, reflected in paragraph 13, were effective January 1, 2017, on a prospective basis with early application permitted.

f. Nonsubstantive revisions to eliminate the modified filing exempt (MFE) method were effective March 31, 2019, with early adoption permitted for year-end 2018. Early adoption was considered an "all or nothing" approach. As such, reporting entities that did not elect to early adopt were required to apply the MFE process to all applicable SSAP No. 43R securities as of year-end 2018, whereas reporting entities that elected to early adopt were not permitted to use the MFE process for any SSAP No. 43R securities for year-end 2018.

g. Revisions adopted April 2019 to explicitly include mortgage-referenced securities in scope of this statement are effective December 31, 2019.

h. Nonsubstantive revisions adopted in November 2021 to clarify that residual tranches or interests (as defined in footnote 10) shall be reported at the lower of amortized cost or fair value on Schedule BA: Other Invested Assets are effective December 31, 2022. Reporting entities may elect to reclassify residual tranches or interests to Schedule BA in advance of the effective date. As of the effective date, residual tranches or interests previously reported on Schedule BA shall be reclassified to the appropriate residual tranche Schedule BA reporting line based on the underlying characteristics of the investment structure.

~~57.~~60. For securities purchased prior to January 1, 1994, where historical cash flows are not readily available for applying the retrospective method, the reporting entity may use January 1, 1994, as the acquisition date and the then book value as the cost for purposes of determining yield adjustments in future periods.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*
- NAIC Valuation of Securities product prepared by the Securities Valuation Office

Relevant Issue Papers

- *Issue Paper No. 43—Loan-Backed and Structured Securities*
- *Issue Paper No. 140—Loan-Backed and Structured Securities, Revised September, 2009*

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EXHIBIT A – QUESTION AND ANSWER IMPLEMENTATION GUIDE

This exhibit addresses common questions regarding the valuation and impairment guidance detailed in SSAP No. 43R.

Index to Questions

No.	Question
1	Are reporting entities permitted to establish an accounting policy to write down a SSAP No. 43R other-than-temporarily impaired security, for which a "non-interest" related decline exists, to fair-value regardless of whether the reporting entity intends to sell, or has the intent and ability to hold?
2	Can a reporting entity avoid completing a cash-flow assessment or testing for a specific other-than-temporarily impaired security when the entity believes there is a clear cash-flow shortage (i.e., non-interest related impairment) and elect to recognize a full impairment for the SSAP No. 43R security (no impairment bifurcation), with fair value becoming the new amortized cost basis, and recognition of the full other-than-temporary impairment as a realized loss?
3	Can reporting entities change their "intend to sell" or "unable to hold" assertions and recover previously recognized other-than-temporary impairments?
4	How do the regulators intend the phrase "intent and ability to hold" as used within SSAP No. 43R to be interpreted?
5	How do contractual prepayments affect the determination of credit losses?
6	Are the disclosure requirements within paragraphs ~~51~~53.f. and ~~51~~53.g. of SSAP No. 43R required to be completed for the current reporting quarter only, or as a year-to-date cumulative disclosure?
7	If an impairment loss is recognized based on the "present value of projected cash flows" in one period is the entity required to get new cash flows every reporting period subsequent or just in the periods where there has been a significant change in the actual cash flows from projected cash flows?
Questions 8-10 are specific to securities subject to the financial modeling process. (This process is limited to qualifying RMBS/CMBS securities reviewed by the NAIC Structured Securities Group.) The guidance in questions 8-10 shall not be inferred to other securities in scope of SSAP No. 43R.	
8	Do LBSS purchased in different lots result in a different NAIC designation for the same CUSIP? Can reporting entities use a weighted average method determined on a legal entity basis?
9	The NAIC Designation process for LBSS may incorporate loss expectations that differ from the reporting entity's expectations related to OTTI conclusions. Should the reporting entities be required to incorporate recovery values obtained from data provided by the service provider used for the NAIC Designation process for impairment analysis as required by SSAP No. 43R?
10	For companies that have separate accounts, can the NAIC designation be assigned based upon the total legal entity or whether it needs to be calculated separately for the general account and the total separate account?

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Questions 8-10 are specific to securities subject to the financial modeling process. (This process is limited to qualifying RMBS/CMBS securities reviewed by the NAIC Structured Securities Group.) The guidance in questions 8-10 shall not be inferred to other securities in scope of SSAP No. 43R.

1. Question - Are reporting entities permitted to establish an accounting policy to write down a SSAP No. 43R other-than-temporarily impaired security, for which a "non-interest" related decline exists, to fair-value regardless of whether the reporting entity intends to sell, or has the intent and ability to hold?

1.1 Pursuant to the guidance in SSAP No. 43R, optionality is not permitted. As such, an accounting policy that differs from SSAP No. 43R would be considered a departure from statutory accounting principles as prescribed by the NAIC *Accounting Practices and Procedures Manual.*

2. Question – Can a reporting entity avoid completing a cash-flow assessment or testing for a specific other-than-temporarily impaired security when the entity believes there is a clear cash-flow shortage (i.e., non-interest related impairment) and elect to recognize a full impairment for the SSAP No. 43R security (no impairment bifurcation), with fair value becoming the new amortized cost basis, and recognition of the full other-than-temporary impairment as a realized loss?

2.1 Under the basis of SSAP No. 43R, an entity is not permitted to elect a write-down to fair value in lieu of assessing cash flows and bifurcating "interest" and "non-interest" impairment components. As noted in paragraph ~~34~~36, if the entity does not have the intent to sell, and has the intent and ability to hold, but does not expect to recover the entire amortized cost basis of the security, the entity shall compare the present value of cash flows expected to be collected with the amortized cost basis of the security. If present value of cash flows expected to be collected is less than the amortized cost basis of the security, the entire amortized cost basis of the security will not be recovered (a non-interest decline exists) and an other-than-temporary impairment shall be considered to have occurred. Pursuant to paragraph ~~37~~39, when an other-than-temporary impairment has occurred because the entity does not expect to recover the entire amortized cost basis of the security even if the entity has no intent to sell and the entity has the intent and ability to hold, the amount of the other-than-temporary impairment recognized as a realized loss shall equal the difference between the investment's amortized cost basis and the present value of cash flows expected to be collected, discounted at the loan-backed or structured security's effective interest rate.

2.2 If the entity does not want to assess cash flows of an impaired security (fair value is less than amortized cost), the entity can designate the security as one the entity intends to sell, or one that the entity does not have the intent and ability to hold, providing it is reflective of the true intent and assessment of the ability of the entity. Once an impaired security has this designation, pursuant to paragraphs ~~32~~34 or ~~33~~35, an other-than-temporary impairment shall be considered to have occurred. As detailed in paragraph ~~36~~38, the amount of the other-than-temporary impairment recognized in earnings as a realized loss shall equal the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date.

2.3 As addressed in question 3 of this Question and Answer Guide, reporting entities are not permitted to change assertions regarding their intent to sell or their lack of intent and ability to hold. Once the security has been identified as one the entity intends to sell, or as a security that the entity does not have the intent and ability to hold, that assertion shall not change as long as the entity continues to hold the security.

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3. Question - Can reporting entities change their "intend to sell" or "unable to hold" assertions and recover previously recognized other-than-temporary impairments?

3.1 No, a reporting entity is not permitted to change assertions and reverse previously recognized SSAP No. 43R other-than-temporary impairments. Although an entity may elect to hold a security due to a favorable change in the security's fair value, once the security has been identified as one the entity intends to sell, or as a security that the entity does not have the intent and ability to hold for purposes of initially recognizing an other-than-temporary impairment, that assertion shall not change as long as the entity continues to hold the security.

3.2 Reporting entities that have recognized an other-than-temporary impairment on a SSAP No. 43R security in a manner corresponding with an assertion on the intent to sell or the lack of the intent and ability to hold, for which a subsequent other-than-temporary impairment has been identified, shall recognize a realized loss for the difference between the current amortized cost (reflecting the previously recognized SSAP No. 43R other-than-temporary impairment) and the fair value at the balance sheet date of the subsequent impairment. Thus, bifurcation of impairment between interest and non-interest related declines is not permitted for securities in which an other-than-temporary impairment was previously recognized on the basis that the reporting entity had the intent to sell, or lacked the intent and ability to hold, regardless if the entity has subsequently decided to hold the security.

3.3 Reporting entities shall reclassify a security as one for which there is an intent to sell, or for which there is not an intent or ability to hold, regardless if a bifurcated other-than-temporary impairment had previously been recognized, as soon as the entity realizes that they can no longer support a previous assertion to hold the security. In making such reclassifications, if the security is impaired, the difference between the amortized cost (reflecting the initial non-interest other-than-temporary impairment recognized) and fair value at the balance sheet date of the reclassification shall be recognized as a realized loss, with fair value reflecting the new amortized cost basis. Once such a reclassification occurs, and the security is classified as one for which there is an intent to sell, or for which there is not an intent and ability to hold, the security must continue to carry that assertion until it is no longer held by the reporting entity.

4. Question – How do the regulators intend the phrase "intent and ability to hold" as used within SSAP No. 43R to be interpreted?

4.1 SSAP No. 43R paragraph ~~33~~35 states in part "…the entity shall assess whether it has the intent and ability to retain the investment in the security for a period of time sufficient to recover the amortized cost basis. If the entity does not have the intent and ability to retain the investment for the time sufficient to recover the amortized cost basis, an other-than-temporary impairment shall be considered to have occurred."

4.2 The intent of this language within SSAP No. 43R is focused on ensuring that, as of the balance sheet date, after considering the entity's own cash or working capital requirements and contractual or regulatory obligations and all known facts and circumstances related to the impaired security, the entity does not have the intention of selling the impaired security and has the current intent and ability to hold the security to recovery. Due to impairment bifurcation provisions provided within SSAP No. 43R, and the amortized cost measurement method generally permitted for loan-backed and structured securities, the assessment of "intent and ability" is intended to be a high standard. Despite the intent of paragraph ~~33~~35, it is identified that information not known to the entity may become known in subsequent periods and/or facts and circumstances

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related to an individual holding or group of holdings may change thereby influencing the entity's subsequent determination of intent and ability with respect to a security or securities.

4.3 If a reporting entity asserts that it has the intent and ability to hold a security, or group of securities, until recovery of the amortized cost, but sells or otherwise disposes the security or securities prior to such recovery, the reporting entity shall be prepared to justify this departure from their original assertion to examiners and auditors. SSAP No. 43R purposely does not identify specific circumstances in which a change in assertion would be justifiable, but requires judgment from management, examiners and auditors on whether future assertions warrant closer review.

4.4 Delaying recognition of other-than-temporary impairments is a cause of serious concern by the regulators, and entities that habitually delay such recognition through false assertions on the "intent and ability to hold" may face increased scrutiny and regulatory action by their domiciliary state. It is imperative that a reporting entity recognize the full other-than-temporary impairment as soon as the entity realizes that they will no longer be able to hold the security until recovery of the amortized cost basis. Greater scrutiny shall be placed on securities sold or otherwise disposed shortly after a financial statement reporting date if such securities had been excluded from the full other-than-temporary impairment recognition on the basis of the reporting entity's intent and ability to hold.

4.5 As noted in paragraph 3.3 of this question and answer guide, once a security is classified as one for which there is an intent to sell, or for which there is not an intent and ability to hold, the security must continue to carry that assertion until the security is no longer held by the reporting entity.

5. Question – How do contractual prepayments affect the determination of credit losses?

5.1 Paragraph ~~34~~36 of SSAP No. 43R states that "A decrease in cash flows expected to be collected on a loan-backed or structured security that results from an increase in prepayments on the underlying assets shall be considered in the estimate of present value of cash flows expected to be collected." Paragraph 16 states that "Loan-backed and structured securities shall be revalued using the currently estimated cash flows, including new prepayment assumptions, using either the prospective or retrospective adjustment methodologies consistently applied by type of securities."

5.2 The language in paragraph ~~34~~36 is consistent with GAAP, and the GAAP guidance related to the treatment of prepayments in the consideration of credit losses was intended to provide clarification for determining the "cash flows expected to be collected" on interest-only securities and other similar securities that can be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of the investment. These securities are generally accounted for in accordance with paragraphs 19-25 of SSAP No. 43R, which requires that an entity estimate cash flows expected to be collected including both amount and timing. Therefore, for securities under SSAP No. 43R, excluding those accounted for under paragraphs 19-25, decreases in cash flows resulting in contractual prepayments should be considered yield adjustments rather than potential credit losses.

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6. Question – Are the disclosure requirements within paragraphs ~~51~~53.f. and ~~51~~53.g. of SSAP No. 43R required to be completed for the current reporting quarter only, or as a year-to-date cumulative disclosure?

6.1 The disclosures should reflect the year-to-date other-than-temporary impairments. The "fair value" reported within the disclosure is intended to reflect the fair value at the date of the other-than-temporary impairment and shall not be updated due to the fluctuations identified at subsequent reporting dates. If a security has more than one other-than-temporary impairment identified during a fiscal reporting year, the security shall be included on the disclosure listing separately for each identified other-than-temporary impairment. Notation shall be included on the disclosure identifying the other-than-temporary impairments that were recognized for each respective reporting period.

7. Question – If an impairment loss is recognized based on the "present value of projected cash flows" in one period is the entity required to get new cash flows every reporting period subsequent or just in the periods where there has been a significant change in the actual cash flows from projected cash flows?

7.1 The guidance in paragraph ~~40~~42 of SSAP No. 43R indicates that a reporting entity shall continue to estimate the present value of cash flows expected to be collected over the life of the loan-backed or structured security. This guidance is explicit that the reporting entity shall continue to estimate the present value of cash flows expected to be collected over the life of the loan-backed or structured security.

7.2 As provided in paragraph 2.2 of this Q&A, if the entity does not want to assess cash flows of an impaired security (fair value is less than amortized cost), the entity can designate the security as one the entity intends to sell, or one that the entity does not have the intent and ability to hold, providing it is reflective of the true intent and assessment of the ability of the entity. Reporting entities subject to the requirements of AVR and IMR should allocate the impairment loss between AVR and IMR accordingly.

8. Question – Do LBSS purchased in different lots result in a different NAIC designation for the same CUSIP? Can reporting entities use a weighted average method determined on a legal entity basis?

8.1 Under the financial modeling process (applicable to qualifying RMBS/CMBS reviewed by the NAIC Structured Securities Group), the amortized cost of the security impacts the "final" NAIC designation used for reporting and RBC purposes. As such, securities subject to the financial modeling process acquired in different lots can result in a different NAIC designation for the same CUSIP. In accordance with the current instructions for calculating AVR and IMR, reporting entities are required to keep track of the different lots separately, which means reporting the different designations. For reporting purposes, if a SSAP No. 43R security (by CUSIP) has different NAIC designations by lot, the reporting entity shall either 1) report the aggregate investment with the lowest applicable NAIC designation or 2) report the investment separately by purchase lot on the investment schedule. If reporting separately, the investment may be aggregated by NAIC designation. (For example, all acquisitions of the identical CUSIP resulting with an NAIC 1 designation may be aggregated, and all acquisitions of the identical CUSIP resulting with an NAIC 3 designation may be aggregated.)

9. Question – The NAIC Designation process for LBSS subject to the financial modeling process may incorporate loss expectations that differ from the reporting entity's expectations related to OTTI conclusions. Should the reporting entities be required to incorporate recovery values obtained from data provided by the service provider used for the NAIC Designation process for impairment analysis as required by SSAP No. 43R?

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9.1 In accordance with *INT 06-07: Definition of Phrase "Other Than Temporary*," reporting entities are expected to "consider all available evidence" at their disposal, including the information that can be derived from the NAIC designation.

10. Question - For companies that have separate accounts, can the NAIC designation be assigned based upon the total legal entity or whether it needs to be calculated separately for the general account and the total separate account?

10.1 The financial modeling process for qualifying RMBS/CMBS securities is required for applicable securities held in either the general or separate account.

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Statement of Statutory Accounting Principles No. 44

Capitalization of Interest

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for capitalization of interest.

SUMMARY CONCLUSION

2. The historical cost of acquiring an asset generally includes the necessary costs incurred to bring it to the condition and location necessary for its intended use. If an asset requires a period of time in which to carry out the activities necessary to bring it to that condition and location, the interest cost incurred during that period as a result of expenditures for the asset shall be included as a part of the historical cost of acquiring the asset.

3. Interest cost shall be capitalized for the following types of assets:

   a. Assets constructed or otherwise produced for an enterprise's own use (including assets constructed or produced for the enterprise by others for which deposits or progress payments have been made);

   b. Assets intended for sale or lease that are constructed or otherwise produced as discrete projects (e.g., real estate developments);

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c. Investments (equity, loans, and advances) accounted for by the equity method while the investee has activities in progress necessary to commence its planned principal operations provided that the investee's activities include the use of funds to acquire qualifying assets for its operations. The equity method is defined in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

4. Interest cost shall not be capitalized for the following types of assets:

a. Assets that are in use or ready for their intended use in the earning activities of the enterprise;

b. Assets that are not being used in the earning activities of the enterprise and that are not undergoing the activities necessary to get them ready for use;

c. Investments accounted for by the equity method after the planned principal operations of the investee begin;

d. Investments in regulated investees that are capitalizing both the cost of debt and equity capital;

e. Assets acquired with gifts and grants that are restricted by the donor or grantor to acquisition of those assets to the extent that funds are available from such gifts and grants. Interest earned from temporary investment of those funds that is similarly restricted shall be considered an addition to the gift or grant for this purpose;

f. Nonadmitted assets.

5. Capitalized interest meets the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and is an admitted asset to the extent it conforms to the requirements of this statement.

Capitalization

6. The amount of interest cost to be capitalized for qualifying assets shall be determined in accordance with paragraphs 12-16 of *FASB Statement No. 34*, *Capitalization of Interest Cost* (FAS 34) and paragraph 6 of *FASB Statement No. 62, Capitalization of Interest Cost in Situations Involving Certain Tax-Exempt Borrowings and Certain Gifts and Grants* (FAS 62).

7. The capitalization period shall be in accordance with paragraphs 17-19 of FAS 34 and paragraph 7 of FAS 62.

Disclosures

8. Disclosures shall be made in the financial statements in accordance with paragraph 21 of FAS 34.

9. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosure in paragraph 8 shall be included in the annual audited statutory financial reports only.

Impairment

10. Capitalized interest shall be assessed for impairment in conjunction with the assessment of the related asset. Interest capitalization shall not cease when such an assessment requires recognition of a lower value for the asset than acquisition cost; rather the provision required to reduce acquisition cost to such lower value shall be increased appropriately.

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Relevant Literature

11. The statutory principles established in this statement adopt the GAAP accounting principles for capitalization of interest cost set forth in FAS 34, *FASB Statement No. 42, Determining Materiality for Capitalization of Interest Cost*, *FASB Statement No. 58, Capitalization of Interest Cost in Financial Statements That Include Investments Accounted for by the Equity Method*, and FAS 62, except that nonadmitted assets are ineligible for capitalization of interest.

Effective Date and Transition

12. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 44—Capitalization of Interest*

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Statement of Statutory Accounting Principles No. 47

Uninsured Plans

STATUS

Type of Issue..... Common Area
Issued ..... Initial Draft
Effective Date ..... January 1, 2001
Affects..... No other pronouncements
Affected by..... No other pronouncements
Interpreted by..... INT 05-05
Relevant Appendix A Guidance ..... None

STATUS **1**
SCOPE OF STATEMENT **1**
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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for all uninsured plans. This statement does not encompass policies written under the National Flood Insurance Program created by the Federal Emergency Management Agency (FEMA). Guidance for policies written under the National Flood Insurance Program is included in *SSAP No. 62R—Property and Casualty Reinsurance*.

SUMMARY CONCLUSION

2. For purposes of this statement, uninsured accident and health plans, including HMO administered plans, and uninsured property and casualty plans (collectively referred to as uninsured plans) are defined as plans for which a reporting entity, as an administrator, performs administrative services such as claims processing for a third party that is at risk, and accordingly, the administrator has not issued an insurance policy, regardless of whether an identification card is issued. In the case of uninsured accident and health plans, the administrator may arrange for the provision of medical services through a contracted or employed provider network. The plan (whether insured by another reporting entity or self insured) bears all of the insurance risk, and there is no possibility of loss or liability to the administrator caused by claims incurred related to the plan. The administrator, however, may be subject to credit risk with regard to the risk bearing entity. An uninsured accident and health plan may be either an Administrative Services Only (ASO) plan or an Administrative Services Contract (ASC) plan. Under an ASO plan, claims are

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paid from a bank account owned and funded directly by the uninsured plan sponsor; or, claims are paid from a bank account owned by the reporting entity, but only after the reporting entity has received funds from the uninsured plan sponsor that are adequate to fully cover the claim payments. Under an ASC plan, the reporting entity pays claims from its own bank accounts, and only subsequently receives reimbursement from the uninsured plan sponsor. No arrangement where the reporting entity receives a capitated payment for providing medical services to a third party shall qualify as an uninsured plan.

3. Uninsured accident and health plans also include Federal, state or other government department funded programs such as Medicare cost contracts where there is no underwriting risk to the reporting entity. Under Medicare cost contracts, service provided to recipients includes the direct delivery of health care for which the reporting entity is reimbursed based on costs incurred as provided for in regulations governing the administration of such contracts. Other such programs may include some Medicaid contracts for which administration or other non-underwriting services are provided.

4. Partially insured or combination plans exist, under which the reporting entity issues an insurance policy for some of the risks related to the claims (e.g. minimum premium and stop loss coverage), but acts as an administrator for some, or all, of the claims paid by the plan. Such plans shall be treated as two plans: an insured plan (the part for which the reporting entity has issued a policy) and an uninsured plan (the part that meets the definition in paragraph 2 of this statement). The components related to uninsured plans shall be accounted for using the accounting principles established in this statement; the components related to insured plans shall be accounted for as insurance.

Revenue/Expense Recognition

5. The administrator's statement of operations shall exclude all income and expenses related to claims, losses, premiums, and other amounts received or paid on behalf of uninsured ASO or uninsured ASC plans. An administrator acting as a provider of services, that provides such services through a salaried network, where the cost allocation of the service provided to insured vs. uninsured plans cannot be reasonably determined, shall report medical and hospital expenses on a gross basis by type of expense and report revenue from uninsured plans on a gross basis as fee for service income.

6. Commissions, expenses, and taxes paid by the administrator to administer such plans shall be reported on a gross basis by type of expense. Where the only functions provided are administrative, administrative fees and related reimbursements from the plan shall be deducted from general expenses. Reporting entities filing the health blank should deduct administrative fees and related reimbursements from general administrative expenses or claim adjustment expenses if the administrative services provided include services for claim adjustment expenses as defined in *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*. Where the reporting entity provides both administration and health care services directly, income from Medicare or similarly structured cost based reimbursement contracts is not recorded as premium but is recorded as revenue in the appropriate category. Health care services rendered as "medical and hospital" categorized by type and administrative expenses by type of expense shall be reported on an incurred basis.

7. Income from cost based reimbursement contracts is recorded as revenue because the service provided is for the direct delivery of care to recipients. There are risks associated with these plans in that all costs incurred under the contract may not be reimbursable and revenues may be adjusted based on subsequent challenges of costs included in filed cost reports. In addition, revenue may also be adjusted based on the performance under the terms of the contract or other external factors.

Amounts Receivable

8. Amounts receivable from uninsured plans for (a) claims and other costs paid by the administrator on behalf of the third party at risk and (b) fees related to services provided by the administrator to the plan meet the definition of assets as set forth in *SSAP No. 4—Assets and Nonadmitted Assets*. A receivable

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shall not be recorded for unpaid claims. A receivable related to Medicare or a similarly structured cost based reimbursement contract shall only be recorded when services have been rendered.

9. Specific funds received as reimbursements (or advance payments) for uninsured claims under a partially uninsured plan, including but not limited to the Medicare Part D program should be accounted for per this statement. These funds include 'Reinsurance Payments' and 'Low-Income Subsidy (cost-sharing portion)'. These funds are paid by the Government for a portion of claims above the out-of-pocket threshold or relate to PDP payments for all or a portion of the deductible, the coinsurance and the co-payment amounts for low-income beneficiaries. Refer to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* for additional information and definitions of terms specifically related to Medicare Part D business.

10. An evaluation shall be made of the amounts receivable to determine any nonadmitted amounts. Next, an evaluation shall be made in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, to determine whether there is an impairment. This two step process is set forth below:

a. Uncollected uninsured plan receivables (excluding Medicare and similar government plans) over ninety days due shall be accounted for as a nonadmitted asset;

b. Remaining amounts determined to be uncollectible shall be written off. If in accordance with SSAP No. 5R, it is "probable" the amount receivable is uncollectible, any uncollectible amount receivable shall be written off against operations in the period such determination is made. If it is "reasonably possible" the amount receivable is uncollectible, the disclosure requirements outlined in SSAP No. 5R, paragraph ~~31~~32, shall be made. This evaluation may consider irrevocable letters of credit to which the administrator is beneficiary, amounts on deposit with the administrator or other unrestricted funds available to the administrator.

11. The following shall provide additional guidance in determining the nonadmitted portion of amounts receivable from uninsured plans:

a. Amounts classified as nonadmitted assets collected subsequent to the date of the statutory financial statements shall not be used to decrease the nonadmitted asset otherwise calculated;

b. The due date is governed by the contractual billing date of the uninsured plan;

c. Medicare and similar government funded plans—Amounts due related to Medicare and similar government plans shall not be nonadmitted when they become over ninety days due. Appropriate reserves shall be established to cover costs incurred which may not be reimbursed upon final determination by the governing agencies under the cost contract or for adjustments to revenues based on performance under the terms of the contract or other external factors.

Liabilities

12. A liability shall be established for funds held by an administrator in its general assets for the benefit of an uninsured plan or for funds which may be owed by the administrator in connection with the administration of an uninsured plan. A liability relating to one plan shall not be offset by an asset relating to a different plan. Administrators shall not record aggregate reserves, claim/loss reserves, or liabilities (except for Medicare or similarly structured cost based reimbursement contracts) for any other claim costs paid by the administrator on behalf of uninsured plans.

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Disclosures

13. The statutory financial statements shall provide the following:

a. Information with regard to the profitability to the administrator of all ASO plans and the uninsured portions of partially insured plans for which the reporting entity serves as an ASO administrator;

For the total and each category separately provided: (i) net reimbursement for administrative expenses (including administrative fees) in excess of actual expenses, (ii) total net other income or expense (including interest paid to or received from plans), and (iii) total net gain or loss from operations and (iv) the claim payment volume;

b. Information with regard to the profitability to the administrator of all ASC plans and the uninsured portions of partially insured plans for which the reporting entity serves as an ASC administrator;

For the total and each category separately provided: (i) gross reimbursement for medical cost incurred, (ii) gross administrative fees accrued, (iii) other income or expense (including interest paid to or received from plans), (iv) gross expenses incurred (claims and administrative), and (v) total net gain or loss from operations.

c. Information with regards to Medicare or similarly structured cost based reimbursement contracts shall include: (i) major components of revenue by payor, (ii) receivables from payors with account balances the greater of 10% of gross amounts receivable relating to uninsured accident and health plans or $10,000, (iii) recorded allowances and reserves for adjustment of recorded revenues, (iv) adjustments to revenue resulting from audit of receivables related to revenues recorded in the prior period.

14. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

15. This statement rejects *ASU 2014-09, Revenue from Contracts with Customers; ASU 2015-14, Revenue From Contracts With Customers; ASU 2016-08, Revenue From Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net); ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing; ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients*; *ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers*; *ASU 2018-18, Collaborative Arrangements (Topic 808), Clarifying the Interaction between Topic 808 and Topic 606*, the Topic 606 guidance included in *ASU 2019-08, Codification Improvements to Stock Compensation (Topic 718) and Share-Based Consideration Payable to a Customer (Topic 606),* *ASU 2021-02, Franchisors—Revenue from Contracts with Customers*, and *ASU 2021-08, Business Combinations, Accounting for Contract Assets and Contract Liabilities from Contracts with Customers*.

Effective Date and Transition

16. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 47—Uninsured Plans*

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Statement of Statutory Accounting Principles No. 48

Joint Ventures, Partnerships and Limited Liability Companies

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 01-10, 04-10 and INT 08-03; Nullifies INT 01-14
Affected by	No other pronouncements
Interpreted by	INT 06-02; INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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Effective Date and Transition 8

REFERENCES **8**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investments in any joint ventures, partnerships, and limited liability companies, including investments in certified capital companies (CAPCO) per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)*, whether or not it is considered to be controlled by or affiliated with the reporting entity. Single real estate property investments that are wholly-owned by an LLC that is directly and wholly-owned by the reporting entity, and that meet the criteria established in *SSAP No. 40R—Real Estate Investments*, are excluded from this statement. This statement does not address the accounting for investments in partnerships and limited liability companies that invest in Low-Income Housing Tax Credit Properties as discussed in *SSAP No. 93—Low-Income Housing Tax Credit Property Investments.* However, investments in certain state Low-Income Housing Tax Credit Property Investments that do not fall within the scope of SSAP No. 93 are covered by the requirements of this statement.

SUMMARY CONCLUSION

2. Investments in joint ventures shall include investments in corporate joint ventures and unincorporated joint ventures (also referred to as undivided interests in ventures). A corporate joint venture is defined as a corporation owned and operated by a small group (the joint venturers) as a separate and specific business or project for the mutual benefit of the members of the group. A corporate joint

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venture usually provides an arrangement under which each joint venturer may participate, directly or indirectly, in the overall management of the joint venture. Joint venturers thus have an interest or relationship other than as passive investors. An unincorporated joint venture is similar in its purpose but is not incorporated.

3. Investments in partnerships shall include investments in general partnership interests and limited partnership interests. A general partnership is defined as an association in which each partner has unlimited liability. Each partner assumes joint and several liability for all partnership debts. A limited partnership shall be defined as a partnership having two classes of partners: (a) general partners who manage the partnership, subject to the partnership agreement, and have personal liability for the general obligations of the partnership and (b) limited partners who are passive investors and have no personal liability beyond their investment.

4. A limited liability company is defined as a business organization which is a hybrid of a corporation and partnership whereby the owners have limited liability like a corporation and profits may pass through to the owners for tax purposes like a partnership if certain criteria are met. The owner's personal liability is limited to his own acts and the owners can fully participate in the management of the business with no adverse impact on their limited liability.

5. Investments in the ventures defined in paragraphs 2-4 meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement. Investments in joint ventures, partnerships, and limited liability companies shall be reported in Other Invested Assets in the financial statements.

6. Investments in these ventures, except for joint ventures, partnerships and limited liability companies with a minor ownership interest[1], shall be reported using an equity method as defined in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*, paragraphs 8.b.i. through 8.b.iv. (The equity method calculation may result with a negative valuation of the investment; therefore, the SSAP No. 97 equity method calculation shall occur regardless of whether the investment is supported by an audit and the reporting entity will nonadmit the investment.) A reporting entity whose shares of losses in a SSAP No. 48 entity exceeds its investment in the SSAP No. 48 entity shall disclose the information required by SSAP No. 97, paragraph 35.a.

7. Investments reported using an equity method from SSAP No. 97, paragraph 8.b.ii. through 8.b.iv. may have fiscal year ends, not calendar year ends. To recognize a change to the reporting year-end of an equity method investee, including changes in, or the elimination of, previously existing differences (lag period) due to the reporting entity's ability to obtain financial results from a reporting period that is more consistent with, or the same as, that of the reporting entity's, the guidance included in *FASB Emerging Issues Task Force No. 06-9: Reporting a Change in (or the elimination of) a Previously Existing Difference Between the Fiscal Year-End of a Parent Company and That of a Consolidated Entity or Between the Reporting Period of an Investor and That of an Equity Method Investee* that defines such reporting period changes as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* shall be followed.

[1] With the identification of whether the reporting entity has a minor ownership interest, reporting entities must also identify whether the investment is a related-party transaction. Pursuant to the concepts reflected in *SSAP No. 25—Affiliates and Other Related Parties*, consideration shall be given to the substance of the transaction and the parties whose action or performance materially impacts the insurance reporting entity holding the security. For example, if the underlying assets within a SSAP No. 48 entity represent assets issued by an affiliate, then the SSAP No. 48 entity shall be considered a related party (affiliate) investment, with the transaction subject to the accounting and reporting provisions of SSAP No. 25. As identified in SSAP No. 25, it is erroneous to conclude that the inclusion of a non-related intermediary, or the presence of non-related assets in a structure predominantly comprised of related party investments, eliminates the requirement to identify and assess the investment transaction as a related party arrangement.

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8. Joint ventures, partnerships and limited liability companies in which the entity has a minor ownership interest (i.e., less than 10%) or lacks control as stipulated in paragraphs 15 and 16, shall be recorded based on the underlying audited U.S. GAAP equity of the investee. The investment shall be nonadmitted if the audited financial statements include substantial doubt about the entity's ability to continue as a going concern. Additionally, the investment shall be nonadmitted on the basis/contents of the audit opinion as detailed in paragraph 21 of SSAP No. 97.

9. If audited U.S. GAAP basis financial statements of the investee are not available, joint ventures, partnerships, and limited liability companies in which the entity has a minor ownership interest (i.e., less than 10%) or lacks control as stipulated in paragraphs 15 and 16 may be recorded based on either of the valuation methodologies allowed under paragraphs 9.a. or 9.b. If either one of the valuation methodologies allowed under paragraphs 9.a. or 9.b. is used to value the investment, documentation must be maintained regarding the reason that audited U.S. GAAP basis financial statements could not be provided.

a. Non-U.S. joint ventures, partnerships, and limited liability companies in which the entity has a minor ownership interest of less than 10% and for which audited U.S. GAAP basis financial statements of the investee are not available, may be recorded based on:

i. the U.S. GAAP basis equity as set forth in the audited footnote reconciliation of the investee's equity and income to U.S. GAAP within the investee's audited foreign GAAP prepared financial statements or,

ii. the IFRS basis equity as set forth in the investee's audited IFRS financial statements prepared in compliance, both annually and quarterly, with IFRS as issued by the International Accounting Standards Board (IASB).

b. If audited U.S. GAAP basis financial statements of the investee are not available, joint ventures, partnerships, and limited liability companies in which the entity has a minor ownership interest of less than 10%, measured at the holding company level, may be recorded based on the underlying audited U.S. tax basis equity. The U.S. tax basis equity audit shall occur at the investee level. For investments recorded based on the underlying audited U.S. tax basis equity, the reporting entity shall review investments held by the joint venture, partnership or limited liability company in accordance with the impairment guidance in paragraphs ~~18~~21 and ~~19~~22. The reporting entity must first attempt to obtain audited U.S. GAAP basis financial statements and, if such financial statements are unavailable, must maintain documentation regarding the reason that audited U.S. GAAP basis financial statements could not be provided.

10. The amount to be recorded shall be defined as the initial investment in an investee at cost (as defined in paragraph 3 of *SSAP No. 68—Business Combinations and Goodwill*) plus subsequent capital contributions to the investee. The carrying amount of the investment shall be adjusted for the amortization of the basis difference (difference between the cost and the underlying GAAP equity), as well as to recognize the reporting entity's share of: (i) the audited U.S. GAAP basis earnings or losses of the investee after the date of acquisition, adjusted for any distributions received, or (ii) if audited U.S. GAAP basis financial statements of the investee are not available, the earnings or losses of the investee after the date of acquisition, adjusted for any distributions received, based on either one of the valuation methodologies allowed under paragraphs 9.a. or 9.b. A reporting entity's share of adjustments, excluding changes in capital contributions to the investee, that are recorded directly to the investee's stockholders' equity shall also be recorded as adjustments to the carrying value of the investment with an offsetting amount recorded to unrealized capital gains and losses on investments.

11. Entities may recognize their investment in joint ventures, partnerships, and limited liability companies in which the entity has a minor ownership interest based on an unaudited basis for investment

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determination (i.e., foreign GAAP, IFRS, or tax basis as allowed under paragraph 9) if annual audited information is not complete as of the annual statement filing deadline. The recorded investment shall be adjusted for annual audit adjustments, if any, as soon as annual audited information is available. If financial statements of an investee are not sufficiently timely for the reporting entity to apply an equity method to the investee's current results of operations, the reporting entity shall record its share of the earnings or losses of an investee from the most recent available financial statements. A lag in reporting shall be consistent from period to period.

12. If an additional investment, in whole or in part, represents, in substance, the funding of prior losses, the entity should recognize previously suspended losses only up to the amount of the additional investment determined to represent the funding of prior losses. Whether the investment represents the funding of prior losses depends on the facts and circumstances.

13. Judgment is required in determining whether prior losses are being funded and that all available information should be considered in performing the related analysis. The following are certain factors to consider in that regard. However, no one factor should be considered presumptive or determinative.

a. Whether the additional investment is acquired from a third party or directly from the investee. When the additional investment is purchased from a third party and the investee does not obtain additional funds either from the investor or the third party, it is unlikely that, in the absence of other factors, prior losses are being funded**.**

b. The fair value of the consideration received in relation to the value of the consideration paid for the additional investment. For example, if the fair value of the consideration received is less than the fair value of the consideration paid, it may indicate that prior losses are being funded to the extent that there is disparity in the value of the exchange.

c. Whether the additional investment results in an increase in ownership percentage of the investee. In instances in which the investment is made directly with the investee, the investor should consider the form of the investment and whether other investors are making simultaneous investments proportionate to their interests. Investments made without a corresponding increase in ownership or other interests, or a pro rata equity investment made by all existing investors, may indicate that prior losses are being funded.

d. The seniority of the additional investment relative to existing equity of the investee. An investment in an instrument that is subordinate to other equity of the investee may indicate that prior losses are being funded.

14. Upon making the additional investment, the investor should evaluate whether it has become otherwise committed to provide financial support to the investee.

15. Control is defined as the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of the investee, whether through the (a) ownership of voting securities, (b) by contract other than a commercial contract for goods or nonmanagement services, (c) by common management, or (d) otherwise. Control shall be presumed to exist if a reporting entity and its affiliates directly or indirectly, own, control, hold with the power to vote, or hold proxies representing 10% or more of the voting interests of the entity.

16. Control as defined in paragraph 15 shall be measured at the holding company level. For example, if one member of an affiliated group has a 5% interest in an entity and a second member of the group has an 8% interest in the same entity, the total interest is 13% and therefore each member of the affiliated group shall be presumed to have control. This presumption will stand until rebutted by an evaluation of all the facts and circumstances relating to the investment based on the criteria in *FASB Interpretation No.*

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35, Criteria for Applying the Equity Method of Accounting for Investments in Common Stock, an Interpretation of APB Opinion No. 18. The corollary is required to demonstrate control when a reporting entity owns less than 10% of the voting interests of an investee. The insurer shall maintain documents substantiating its determination for review by the domiciliary commissioner. Examples of situations where the presumption of control may be in doubt include the following:

a. Any limited partner investment in a Limited Partnership, unless the limited partner is affiliated with the general partner.

b. An entity where the insurer owns less than 50% of an entity and there is an unaffiliated individual or group of investors who own a controlling interest.

c. An entity where the insurer has given up participation rights as a shareholder to the investee.

17. The reporting entity's share of undistributed earnings and losses of the investee shall be included in unrealized gains and losses of the reporting entity. The reporting entity's share of other changes in the investee's surplus (e.g., the change in the investee's nonadmitted assets) shall be recorded by the investor as a component of unrealized capital gains and losses on investments. Distributions received from an investee shall be recognized in investment income when declared to the extent that they are not in excess of the undistributed accumulated earnings attributable to the investee. Distributions declared in excess of the undistributed accumulated earnings attributable to the investee shall reduce the carrying amount of the investment.

Residual Interests and Reporting

18. Investments in scope of this statement are reported on *Schedule BA: Other Long-Term Assets*. Schedule BA includes dedicated reporting categories for joint ventures, partnerships, and limited liability company investments as well as for residual interests, both with reporting lines in accordance with underlying asset characteristics. Investments within scope of this standard shall be divided within these reporting categories, with investments that reflect residual interests, or that predominantly hold residual interests captured in the residual interest reporting category.

19. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.

20. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a

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residual should be based on the substance of the investment and how cash flows to the holder are determined.

a. Residuals often do not have contractual principal or interest.

b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.

c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.

d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.

e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.

Impairment

~~18.~~21. For any decline in the fair value of an investment in a joint venture, partnership, or limited liability company which is determined to be other than temporary(INT 06-07), the investment shall be written down to fair value as the new cost basis and the amount of the write down shall be accounted for as a realized loss. The write down shall first be considered as an adjustment to any portion of the investment that is nonadmitted (e.g., goodwill). The new cost basis shall not be changed for subsequent recoveries in fair value. Future declines in fair value, which are determined to be other than temporary, shall be recorded as realized losses.

~~19.~~22. An impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to recover the carrying amount of the investment or there is evidence indicating inability of the investee to sustain earnings which would justify the carrying amount of the investment. Even if the fair value of an investment is below the carrying amount it is not necessarily indicative of a loss in value that is other than temporary. Similarly, the existence of investee operating losses may indicate a loss in value; however, it is not necessarily indicative of a loss in value that is other than temporary.

Disclosures

~~20.~~23. The significance of an investment to the reporting entity's financial position and results of operations shall be considered in evaluating the extent of disclosures of the financial position and results of operations of an investee. Disclosures as follows shall be made for all investments in joint ventures, partnerships, or limited liability companies that exceed 10% of the total admitted assets of the reporting entity:

a. (1) the name of each joint venture, partnership or limited liability company and percentage of ownership, (2) the accounting policies of the reporting entity with respect to investments in joint ventures, partnerships and limited liability companies and (3) the difference, if any, between the amount at which the investment is carried and the amount of underlying equity in net assets (i.e., nonadmitted goodwill or other nonadmitted assets) and the accounting treatment of the difference;

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b. For joint ventures, partnerships, and limited liability companies for which a quoted market price is available, the aggregate value of each joint venture, partnership, or limited liability company investment based on the quoted market price; and

c. Summarized information as to assets, liabilities, and results of operations for joint ventures, partnerships, and limited liability companies either individually or in groups.

~~21.~~24. Any commitment or contingent commitment (e.g., guarantees or commitments to provide additional capital contributions) to a joint venture, partnership, or limited liability company shall be disclosed.

~~22.~~25. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment and how fair value was determined.

~~23.~~26. Any change due to the requirements of paragraph 7 shall be disclosed per SSAP No. 3.

~~24.~~27. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

~~25.~~28. This statement adopts with modification *FASB Emerging Issues Task Force No. 06-9: Reporting a Change in (or the elimination of) a Previously Existing Difference between the fiscal Year-End of a Parent Company and That of a Consolidated Entity or between the Reporting Period of an Investor and That of an Equity Method Investee*. The modifications include:

a. Adopt the guidance that defines such reporting period changes as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors,* modified to apply only to equity method investments. For instances in which this change in accounting principle occurs, disclosure requirements of SSAP No. 3 shall be followed.

b. The consolidation guidance in EITF 06-9 is rejected.

c. Changes affecting companies reporting investments in SCA entities using the equity method: Investments in SSAP No. 97 paragraph 8.b.i. entities are required to be calendar year-end. Investments in SSAP No. 97 paragraphs 8.b.ii. through 8.b.iv. entities may have other fiscal year ends; thus this issue could apply to equity method investments under 8.b.ii. through 8.b.iv. or under equity method valued investments that fall within the scope of SSAP No. 48.

~~26.~~29. This statement adopts *ASU 2016-07, Investments-Equity Method and Joint Ventures*, providing guidance for the prospective application of equity method accounting, modified to reflect statutory terms including the definition of control and statutory reporting concepts.

~~27.~~30. This statement is inconsistent with the guidance in paragraph 17 of *APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock* (APB 18), which addresses when control exists. APB 18 is addressed in its entirety and rejected in SSAP No. 97. This statement also rejects AICPA *Statement of Position 78-9, Accounting for Investments in Real Estate Ventures* and *FASB Emerging Issues Task Force No. 00-01, Investor Balance Sheet and Income Statement Display under the Equity Method for Investments in Certain Partnerships and Other Ventures*.

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Effective Date and Transition

~~28.~~31. This statement rejects *ASU 2020-01, Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815), Clarifying the Interactions between Topic 321, Topic 323 and Topic 815.*

~~29.~~32. This statement is effective for years beginning January 1, 2001. For investments made in joint ventures, partnerships and limited liability companies prior to January 1, 2001, if the joint venture, partnership or limited liability company does not prepare audited GAAP financial statements, and the reporting entity together with all other investors subject to this statement does not have sufficient voting power (pursuant to the joint venture, partnership or limited liability agreement) to force the preparation of audited GAAP financial statements, the reporting entity may then value its investment based on unaudited GAAP or audited tax-basis financial statements. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance in paragraph 1 was previously included within *SSAP No. 93—Low-Income Housing Tax Credit Property Investments* and was effective for reporting periods beginning on January 1, 2006, and thereafter, with early adoption permitted. The original guidance included in this standard, and the substantive revisions reflected in SSAP No. 93 are retained for historical purposes in *Issue Paper No. 125—Accounting for Low-Income Housing Tax Credit Property Investments*. Guidance in paragraph 7 was previously included within *INT 08-03: EITF 06-9: Reporting a Change in (or the elimination of) a Previously Existing Difference between the fiscal Year-End of a Parent Company and That of a Consolidated Entity or between the Reporting Period of an Investor and That of an Equity Method Investee* and was effective for periods beginning May 31, 2008. Guidance reflected in paragraphs 12, 13 and 14 incorporated from *INT 04-10: Accounting for Subsequent Investments in an Investee after Suspension of Equity Method Loss Recognition*, was originally effective December 5, 2004. Revisions adopted to paragraph 10 in August 2012 to clarify the requirement for the amortization of the basis differences shall be initially effective January 1, 2013, unless the company was previously amortizing the basis difference. (Companies that have previously amortized the basis difference shall not be impacted by these revisions.) For companies initially applying on January 1, 2013, the revisions should be applied prospectively for both new and existing minority-owned investments, with the effective date for this revision being used as the measurement date to determine any basis difference, which is attributable to goodwill, to be amortized on existing minority-owned investments.

~~30.~~33. The substantive revisions to incorporate single real estate property investments wholly-owned by an LLC that is directly and wholly-owned by the reporting entity in accordance with the criteria detailed in SSAP No. 40R are effective as of January 1, 2015. For these investments previously reported within the scope of this statement, the reporting entity shall follow the transition guidance in SSAP No. 40R.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 48—Investments in Joint Ventures, Partnerships and Limited Liability Companies*
- *Issue Paper No. 125—Accounting for Low-Income Housing Tax Credit Property Investments*
- *Issue Paper No. 149—Wholly-Owned Single Real Estate Property in an LLC*

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Statement of Statutory Accounting Principles No. 49

Policy Loans

STATUS

Type of Issue	Life, Accident and Health
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 01-05
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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EXHIBIT A – ILLUSTRATION OF ENTRIES FOR POLICY LOANS RELATED TO THE SEPARATE ACCOUNT **4**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for policy loans.

SUMMARY CONCLUSION

2. A policy (or contract) loan shall be defined as a loan to a policyholder, under the provisions of an insurance contract that is secured by the cash surrender value or collateral assignment of the related policy or contract. Policy loans shall include:

   a. Cash loans, including loans resulting from early payment benefits or accelerated payment benefits, on contracts when the terms of the contract specify that such payments are policy loans secured by the policy;

   b. Automatic premium loans, which are loans made in accordance with policy provisions whereby delinquent premium payments are automatically paid from the cash value at the end of the established grace period for premium payments.

3. Policy loans meet the definition of assets, as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets, except as specified in paragraphs 5 and 6 of this statement. Policy loans are readily available to satisfy policyholder obligations as the terms of the policy loan allow the reporting entity to offset an outstanding policy loan balance against the cash surrender value of the policy.

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4. Policy loans shall be reported in the general account and carried at the unpaid balance of the loan. (Paragraph 9 and paragraph 10 provide specific accounting and reporting guidance for policy loans related to separate account policies.) The unpaid balance of the loan shall include any unpaid principal plus any accrued interest which is 90 days or more past due.

5. If the unpaid balance of the loan exceeds the cash surrender value or policy reserves established for the policy, the policy generally lapses. Cash surrender value shall be defined as the cash value of the basic policy plus cash value of any policy accumulations such as paid-up additions. The excess of the unpaid balance of the loan over the cash surrender value shall be evaluated for collectibility. If the amount is considered uncollectible, it shall be written off as a reduction of investment income in the statement of operations during the period it is determined to be uncollectible. Except for collateral assignment loans, all other amounts in excess of the cash surrender value shall be considered nonadmitted assets. The change in this nonadmitted asset shall be recorded as a change in nonadmitted assets as applicable.

6. A loan resulting from early payment benefits or accelerated payment benefits and secured by an assignment of the policy to the reporting entity as collateral for the loan shall be an admitted asset, except that the amount of any loan (including accrued interest) in excess of the policy reserve for that policy shall be nonadmitted. Upon death, the entire death benefit is recorded as a death benefit expense. The policy proceeds shall be used to repay the loan. Any proceeds in excess of that needed to repay the loan are payable to the named beneficiary.

7. Interest income on policy loans shall be recorded as earned and included in investment income consistent with *SSAP No. 34—Investment Income Due and Accrued*. For interest received before it is earned, unearned interest income shall be recorded as a liability in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*.

8. Accrued interest income on policy loans that is past due 90 days[1] or more shall be reclassified from Investment Income Due and Accrued and included in the unpaid balance of the policy loan as defined in paragraph 4.

Policy Loans Related to Separate Account Policies

9. Policy loans related to separate account policies are reported in the general account. Pursuant to *SSAP No. 56—Separate Accounts*, policy loans relating to the separate account are recorded as expense transfers to the general account in the Summary of Operations. Exhibit A provides an illustration of the reporting process to record policy loans related to the separate account.

10. Policy loans related to the separate account (for both insulated and non-insulated separate account policies) must be settled with the general account in order for the policy loan to be admitted in the general account. This settlement requires a transfer of assets (generally cash) from the separate account to the general account to fund the policy loan. Policy loans that have not been settled with a transfer of assets from the separate account shall be nonadmitted.

Effective Date and Transition

11. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in the footnote to paragraph 8 was originally contained within *INT 01-05: Classification of Accrued Interest on Policy Loans* and was effective March 26, 2001.

[1] Interest less than 90 days due is allowed to be reclassified from Investment Income Due and Accrued and included in the unpaid policy loan balance earlier. This is a classification issue and would not result in any amounts being admitted that would otherwise be nonadmitted.

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 49—Policy Loans*

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EXHIBIT A – ILLUSTRATION OF ENTRIES FOR POLICY LOANS RELATED TO THE SEPARATE ACCOUNT

The following exhibit illustrates the entries when there is a policy loan related to separate account business. Key concepts within the reporting shall include:

1. All policy loans shall be reported in the general account.

2. All policy loans related to the separate account shall be reflected with an expense transfer between the separate and general account.

3. All policy loans related to the separate account must be "funded" to the general account in order for the policy loan to be admitted.

4. Separate account and general account reserves must be adjusted to reflect the policy loan. For the separate account, reserves shall be reduced, and the general account reserves shall be increased.

Separate Account		General Account	
Dr. Transfers on Account of Policy Loans	100	Dr. Transfers to SA due or accrued (net)	100
Cr. Other Transfers to GA due or accrued (net)	100	Cr. Net Transfers to / from SA	100
Records the expense transfer in the Summary of Operations and the liability owed from the SA.		*Records the expense transfer in the Summary of Operations and the asset due from the SA. Since this is a net presentation on the liability page, this asset may be recorded as a contra-liability.*	
Dr. Cash	100	Dr. Policy Loan	100
Cr. Separate Account Assets	100	Cr. Cash	100
Records the liquidation of separate account assets to fund the policy loan.		*Records the issuance of the policy loan to the policyholder.*	
		Dr. Change in Nonadmitted	100
		Cr. Unassigned Funds	100
		The policy loan is nonadmitted until funded from the separate account. If the loan is simultaneously funded, then this entry would not occur.	
Dr. Other Transfers to GA due or accrued (net)	100	Dr. Cash	100
Cr. Cash	100	Cr. Net Transfers to / from SA	100
Settles the amount due to the general account with the issuance of the policy loan.		*Settles the amount due from the separate account with the issuance of a policy loan.*	

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Separate Account		General Account	
		Dr. Unassigned Funds	100
		Cr. Change in Nonadmitted	100
		Removes nonadmittance of the policy loan as the loan has been funded from the separate account.	
Dr. Separate Account Liability	100	Dr. Change in Reserve	100
Cr. Change in Reserve	100	Cr. Reserve Liability	100
Reduces the amount of the separate account liability for the amount of the policy loan.		*Establishes a reserve in the general account for the amount of the policy loan.*	

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Statement of Statutory Accounting Principles No. 50

Classifications of Insurance or Managed Care Contracts

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 08-08; Nullifies INT 00-23 and INT 01-23
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement provides a general framework for classifying insurance or managed care contracts into categories where the recognition of contract and policy reserves and related revenue, benefits, and claims is fundamentally different. Separate statements will establish the accounting principles for premium and income recognition and policy benefit and claim reserves for all contracts defined herein.

SUMMARY CONCLUSION

Overview

2. The primary purpose of insurance, including managed care coverage, is to provide economic protection from identified risks occurring or discovered within a specified period. These risks include death, disability, health benefits, outliving one's financial assets, and damage to property by an insured

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peril or damage or injury to the insured or third parties. The accounting for the contract is significantly influenced by the terms of the insurance or managed care contract.

3. In order to provide for a conservative, consistent, and comparable method of accounting for insurance or managed care contracts, premiums and related benefits shall be recognized considering the policy term, premium payment requirements, risks assumed and benefits provided under the contract using conservative assumptions as to interest, mortality, morbidity, and incurred costs for health benefits as applicable. The reserve and income recognition methods reflect the premium payment pattern and the insurance protection and/or benefits provided for in the insurance or managed care contract.

4. This statement establishes an overall framework for existing insurance or managed care contracts by identifying four broad categories of insurance or managed care contracts where the premium payment pattern and the protection and/or benefits provided are fundamentally different and, therefore, require different income recognition and reserving methods.

5. Insurance contracts providing any protection against death, disability, accident or illness in which the reporting entity assumes mortality or morbidity risk shall be classified as life or accident and health contracts, as applicable. Managed care contracts provide defined health care services to subscribers, members or policyholders, collectively referred to hereafter as subscribers, in return for fixed, periodic premiums (usually paid monthly) that are generally due at or before the beginning of the coverage period and shall be classified as health contracts. Contracts which insure against damage to property by an insured peril or damage or injury to the insured or third parties, generally over a fixed/limited period of time, shall be classified as property and casualty contracts. Contracts in which the reporting entity does not assume any mortality, morbidity, health benefit costs incurred, or casualty risk and which act exclusively as investment vehicles shall be classified as deposit-type contracts. Such classification shall be made at the inception of the contract and shall not change.

Life Contracts

6. The primary purpose of life insurance is to provide financial assistance to a beneficiary at the insured's death. The long period of coverage involving the risk of death, a risk which usually increases with age, is the distinguishing characteristic by which life insurance is set apart from other forms of insurance. Life insurance is often sold on a level premium basis under which the annual premium remains constant even though the expected policy benefits and services do not occur evenly over the duration of the contract. Premium revenue generally exceeds expected policy benefits in the early years of the contract and it is necessary to accrue, as premium revenue is recognized, a liability for costs that are expected to be paid in the later years of the contract.

7. The liability for expected costs relating to most types of life contracts is accrued over the current and expected renewal periods of the contracts. The net valuation premium is based upon an assumed interest rate and upon the frequency of death derived from mortality tables. The net premiums collected, after deducting benefits and other costs each year, are accumulated at interest. This accumulation, when combined with future net premiums and future investment income theoretically generates a sum sufficient to pay the claims resulting from the death or disabilities of the insured.

8. The liability which corresponds to this fund is referred to as the policy reserve. These contracts are generally expected to be in force for an extended period of time and require the performance of various functions and services for an undefined period of time and are generally not subject to unilateral changes in their provisions. The policy reserve is generally calculated as the excess of the present value of future benefits to be paid to or on behalf of policyholders less the present value of future net premiums, discounted at valuation interest and mortality.

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9. Life insurance contracts shall include contracts with life contingencies, including, but not limited to:

a. Whole life contracts

b. Endowment contracts

c. Term life contracts

d. Supplementary contracts

e. Group life contracts

f. Franchise life contracts

g. Universal life type contracts

h. Variable life contracts

i. Limited payment contracts

j. Credit life contracts

k. Annuity contracts

Life Contracts—Definitions

10. The contract for ordinary life insurance is between the company and the policy owner (often the insured). Many variations of ordinary life coverages are available to a purchaser of insurance, including participating, limited-payment periods, combinations of coverages, and decreasing (or increasing) death benefits. Industrial life insurance, also called "debit" insurance, is insurance under which premiums are paid monthly or more often, the face amount of the policy does not exceed a stated amount, and the words "industrial policy" are printed in prominent type on the face of the policy. Ordinary and industrial life insurance contracts are considered life contracts and include the types of coverage as described in paragraphs 11-20.

11. Whole life contracts provide a fixed amount of insurance coverage over the life of the insured and the related benefits are normally payable only upon the insured's death. Premiums are paid over various periods as allowed by the terms of the policy contract. Whole life insurance contracts provide for nonforfeiture values, some common types being reduced paid up insurance, extended term insurance, and cash values, and some provide for the payment of policy dividends. A level premium is usually paid for policies of this type, and the premium may be paid in annual or more frequent modes. An ordinary life (straight-life) policy stipulates that premiums are to be paid during the life of the insured.

12. Endowment contracts are principally savings contracts which incorporate an element of life insurance protection. Endowment insurance contracts provide a benefit if the insured survives the endowment period or the amount is paid to a beneficiary if the insured does not survive. A pure endowment contract only provides a benefit to the insured if he/she survives the endowment period. Endowment policies mature at a specified attained age of the insured or at the end of a specified period. Premium payments for endowment contracts are made over a specified period, but may also be made under a single-premium or limited-payment plan. Both whole life and endowment policies contain nonforfeiture or similar clauses which provide for a value in cash or some other form of insurance to be available in the event of failure to continue the required premiums.

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13. Term life contracts provide insurance over a specified period of time. If the insured dies during this term, the face amount of the policy will be paid to the beneficiary. Policies for term insurance which are written for relatively short periods of time commonly grant the policyholder the right to renew for an additional period or periods up to a maximum age, such as 60 or 65, without requiring additional evidence of insurability. Rights to convert to whole life or endowment contracts may also be included in the contract. Term contracts may also be made for a period which will end when the insured reaches a certain age (for example, age 60 or 65). Such policies do not usually provide nonforfeiture values.

14. Supplementary contracts with life contingencies are a type of agreement between the insurance company and either the insured or the beneficiary, usually to provide for full or partial settlement of the amount payable upon the termination of an original contract. Generally, the proceeds are paid over the lifetime of one or more beneficiaries. This differs from a supplementary contract without life contingencies under which the proceeds are paid over a definite period without regard to the life of the beneficiary.

15. Group life contracts are insurance on the lives of a group of persons under a single master contract. Insurance of this type is customarily written on a yearly renewable term basis although some permanent group life is sold. Group life insurance is based on a master policy which usually precludes or disallows individual selection and is for the benefit of persons other than the policyholder. The individual insured members may receive certificates of insurance which evidence the contract. The contract is made by the policyholder and the insurer; there is no contract of insurance between the policyholder and the members. State statutes vary as to what constitutes a group and as to who may be a policyholder. Some states permit only employee-employer relationships in a group contract. Others permit union members, credit union members, or similar relationships in group contracts.

16. Franchise life contracts usually consist of individual policies offered to all persons in a general class (usually a work profession) who are related in some way such as belonging to a certain association.

17. Universal life and variable life contracts include those contracts which have terms that are not fixed and guaranteed relative to premium amounts, expense assessments, or benefits accruing to the policyholder. These contracts generally provide for death benefits and nonforfeiture values and may be issued on a fixed premium basis or on a flexible premium basis where the premiums are paid at the insured's discretion.

18. Limited-payment contracts are contracts with terms that are fixed and guaranteed and for which premiums are paid over a specified number of years or to a specified age. The insurance coverage continues for the remainder of the insured's life. A single-premium policy requires a lump-sum payment at the inception of the policy.

19. Credit life contracts are sold in connection with loans or other credit transactions not exceeding a stated duration and provide insurance protection against death. This form of insurance is generally issued in connection with the issuance of credit to an individual by a bank, retailer, finance company, or other similar organizations. This type of insurance most often protects the creditor to the extent of the unpaid balance of the loan in the form of decreasing term insurance; however, some credit life insurance is sold on a level-term basis.

20. An annuity contract is an arrangement whereby an annuitant is guaranteed to receive a series of stipulated amounts commencing either immediately or at some future date. The contract shall be issued to or for the benefit of an identifiable individual or group of individuals. Such a contract containing well-defined class-based (e.g. age, gender) annuity purchase rates used in defining either a specific or maximum purchase rate guarantee would constitute an annuity contract containing a life contingency that would require it to be classified as a life contract. Some examples of contracts issued for the benefit of a group of individuals include pension plan sponsors purchasing contracts for the benefit of their plan participants, employers or associations purchasing contracts for the benefit of their employees or

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members, and collective trusts purchasing contracts for the benefit of participating pension plans and their plan participants. The main types of annuity contracts with life contingencies are discussed below.

a. A deferred annuity provides for the accumulation of funds to be applied at some future period designated by the policyholder. Premium payments can be made in a lump sum amount (single premium deferred annuity), or periodically (flexible or fixed premium deferred annuity) as allowed by the policy contract. At the end of the accumulation period, the policyholder may elect to receive a lump sum distribution or may elect to receive periodic payments for life, or over a specific period, or some combination thereof;

b. A variable annuity is an annuity which includes a provision for benefit payments which vary in accordance with the rate of return of the underlying investment portfolio selected by the policyholder. The considerations for a variable annuity are usually invested in a separate account in which the value of the contract share varies according to the performance of the separate account before the commencement of annuity payments as well as after. Premium payments can be made in lump sum amounts or periodically as allowed by the policy contract. A minimum death benefit is often guaranteed during the annuity consideration accumulation period and these contracts are, therefore, classified as life contracts;

c. A straight-life annuity provides for periodic payments to the annuitant as long as the annuitant lives. Death of the annuitant constitutes completion of the contract and no further payments are made by the insurance company;

d. A life annuity with a period certain works essentially the same way as the straight-life annuity as the annuitant receives periodic payments for as long as the annuitant lives. However, if the annuitant dies before the end of the specified "certain" period, payments are continued to a beneficiary until the specified number of "certain" payments (i.e., the specified period in the contract) is completed;

e. A refund annuity is similar to the life annuity with a period certain in which the annuitant receives periodic payments for as long as the annuitant lives. There are two variants of this type of annuity. Under the cash refund annuity, a lump-sum payment is made at the death of the annuitant equal to the excess, if any, of the purchase price of the annuity over the sum of the annuity payments made to date of death. The installment refund annuity provides that annuity payments are to continue to a beneficiary after the death of the annuitant until the sum of all payments made equals the purchase price;

f. A joint and survivorship annuity provides for the continuation of payments after the death of one of the annuitants during the lifetime of the surviving annuitant.

Accident and Health Contracts

21. Health insurance policies or managed care contracts, offered by a health maintenance or similar organization, many life insurance and some property and casualty companies, may provide hospital, surgical, medical, loss of income, accidental death and dismemberment, or long term care coverage as well as other health related benefits. The insurance protection involving economic loss resulting from a medical condition (e.g., medical care expenses or the risk of disability) is the distinguishing characteristic by which accident and health insurance or managed care contracts are set apart from other forms of insurance. Health coverage is currently furnished under group or individual contracts. Coverage sold to individuals can be subdivided according to the reporting entity's right to continue the policy, limitations on the reporting entity's right to increase premiums, as well as other factors.

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22. Accident and health contracts also include risk contracts with Medicaid and Medicare whereby the reporting entity assumes insurance risk.

23. Managed care contracts are contracts that provide defined health care services to subscribers in return for fixed, periodic premiums (usually paid monthly) that are generally due at or before the beginning of the coverage period. Managed care means a system or technique(s) generally used by reporting entities to affect access to and control payment for health care services. Managed care techniques most often include one or more of the following: 1) review of the medical necessity and appropriateness of services or site of services; 2) contracts with selected providers; 3) financial incentives for enrollees to use specific providers, services, or service sites; 4) controlled access to and coordination of services by a case manager; and 5) payor efforts to identify treatment alternatives and modify benefit restrictions for high cost patient care. Expenses for medical, hospital, pharmacy and other benefits are recognized based on the way the reporting entity provides for the contracted services. In some instances, this is through the payment of claims to providers as services are rendered which require a claims liability to be recorded as addressed in *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* or through capitated arrangements based on contracts with providers, where expense is recognized ratably over the contract period in accordance with SSAP No. 55.

24. Similar to life insurance contracts, a significant amount of accident and health contracts is sold to individuals and groups on a level premium basis under which the annual premium remains constant even though the expected policy benefits and services may not occur evenly over the duration of the contract. Premium revenue for level premium contracts generally exceeds expected policy benefits in the early years of the contracts and it is necessary to accrue, as premium revenue is recognized, a liability for costs that are expected to be paid in the later years of the contracts.

25. The liability for expected costs relating to accident and health contracts sold on a level premium basis is accrued over the current and expected renewal periods of the contracts. The net valuation premium is based upon an assumed interest rate, persistency, and the frequency of expected death and disability claims, generally derived from mortality and morbidity tables. The net premiums collected, after deducting benefits and other costs each year, are accumulated with interest. Similar to life insurance, this accumulation or policy reserve, when combined with future net premiums and future investment income theoretically generate a sum sufficient to pay the claims resulting from the death or disabilities of the insured or subscriber. The reserve is generally calculated as the excess of the present value of future benefits to be paid to or on behalf of insureds or subscribers less the present value of future net premiums, discounted at valuation interest, mortality, and morbidity.

26. Accident and health contracts shall include contracts with health benefits or disability contingencies, including, but not limited to:

a. Managed care contracts

b. Income replacement contracts

c. Expense reimbursement contracts

d. Credit accident and health contracts

e. Continuing care contracts

f. Long-term care contracts

g. Accidental death and dismemberment contracts

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Accident and Health Contracts—Definitions

27. Accident and health contracts provide protection against economic losses resulting from accident, sickness or medical condition. This coverage may be provided under individual policies, under group or franchise policies, managed care contracts, Medicaid or Medicare risk contracts or it may be provided under certain special types of policies, such as credit accident and health insurance.

28. The economic losses which accident and health policies cover, or the types of benefits provided, will vary with different policies. The broad categories of economic losses protected against are medical and hospital expense and income replacement. For example, payments for hospital, surgical, or medical expenses may be provided under a hospital expense policy, while under other policies, a more comprehensive form of coverage, known as major medical insurance, may be offered. Similarly, policies may provide monthly benefits for loss of income from disability, either on a short-term or a long-term basis, or only for disabilities due to accident. Loss of life from accident may be covered under accidental death policies, while under certain limited accident policies, only accidental death from air travel may be covered.

29. Accident and health policies may be categorized by the form of policy through which the coverage is provided; it may be categorized according to the benefits provided by the policy; or it may be categorized by the contingencies insured against. These variations in types of policies and the benefits provided must be considered in discussing the reserves for accident and health policies.

30. Credit accident and health insurance contracts are similar to credit life insurance except the insurance protection is in the form of disability insurance.

31. Long-term care contracts represent any contract or policy rider providing coverage for not less than 12 consecutive months for each covered person for one or more necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital. Under long-term care contracts, the insured event is generally the inability of the contract holder to perform certain activities of daily living as compared to medical contracts which generally provide insurance protection against accident or sickness or disabilities contracts which generally provide income replacement protection.

Property and Casualty Contracts

32. Contracts which insure against damage to property by an insured peril or damage or injury to the insured or third parties shall be classified as property and casualty contracts. Damages shall include both physical and financial damages. Premiums from property and casualty contracts are generally recognized as earned over the exposure period of the contract in proportion to the amount of insurance protection provided.

33. The exposure to insurance risk for most property and casualty insurance contracts does not vary significantly during the duration of the contract. Premiums from property and casualty contracts shall be recognized as earned premium as discussed in *SSAP No. 53—Property and Casualty Contracts—Premiums*.

34. These contracts shall include but shall not be limited to:

a. Traditional property and casualty insurance contracts

b. Title insurance contracts

c. Mortgage and financial guaranty contracts

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Property and Casualty Contracts—Definitions

35. Property and casualty contracts include a variety of types of coverage, including, but not limited to, fire, workers' compensation, automobile, multiple peril, professional and miscellaneous liability, and fidelity and surety bonds as further discussed below.

36. Types of insurance represent the perils that are insured by property and liability insurance companies and classified as property and casualty contracts. Some of the more important types of insurance are as follows:

a. Fire and allied lines, which include coverage for fire, windstorm, hail, and water damage (but not floods);

b. Ocean marine, which includes coverage for ships and their equipment, cargos, freight or money to be paid for use of the ships, and liability to third parties for damages. This type of insurance includes inland as well as ocean water transportation;

c. Inland marine, which covers property in transit. (It also includes floaters, which are policies that cover movable property, such as a tourist's personal property);

d. Workers' compensation, which compensates employees for injuries or illness sustained in the course of their employment;

e. Automobile, which covers personal injury or automobile damage sustained by the insured and the related liability to third parties for losses caused by the insured;

f. Multiple peril, which is a package coverage including most property and liability coverage except workers' compensation, automobile insurance, and surety bonds;

g. Professional liability, which covers physicians, surgeons, dentists, hospitals, engineers, architects, accountants, attorneys, and other professionals from liability arising from error or misconduct in providing or failing to provide professional service;

h. Miscellaneous liability, which covers most other physical and property damages not included under workers' compensation, automobile liability, and multiple peril policies. (Damages include death, cost of care, and loss of services resulting from bodily injury, as well as loss of use of property);

i. Fidelity bonds, which cover employers against dishonest acts by employees. Blanket fidelity bonds cover groups of employees;

j. Surety bonds, which provide for monetary compensation to third parties for failure by the insured to perform specifically covered acts within a stated period. (Most surety bonds are issued for persons doing contract construction, persons connected with court actions, and persons seeking licenses and permits. Surety bonds also include financial guarantees.); and

k. Prepaid legal expense plans are established through group policies purchased by companies who in turn offer coverage to electing employees. The plans are offered as an employee benefit to help certificate holders more cost effectively solve their legal problems. For a small monthly premium, employees may consult with and/or receive representation from a plan attorney regarding any one of several covered services (such as will preparation, divorce, child adoption, etc.). The group policies are written for a set period, generally one year (and can be up to three-years), with the sponsoring company as the group policyholder. Policies may be canceled by the policyholder with 45 days'

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notice. The reporting entity sends monthly premium bills to participating employers based on the previous month's actual employee count. Monthly premium installments are withheld from the participating employee's paycheck and are remitted to the insurance company along with a detailed listing of the number of plan participants that month. Similar to group accident and health policies, premium amounts vary from month to month depending on the number of employees participating in the plan that month.

37. In addition to these types, insurance is provided by excess and surplus lines. Excess liability covers the insured against loss in excess of a stated amount, but only for losses as covered and defined in an underlying policy. The underlying amount is usually insured by another policy but can be retained by the insured. Surplus lines include coverage for risks that do not fit normal underwriting patterns, risks that are not commensurate with standard rates, or risks that will not be written by standard carriers because of general market conditions. These kinds of policies are generally written by carriers not licensed in the jurisdiction where the risk is located and generally are not subject to regulations governing premium rates or policy language.

38. Insurance is generally available to the individual as a means of protection against loss. There are instances, however, in which a person cannot obtain insurance in the voluntary insurance market. States have established involuntary plans to provide insurance to those with high risks whom otherwise would be excluded from obtaining coverage. A common example is the Automobile Insurance Plan (formerly called the Assigned Risk Plan). Under this plan, all companies writing automobile insurance in a state are allocated a share of the involuntary business on an equitable basis. Other states use a reinsurance plan, under which each insurer accepts all applicants but may place high-risk drivers in a reinsurance pool, with premiums paid to and losses absorbed by the pool. Still another approach is a joint underwriting association, in which one or more servicing companies are designated to handle high-risk drivers. All insurers in the state may be required to participate in the underwriting results. Another example of involuntary plans includes Fair Access to Insurance Requirements (FAIR) plans. FAIR plans are federally approved, state-supervised programs established to provide coverage for property in high-risk areas. Companies that operate in the state are assessed for any underwriting losses experienced by the FAIR plan.

39. Medical malpractice pools were established when health-care professionals and institutions were experiencing difficulty in obtaining liability insurance in the voluntary insurance market. The pools were established by law and currently exist in the majority of states. All insurers writing related liability insurance in such states are considered mandatory participants in the pools as a condition for their continuing authority to transact business in such states.

40. Workers' compensation pools are similar to FAIR plans. As with FAIR plans, companies operating in a given state are assessed a proportionate share, based on direct writings, of the underwriting results of the pool.

41. Title insurance insures, guarantees, or indemnifies owners of real property or the holders of liens or encumbrances thereon against loss or damage suffered by unidentified instances of defective titles, liens or encumbrances or the unmarketability of the title.

42. Mortgage guaranty insurance protects a lender against loss of all or a portion of the principal amount of a mortgage loan upon default of the mortgagor. This type of insurance provides no protection other than against loss due to default.

Deposit-Type Contracts

43. Deposit-type contracts do not incorporate insurance risk. Contracts issued by insurers that do not incorporate risk from the death or disability of policyholders (mortality or morbidity risk) are more

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comparable to financial or investment instruments issued by other financial institutions than to insurance contracts.

44. Deposit-type contracts shall include contracts without any life or disability contingencies, including, but not limited to, certain types of the following policy categories:

a. Supplemental contracts

b. Lottery payouts

c. Structured settlements

d. Guaranteed interest contracts

e. Income settlement options

f. Dividend and coupon accumulations

g. Annuities certain

h. Premium and other deposit funds

i. Funding Agreements without well-defined class-based (e.g. age, gender) annuity purchase rates defining either specific or maximum purchase rate guarantees (see SSAP No. 15, paragraph 19, paragraph 20 of this statement and *SSAP No. 52—Deposit-Type Contracts*, paragraph 21.)

45. Under deposit-type contracts, the policyholder may assume all, some, or none of the investment risk, depending on the contract terms. Amounts can be deposited in lump sum, or periodically as allowed by the policy contract. Deposit-type contracts would include annuities certain, whose income payments have no reference to life contingencies and benefits are paid over a specified period (i.e., 10 years, 20 years, etc.).

Relevant Literature

46. This statement rejects the U.S. GAAP classifications (i.e., short-duration and long-duration) found in *ASU 2022-05, Transition for Sold Contracts, ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts, FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises*, *FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*, and *FASB Statement No. 120, Accounting and Reporting by Mutual Life Insurance Enterprises and by Insurance Enterprises for Certain Long Duration Participating Contracts*.

Effective Date and Transition

47. This statement is effective for years beginning January 1, 2001. The guidance in paragraph 36.k. was originally contained within *INT 01-23: Prepaid Legal Insurance Premium Recognition* and was effective June 11, 2001.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 50—Classifications and Definitions of Insurance or Managed Care Contracts In Force*

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Statement of Statutory Accounting Principles No. 51 – Revised

Life Contracts

STATUS

Type of Issue	Life, Accident and Health
Issued	Initial draft; Substantively revised June 9, 2016
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 154 effective January 1, 2017
Affects	Supersedes SSAP No. 80 with guidance incorporated November 2011; Nullifies and incorporates INT 00-30 and INT 01-26
Affected by	No other pronouncements
Interpreted by	INT 00-03
Relevant Appendix A Guidance	A-200; A-225; A-235; A-585; A-620; A-641; A-695; A-812; A-815; A-817; A-820; A-821; A-822; A-830

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for income recognition and policy reserves for all contracts classified as life contracts defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*, except for credit insurance contracts which are discussed in *SSAP No. 59—Credit Life and Accident and Health Insurance Contracts* and separate account products which are discussed in *SSAP No. 56—Separate Accounts*.

SUMMARY CONCLUSION

Types of Premiums

2. The gross premium is the amount charged to the policyholder and taken into operations as premium income.

3. The net premium is the amount calculated on the basis of the interest and mortality table used to calculate the reporting entity's statutory policy reserves.

4. The difference between the gross premium and the net premium is referred to as "loading." Loading generally includes allowances for acquisition costs and other expenses but also includes the differences in mortality and interest assumptions utilized for pricing and statutory reserving purposes.

Premium Income Recognition

5. Premiums shall be recognized as income on the gross basis (amount charged to the policyholder) when due from policyholders under the terms of the insurance contract. As a result, premium income shall include first year and renewal premiums, as well as any related premium adjustments (i.e., retrospective premium contracts which are discussed in *SSAP No. 66—Retrospectively Rated Contracts*) provided for by the contract. The contractual due date shall be established through the predetermined billing procedure agreed to by the parties. In addition, premium income shall include single and flexible premium amounts when received from the policyholder. Further, the recognition of premium income and the change in loading shall be consistent with the assumptions made in calculating the related policy reserve.

6. Premium income shall include dividends, coupons, guaranteed annual pure endowments, and similar benefits provided by the insurance contract when such amounts are applied by the terms of the contract to provide additional paid-up insurance, annuities, or to shorten the endowment or premium-paying period. Premiums and considerations waived by the reporting entity under disability provisions contained in its policies and contracts, and reported in operations as a disability benefit, are included in premium income.

7. Premium income shall exclude premiums that have been received by the reporting entity prior to the reporting date but which are due on or after the next policy anniversary date (i.e., advance premiums as discussed in paragraph 29).

8. Premium income shall be reduced for premiums returned and allowances to industrial policyholders for the direct payment of premiums.

9. Premium income shall be increased by reinsurance premiums assumed and reduced by reinsurance premiums ceded. Reinsurance premiums assumed and ceded are defined and addressed in *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*.

10. Death or other benefits used to fund new policies shall be accounted for as a benefit payment and as a new premium, another type of income, or a liability, as appropriate.

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Premium Adjustments

11. In the summary of operations, the change in gross deferred and uncollected premiums is recorded as premium income. Deferred premiums are further discussed in paragraphs 25-27. Since only the net premiums are included in the computation of reserves and reported as an asset, it is necessary to adjust the gross premium for an amount representing the change in loading on deferred and uncollected premiums. The change in loading is included as an expense in the summary of operations and is not shown as a reduction to premium income.

Uncollected Premium Balances

12. Gross premiums that are due and unpaid as of the reporting date, net of loading, shall be classified as uncollected premiums. Uncollected premium balances which are less than 90 days past due meet the definition of an asset, as defined in *SSAP No. 4—Assets and Nonadmitted Assets,* and are admitted assets to the extent they conform to the requirements of this statement.

Other Considerations Received

13. Considerations for supplementary contracts, dividends left on deposit to accumulate interest, and amounts deposited and accumulated for guaranteed interest and group annuity contracts shall be recognized as deposit-type funds or considerations for supplemental contracts, as appropriate. These amounts are further discussed in *SSAP No. 52—Deposit-Type Contracts*.(INT 00-03)

Waiver of Monthly Deductions for Flexible Premium Universal Life Insurance Policies

14. Flexible premium universal life insurance policies do not require specified premiums as traditional policies do. The "waiver" benefit entities offer is a "waiver of monthly deductions" benefit as opposed to a "waiver of premium" benefit. The difference being specific premiums may or may not be required under the policy regardless of whether the insured is disabled or not. Waiver of a deduction is not to be considered revenue nor a benefit paid, therefore a calculation of the amount of the deduction need not be made for flexible premium universal life insurance policies.

Policy Reserves

15. Statutory policy reserves shall be established for all unmatured contractual obligations of the reporting entity arising out of the provisions of the insurance contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. These statutory policy reserves have historically been calculated as the excess of the present value of future benefits to be paid to or on behalf of policyholders less the present value of future net premiums. For policies issued on or after the operative date of the *Valuation Manual*, these formulaic calculations will be supplemented for some policies with more advanced deterministic and stochastic reserve methodologies to better reflect company experience, possible economic conditions and inherent policy risks. Statutory policy reserves meet the definition of liabilities as defined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. The actuarial methodologies referred to in paragraph 16 meet the criteria required for reasonable estimates in SSAP No. 5R.

16. The reserving methodologies and assumptions used in computation of policy reserves shall meet the provisions of Appendices A-820 and A-822. Policies written prior to the operative of the *Valuation Manual* shall additionally follow the actuarial guidelines found in Appendix C of this Manual. Policies written on or after operative of the *Valuation Manual* shall additionally follow the *Valuation Manual* and be subject to the actuarial guidelines referenced therein. Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

17. Paragraphs 15 and 16 of this statement summarize the general reserve requirements for all types of life contracts. Paragraphs 18-21 provide additional detail for specific products for policies that are

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issued prior to the operative data of the *Valuation Manual* or otherwise not subject to the *Valuation Manual*.

18. In addition to these general reserve requirements, Appendix A-820 provides additional guidance with respect to certain types of accumulation annuities that have flexible features (e.g., guaranteed nonforfeiture benefits such as interest guarantees, annuitization options, bailout features, partial withdrawals) which can create varying benefit streams if elected by the policyholder. Specific policies with such flexible features include most individual and some group annuity contracts, but exclude any disability and accidental death benefits in these contracts. For benefits under these contracts, reserves shall be established according to the Commissioners' Annuity Reserve Valuation Method (CARVM). Generally under CARVM, the difference between all possible future guaranteed benefits streams, including guaranteed nonforfeiture benefits, over the future considerations is computed as of the end of each contract year. Each of these differences is discounted to the reporting date at the applicable valuation interest rate. A reserve is then recorded based on the greatest present value difference of each of the contract year calculations.

19. Unlike traditional life insurance contracts, flexible premium universal life-type contracts do not have guaranteed premiums and some assumption as to future premiums is required. Appendix A-585 establishes a minimum reserving method for universal life-type contracts by providing guidance on how to estimate future premiums on flexible premium universal life-type contracts so that traditional valuation methodologies can be used. Alternative minimum reserves shall be required, if applicable, for flexible premium universal life-type contracts if the guaranteed maturity premium is less than the valuation net premium. Appendix A-585 shall be used in establishing reserves for flexible premium universal life-type contracts.

20. Policy reserves for fixed premium universal life-type contracts shall also follow guidance in Appendix A-585. Certain fixed premium products offer the policyholder a secondary guarantee. A secondary guarantee provides the policyholder a guaranteed set of cash values, death benefits, and maturity benefits that will be provided regardless of the performance of the policy value. Appendix A-585 requires all guarantees to be considered when establishing policy reserves and shall be followed in establishing reserves for fixed premium universal life-type contracts.

21. Statutory policy reserves for those group annuity contracts or other contracts that, in whole or in part, establish the insurer's obligations by reference to a segregated portfolio of assets not owned by the insurer shall be established in accordance with the guidance in Appendix A-695. Statutory policy reserves for those contracts with nonlevel premiums or benefits, or contracts with secondary guarantees shall be established in accordance with the guidance in Appendix A-830. Statutory policy reserves for those group life contracts utilizing a separate account that meet the requirements outlined in paragraph 1 of Appendix A-200 shall be computed in accordance with the guidance in that appendix.

22. For life and annuity policies issued on or after the operative date of the *Valuation Manual*, reserves shall use the requirements of the *Valuation Manual*. As required by Appendix A-820, reserves are required to be determined using the methodologies and processes described in the *Valuation Manual*. For policies unable to meet the *Valuation Manual* criteria for exemption from deterministic or stochastic reserves, the *Valuation Manual* supplements formulaic life insurance policy reserve methodologies with more advanced deterministic and stochastic reserve methodologies to produce reserves that better reflect company experience, possible economic conditions and inherent policy risks.

Valuation (Reserve) Method and Deferred Premiums

23. Reserves shall be established for all benefits guaranteed under the terms of the policy as of the reporting date using appropriate valuation methods, interest rates, mortality and morbidity rates, as applicable. However, as a practical expedient, reserves have been generally calculated as of the policy anniversary date (i.e., terminal reserves), not the reporting date. As a result, it is necessary to adjust the

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terminal reserve back to the reporting date. The components used to compute a terminal reserve shall include an interest rate, lapse rates, a mortality and/or morbidity table, and a valuation method (e.g., net level, full preliminary term, Commissioners' Reserve Valuation Method (CRVM), or CARVM). A terminal reserve is based on the assumption that all net premiums have been received, all interest earned, and all benefits paid to the end of the policy year.

24. Since terminal reserves are computed as of the end of a policy year and not the reporting date, the terminal reserve as of policy anniversaries immediately prior and subsequent to the reporting date are adjusted to reflect that portion of the net premium that is unearned at the reporting date. This is generally accomplished using either the mean reserve method or the mid-terminal method as discussed in paragraphs 25-28. Other appropriate methods, including an exact reserve valuation, may also be used.

Mean Reserve Method

25. Under the mean reserve method, the policy reserve equals the average of the terminal reserve at the end of the policy year and the initial reserve (the initial reserve is equal to the previous year's terminal reserve plus the net annual valuation premium for the current policy year). When reserves are calculated on the mean reserve basis, it is assumed that the net premium for a policy is collected annually at the beginning of the policy year and that policies are issued ratably over the calendar year.

26. However, as premiums are often received in installments more frequently than annually and since the calculation of mean reserves assumes payment of the current policy year's entire net annual premium, the policy reserve is overstated by the amount of net modal premiums not yet received for the current policy year as of the valuation date. As a result, it is necessary to compute and report a special asset to offset the overstatement of the policy reserve.

27. This special asset is termed "deferred premiums." Deferred premiums are computed by taking the gross premium (or premiums) extending from (and including) the modal (monthly, quarterly, semiannual) premium due date or dates following the valuation date to the next policy anniversary date and subtracting any such deferred premiums that have actually been collected. Deferred premium assets shall also be reduced by loading. Since the calculation of mean reserves assumes payment of the current policy year's entire net annual premium, deferred premium assets are considered admitted assets to compensate for the overstatement of the policy reserve. For policies subject to the *Valuation Manual* requirements, the deferred premium asset will continue to be calculated for the net premium reserve component of the total principle-based reserve.

Mid-Terminal Method

28. Under the mid-terminal method, the policy reserves are calculated as the average of the terminal reserves on the previous and the next policy anniversaries. These reserves shall be accompanied by an unearned premium reserve consisting of the portion of valuation premiums paid or due covering the period from the valuation date to the next policy anniversary date. For policies subject to the *Valuation Manual* requirements, the adjustment to the unearned premium reserve will continue to be calculated for the net premium reserve component of the total principle-based reserve.

Advance Premiums

29. Advance premiums are those premiums that have been received by the reporting entity prior to the valuation date but which are due on or after the next policy anniversary date. The policyholder may remit one or more premiums in advance of specific due dates. Where premiums are remitted sufficiently far in advance, the premiums charged to the policyholder may be reduced or discounted to reflect the time value of money. The difference between the gross and discounted premium is ratably charged as interest in the summary of operations from the date of payment to the premium due date. At the premium due date, the amount received from the policyholder plus the accumulated interest equals the gross premium

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necessary to fund the policy. The total amount of such advance premiums, less any discount as of the valuation date, is reported as a liability in the statutory financial statement and is not considered premium income until due. The gross premium, not the net valuation premium, is recorded as the advance premium in recognition of the reporting entity's liability to refund such premiums in the event the policy is terminated.

Policyholder Dividend Liability

30. A reporting entity shall accrue, as applicable, the following items relating to participating policies. They are dividends due and unpaid, dividends apportioned (or not yet apportioned) for payment in the following twelve months, and dividends left on deposit to accumulate interest.

31. Dividends due and unpaid represent dividends payable to the policyholder in the current year but which have not been disbursed or otherwise applied at the reporting date.

32. Dividends payable in the following calendar year represent the estimated amount of all dividends declared by a reporting entity's board of directors prior to the end of the statement year which are not yet paid or due at the end of the year (dividends apportioned for payment) as well as all dividends payable in the following calendar year that have not been declared (dividends not yet apportioned for payment). For individual insurance, the amount of this liability shall be equal to the aggregate amount of the dividends estimated to be payable in the following calendar year whether or not declared or apportioned. For group insurance and pensions, the amount of liability is generally equal to the portion of the dividend payable in the following calendar year which has been earned in the current calendar year.

33. Dividends left on deposit with the reporting entity shall be recorded in the amount of the deposit and accrued interest thereon. At the balance sheet date, the interest accrued but not yet credited to the policyholders' accounts shall be established as part of this liability.

Coupons

34. Some entities issue policies that guarantee an annual return, usually evidenced by a coupon that is part of the policy and matures on the policy's anniversary. This return represents an annual pure endowment and is essentially a return of premium previously paid by the policyholder. For matured coupons that have been left to accumulate, the liability is determined in the same way as the liability for dividend accumulations. Interest accrued is calculated for each coupon from the date each matures. The liability for unmatured policyholder coupons shall be the face value of the coupon, discounted at interest and mortality.

Reserve Recognition

35. The difference between the policy reserves for life contracts at the beginning and end of the reporting period shall be reflected as the change in reserves in the summary of operations, except for any difference due to a change in valuation basis.

Change In Valuation Basis

36. A change in valuation basis for reserves determined under paragraphs 17-21, except for reserves defined under *Actuarial Guideline XLIII—CARVM: For Variable Annuities* (AG 43), as detailed in Appendix C of this Manual, shall be defined as a change in the interest rate, mortality assumption, or reserving method (e.g., net level, preliminary term, etc.) or other factors affecting the reserve computation of policies in force and meets the definition of an accounting change as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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37. Changes in reserves developed under paragraph 22 or AG 43 shall be reviewed to determine whether the change represents a change in valuation basis and if it meets the definition of a change in accounting as defined in SSAP No. 3.

a. Changes in principle-based reserving assumptions are often the result of updating assumptions and other factors required by the existing reserving methodology. Reserve changes resulting from the application of principle-based reserving methodology including, but not limited to, updating assumptions based on reporting entity, industry or other experience, and having the reported reserve transition between net premium reserve, deterministic reserve or stochastic reserve, as required under existing guidance, shall not be considered a change in valuation basis. These types of changes also include, but are not limited to, periodic updates in *Valuation Manual* tables, such as industry valuation basic tables, asset spread tables and default cost tables.

b. A change in valuation basis for principle-based reserves shall include cases where the required reserve methodology has changed or the insurer makes a voluntary decision to choose one allowable reserving method over another. These types of changes include, but are not limited to, new standardized mortality tables such as Commissioners Standard Ordinary tables and regulatory changes in methodology. Voluntary decisions to choose one allowable reserving methodology over another, which require commissioner approval under the *Valuation Manual*, shall be reported as a change in valuation basis.

38. Consistent with SSAP No. 3, any increase (strengthening) or decrease (destrengthening) in actuarial reserves resulting from such a change in valuation basis shall be recorded directly to surplus (under changes to surplus in the change in valuation basis annual statement line) rather than as a part of the reserve change recognized in the summary of operations.

39. The impact of a change in valuation basis on surplus is based on the difference between the reported reserve under the old and new methods as of the beginning of the year. This difference shall not be phased in over time unless this statement or the *Valuation Manual,* Section VM-21 Requirements for Principle-Based Reserves for Variable Annuities (VM-21), prescribes a new method and a specific transition that allows for grading. Some changes will meet the definition of a change in accounting as defined in SSAP No. 3 and a change in valuation basis as described in paragraphs 36-38 of this statement, but the adjustment to surplus will be zero. This can happen when the change in valuation basis is prospective and only applies to new policies and reserves meaning that policies inforce for the prior year-end are not affected, or situations in which the change in reserving methodology did not change the reserves reported in the financial statements. The changes remain subject to the disclosures prescribed in SSAP No. 3. Effective January 1, 2020, if VM-21 (on variable annuities) or this statement prescribes or permits a phase-in period or provides the option of multiple phase-in periods, reporting entities shall also include in the change in accounting disclosures required by SSAP No. 3, disclosure of the following:

a. The phase-in period being applied, and the remaining time period of the phase-in;

b. Any adjustments to the phase-in period;

c. Amount of change in valuation basis phase-in; and

d. The remaining amount to be phased in.

40. The *Valuation Manual* is effective prospectively for policies written on or after the operative date; however, as the CARVM methodology was already principles-based, some changes to the CARVM methodology in VM-21 (on variable annuities) and to the related AG 43 may result in retroactive application to the reserving for existing contracts. Therefore, upon the initial prospective adoption of principle-based reserving, the change in valuation basis reflected as an adjustment to surplus for most

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entities will be zero. After initial adoption of the *Valuation Manual*, changes in valuation basis will need to be evaluated to determine the amount of any surplus adjustments.

Supplemental Benefits

41. In addition to the basic policy benefit, the insurance contract may provide supplemental benefits. Supplemental benefits include, but are not limited to, accidental death benefits and waiver of premium benefits. If the terms of the contract provide for these benefits, appropriate reserves shall be established in accordance with the applicable standards within the *Accounting Practices and Procedures Manual*.

Unearned Income

42. Amounts assessed that represent compensation to the reporting entity for services to be provided in future periods and which are required to be refunded upon policy termination are not earned in the period assessed. Such amounts, if not already considered in the policy reserve, shall be reported as unearned income, a liability, and recognized as income as the related services are provided.

Accelerated Benefits

43. Accelerated benefits are benefits payable under a life insurance contract to a policyholder or certificateholder during the lifetime of the insured, in anticipation of death or upon the occurrence of specified life-threatening or catastrophic conditions as defined by the policy or rider. These benefits reduce the death benefit otherwise payable under the life insurance contract and are payable upon the occurrence of a single qualifying event which results in the payment of a benefit amount fixed at the time of acceleration. When benefits are provided through the acceleration of benefits under group or individual life policies or riders to such policies, policy reserves shall be determined in accordance with Appendices A-820 and A-620. Reserves for such benefits in the aggregate shall be sufficient to cover policies upon which no claim has yet arisen as well as policies upon which an accelerated claim has arisen. Accounting guidance for accelerated benefit payments made in the form of a loan are addressed in *SSAP No. 49—Policy Loans*. In addition, accelerated benefit payments, for those accelerated benefits that reduce the policy, shall not be deferred but shall be charged to the summary of operations as a benefit expense when paid to the policyholder.

Additional Reserves Not Included Elsewhere

44. Additional actuarial liabilities are commonly held for such items as:

a. Provision for either nondeduction of deferred fractional premiums or return of premiums at death of the insured; and

b. Surrender values in excess of reserves otherwise required or carried.

Disclosures

45. For life and annuity reserves the financial statements shall disclose the following:

a. A description of reserve practices concerning the following:

i. Waiver of deduction of deferred fractional premiums upon death of insured;

ii. Return of portion of final premium for periods beyond the date of death; and

iii. Amount of any surrender value promised in excess of the reserve as legally computed;

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b. The methods employed in the valuation of substandard policies;

c. The amount of insurance, if any, for which the gross premiums are less than the net premiums according to the valuation standards;

d. The method used to determine tabular interest, tabular less actual reserves released, and tabular cost (by formula or from the basic data for such items); and

e. The nature of significant other reserve changes.

46. For the disclosures noted below, disclose the amount of annuity actuarial reserves and deposit liabilities by withdrawal characteristics for the categories of general account, separate account with guarantees, separate account nonguaranteed as well as the total and percentage of the total, include a separate section for individual Annuities, Group Annuities, and Deposit-Type Contracts (with no life contingencies). Supplementary contracts with life contingencies are reported in the appropriate Annuities section (Individual or Group).

a. Subject to discretionary withdrawal:

i. With market value adjustment, where withdrawal of funds is payable at all times, or prior to specified maturity dates where such dates are more than one year after the statement date and;

(a) In a lump sum with adjustments to reflect general changes in interest rates, or asset values since receipt of funds by the insurer;

(b) In installments over five years or more, with or without a reduction in the interest rate during the installment period;

ii. At book value less current surrender charge, where the withdrawal of funds is payable at all times, or at any time within one year from the statement date in a lump sum subject to a current fixed surrender charge of 5% or more and it does not contain a meaningful bail out rate as described in paragraph 46.a.v.(d);

iii. At fair value, where the withdrawal of funds is payable at current fair value of the assets supporting the liabilities, the assets are stated at current fair value, and the liabilities are stated at the current fair value or per unit value of the assets supporting the liabilities. These liabilities are for contracts where the customer bears the entire investment risk;

iv. Total with adjustment or at fair value;

v. At book value without adjustment (minimal or no charge or adjustment), where the withdrawal of funds is either payable at all times, or at any time (including a withdrawal on a scheduled payment date) within one year from the statement date and:

(a) In a lump sum without adjustment;

(b) In installments over less than five years, with or without a reduction in interest rate during the installment period;

(c) In a lump sum subject to a fixed surrender charge of less than 5%;

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(d) In a lump sum subject to surrender charge, but such charge is waived if the credited rate falls below a specified "bail out" rate and the "bail out" rate is more than the maximum statutory valuation rate for life insurance policies for more than 20 years for new issues;

b. Not subject to discretionary withdrawal;

c. Total gross;

d. Reinsurance ceded;

e. Total net;

f. Amount with current surrender charge of 5% or more included in the current year in paragraph 46.a.ii. that will have less than a 5% surrender charge (and thus be reported with the amounts at book value with minimal or no charge or adjustment noted in paragraph 46.a.v.) for the first time within the year subsequent to the balance sheet year. (Note that percentage of total is not required for this item.)

47. Disclose the amounts of account value, cash value and reserve for the breakouts of life insurance by withdrawal characteristics, separately for General Account products, Separate Account Guaranteed products, and Separate Account Nonguaranteed products as follows:

a. Subject to discretionary withdrawal, surrender values, or policy loans:

i. Term Policies with Cash Value

ii. Universal Life

iii. Universal Life with Secondary Guarantees

iv. Indexed Universal Life

v. Indexed Universal Life with Secondary Guarantees

vi. Indexed Life

vii. Other Permanent Cash Value Life Insurance

viii. Variable Life

ix. Variable Universal Life

x. Miscellaneous Reserves

b. Not subject to discretionary withdrawal or no cash value:

i. Term Policies without Cash Value

ii. Accidental Death Benefits

iii. Disability – Active Lives

iv. Disability – Disabled Lives

v. Miscellaneous Reserves

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c. Total gross (Direct + Assumed)

d. Reinsurance ceded

e. Total net (Net: Total gross (paragraph 47.c.) less Reinsurance ceded (paragraph 47.d.))

The difference between the account value and the cash value is the surrender charge, if any. After the surrender period is over, there is no difference. Some contract types have no account value such as traditional whole life, term, etc. So, if there is no account value, leave it blank. UL typically has an account value and a cash surrender value. Just as account values are not reduced for policy loans taken and outstanding, the cash value amount reported in this disclosure should not be reduced for policy loans taken and outstanding. This will ensure the difference between account value and cash value is the actual surrender charge.

48. Reconcile total life insurance reserves amount disclosed to the appropriate sections of the Aggregate Reserves for Life Policies and Contracts Exhibit (Exhibit 5) of the Life, Accident and Health Annual Statement and the corresponding lines in the Separate Accounts Statement. The reconciliation is a single presentation including all amounts from the sections on Individual Life Insurance and Group Life Insurance.

49. Reconcile the total annuity reserves and deposit fund liabilities amount disclosed in the (non-life reserves) annual statement Aggregate Reserve for Life Contracts Exhibit 5 and the deposit-type contract fund liabilities from the Deposit-Type Contracts Exhibit 7, of the Life, Accident & Health Annual Statement and the corresponding lines in the Separate Accounts Statement. The reconciliation is a single presentation including all amounts from the sections on Individual Annuities, Group Annuities and Deposit-Type Contracts.

50. If the reporting entity has reported life insurance premiums and annuity considerations deferred and uncollected on policies in force as of the financial statement date, disclose separately the amounts and the loading excluded for each of the following lines of business:

a. Industrial business;

b. Ordinary new business;

c. Ordinary renewal;

d. Credit life;

e. Group life;

f. Group annuity.

51. Disclose the aggregate amount of direct premiums written through managing general agents or third party administrators. For purposes of this disclosure, a managing general agent means the same as in Appendix A-225. If this amount is equal to or greater than 5% of surplus, provide the following information for each managing general agent and third party administrator:

a. Name and address of managing general agent or third party administrator;

b. Federal Employer Identification Number;

c. Whether such person holds an exclusive contract;

d. Types of business written;

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e. Type of authority granted (i.e., underwriting, claims payment, etc.);

f. Total premium written.

52. Reporting entities shall disclose the relative percentage of participating insurance, the method of accounting for policyholder dividends, the amount of dividends, and the amount of any additional income allocated to participating policyholders in the financial statements.

53. Reporting entities shall disclose if the reserve amount calculated on the state prescribed or permitted valuation basis is materially different from the reserve amount calculated on the A-820 valuation basis[1]. Although the A-820 standard is viewed as a minimum one, it represents the baseline from which deviations are measured. The determination of whether difference meets the standard of materiality is subjective. Refer to the Preamble regarding further guidance on the criterion of materiality.

54. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

55. This statement incorporates the requirements of Appendices A-225, A-235, A-585, A-620, A-641, A-695, A-812, A-815, A-817, A-820, A-821, A-822, A-830, the Actuarial Standards Board *Actuarial Standards of Practice,* and the actuarial guidelines found in Appendix C of this Manual.

56. This statement rejects *ASU 2022-05, Transition for Sold Contracts, ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts, FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises, FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments, FASB Statement 120, Accounting and Reporting by Mutual Life Insurance Enterprises and by Insurance Enterprises for Certain Long-Duration Participating Contracts,* AICPA *Practice Bulletin No. 8, Application of FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses From the Sale of Investments, to Insurance Enterprises,* the AICPA *Audit and Accounting Guide—Audits of Stock Life Insurance Companies,* AICPA *Statement of Position 95-1, Accounting for Certain Activities of Mutual Life Insurance Enterprises* relating to accounting and reporting for policy reserves for short and long duration contracts, and *FASB Interpretation No. 40, Applicability of Generally Accepted Accounting Principles to Mutual Life Insurance and Other Enterprises, an interpretation of FASB Statements No. 12, 60, 97, and 113.*

Effective Date and Transition

57. This statement is effective for years beginning January 1, 2001. Contracts issued prior to January 1, 2001 shall be accounted for based on the laws and regulations of the domiciliary state. State laws and regulations shall be understood to include anything considered authoritative by the domiciliary state under the individual state's statutory authority and due process procedures. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance in paragraph 14 was originally contained within *INT 00-30: Application of SSAP No. 51 Paragraph 6 to Waiver of Deduction on Flexible Premium Universal Life Insurance Policies* and was effective December 4, 2000. The guidance in paragraph 51 was originally contained within *INT 01-26: SSAP No. 51 and Reserve Minimum or Required Amount* and was effective January 1, 2001. The revisions adopted in November 2018 to expand liquidity disclosures are effective year-end 2019, concurrent with the inclusion of data-captured financial statement disclosures.

58. Substantive changes that reference the *Valuation Manual* in this statement are effective for January 1, 2017, and thereafter. However, the *Valuation Manual* provides for a 3-year period, starting

[1] This issue applies to contracts issued January 1, 2001, and thereafter.

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from the operative date, during which companies are able to continue using the current reserve methodologies, as described in paragraphs 17-21.

REFERENCES

Other

- *NAIC Financial Condition Examiners Handbook*
- *Actuarial Standards Board Actuarial Standards of Practice*

Relevant Issue Papers

- *Issue Paper No. 51—Life Contracts*
- *Issue Paper No. 56—Universal Life-Type Contracts, Policyholder Dividends, and Coupons*
- *Issue Paper No. 110—Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts, and SSAP No. 56—Separate Accounts*
- *Issue Paper No. 154—Implementation of Principle-Based Reserving*

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Statement of Statutory Accounting Principles No. 52

Deposit-Type Contracts

STATUS

Type of Issue	Life, Accident and Health
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 80 with guidance incorporated November 2011; Nullifies and incorporates INT 08-08; Nullifies INT 00-23
Affected by	No other pronouncements
Interpreted by	INT 00-03
Relevant Appendix A Guidance	A-200; A-235; A-695; A-820; A-822; A-830

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for income recognition and policy reserves for all contracts classified as deposit-type contracts defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*.

SUMMARY CONCLUSION

Introduction

2. As discussed in SSAP No. 50, deposit-type contracts are those contracts that do not subject the reporting entity to any risks arising from policyholder mortality or morbidity. A mortality or morbidity risk is present if, under the terms of the contract, the reporting entity is required to make payments or

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forego required premiums contingent upon the death or disability (in the case of life and disability insurance contracts) or the continued survival (in the case of annuity contracts) of a specific individual or group of individuals.

3. Deposit-type contracts frequently grant policyholders significant discretion over the amount and timing of deposits and withdrawals. Reporting entities are frequently granted significant discretion over amounts that accrue to or that are assessed against policyholders.

4. Due to the absence of mortality and/or morbidity risk and the discretionary characteristics noted in paragraph 3, the accounting principles for income recognition and policy reserves for deposit-type contracts differ from the accounting for life contracts set forth in *SSAP No. 51R—Life Contracts,* accident and health contracts established in *SSAP No. 54R—Individual and Group Accident and Health Contracts*, and credit insurance contracts as discussed in *SSAP No. 59—Credit Life and Accident and Health Insurance Contracts*.

5. Categories of contracts that may not subject the reporting entity to risks arising from policyholder mortality or morbidity include, but are not limited to, certain types of the following policy categories:

a. Supplemental contracts

b. Lottery payouts

c. Structured settlements

d. Guaranteed interest contracts

e. Income settlement options

f. Dividend and coupon accumulations

g. Annuities certain

h. Premium and other deposit funds

Income Recognition

6. Contracts issued by a reporting entity that do not incorporate mortality or morbidity risk shall not be accounted for as insurance contracts. Amounts received as payments for such contracts shall not be reported as revenues but shall be recorded directly to an appropriate policy reserve account.(INT 00-03)

Policy Reserves

7. Statutory policy reserves shall be established for all contractual obligations of the reporting entity arising out of the provisions of the contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. Statutory policy reserves meet the definition of liabilities as defined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. The actuarial methodologies referred to in paragraph 8 meet the criteria required for reasonable estimates in SSAP No. 5R.

8. The reserving methodologies and assumptions used in computation of policy reserves shall meet the provisions of Appendices A-820 and A-822, and the actuarial guidelines found in Appendix C of this Manual. Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

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9. The policy reserve for contracts without life contingencies where the future benefits are fixed and guaranteed (e.g., certain supplemental contracts, lottery payouts, structured settlements, guaranteed interest contracts, income settlement options, annuities certain, and unmatured coupon accumulations) shall be based on the present value of the future guaranteed benefits discounted at the valuation interest rate. The policy reserve for all other contracts (e.g., certain premium and other deposit funds, and dividend and matured coupon accumulations) shall be based on the accumulated amounts paid plus an income accumulation based on the contract provisions, less any withdrawals and applicable surrender charges.

10. Statutory policy reserves for those group annuity contracts or other contracts that, in whole or in part, establish the insurer's obligations by reference to a segregated portfolio of assets not owned by the insurer shall be established in accordance with the guidance in Appendix A-695. Statutory policy reserves for those contracts with nonlevel premiums or benefits, or contracts with secondary guarantees shall be established in accordance with the guidance in Appendix A-830. Statutory policy reserves for those group life contracts utilizing a separate account that meet the requirements outlined in paragraph 1 of Appendix A-200 shall be computed in accordance with the guidance in that appendix.

11. Policy reserves shall be increased for reinsurance assumed and decreased for reinsurance ceded as further described in *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*.

Structured Settlements

12. Reporting entities that have accepted an assignment of obligations under structured settlements shall record those obligations consistent with the accounting and reporting provided for structured settlements in *SSAP No. 65—Property and Casualty Contracts*.

Cost Recognition

13. Interest credited to deposit-type contracts shall be recorded as an expense in the summary of operations when earned under the terms of the contract. Payments that represent a return of policyholder balances shall not be recorded as expenses. To the extent such payments differ from the recorded reserve, the difference shall be recorded in the summary of operations as a benefit expense.

Change In Valuation Basis

14. A change in valuation basis shall be defined as a change in the interest rate assumption or other factor affecting the reserve computation of policies in force and meets the definition of an accounting change as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors*. Consistent with SSAP No. 3, any increase (strengthening) or decrease (destrengthening) in actuarial reserves resulting from such a change in valuation basis shall be recorded directly to surplus rather than as a part of the reserve change recognized in the summary of operations. The impact on surplus is based on the difference between the reserve under the old and new methods as of the beginning of the year. This difference shall not be graded in over time unless an actuarial guideline adopted by the NAIC prescribes a specific transition that allows for grading. Voluntary decisions to choose one allowable reserving methodology over another, which require commissioner approval under the *Valuation Manual*, shall be reported as a change in valuation basis.

Unearned Income

15. Amounts assessed that represent compensation to the reporting entity for services to be provided in future periods and which are required to be refunded upon policy termination are not earned in the period assessed. Such amounts, if not already considered in the policy reserve, shall be reported as unearned income, a liability, and recognized as income as the related services are provided.

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Additional Reserves Not Included Elsewhere

16. Additional actuarial liabilities are commonly held for such items as:

a. Surrender values in excess of reserves otherwise required or carried; and

b. Additional reserves required based on asset adequacy analysis as discussed in Appendix A-822.

17. Funding agreements issued to a Federal Home Loan Bank (FHLB) shall be evaluated on an individual basis, and shall be accounted for according to the substance of the individual arrangement and entity licensing. If the arrangement is in substance a funding agreement, including that the funds are used in an investment spread capacity, it shall be accounted for consistent with other funding agreements in accordance with this statement. If the arrangement is in substance a borrowing agreement, it shall be accounted for in accordance with *SSAP No. 15—Debt and Holding Company Obligations*, consistent with other borrowed money.

Disclosures

18. For life and annuity reserves, the financial statements shall disclose the following:

a. A description of reserve practices including the amount of any surrender value promised in excess of the reserve as legally computed;

b. The method of determination of tabular interest on funds not involving life contingencies; and

c. The nature of significant other reserve changes.

19. For the disclosures noted below, disclose the amount of annuity actuarial reserves and deposit liabilities by withdrawal characteristics for the categories of general account, separate account with guarantees, separate account nonguaranteed as well as the total and percentage of the total, include a separate section for Individual Annuities, Group Annuities, and Deposit-Type Contracts (with no life contingencies). Supplementary contracts with life contingencies are reported in the appropriate Annuities section (Individual or Group).

a. Subject to discretionary withdrawal:

i. With market value adjustment, where withdrawal of funds is payable at all times, or prior to specified maturity dates where such dates are more than one year after the statement date and;

(a) In a lump sum with adjustments to reflect general changes in interest rates, or asset values since receipt of funds by the reporting entity; and

(b) In installments over five years or more, with or without a reduction in the interest rate during the installment period.

ii. At book value less current surrender charge, where the withdrawal of funds is payable at all times, or at any time within one year from the statement date in a lump sum subject to a current fixed surrender charge of 5% or more and it does not contain a meaningful bail-out rate as described in paragraph 19.a.v.(d);

iii. At fair value, where the withdrawal of funds is payable at current fair value of the assets supporting the liabilities, the assets are stated at current fair value, and the

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liabilities are stated at the current fair value or per unit value of the assets supporting the liabilities. These liabilities are for contracts where the customer bears the entire investment risk;

iv. Total with adjustment or at fair value;

v. At book value without adjustment (minimal or no charge or adjustment), where the withdrawal of funds is either payable at all times, or at any time (including a withdrawal on a scheduled payment date) within one year from the statement date and:

(a) In a lump sum without adjustment;

(b) In installments over less than five years, with or without a reduction in interest rate during the installment period;

(c) In a lump sum subject to a fixed surrender charge of less than 5%;

(d) In a lump sum subject to surrender charge, but such charge is waived if the credited rate falls below a specified "bail out" rate and the "bail out" rate is more than the maximum statutory valuation rate for life insurance policies for more than 20 years for new issues;

b. Not subject to discretionary withdrawal;

c. Total gross (Direct + Assumed);

d. Reinsurance ceded;

e. Total net (Net: Total gross (paragraph 19.c.) less Reinsurance ceded (paragraph 19.d.));

f. Amount with current surrender charge of 5% or more included in the current year in paragraph 19.a.ii that will have less than a 5% surrender charge (and thus be reported with the amounts at book value with minimal or no charge or adjustment noted in paragraph 19.a.v.) in the year subsequent to the balance sheet year. (Note that percentage of total is not required for this item.)

20. Reconcile the total annuity reserves and deposit fund liabilities amount disclosed in the (non-life reserves) annual statement Aggregate Reserve for Life Contracts Exhibit 5 and the deposit-type contract fund liabilities from the Deposit-Type Contracts Exhibit 7, of the Life, Accident & Health Annual Statement and the corresponding lines in the Separate Accounts Statement. The reconciliation is a single presentation including all amounts from the sections on Individual Annuities, Group Annuities and Deposit-Type Contracts.

21. For FHLB agreements accounted for under this statement, include information for the FHLB funding agreements with other reporting and disclosure requirements for deposit-type contracts under this statement and complete additional disclosure requirements in *SSAP No. 30R—Unaffiliated Common Stock*, paragraph ~~18~~19.

22. For life insurance claims, disclose the following information regarding the reporting entity's use of retained asset accounts for beneficiaries. For purposes of this disclosure, retained asset accounts represent settlement of life insurance proceeds, which are retained by the insurance entity within their general account for the benefit of the beneficiaries. Amounts held outside of the insurance entity, for example in a non-insurance subsidiary, affiliated or controlled entity accounted for under *SSAP No. 97—Investments in Subsidiary, Controlled, and Affiliated Entities*, such as an interest bearing account

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established in the beneficiary's name with a bank or thrift institution (and subject to applicable Federal Deposit Insurance Corporation coverage) are only required to be described in the context of the structure of the reporting entity's program in accordance with paragraph 22.a., but quantitative information regarding retained asset accounts transferred outside of the reporting entity are not required.

a. A narrative description of how the accounts are structured and reported within the reporting entity's financial statements (e.g., as drafts written by the reporting entity and reported within cash and supplemental contracts without life contingencies; as accounts transferred into the beneficiary's name to an affiliated or unaffiliated bank or other financial institution in which the reporting entity has disposed of its liabilities and related assets, etc.). This description should include all of the different interest rates paid to retained asset account holders during the reporting year and the number of times changes in rates were made during the reporting year. The description should also include a listing of all applicable fees charged by the reporting entity that are directly or indirectly associated with the retained asset accounts. Also, indicate if the retained asset account is the default method for satisfying life insurance claims.

b. Number and balance of retained asset accounts in force at the end of the current year and prior year segregated within "aging categories" of "up to 12 months," "13 to 24 months," "25 to 36 months," "37 to 48 months," "49 to 60 months," "over 60 months;"

c. Number and balance of retained asset accounts in force at the beginning of the year segregated between individual and group contracts;

d. Number and amount of retained asset accounts issued during the year segregated between individual and group contracts;

e. Investment earnings credited to retained asset accounts segregated between individual and group contracts;

f. Fees and other charges assessed to retained asset accounts during the year segregated between individual and group contracts;

g. Number and amount of retained asset accounts transferred to state unclaimed property funds segregated between individual and group contracts;

h. Number and amount of retained asset accounts closed/withdrawn during the year segregated between individual and group contracts;

i. Number and balance of retained asset accounts in force at the end of the year segregated between individual and group contracts.

23. The disclosures in paragraph 22 are not required in the annual audited financial statements. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

24. This statement incorporates the requirements of Appendices A-235, A-695, A-820, A-822, the Actuarial Standards Board *Actuarial Standards of Practice*, and the actuarial guidelines found in Appendix C of this Manual.

25. This statement rejects *ASU 2022-05, Transition for Sold Contracts, ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts*, *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises*, *FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of*

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Investments, *FASB Statement 120, Accounting and Reporting by Mutual Life Insurance* Enterprises *and by Insurance Enterprises for Certain Long-Duration Participating Contracts*, AICPA *Practice Bulletin No. 8, Application of FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses From the Sale of Investments, to Insurance Enterprises,* the AICPA *Audit and Accounting Guide—Audits of Stock Life Insurance Companies*, AICPA *Statement of Position 95-1, Accounting for Certain Activities of Mutual Life Insurance Enterprises* relating to accounting and reporting for policy reserves for short and long duration contracts, and *FASB Interpretation No. 40, Applicability of Generally Accepted Accounting Principles to Mutual Life Insurance and Other Enterprises, an interpretation of FASB Statements No. 12, 60, 97, and 113*.

Effective Date and Transition

26. This statement is effective for years beginning January 1, 2001. Contracts issued prior to January 1, 2001 shall be accounted for based on the laws and regulations of the domiciliary state. State laws and regulations shall be understood to include anything considered authoritative by the domiciliary state under the individual state's statutory authority and due process procedures. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. Guidance in paragraph 17 was previously included within *INT 08-08: Balance Sheet Presentation of Funding Agreements Issued to a Federal Home Loan Bank* and was effective for periods beginning March 15, 2009. Guidance in paragraph 21 related to FHLB agreements was initially effective January 1, 2014. The revisions adopted in November 2018 to expand liquidity disclosures are effective year-end 2019, concurrent with the inclusion of data-captured financial statement disclosures.

REFERENCES

Other

- *NAIC Financial Condition Examiners Handbook*
- *Actuarial Standards Board Actuarial Standards of Practice*

Relevant Issue Papers

- *Issue Paper No. 52—Deposit-Type Contracts*
- *Issue Paper No. 110—Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts, and SSAP No. 56—Separate Accounts*

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Statement of Statutory Accounting Principles No. 53

Property and Casualty Contracts—Premiums

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 99-23, INT 01-23, INT 02-11 and INT 05-06
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-225

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement establishes general statutory accounting principles for the recording and recognition of premium revenue for property and casualty contracts as defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*.

2. Specific statutory requirements for certain property and casualty premiums are addressed in the following statements: (a) *SSAP No. 57—Title Insurance*, (b) *SSAP No. 58—Mortgage Guaranty Insurance,* (c) *SSAP No. 60—Financial Guaranty Insurance,* (d) *SSAP No. 62R—Property and Casualty Reinsurance,* (e) *SSAP No. 65—Property and Casualty Contracts,* and (f) *SSAP No. 66—Retrospectively Rated Contracts and Contracts*.

SUMMARY CONCLUSION

3. Except as provided for in paragraph 4, written premium is defined as the contractually determined amount charged by the reporting entity to the policyholder for the effective period of the contract based on the expectation of risk, policy benefits, and expenses associated with the coverage provided by the

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terms of the insurance contract. Frequently, insurance contracts are subject to audit by the reporting entity and the amount of premium charged is subject to adjustment based on the actual exposure. Premium adjustments are discussed in paragraphs 10-13 of this statement.

4. For workers' compensation contracts, which have a premium that may periodically vary based upon changes in the activities of the insured, written premiums may be recorded on an installment basis to match the billing to the policyholder. Under this type of arrangement, the premium is determined and billed according to the frequency stated in the contract, and written premium is recorded on the basis of that frequency.

5. Premiums for prepaid legal expense plans shall be recognized as income on the gross basis (amount charged to the policyholder or subscriber exclusive of copayments or other charges) when due from policyholders or subscribers, but no earlier than the effective date of coverage, under the terms of the contract. Due and uncollected premiums shall follow the guidance in *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*, to determine the admissibility of premiums and related receivables.

6. Written premiums for all other contracts shall be recorded as of the effective date of the contract. Upon recording written premium, a liability, the unearned premium reserve, shall be established to reflect the amount of premium for the portion of the insurance coverage that has not yet expired. Flat fee service charges on installment premiums[1] (fees charged to policyholders who pay premiums on an installment basis rather than in full at inception of contract) are reported in the Other Income section of the Underwriting and Investment Exhibit as Finance and Service Charges. Flat fee service charges on installment premiums, which do not meet the requirements outlined in footnote 1 (e.g., policy may be cancelled for non-payment of fee or fee is refundable), shall be recorded as written premium on the effective date of the contract and subject to the unearned premium guidelines included in paragraph 8.

7. The exposure to insurance risk for most property and casualty insurance contracts does not vary significantly during the contract period. Therefore, premiums from those types of contracts shall be recognized in the statement of income, as earned premium, using either the daily pro-rata or monthly pro-rata methods as described in paragraph 8. Certain statements provide for different methods of recognizing premium in the statement of operations for specific types of contracts. For contracts not separately identified in specific statements where the reporting entity can demonstrate the period of risk differs significantly from the contract period, premiums shall be recognized as revenue over the period of risk in proportion to the amount of insurance protection provided.

8. One of the following methods shall be used for computation of the unearned premium reserve:

   a. Daily pro rata method—Calculate the unearned premium on each policy—At the end of each period, the calculation is made on each item of premium to ascertain the unexpired portion and to arrive at the aggregate unearned premium reserve;

   b. Monthly pro rata method—This method assumes that, on average, the same amount of business is written each day of any month so that the mean will be the middle of the

[1] If the policyholder elects to pay an installment rather than the full amount or the full remaining balance, the policyholder is traditionally charged a flat fee service charge on the subsequent billing cycle(s). The amount charged is primarily intended to compensate the insurer for the additional administrative costs associated with processing more frequent billings and has no relationship to the amount of insurance coverage provided, the period of coverage, or the lost investment income associated with receiving the premium over a period of time rather than in a lump sum. As described, there is no underwriting risk associated with this service charge. If a policyholder does not pay the service charge, the policy is not cancelled (unlike non-payment of premium), but instead the policy is converted back to an annual pay plan. If a policyholder cancels coverage, the premium is returned but the service charge is not, as the service charge is not a part of premium. Note that this footnote on flat fee service charges on installment premium is intentionally narrow and specific, and this guidance should not be applied to other fees or service charges. Reporting of installment fees in finance and service charges as other income should not be construed as having any bearing on whether such charges are subject to premium taxation, which remains an issue of state law and regulation.

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month. For example, one-year premiums written during the first three months of the year have, at the end of the year, the following unearned fractions: January-1/24; February-3/24; March-5/24.

9. Additional premiums charged to policyholders for endorsements and changes in coverage under the contract shall be recorded on the effective date of the endorsement and accounted for in a manner consistent with the methods discussed in paragraphs 4-8. This is done so that, at any point in time, a liability is accrued for unearned premium related to the unexpired portion of the policy endorsement.

Earned but Unbilled Premium

10. Adjustments to the premium charged for changes in the level of exposure to insurance risk (e.g., audit premiums on workers' compensation policies) are generally determined based upon audits conducted after the policy has expired. Reporting entities shall estimate audit premiums, the amount generally referred to as earned but unbilled (EBUB) premium, and shall record the amounts as an adjustment to premium, either through written premium or as an adjustment to earned premium. The estimate for EBUB may be determined using actuarially or statistically supported aggregate calculations using historical company unearned premium data, or per policy calculations.

11. EBUB shall be adjusted upon completion of the audit and the adjustment shall be recognized as revenue immediately. Upon completion of an audit that results in a return of premiums to the policyholder, earned premiums shall be reduced.

12. Reporting entities shall establish all of the requisite liabilities associated with the asset such as commissions and premium taxes. These liabilities shall be determined based on when premium is earned, not collected[2].

13. Ten percent of EBUB in excess of collateral specifically held and identifiable on a per policy basis shall be reported as a nonadmitted asset. To the extent that amounts in excess of the 10% are not anticipated to be collected, they shall be written off against operations in the period the determination is made.

Earned but Uncollected Premium

14. Reporting entities may utilize a voluntary procedure whereby policies are not cancelled for non-payment of the premium until after an extended cancellation period (example 30 days), as opposed to the shorter statutory cancellation period. There are other instances when a reporting entity provides coverage for periods when the payment has not been received. Prior to the cancellation of the policy the reporting entity acknowledges it is "at risk" and subject to "actual exposure" for a valid claim despite the fact that the reporting entity may not have received payment of the premium for this exposure. Reporting entities shall record earned but uncollected premium as direct and assumed written premium since the reporting entity is "at risk" and subject to "actual exposure" for the extended period of time when the policy is still in force and effective, whether or not the reporting entity collects a premium for this time period. Earned but uncollected premium would be charged to expenses **"**net gain or (loss) from agents or premium balances charged off" when it is determined to be uncollectible.

Advance Premiums

15. Advance premiums result when the policies have been processed, and the premium has been paid prior to the effective date. These advance premiums are reported as a liability in the statutory financial

[2] If an entity feels comfortable enough in their ability to collect the premium that an asset is recorded, they should also book the associated liabilities. Once an estimate of the premium has been made and the entity feels certain that it will be collected, it should also book the liabilities that will be due when they receive the cash. If the premiums were unearned and the policyholder had the ability to cancel, the definition of a liability has not been met.

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statement and not considered income until due. Such amounts are not included in written premium or the unearned premium reserve.

Premium Deposits on Perpetual Fire Deposits

16. Premium deposits on perpetual fire insurance risks should be charged as a liability to the extent of at least 90% of the gross amount of such deposit.

Premium Deficiency Reserve

17. When the anticipated losses, loss adjustment expenses, commissions and other acquisition costs, and maintenance costs exceed the recorded unearned premium reserve, and any future installment premiums on existing policies, a premium deficiency reserve shall be recognized by recording an additional liability for the deficiency, with a corresponding charge to operations. Commission and other acquisition costs need not be considered in the premium deficiency analysis to the extent they have previously been expensed. For purposes of determining if a premium deficiency exists, insurance contracts shall be grouped in a manner consistent with how policies are marketed, serviced and measured. A liability shall be recognized for each grouping where a premium deficiency is indicated. Deficiencies shall not be offset by anticipated profits in other policy groupings.

18. If a premium deficiency reserve is established in accordance with paragraph 17, disclose the amount of that reserve. If a reporting entity utilizes anticipated investment income as a factor in the premium deficiency calculation, the reporting entity's disclosures shall include a statement that anticipated investment income was utilized; however, the dollar amount need not be included. Reporting entities need to disclose by statement only that anticipated investment income was utilized in the calculation of premium deficiency reserves whether a reserve is recorded or not (i.e., the use of anticipated investment income mitigated the need for recording a premium deficiency reserve).

Disclosures

19. Disclose the aggregate amount of direct premiums written through managing general agents or third party administrators. For purposes of this disclosure, a managing general agent means the same as in Appendix A-225. If this amount is equal to or greater than 5% of surplus, provide the following information for each managing general agent and third party administrator:

a. Name and address of managing general agent or third party administrator;

b. Federal Employer Identification Number;

c. Whether such person holds an exclusive contract;

d. Types of business written;

e. Type of authority granted (i.e., underwriting, claims payment, etc.); and

f. Total premium written.

20. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

21. This statement rejects *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises*.

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Effective Date and Transition

22. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in paragraph 5 was originally contained within *INT 01-23: Prepaid Legal Insurance Premium Recognition* and was effective June 11, 2001. The guidance reflected in paragraph 12, incorporated from *INT 02-11: Recognition of Amounts Related to Earned but Unbilled Premium*, was effective September 10, 2002. The guidance reflected in paragraph 14, incorporated from *INT 05-06: Earned but Uncollected Premium*, was effective December 3, 2005. The guidance in paragraph 18 incorporated from *INT 99-23: Disclosure of Premium Deficiency Reserves* was effective December 6, 1999.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 53—Property Casualty Contracts—Premiums*

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Statement of Statutory Accounting Principles No. 54 – Revised

Individual and Group Accident and Health Contracts

STATUS

Type of Issue	Common Area
Issued	Finalized March 13, 2000; Substantively revised December 10, 2016
Effective Date	January 1, 2001; Substantive revisions detailed in Issue Paper No. 154 effective January 1, 2017
Affects	Nullifies and incorporates INT 00-23 and INT 01-23
Affected by	No other pronouncements
Interpreted by	INT 05-05
Relevant Appendix A Guidance	A-010; A-225; A-641; A-820; A-822

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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EXHIBIT A – LONG-TERM CARE ILLUSTRATION ON INTERACTION BETWEEN SSAP NO. 54R AND A-010 AND AG 51 ..... **9**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for income recognition and policy reserves for all contracts classified as individual and group accident and health contracts as defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*, except for credit accident and health contracts which are discussed in *SSAP No. 59—Credit Life and Accident and Health Contracts*.

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SUMMARY CONCLUSION

Premium Income Recognition

2. Premiums shall be recognized as income on the gross basis (amount charged to the policyholder or subscriber exclusive of copayments or other charges related to the receipt of health care services) when due from policyholders or subscribers, but no earlier than the effective date of coverage, under the terms of the contract. Due and uncollected premiums shall follow the guidance in *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*, to determine the admissibility of premiums and related receivables. Premiums waived by the reporting entity under disability provisions contained in its policies and contracts, and reported in operations as a disability benefit, are included in premium income.

3. Premium income shall exclude premiums that have been received by the reporting entity on or prior to the valuation date but which are due after the valuation date (i.e., advance premiums as discussed below).

4. Premium income shall be reduced for premiums returned and allowances to industrial policyholders for the direct payment of premiums.

5. Premium income shall be increased by reinsurance premiums assumed and reduced by reinsurance premiums ceded. Reinsurance premiums assumed and ceded are defined and addressed in *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*.

6. Advance premiums are those premiums that have been received by the reporting entity prior to or on the valuation date but which are due after the valuation date. The total amount of such advance premiums is reported as a liability in the statutory financial statements and is not considered premium income until due. The gross premium, not the net valuation premium, is recorded as the advance premium in recognition of the reporting entity's liability to refund such premiums in the event the policy is terminated.

7. As discussed in *SSAP No. 47—Uninsured Plans*, amounts received on behalf of uninsured plans or the uninsured portion of partially insured plans shall not be reported as premium income. Administrative fees for servicing the uninsured plans shall be deducted from general expenses. Conversely, income relating to the insured portion of any plan shall be reported as premium income.

8. Specific funds to be received under the Medicare Part D program received as premiums for coverage that is not retrospectively rated should be accounted for under this statement. These funds include 'Beneficiary Premium (supplemental benefit portion)', as these payments are considered to be standard premium payments that do not meet the definitions under SSAP No. 47 or *SSAP No. 66—Retrospectively Rated Contracts*. Refer to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* for additional information and definitions of terms specifically related to Medicare Part D business.

Reserve Requirements

9. The aggregate reserve for individual and group accident and health contracts generally consists of a policy reserve and a claim reserve as well as certain other miscellaneous reserves discussed in paragraph 24. The aggregate reserve reflects the future liabilities arising under accident and health policies. Policy reserves have traditionally been referred to as active life reserves and include unearned premium reserves. Policy reserves reflect that premiums cover future liabilities in addition to current claim costs and expenses. Claim reserves, sometimes referred to as disabled life reserves, are required on claims which involve continuing loss. The reserve in this case is a measure of the present value of future benefits or amounts not yet due as of the statement date (the unaccrued portion) which are expected to arise under claims which have been incurred as of the statement date. The aggregate reserve for individual

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and group accident and health contracts does not include claim liabilities which are the amounts payable at the reporting date (the accrued portion) and reflect the reporting entity's liability for benefits due as of the statement date. Claim liabilities are further discussed in *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*.

10. Policy reserves for individual and group accident and health contracts shall include an unearned premium reserve and, as applicable, an additional or contract reserve where constant or level premiums are assumed for certain noncancelable or guaranteed renewable contracts. The claim reserve shall consist of a reserve for the present value of amounts not yet due.

11. Statutory policy reserves shall be established for all unmatured contractual obligations of the reporting entity arising out of the provisions of the contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. A prospective gross premium valuation is the ultimate test of reserve adequacy as of a given valuation date. Statutory reserves meet the definition of liabilities as defined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. The actuarial methodologies referred to in paragraph 12 meet the criteria required for reasonable estimates in SSAP No. 5R.

12. The reserving methodologies and assumptions used in calculating individual and group accident and health reserves shall meet the provisions of Appendices A-010, A-641, A-820, A-822 (as applicable), the *Valuation Manual* and the actuarial guidelines found in Appendix C of this Manual (as applicable). Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

Policy Reserves

13. Unearned premium reserves shall be required for all accident and health contracts for which premiums have been reported for a period beyond the date of valuation other than premiums paid in advance. The minimum unearned premium reserve that applies to the premium period beyond the valuation date shall be based on the valuation net modal premium if contract reserves are required and the gross modal unearned premium reserve if contract reserves are not required. If premiums due and unpaid are carried as an asset, such premiums must be treated as premiums in force, subject to unearned premium reserve determination. The value of unpaid commissions, premium taxes, and the cost of collection associated with due and unpaid premiums must be carried as an offsetting liability. In no event shall the aggregate policy reserve for all contracts be less than the unearned gross premium under such contracts. Additionally, the reserve shall never be less than the expected claims for the period beyond the valuation date represented by the unearned premium reserve, to the extent not provided for elsewhere.

14. Contract or additional reserves on accident and health contracts shall be recorded when premiums and benefits are not earned or incurred at the same incidence over the policy period (e.g., contracts having premiums determined on an issue-age basis where premiums and related morbidity, risk of loss, and the cost of coverage are not evenly matched). This evaluation may be applied on a rating block basis if the total premiums for the block were developed to support the total risk assumed and expected expenses for the block each year, and a qualified actuary certifies the premium development (e.g., community-rated contracts). The additional reserves shall be set aside from the early years' level premiums to pay the claims that experience indicates will be incurred as the policy continues in force. The fact that the reporting entity may have the right to increase premiums or to decline renewal of the policies for certain reasons has no bearing on whether or not a contract or additional reserve should be held. These reserves shall apply regardless of whether or not benefits are currently being received and are in addition to unearned premium reserves discussed in paragraph 13.

15. Contract or additional reserves shall also be recorded where, due to the gross premium structure, the future benefits exceed the future net premiums (e.g., group conversion policies) or where the contract

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provides for the extension of benefits after the termination of the coverage (e.g., deferred maternity and other similar benefits).

16. A terminal reserve for accident and health contracts is the policy reserve at the end of a policy year to cover the assumed difference between future benefits and future net premiums. The components used to compute a terminal reserve shall consist of an interest rate, a mortality and/or morbidity table, and a valuation method (e.g., net level, one-year full preliminary term, and two-year full preliminary term) and where allowed, other assumptions. A terminal reserve is based on the assumption that all net premiums have been received, all interest earned, and all benefits paid to the end of the policy year.

17. Since terminal reserves are computed as of the end of a policy year and not the reporting date, the terminal reserve as of policy anniversaries immediately prior to and subsequent to the reporting date are adjusted to reflect that portion of the net premium that is unearned at the reporting date. This is generally accomplished using either the mean reserve method or the mid-terminal method as discussed in paragraphs 25-28 of *SSAP No. 51R—Life Contracts*. Other appropriate methods, including an exact reserve valuation, may also be used.

18. For individual and group accident and health contracts, negative reserves on any benefit shall be offset against positive reserves for other benefits in the same policy but the mean reserve on any policy shall never be taken as less than one-half the valuation net premium. The majority of group accident and health policies are written in conjunction with group life or other policies. If these policies are an experience rated package, positive or favorable margins on one of the contracts can offset the need to establish additional reserves on the other contracts.

Additional Reserves (Premium Deficiency Reserves)

19. When the expected claims payments or incurred costs, claim adjustment expenses and administration costs exceed the premiums to be collected for the remainder of a contract period plus any contract reserve, a premium deficiency reserve shall be recognized by recording an additional liability for the deficiency, with a corresponding charge to operations. For purposes of determining if a premium deficiency exists, contracts shall be grouped in a manner consistent with how policies are marketed, serviced and measured. A liability shall be recognized for each grouping where a premium deficiency is indicated. Deficiencies shall not be offset by anticipated profits in other policy groupings. Such accruals shall be made for any loss contracts, even if the contract period has not yet started.

Claim Reserves

20. Claim reserves shall be accrued for estimated costs of future health care services to be rendered that the reporting entity is currently obligated to provide or reimburse as a result of premiums earned to date and that would be payable after the reporting date under the terms of arrangements, regulatory requirements or other requirements if the insured's or subscriber's illness or disability were to continue. It shall include a reserve for disability benefits covered under premium waiver provisions. For individual and group disability claims with a duration of less than two years, reserves may be based on the reporting entity's experience, if credible, or other methods, as appropriate. Generally, reserves for disability income claims with durations of greater than two years shall be determined based on a tabular method using the age of the insured at the date of disablement, the number of months the insured already has been disabled, and the number of months remaining in the benefit period.

Reserve Recognition

21. The difference between the aggregate reserve for accident and health contracts at the beginning and end of the reporting period shall be reflected as the change in reserves in the summary of operations, except for any difference due to a change in valuation basis.

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Change in Valuation Basis

22. A change in valuation basis shall be defined as a change in the interest rate, mortality and morbidity assumptions, or reserving method (e.g., net level, preliminary term, etc.) or other factors affecting the reserve computation of policies in force and meets the definition of an accounting change as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors*. Changing morbidity assumptions regarding the length of claim continuance based on regularly updated credible experience as required for products subject to *Actuarial Guideline XLVII—The Application of Company Experience in the Calculation of Claim Reserves Under the 2012 Group Long-Term Disability Valuation Table* (AG 47) and *Actuarial Guideline L—2013 Individual Disability Income Valuation Table* (AG 50) are not considered a change in valuation basis. Other uses of regularly updated credible experience required to be used for morbidity assumptions by Appendix A-010 regarding continuing claim payments are generally not considered a change in valuation basis. Voluntary decisions to choose one allowable reserving methodology over another, which require commissioner approval under the *Valuation Manual,* shall be reported as a change in valuation basis. Consistent with SSAP No. 3, any increase (strengthening) or decrease (destrengthening) in actuarial reserves resulting from such a change in valuation basis shall be recorded directly to surplus (under changes to surplus in the change in valuation basis annual statement line for life, accident and health, and health reporting entities) rather than as a part of the reserve change recognized in the summary of operations. The impact on surplus is based on the difference between the reserve under the old and new methods as of the beginning of the year. Some changes will meet the definition of a change in accounting as defined in SSAP No. 3 and a change in valuation basis as described in this paragraph, but the adjustment to surplus will be zero. This can happen when the change in valuation basis is prospective and only applies to new policies and reserves meaning that policies inforce for the prior year-end are not affected, or situations in which the change in reserving methodology did not change the reserves reported in the financial statements. The changes remain subject to the disclosures prescribed in SSAP No. 3. This difference shall not be graded in over time unless this statement prescribes a new method and a specific transition that allows for grading.

Supplemental Benefits

23. In addition to the basic policy benefit, the contract may provide supplemental benefits. Supplemental benefits include, but are not limited to, accidental death benefits, dental and waiver of premium benefits. If the terms of the contract provide for these benefits, appropriate reserves shall be established in accordance with the applicable standards within the *Accounting Practices and Procedures Manual* and the *Valuation Manual*.

Reserve Adequacy

24. As discussed in Appendix A-010, a prospective gross premium valuation is the ultimate test of the adequacy of a reporting entity's accident and health reserves as of a given valuation date and shall be determined on the basis of unearned premium reserves, contract reserves, additional reserves, claim reserves (including claim liabilities), and miscellaneous reserves combined; however, each component shall be computed separately. Pursuant to Appendix A-010, paragraph 26, an entity's accident and health reserves in total must be adequate under a gross premium valuation. The requirements of *Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves (AG 51)* provide a test which indicates whether reserves in addition to the requirements of A-010 are indicated. AG 51 does not change the base requirements of A-010. (See Long-Term Care Illustration in Exhibit A).

Additional Reserves Not Included Elsewhere

25. Reserves for experience-rating refunds or the dividend liability in group policies are discussed in SSAP No. 66.

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26. Additional actuarial or other liabilities are commonly held for such items as:

a. Surrender values in excess of reserves otherwise required or carried;

b. Additional reserves required based on asset adequacy analysis as discussed in Appendix A-822; and

c. Additional reserves for policies which contain conversion privileges or future contingent benefits.

Contracts Subject to Redetermination

27. This statement also applies to other contracts which are subject to redetermination such as Federal (and State) Groups – subject to rate adjustments through audits by the Office of Personnel Management (OPM). Reporting entities are required to give Federal Groups the lowest rates that are being charged to similar groups.

28. Amounts due from insureds or subscribers and amounts due to insureds or subscribers under contracts subject to redetermination meet the definitions of assets and liabilities as set forth in *SSAP No. 4—Assets and Nonadmitted Assets* and SSAP No. 5R, respectively.

29. Contract redeterminations shall be estimated based on the experience to date. The method used to estimate the liability shall be reasonable based on the reporting entity's procedures, and consistent among reporting periods. An examination of contract requirements in relation to the rates being charged and the current status of applicable audits (e.g., OPM, Centers for Medicare and Medicaid Services (or such other name that this entity shall be known as) and other Federal, state or government department) is a common method used to estimate such contract redeterminations.

30. Premium adjustments for contracts subject to redetermination are estimated for the portion of the policy period that has expired and shall be considered an immediate adjustment to premium. Accrued premium adjustments shall be recorded in premium and considerations receivable with a corresponding entry to written premiums. Accrued return premium adjustments shall be recorded as a liability with a corresponding entry to written premiums, the annual statement liability lines will vary by the type of annual statement the reporting entity files. Managed care/accident and health reporting entities report as aggregate health policy reserves; life and accident and health reporting entities report as aggregate reserves for accident and health contracts; property and casualty reporting entities report as aggregate write-ins for liabilities.

31. If, in accordance with SSAP No. 5R, it is probable that the additional premium adjustment is uncollectible, any uncollectible premium shall be written off against operations in the period the determination is made and the disclosure requirements outlined in SSAP No. 5R shall be made.

32. Premium adjustments for contracts subject to redetermination shall be determined and billed or refunded in accordance with the policy provisions or contract provisions. If such premiums are not billed in accordance with the policy provisions or contract provisions, or the policy provisions or contract provisions do not address the due date of such premiums, the accrual shall be nonadmitted. This is consistent with the guidance for audit premiums established in SSAP No. 6.

Disclosures

33. Disclose the aggregate amount of direct premiums written through managing general agents or third party administrators. For purposes of this disclosure, a managing general agent means the same as in Appendix A-225. If this amount is equal to or greater than 5% of surplus, provide the following information for each managing general agent and third party administrator:

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a. Name and address of managing general agent or third party administrator;

b. Federal Employer Identification Number;

c. Whether such person holds an exclusive contract;

d. Types of business written;

e. Type of authority granted (i.e., underwriting, claims payment, etc.); and

f. Total premium written.

34. Reporting entities shall disclose the relative percentage of participating insurance, the method of accounting for policyholder dividends, the amount of dividends, and the amount of any additional income allocated to participating policyholders in the financial statements.

35. If a premium deficiency reserve is established in accordance with paragraph 19, disclose the amount of that reserve. If a reporting entity utilizes anticipated investment income as a factor in the premium deficiency calculation, disclosure of such shall be made in the financial statements.

36. The financial statements shall disclose the method used by the reporting entity to estimate premium adjustments for contracts subject to redetermination. The amount of net premiums that are subject to such adjustments, as well as the corresponding percentage to total net premiums, shall be disclosed.

37. Management's policy for providing charity care,[1] as well as the level of charity care provided, shall be disclosed in the financial statements. Such disclosure shall be measured based on the provider's direct and indirect costs of providing charity care services. If costs cannot be specifically attributed to services provided to charity care patients (for example, based on a cost accounting system), management may estimate the costs of those services using reasonable techniques with the method used to identify or estimate such costs disclosed. Funds received to offset or subsidize charity services provided (for example, from gifts or grants restricted for charity care or from an uncompensated care fund), also shall be disclosed.

38. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

39. This statement adopts the definition of charity care and adopts with modification the disclosure within *ASU 2010-23, Health Care Entities, Measuring Charity Care*, as applicable.

40. This statement incorporates the requirements of Appendices A-010, A-225, A-641, A-820, A-822 (as applicable), the *Valuation Manual,* the Actuarial Standards Board *Actuarial Standards of Practice* and the actuarial guidelines found in Appendix C of this manual (as applicable).

41. This statement rejects *ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts*, *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises* relating to accounting and reporting for individual and group accident and health contracts.

[1] Charity care represents health care services that are provided but are never expected to result in cash flows. Charity care is provided to a patient with demonstrated inability to pay. Each entity establishes its own criteria for charity care consistent with its mission statement and financial ability.

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Effective Date and Transition

42. This statement is effective for years beginning January 1, 2001. Contracts issued prior to January 1, 2001 shall be accounted for based on the laws and regulations of the domiciliary state. State laws and regulations shall be understood to include anything considered authoritative by the domiciliary state under the individual state's statutory authority and due process procedures. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The disclosure related to charity care shall be applied prospectively beginning June 17, 2015. Application of references to the *Valuation Manual* is effective January 1, 2017.

REFERENCES

Other

- *NAIC Financial Condition Examiners Handbook*
- *Actuarial Standards Board Actuarial Standards of Practice*

Relevant Issue Papers

- *Issue Paper No. 54—Individual and Group Accident and Health Contracts*
- *Issue Paper No. 154—Implementation of Principle-Based Reserving*

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EXHIBIT A – LONG-TERM CARE ILLUSTRATION ON INTERACTION BETWEEN SSAP NO. 54R, AND A-010 AND AG 51

This illustration is to address the interaction in long-term care reserving requirements noted in this statement, *Appendix A-010, Minimum Reserve Standards for Individual and Group Accident and Health Insurance Contracts*, and *Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves* (AG 51). At a high level, A-010 is from Model #10 of the same name which provides the minimum requirements. AG 51 is an actuarial guideline which provides a test for whether additional reserves are indicated. AG 51 does not change the base requirements of A-010.

Consider the following illustrative, simplified example:

1. Company XYZ has three lines of business: long-term care insurance, Medicare Supplement (Med Sup) insurance, and whole life insurance.

2. Cash flow testing performed for the long-term care block in isolation, in accordance with Actuarial Guideline LI (AG 51), shows deficiencies in all tested scenarios.

3. Cash flow testing performed for the entity as a whole, including both the Life and A&H business combined, shows significant sufficiency at the entity level in all tested scenarios.

4. A gross premium valuation performed on the long-term care reserves, in isolation, indicates that those reserves are deficient by $250 million.

5. A gross premium valuation performed on the Medicare Supplement reserves, in isolation, indicates that those reserves contain $150 million of sufficiency.

Given these facts, does Company XYZ need to strengthen its accident and health reserves in order to comply with the requirements of the NAIC *Accounting Practices and Procedures Manual*?

Response: Yes. Company XYZ needs to strengthen its accident and health reserves by $100 million. This number is determined by the following:

	Millions
Long-term care GPV reserves are deficient by	($250)
Medicare Supplement GPV reserves sufficiency of	$150
Accident and Health GPV reserve net deficiency of	$100

Appendix A-010, paragraph 26, and SSAP No. 54R, paragraph 24, both require gross premium valuation.

AG 51 is a test for additional reserves. That is, passing AG 51 does not relieve the reporting entity of the requirement of SSAP No. 54R and A-010 to have adequate accident and health reserves indicated by gross premium valuation.

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Statement of Statutory Accounting Principles No. 55

Unpaid Claims, Losses and Loss Adjustment Expenses

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 85 with guidance incorporated August 2011; Nullifies and incorporates INT 00-31, INT 01-28, INT 02-21, INT 03-17 and INT 06-14
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SUMMARY CONCLUSION **2**

Property/Casualty 2
Life, Accident and Health 4
Managed Care 4
Managed Care and Accident and Health 5
General 7
Disclosures 8
Relevant Literature 9
Effective Date and Transition 9

REFERENCES **10**

Relevant Issue Papers 10

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for recording liabilities for unpaid claims and claim adjustment expenses for life insurance contracts and accident and health contracts and unpaid losses and loss adjustment expenses for property and casualty insurance contracts. This guidance applies equally to those entities with direct and reinsurance-assumed obligations. This statement applies to all insurance contracts as defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*.

2. This statement does not address policy reserves for life and accident and health policies. These reserves are addressed in *SSAP No. 51R—Life Contracts*, *SSAP No. 52—Deposit-Type Contracts*, *SSAP No. 54R—Individual and Group Accident and Health Contracts*, and *SSAP No. 59—Credit Life and Accident and Health Insurance Contracts.*

3. This statement does not address liabilities for punitive damages. These liabilities shall be recorded in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*.

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SUMMARY CONCLUSION

4. Claims, losses, and loss/claim adjustment expenses shall be recognized as expenses when a covered or insured event occurs. In most instances, the covered or insured event is the occurrence of an incident which gives rise to a claim or the incurring of costs. For claims-made type policies, the covered or insured event is the reporting to the entity of the incident that gives rise to a claim. Until claim payments and related expense payments are made subsequent to the occurrence of a covered or insured event, and in order to recognize the expense of a covered or insured event that has occurred, it is necessary to establish a liability. Liabilities shall be established for any unpaid claims and unpaid losses (loss reserves), unpaid loss/claim adjustment expenses (loss/claim adjustment expense reserves) and incurred costs, with a corresponding charge to income. Claims related extra contractual obligations losses and bad-faith losses shall be included in losses. See individual business types for the accounting treatment for adjustment expenses related to extra contractual obligations and bad-faith lawsuits.

5. The liability for unpaid LAE shall be established regardless of any payments made to third-party administrators, management companies or other entities except for capitated payments under managed care contracts for which the liability is established net of capitated payments to providers.

Property/Casualty

6. The following are types of future costs relating to property and casualty contracts, as defined in SSAP No. 50, which shall be considered in determining the liabilities for unpaid losses and loss adjustment expenses:

a. Reported Losses: Expected payments for losses relating to insured events that have occurred and have been reported to, but not paid by, the reporting entity as of the statement date;

b. Incurred But Not Reported Losses (IBNR): Expected payments for losses relating to insured events that have occurred but have not been reported to the reporting entity as of the statement date. As a practical matter, IBNR may include losses that have been reported to the reporting entity but have not yet been entered to the claims system or bulk provisions. Bulk provisions are reserves included with other IBNR reserves to reflect deficiencies in known case reserves;

c. Loss Adjustment Expenses: Expected payments for costs to be incurred in connection with the adjustment and recording of losses defined in paragraphs 6.a. and 6.b. Examples of expenses incurred in these activities are estimating the amounts of losses, disbursing loss payments, maintaining records, general clerical, secretarial, office maintenance, occupancy costs, utilities, computer maintenance, supervisory and executive duties, supplies, and postage. Loss adjustment expenses can be classified into two broad categories: Defense and Cost Containment (DCC) and Adjusting and Other (AO):

i. DCC include defense[1], litigation, and medical cost containment expenses, whether internal or external. DCC include, but are not limited to, the following items:

(a) Surveillance expenses;

[1] Legal defense costs incurred under the definition of covered damages or losses as the only insured peril would be accounted for as losses, while legal defense costs incurred under a duty to defend would be accounted for as Defense and Cost Containment (DCC). For policies where legal costs are the only insured peril, the insurer would record the legal costs that reimburse the policyholder as loss and, to the extent the insurer participated in the defense, would record its legal costs as DCC. This is not intended to change the classifications of legal expenses for existing long tailed lines of liability coverage, such as medical malpractice and workers' compensation insurance.

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(b) Fixed amounts for medical cost containment expenses;

(c) Litigation management expenses;

(d) Loss adjustment expenses for participation in voluntary and involuntary market pools if reported by accident year;

(e) Fees or salaries for appraisers, private investigators, hearing representatives, reinspectors and fraud investigators, if working in defense of a claim, and fees or salaries for rehabilitation nurses, if such cost is not included in losses;

(f) Attorney fees incurred owing to a duty to defend, even when other coverage does not exist; and

(g) The cost of engaging experts;

ii. AO are those expenses other than DCC as defined in (i) above assigned to the expense group "Loss Adjustment Expense". AO include, but are not limited to, the following items:

(a) Fees and expenses of adjusters and settling agents;

(b) Loss adjustment expenses for participation in voluntary and involuntary market pools if reported by calendar year;

(c) Attorney fees incurred in the determination of coverage, including litigation between the reporting entity and the policyholder;

(d) Fees and salaries for appraisers, private investigators, hearing representatives, reinspectors and fraud investigators, if working in the capacity of an adjuster; and

(e) Adjustment expenses arising from claims related lawsuits such as extra contractual obligations and bad faith lawsuits.

d. The contractual terms for arrangements (i.e., variable, fixed or bundled amounts) to third-party administrators, management companies, or other entities for unpaid claims, losses and losses/claims adjustment expenses, shall be evaluated to determine if the arrangement meets the criteria to be reported as a prepaid asset and nonadmitted in accordance with *SSAP No. 29—Prepaid Expenses*. These payments shall not be offset against any amounts required to be reported in accordance with paragraph 4 or paragraph 5 within this guidance. Only when loss/claim and related adjusting expense payments, which are made by the third-party administrators, management companies or other entities, to the policyholder or claimant, shall the insurer's liability (loss/claim or loss/claim adjustment expense reserves) be reduced.

e. Prepayments to third-party administrators, management companies or other entities that do not relate to services or adjusting for the underlying direct policy benefits are reported as aggregate write-ins for miscellaneous underwriting benefits in the Underwriting and Investment Exhibit Part 3.

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Life, Accident and Health

7. The following future costs relating to life and accident and health indemnity contracts, as defined in SSAP No. 50, shall be considered in determining the liability for unpaid claims and claim adjustment expenses:

a. Accident and Health Claim Reserves: Reserves for claims that involve a continuing loss. This reserve is a measure of the future benefits or amounts not yet due as of the statement date which are expected to arise under claims which have been incurred as of the statement date. This shall include the amount of claim payments that are not yet due such as those amounts commonly referred to as disabled life reserves for accident and health claims. The methodology used to establish claim reserves is discussed in SSAP No. 54R.

b. Claim Liabilities for Life/Accident and Health Contracts:

i. Due and Unpaid Claims: Claims for which payments are due as of the statement date;

ii. Resisted Claims in Course of Settlement: Liability for claims that are in dispute and are unresolved on the statement date. The liability either may be the full amount of the submitted claim or a percentage of the claim based on the reporting entity's past experience with similar resisted claims;

iii. Other Claims in the Course of Settlement: Liability for claims that have been reported but the reporting entity has not received all of the required information or processing has not otherwise been completed as of the statement date;

iv. Incurred But Not Reported Claims: Liability for which a covered event has occurred (such as death, accident, or illness) but has not been reported to the reporting entity as of the statement date.

c. Claim Adjustment Expenses for Accident and Health Reporting Entities are those costs expected to be incurred in connection with the adjustment and recording of accident and health claims defined in paragraphs 7.a. and 7.b. Certain claim adjustment expenses reduce the number or cost of health services thereby resulting in lower premiums or lower premium increases. These claim adjustment expenses shall be classified as cost containment expenses.

d. Claim Adjustment Expenses for Life Reporting Entities: Costs expected to be incurred (including legal and investigation) in connection with the adjustment and recording of life claims defined in paragraph 7.b. This would include adjustment expenses arising from claims-related lawsuits such as extra contractual obligations and bad-faith lawsuits.

e. In cases where insurers advance funds to third-party administrators, management companies or other entities prior to the occurrence of the claim who then, on behalf of the insurer, adjudicate the claim and make payments to insureds or other claimants, the guidance in paragraph 9 applies.

Managed Care

8. The following costs relating to managed care contracts as defined in SSAP No. 50 shall be considered in determining the claims unpaid and claims adjustment expenses:

a. Claims unpaid for Managed Care Reporting Entities:

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i. Unpaid amounts for costs incurred in providing care to a subscriber, member or policyholder including inpatient claims, physician claims, referral claims, other medical claims, resisted claims in the course of settlement and other claims in the course of settlement;

ii. Incurred But Not Reported Claims: Liability for which a covered event has occurred (such as an accident, illness or other service) but has not been reported to the reporting entity as of the statement date;

iii. Additional unpaid medical costs resulting from failed contractors under capitation contracts and provision for losses incurred by contractors deemed to be related parties for which it is probable that the reporting entity will be required to provide funding;

b. Claim Adjustment Expenses for Managed Care Reporting Entities are those costs expected to be incurred in connection with the adjustment and recording of managed care claims defined in paragraph 8.a. Certain claim adjustment expenses reduce the number or cost of health services thereby resulting in lower premiums or lower premium increases. These claim adjustment expenses shall be classified as cost containment expenses.

c. Liabilities for percentage withholds ("withholds") from payments made to contracted providers;

d. Liabilities for accrued medical incentives under contractual arrangements with providers and other risk-sharing arrangements whereby the health entity agrees to share savings with contracted providers.

e. In cases where insurers advance funds to third-party administrators, management companies or other entities prior to the occurrence of the claim who then, on behalf of the insurer, adjudicate the claim and make payments to insureds or other claimants, the guidance in paragraph 9 applies.

Managed Care and Accident and Health

9. In some instances, insurers advance funds to third-party administrators, management companies or other entities prior to the occurrence of the claim who then, on behalf of the insurer, adjudicate the claim and make payments to insureds or other claimants. In such cases the following guidance applies:

a. For capitated payments under managed care contracts, the liability for claims and claim adjusting expenses shall be established in an amount necessary to adjudicate and pay all unpaid claims irrespective of payments to third-party administrators, management companies or other entities, and is reported net of capitated payments to providers.

b. For non-capitated advance payments, the liability for unpaid losses/claims and related adjustment expenses shall be established regardless of any payments made to third-party administrators, management companies or other entities, and such payments shall be reported by the insurer as prepayments. All prepayments (i.e., variable, fixed or bundled amounts) to third-party administrators, management companies, or other entities for unpaid claims, losses and losses/claims adjustment expenses, shall be initially reported as a prepaid asset and nonadmitted in accordance with SSAP No. 29. These payments shall not be offset against any amounts required to be reported in accordance with paragraph 4 or paragraph 5 within this guidance. Only when loss/claim and related adjusting expense payments which are made by the third-party administrators, management companies or

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other entities, to the policyholder or claimant, shall the insurer's liability (loss/claim or loss/claim adjustment expense reserves) be reduced.

c. Prepayments to third-party administrators, management companies or other entities that do not relate to services or adjusting for the underlying direct policy benefits are reported as (1) aggregate write-ins for expenses - Life/Health (Exhibit 2 – General Expenses) or (2) aggregate write-ins for expenses (General Administrative Expenses) - Health (Underwriting and Investment Exhibit Part 3).

Note that the guidance in paragraph 9 does not alter existing guidance regarding the admissibility of loans and advances to providers which apply to health insurance and managed care contracts which is addressed in *SSAP No. 84—Health Care and Government Insured Plan Receivables.*

10. Claim adjustment expenses for accident and health contracts and managed care contracts (identified in paragraphs 7.c. and 8.b.), including legal expenses, can be subdivided into cost containment expenses and other claim adjustment expenses:

a. Cost containment expenses: Expenses that actually serve to reduce the number of health services provided or the cost of such services. The following are examples of items that shall be considered "cost containment expenses" only if they result in reduced levels of costs or services:

i. Case management activities;

ii. Utilization review;

iii. Detection and prevention of payment for fraudulent requests for reimbursement;

iv. Network access fees to Preferred Provider Organizations and other network-based health plans (including prescription drug networks), and allocated internal salaries and related costs associated with network development and/or provider contracting;

v. Consumer education solely relating to health improvement and relying on the direct involvement of health personnel (this would include smoking cessation and disease management programs, and other programs that involve hands on medical education); and

vi. Expenses for internal and external appeals processes.

b. Other claim adjustment expenses: Claim adjustment expenses as defined in paragraph 7.c. or 8.b. that are not cost containment expenses. Examples of other claim adjustment expenses are:

i. Estimating the amounts of losses and disbursing loss payments;

ii. Maintaining records, general clerical, and secretarial;

iii. Office maintenance, occupancy costs, utilities, and computer maintenance;

iv. Supervisory and executive duties;

v. Supplies and postage;

vi. This would include adjustment expenses arising from claims-related lawsuits such as extra contractual obligations and bad-faith lawsuits; and

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vii. Interest paid in accordance with prompt payment laws or regulations to claimants. (Interest paid to regulatory authorities is reported as regulatory fines and fees.)

General

11. The liability for claim reserves and claim liabilities, unpaid losses, and loss/claim adjustment expenses shall be based upon the estimated ultimate cost of settling the claims (including the effects of inflation and other societal and economic factors), using past experience adjusted for current trends, and any other factors that would modify past experience. These liabilities shall not be discounted unless authorized for specific types of claims by specific SSAPs, including SSAP No. 54R and *SSAP No. 65—Property and Casualty Contracts*.

12. Various analytical techniques can be used to estimate the liability for IBNR claims, future development on reported losses/claims, and loss/claim adjustment expenses. These techniques generally consist of statistical analysis of historical experience and are commonly referred to as loss reserve projections. The estimation process is generally performed by line of business, grouping contracts with like characteristics and policy provisions. The decision to use a particular projection method and the results obtained from that method shall be evaluated by considering the inherent assumptions underlying the method and the appropriateness of those assumptions to the circumstances. No single projection method is inherently better than any other in all circumstances. The results of more than one method should be considered.

13. For each line of business and for all lines of business in the aggregate, management shall record its best estimate of its liabilities for unpaid claims, unpaid losses, and loss/claim adjustment expenses. Because the ultimate settlement of claims (including IBNR for death claims and accident and health claims) is subject to future events, no single claim or loss and loss/claim adjustment expense reserve can be considered accurate with certainty. Management's analysis of the reasonableness of claim or loss and loss/claim adjustment expense reserve estimates shall include an analysis of the amount of variability in the estimate. If, for a particular line of business, management develops its estimate considering a range of claim or loss and loss/claim adjustment expense reserve estimates bounded by a high and a low estimate, management's best estimate of the liability within that range shall be recorded. The high and low ends of the range shall not correspond to an absolute best-and-worst case scenario of ultimate settlements because such estimates may be the result of unlikely assumptions. Management's range shall be realistic and, therefore, shall not include the set of all possible outcomes but only those outcomes that are considered reasonable. Management shall also follow the concept of conservatism included in the Preamble when determining estimates for claim and loss and loss/claim adjustment expense reserves. However, there is not a specific requirement to include a provision for adverse deviation in claims.

14. In the rare instances when, for a particular line of business, after considering the relative probability of the points within management's estimated range, it is determined that no point within management's estimate of the range is a better estimate than any other point, the midpoint within management's estimate of the range shall be accrued. It is anticipated that using the midpoint in a range will be applicable only when there is a continuous range of possible values, and no amount within that range is any more probable than any other. For purposes of this statement, it is assumed that management can quantify the high end of the range. If management determines that the high end of the range cannot be quantified, then a range does not exist, and management's best estimate shall be accrued. This guidance is not applicable when there are several point estimates which have been determined as equally possible values, but those point estimates do not constitute a range. If there are several point estimates with equal probabilities, management should determine its best estimate of the liability.

15. If a reporting entity chooses to anticipate salvage and subrogation recoverables (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), the recoverables shall be estimated in a manner consistent with

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paragraphs 11-13 of this statement. Estimated salvage and subrogation recoveries (net of associated recovery expenses) shall be deducted from the liability for unpaid claims, unpaid losses, and unpaid loss/claim adjustment expenses, depending on whether the subrogation represents a recovery of claims/losses or loss/claims adjustment expenses. If a reporting entity chooses to anticipate coordination of benefits (COB) recoverables of Individual and Group Accident and Health Contracts, the recoverables shall be estimated in a manner consistent with paragraphs 11-13 of this statement and shall be deducted from the liability for unpaid claims or losses. A separate receivable shall not be established for these recoverables. In addition, all of these recoverables are also subject to the impairment guidelines established in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* and an entity shall not reduce its reserves for any recoverables deemed to be impaired. Salvage and subrogation recoveries received (net of associated recovery expenses) are reported as a reduction to paid losses/claims and/or paid loss/claim adjustment expenses. Coordination of benefits (COB) recoveries received of Individual and Group Accident and Health Contracts (net of associated recovery expenses) are reported as a reduction to paid claims.

16. Changes in estimates of the liabilities for unpaid claims or losses and loss/claim adjustment expenses resulting from the continuous review process, including the consideration of differences between estimated and actual payments, shall be considered a change in estimate and shall be recorded in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. SSAP No. 3 requires changes in estimates to be included in the statement of operations in the period the change becomes known. This guidance also applies to the period subsequent to the March 1 filing deadline for annual financial statements through the filing deadline of June 1 for audited annual financial statements.

Disclosures

17. The financial statements shall include the following disclosures for each year full financial statements are presented. The disclosure requirement in paragraph 17.d. is also applicable to the interim financial statements if there is a material change from the amounts reported in the annual filing. Life and annuity contracts are not subject to this disclosure requirement.

a. The balance in the liabilities for unpaid claims and unpaid losses and loss/claim adjustment expense reserves at the beginning and end of each year presented;

b. Incurred claims, losses, and loss/claim adjustment expenses with separate disclosures of the provision for insured or covered events of the current year and increases or decreases in the provision for insured or covered events of prior years;

c. Payments of claims, losses, and loss/claim adjustment expenses with separate disclosures of payments of losses and loss/claim adjustment expenses attributable to insured or covered events of the current year and insured or covered events of prior years;

d. The reasons for the change in the provision for incurred claims, losses, and loss/claim adjustment expenses attributable to insured or covered events of prior years. The disclosure should indicate whether additional premiums or return premiums have been accrued as a result of the prior-year effects. (For Title reporting entities, “provision” refers to the known claims reserve included in Line 1 of the Liabilities page, and “prior years” refers to prior report years);

e. Information about significant changes in methodologies and assumptions used in calculating the liability for unpaid claims and claim adjustment expenses, including reasons for the change and the effects on the financial statements for the most recent reporting period presented;

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f. A summary of management's policies and methodologies for estimating the liabilities for losses and loss/claim adjustment expenses, including discussion of claims for toxic waste cleanup, asbestos-related illnesses, or other environmental remediation exposures;

g. Disclosure of the amount paid and reserved for losses and loss/claim adjustment expenses for asbestos and/or environmental claims, on a direct, assumed and net of reinsurance basis (the reserves required to be disclosed in this section shall exclude amounts relating to policies specifically written to cover asbestos and environmental exposures). Each company should report only its share of a group amount (after applying its respective pooling percentage) if the company is a member of an intercompany pooling agreement; and

h. Estimates of anticipated salvage and subrogation (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), deducted from the liability for unpaid claims, losses or their associated adjusting expenses.

18. All reporting entity types are required to disclose the dollar amount of any claims/losses related to extra contractual obligation lawsuits or bad faith lawsuits paid during the reporting period on a direct basis. The number of such claims paid shall be disclosed in a note.

19. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

20. Although FASB *Statement No. 60, Accounting and Reporting by Insurance Enterprises* (FAS 60), is rejected in SSAP No. 50, this statement is consistent with the guidance provided for the recognition of claim costs in FAS 60 with the exception of the statutory requirement to accrue the midpoint of a range of loss or loss adjustment expense reserve estimates when no point within management's continuous range of reasonably possible estimates is determined to be a better estimate than any other point.

21. This statement also rejects *ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts*, *AICPA Statement of Position 92-4, Auditing Insurance Entities' Loss Reserves* and *ASU 2015-09, Disclosures about Short-Duration Contracts.* Although the disclosures in ASU 2015-09 are similar to existing statutory accounting disclosures on claims development, the U.S. GAAP disclosures would reflect consolidated information, with potential for different aggregations than what is used for a legal entity basis under statutory accounting. As such, ASU 2015-09 is rejected for statutory accounting, and reporting entities shall follow the established statutory accounting disclosures.

22. Guidance in paragraphs 7.c., 8.b. and 10 was incorporated from SSAP No. 85. SSAP No. 85 was issued in 2002 to amend SSAP No. 55 and provide clarification regarding what costs should be classified as claim adjustment expenses on accident and health contracts. In August 2011, SSAP No. 85 was nullified and the guidance was incorporated into this SSAP. *Issue Paper No. 116—Claim Adjustment Expenses, Amendments to SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* provides historical reference on the original guidance included in SSAP No. 55 as well as the revisions originally reflected in SSAP No. 85.

Effective Date and Transition

23. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. Guidance reflected in paragraphs 7.c., 8.b. and 10, incorporated from SSAP No. 85, is effective for years ending on and after December 31, 2003. The guidance incorporated into paragraphs 1, 3, 6.c.ii., 7.d. and 10.b.vi. was originally included in *INT 03-17: Classification of Liabilities from Extra*

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Contractual Obligation Lawsuits and was initially effective March 10, 2004. The guidance in paragraph 5 was previously included in *INT 02-21: Accounting for Prepaid Loss Adjustment Expenses and Claim Adjustment Expenses* effective for reporting periods ending on or after December 31, 2002, for all contracts except for capitated managed care contracts and December 31, 2006, for capitated managed care contracts. The guidance in paragraph 13 related to conservatism and adverse deviation was originally contained in *INT 01-28: Margin for Adverse Deviation in Claim Reserve* and was effective October 16, 2001. The guidance in paragraph 15 related to coordination of benefits was originally contained within *INT 00-31: Application of SSAP No. 55 Paragraph 12 to Health Entities* and was effective December 4, 2000. The guidance reflected in footnote 1, incorporated from *INT 06-14: Reporting of Litigation Costs Incurred for Lines of Business in which Legal Expenses Are the Only Insured Peril*, was effective June 2, 2007. The guidance in paragraph 10.b.vii. regarding interest on managed care and accident and health claims is effective January 1, 2020, with early adoption permitted, and shall be applied prospectively.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*
- *Issue Paper No. 116—Claim Adjustment Expenses, Amendments to SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*

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Statement of Statutory Accounting Principles No. 56

Separate Accounts

STATUS

Type of Issue	Life, Accident and Health
Issued	Finalized March 13, 2000
Effective Date	January 1, 2001—Revised disclosures adopted September 2009 were required within the 2010 annual financial statements
Affects	Supersedes SSAP No. 80 with guidance incorporated August 2011
Affected by	No other pronouncements
Interpreted by	INT 00-03
Relevant Appendix A Guidance	A-200; A-250; A-255; A-270; A-585; A-588; A-620; A-695; A-812; A-820; A-821; A-822; A-830

STATUS **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for accounting and reporting for separate accounts in both the general account and separate account statements.

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SUMMARY CONCLUSION

Introduction

2. Separate accounts are used to fund variable life insurance, variable annuities, modified guaranteed annuities and modified guaranteed life insurance, or various group contracts under pension or other employee benefit plans where funds are held in a separate account to support a liability. When separate accounts are established and filed accordingly, they may be used to fund guaranteed benefits. Separate account contracts may also be used to accumulate funds which are intended to be applied at some later time to provide life insurance or to accumulate proceeds applied under settlement or dividend options.

3. Assets held in separate accounts are owned by the insurer. All investment income and realized and unrealized capital gains and losses from assets allocated to a separate account, net of related investment expenses, are generally reflected in the separate account and, except for modified guaranteed annuities, modified guaranteed life insurance, and separate accounts established and filed to provide guaranteed benefits, investment performance is generally not guaranteed by the insurer. Charges relating to contract guarantees, administration, and investment management are deducted from separate accounts.

General Account Reporting

4. Insurance activities such as sales, underwriting and contract administration, premium collection and payment of premium taxes, claims, and benefits are functions of the insurance company distinct from the separate account and shall be accounted for as transactions of the general account.

5. For those separate account contracts classified as life contracts under *SSAP No. 50—Classification of Insurance or Managed Care Contracts,* premiums and annuity considerations shall be recorded as income in the Summary of Operations of the general account, and as transfers to premiums and considerations in the separate account statement. Deposit-type contracts shall be recorded in the general account in accordance with *SSAP No. 52—Deposit-Type Contracts*.[INT 00-03] Charges (e.g., fees associated with investment management, administration, and contract guarantees) assessed on the separate accounts, as well as the net gain from operations of the separate account, shall be recorded as income in the Summary of Operations of the general account. Expenses relating to investment management, administration, and contract guarantees pertaining to separate account operations, as well as benefits and surrenders incurred on behalf of separate account contracts classified as life contracts, net transfers between separate accounts, commissions, and premium taxes (if any) shall be recorded as expenses in the Summary of Operations of the general account.

6. The general account shall include the total assets and liabilities, including transfers due or accrued, of any separate accounts business which it maintains and, therefore, the surplus, if any, of its separate accounts business. Transfers to the general account due or accrued shall be reported on a net basis so that the asset and the liability totals of the general account are not overstated. Changes in the surplus of the separate accounts business of an insurer, except for changes resulting from the net gain from operations of the separate account, shall be charged or credited directly to the unassigned funds (surplus) of the general account.

7. Where a variable annuity contract or variable life insurance contract contains a guaranteed minimum death benefit, any reserve liability for such death benefit provision shall be recorded and held in the general account based on the reserving guidance in paragraphs 25 and 26. Any differences between the benefit paid and the separate account asset value of the contract shall be charged against or credited to the general account in its net gain from operations.

8. Separate account surplus may not become negative. For example, for separate account contracts which have annuitized (i.e., contracts in the payout stage), lower than expected mortality on variable

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annuity contracts containing mortality guarantees may cause a deficiency in the investment funds underlying the contract reserves. Thus the general account incurs an expense and the separate account realizes revenue to cover the deficiency, if necessary. Conversely, excess funds from higher than expected mortality will result in mortality gains, which are included in the Summary of Operations of the separate account and are ultimately recorded as equity in net income from separate account operations as discussed in paragraph 5.

9. Separate account surplus created through the use of the commissioners' reserve valuation method (CRVM), commissioners' annuity reserve valuation method (CARVM), or other reserving methods, shall be reported by the general account as an unsettled transfer from the separate account. The net change on such transfers shall be included as a part of the net gain from operations in the general account.

10. Surplus funds transferred from the general account to the separate account, commonly referred to as seed money, and earnings accumulated thereon shall be reported as surplus in the separate accounts until transferred or repatriated to the general account. The transfer of such funds between the separate account and the general account shall be reported as surplus contributed or withdrawn during the year.

11. If an Asset Valuation Reserve (AVR) is required for investments held by separate accounts, it is combined with the general account AVR and accounted for in the general account financial statements (see *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*). The criteria for determining when an AVR is required for separate accounts are described in paragraph 18 of this statement.

12. Reporting entities collect fees for managing Separate Account Guaranteed Investment Contracts (GICs), Synthetic GICs, as well as participating separate account group annuities. These are in the form of administrative fees, risk fees and some investment management fees. For defined contribution business, these are in the form of fees related to mutual fund management. These fees are meant to offset expenses and generate some profit.

13. Amounts receivable from contractholders for separate account management fees meet the definition of assets as set forth in *SSAP No. 4—Assets and Nonadmitted Assets*.

14. An evaluation shall be made of the amounts receivable to determine any nonadmitted amounts. Next, an evaluation shall be made in accordance with *SSAP No. 5R—Liabilities, Contingencies and* Impairments *of Assets*, to determine whether there is an impairment. This two-step process is set forth below:

a. Uncollected separate account management fees receivable over ninety days due shall be accounted for as a nonadmitted asset. Reporting entities shall begin aging the receivable when it is contractually required to be billed, or in the absence of contract specifications, when the reporting entity actually sends the bill to the contractholder;

b. Remaining amounts determined to be uncollectible shall be written off. If in accordance with SSAP No. 5R, it is "probable" the amount receivable is uncollectible, any uncollectible amount receivable shall be written off against operations in the period such determination is made. If it is "reasonably possible" the amount receivable is uncollectible, the disclosure requirements outlined in SSAP No. 5R, paragraph ~~31~~32, shall be made.

Separate Account Reporting

15. The separate accounts annual statement is concerned with the flow of funds related to investment activities and obligations of the separate accounts and with the transfer of funds between the separate account and the general account. As a result, the separate account statement shall report only the assets, liabilities, and operations of the separate account and shall not include general account expenses related to

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investment management, administration, or contract guarantees pertaining to separate account operations which are recorded in the general account.

16. The separate account records premiums, considerations (net of loading for sales charges such as commissions and premium taxes) and receipts (other than for net investment income and realized capital gains and losses) as income transfers from the general account. Net investment income and realized and unrealized capital gains and losses relating to the investment operations of the separate account are recorded as income in the Summary of Operations. When the contract provides for such, expenses and taxes associated with the separate account investment operations shall be deducted in the determination of net investment income. Deposits and withdrawals on deposit-type contracts shall be recorded in the Summary of Operations. Benefits and surrenders, reserve transfers, policy loans[1], policyholder charges (e.g., fees associated with investment management, administration, and contract guarantees), and federal income taxes relating to the separate account are recorded as expense transfers to the general account in the Summary of Operations. The net change in aggregate reserves relating to separate account contracts is reported as an expense in the Summary of Operations.

17. Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, will be recorded as if the assets were held in the general account. Assets supporting all other contractual benefits shall be recorded at fair value on the date of valuation, or if there is no readily available market, then in accordance with the valuation procedures in the applicable contract.

Separate Account AVR and IMR Reporting

18. An AVR is generally required for separate accounts when the insurer, rather than the policyholder/contractholder, suffers the loss in the event of asset default or fair value loss. An AVR is required unless:

a. The asset default or fair value risk is borne directly by the policyholders; or

b. The regulatory authority for such separate accounts already explicitly provides for a reserve for asset default risk, where such reserves are essentially equivalent to the AVR.

19. Assets supporting traditional variable annuities and variable life insurance generally do not require an AVR because the policyholders/contractholders bear the risk of change in the value of the assets. However, an AVR is required for that portion of the assets representing the insurer's equity interest in the investments of the separate account (e.g., seed money).

20. Assets supporting typical modified guaranteed contracts, market value adjusted contracts, and contracts with book value guarantees similar to contracts generally found in the general account do require an AVR because the insurer is responsible for credit related asset or fair value loss.

21. Certain separate accounts are also required to maintain an Interest Maintenance Reserve (IMR). The IMR requirements for investments held in separate accounts are applied on an account by account basis. If an IMR is required for a separate account, all of the investments in that separate account are subject to the requirement. If an IMR is not required for a separate account, none of the investments in that separate account are subject to the requirement.

[1] Policy loans related to separate account products shall follow the guidance in *SSAP No. 49—Policy Loans*. As detailed within SSAP No. 49, as part of the expense transfer, policy loans related to separate account products require a liquidation of the separate account assets to fund the loan issued by the general account. A transfer of assets from the separate account to the general account must have occurred to fund the policy loan issuance; otherwise the policy loan is nonadmitted in the general account.

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22. An IMR is required for separate accounts with assets recorded at book value, but is not required for separate accounts with assets recorded at fair value. For example, separate accounts for traditional variable annuities or variable life insurance do not require an IMR because assets and liabilities are valued at fair value.

23. If an IMR is required for investments held by separate accounts, it is kept separate from the general account IMR and accounted for in the separate accounts statement.

24. The AVR and IMR shall be calculated and reported in accordance with the NAIC *Annual* Statement Instructions *for Life, Accident and Health Insurance Companies*.

Policy Reserves

25. Statutory policy reserves shall be established for all contractual obligations of the insurer arising out of the provisions of the insurance contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. These statutory policy reserves are generally calculated as the excess of the present value of future benefits to be paid to or on behalf of policyholders less the present value of future net premiums. Statutory policy reserves meet the definition of liabilities as defined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. The actuarial methodologies referred to in the following paragraph meet the criteria required for reasonable estimates in SSAP No. 5R.

26. The reserving methodologies and assumptions used in computation of policy reserves shall also meet the provisions of Appendices A-200, A-250, A-255, A-270; A-585, A-588, A-620, A-695, A-820, A-822 and the actuarial guidelines found in Appendix C of this Manual. Where separate account contracts have guaranteed elements, the basis for determining the value of the liability shall be consistent with the basis used for asset values (i.e., valuation interest rates as defined in Appendix A-820 shall be used when assets are recorded as if held in the general account and current interest rates based on market rates shall be used when assets are recorded at fair value). Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

27. Statutory policy reserves for those group annuity contracts or other contracts that, in whole or in part, establish the insurer's obligations by reference to a segregated portfolio of assets not owned by the insurer shall be established in accordance with the guidance in Appendix A-695. Statutory policy reserves for those contracts with nonlevel premiums or benefits, or contracts with secondary guarantees shall be established in accordance with the guidance in Appendix A-830. Statutory policy reserves for those group life contracts utilizing a separate account that meet the requirements outlined in paragraph 1 of Appendix A-200 shall be computed in accordance with the guidance in that appendix.

Other Liabilities

28. The separate account shall accrue as a liability, subject to contractual provisions, amounts payable, including, but not limited to:

a. Fees associated with investment management, administration, and contract guarantees;

b. Investment expenses;

c. Investment taxes, licenses, and fees (Investment taxes such as real estate taxes, licenses and fees (excluding federal income taxes) are usually paid directly by the separate account but may be transferred to the general account for payment);

d. Federal income taxes;

e. Unearned investment income;

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f. Net transfer due to (from) the general account;

g. Remittances and items not allocated;

h. Payable for investments purchased;

i. Net adjustments in assets and liabilities due to foreign exchange rates.

Seed Money

29. When a new separate account is initiated, the insurer may make a temporary transfer of surplus funds commonly referred to as seed money to the separate account. Such funds and earnings accumulated thereon shall be reported as surplus in the separate accounts statement until transferred or repatriated to the general account. The transfer of such funds to and from the separate account shall be reported as surplus contributed or withdrawn during the year.

Disclosures

30. Paragraphs 31-35 detail the separate account disclosure requirements that shall be included within the Life, Accident and Health Annual Statement Blank. Paragraphs 36-38 detail the separate account disclosure requirements that shall be included within the Separate Account Annual Statement Blank.

31. The general account financial statement shall include detailed information on the reporting entity's separate account activity. These disclosures shall include:

a. A narrative of the general nature of the reporting entity's separate account business.

b. Identification of the separate account assets that are legally insulated from the general account claims.

c. Identification of the separate account products that have guarantees backed by the general account. This shall include:

i. Amount of risk charges paid by the separate account to the general account for the past five (5) years[2] as compensation for the risk taken by the general account; and

ii. Amount paid by the general account due to separate account guarantees during the past five (5) years.

d. Discussion of securities lending transactions within the separate account, separately including the amount of any loaned securities within the separate account, and if policy and procedures for the separate account differ from the general account.

32. For each grouping (as detailed in paragraph 33), the following shall be disclosed:

a. Premiums, considerations or deposits received during the year;

b. Reserves by the valuation basis of the investments supporting the reserves at the financial statement date. List reserves for separate accounts whose assets are carried at fair value separately from those whose assets are carried at amortized cost/book value;

[2] Reporting entities are permitted to prospectively 'build' the five-year disclosure. Thus, upon the first year of application of the disclosure requirements, reporting entities should illustrate one year of the disclosure requirement. In the second year, the reporting entity would disclose two years, and so forth until the disclosure includes five years of disclosures.

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c. Reserves by withdrawal characteristics, including whether or not the separate account is subject to discretionary withdrawal. For reserves subject to discretionary withdrawal, the below categories are included if applicable:

i. With market value adjustment;

ii. at book value without market value adjustment and with surrender charge of 5% or more;

iii. at fair value;

iv. at book value without market value adjustment and with surrender charge of less than 5%;

d. Reserves for asset default risk, as described in paragraph 18.b., that are recorded in lieu of AVR.

33. For the disclosures required in paragraph 32, separate accounts shall be addressed in the following groupings (which are the same as those used for risk-based capital):

a. Separate Accounts with Guarantees:

i. Indexed separate accounts, which are invested to mirror an established index which is the basis of the guarantee;

ii. Nonindexed separate accounts, with reserve interest rate at no greater than 4% and/or fund long-term interest guarantee in excess of a year that does not exceed 4%;

iii. Nonindexed separate accounts, with reserve interest rate at greater than 4% and/or fund long-term interest guarantee in excess of a year that exceeds 4%.

b. Nonguaranteed Separate Accounts—Variable separate accounts, where the benefit is determined by the performance and/or fair value of the investments held in the separate account. Include variable accounts with incidental risks, nominal expense, and minimum death benefit guarantees.

34. Provide a reconciliation of the amount reported as transfers to and from separate accounts in the Summary of Operations of the separate accounts statement and the amount reported as net transfers to or from separate accounts in the Summary of Operations of the general accounts statement.

35. The disclosures in *SSAP No. 51R—Life Contracts*, and *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* related to the withdrawal characteristics of products include separate account products and shall be completed in the general account disclosures.

36. The Separate Account Annual Statement Blank shall include detailed information on the characteristics of the separate account assets, specifically categorizing separate account assets in accordance with the following characteristics:

a. Identification of separate account assets that are legally insulated from the general account and those which are not legally insulated.

b. Aggregation of separate account assets from products registered with the SEC and separate account assets from products excluded from registration. In addition to the overall aggregation, this disclosure shall specifically identify separate account assets

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from private placement variable annuities (PPVA) and private placement life insurance (PPLI). The disclosures in this paragraph (36.b.) are effective December 31, 2018.

c. Amount of separate account assets that represent seed money, other fees and expenses due to the general account, and additional required surplus amounts.[3] This disclosure shall include the amount of seed money and other fees and expenses currently included in the separate account, as well as the amount of seed money received and repaid to the general account during the current year. This disclosure shall also include information on insulation (if applicable)[4], the time duration for which seed money and other fees and expenses due the general account are retained in the separate account, and information on how whether seed money is invested pursuant to general account directives or in accordance with stated policies and procedures.

d. Identification of the separate account assets in which the investment directive is not determined by a contractholder. (In most instances, having multiple investment choices at the option of a contractholder would be considered a situation in which the investment directive is determined by a contractholder. This is not true for situations in which the asset is invested in a manner that mirrors the investment directives of the general account.) Situations in which the investment directive is not determined by the contractholder (and situations in which the reporting entity is the contractholder) shall include disclosure regarding whether the investments of the respective separate account assets, if included within the general account investments, would have resulted with the reporting entity exceeding any investment limitations imposed on the general account.

e. Identification of the separate account assets in which less than 100% of investment proceeds are attributed to a contractholder. This shall include identification of the separate account investment income attributed to the reporting entity during the reporting period and whether such income was transferred to the general account or reinvested within the separate account. Instances in which such income is reinvested within the separate account shall include disclosure on whether the subsequent investments, if categorized with investments in the general account, would have exceeded investment limitations imposed on the general account.

37. For all separate account assets not reported at fair value, indicate the measurement basis (amortized cost or other method) for each asset (or asset class) and whether the measurement method was grandfathered in under the transition guidance in this SSAP, or whether the measurement method is allowed under a prescribed or permitted practice. This disclosure shall include a comparison of the assets' reported value to fair value with identification of the resulting unrealized gain/loss that would have been recorded if the assets had been reported at fair value.

38. For all separate accounts that include securities lending transactions, disclose the reporting entity's use and policy of securities lending within the separate account, including the amount of loaned securities from the separate account at the reporting date, the percentage of separate account assets lent as of that date, a description for which type of accounts (e.g., book value accounts, market value account accounts) are lent, if the separate account policyholder is notified or approves of such practices, the policy for requiring collateral, whether the collateral is restricted and the amount of collateral for transactions that extend beyond one year from the reporting date. This disclosure requires the entity to provide the following information as of the date of the statement of financial position: (1) the aggregate amount of contractually obligated open collateral positions (aggregate amount of securities at current fair value or

[3] Additional Required Surplus Amounts is defined as additional or permanent surplus that is required to be retained in the separate account in accordance with state law or regulations. These amounts should not include reinvested separate account investment proceeds that have not been allocated to separate account contract holders.

[4] As seed money is considered a temporary transfer of funds, it is generally not considered insulated.

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cash received for which the borrower may request the return of on demand) and the aggregate amount of contractually obligated collateral positions under 30-day, 60-day, 90-day, and greater than 90-day terms, (2) the aggregate fair value of all securities acquired from the sale, trade and use of the accepted collateral (reinvested collateral), and (3) information about the sources and uses of that collateral.

39. Identify all products reported as a separate account product under statutory accounting principles and identify whether each product was classified differently under GAAP. For products that resulted with different classifications between GAAP and SAP, identify the characteristic(s) of the product that prevented it from receiving a separate account classification under GAAP. This disclosure is applicable for all reporting entities. Thus, if GAAP financial statements were not filed, the reporting entity should complete this disclosure as if GAAP financials had been completed.

40. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

41. This statement rejects *ASU 2022-05, Transition for Sold Contracts*, *ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts*, and AICPA *Statement of Position 03-1, Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts* (SOP 03-1). The disclosure elements included within this SSAP are derived from the criteria for separate account reporting under SOP 03-1; however, this SSAP does not restrict separate account reporting pursuant to the criteria established in SOP 03-1.

42. This statement incorporates the requirements of Appendices A-200, A-250, A-255, A-270, A-585, A-588, A-620, A-695, A-812, A-820, A-821, A-822 the Actuarial Standards Board *Actuarial Standards of Practice*, and the actuarial guidelines found in Appendix C of this Manual.

Effective Date and Transition

43. This statement is effective for years beginning January 1, 2001. Contracts with assets held in a Separate Account that were issued in accordance with applicable state laws and regulations and issued prior to that effective date, for which assets and liabilities have been recorded using a consistent basis since issue, i.e., both assets and liabilities are recorded either as if in the general account ("book value") or as at fair value (current interest rates based on market rates shall be used for liabilities when assets are recorded at fair value), shall continue to be recorded using such basis until such time as the applicable contract terms or provisions are substantially changed, such as by a contract amendment modifying interest rate or withdrawal provisions. State laws and regulations shall be understood to include anything considered authoritative by the domiciliary state under the individual state's statutory authority and due process procedures. Changes that do not require change in the basis of recording would include: address changes, continued deposits, and other non-substantive changes such as these. For example, additional funds received after January 1, 2001 under contracts issued prior to January 1, 2001 may continue to be recorded using the basis in effect prior to January 1, 2001 until such time as a triggering change is made. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

44. Disclosure revisions adopted in September 2009 to paragraphs 30-39 shall initially be reported within the 2010 annual financial statements, with annual reporting thereafter.

REFERENCES

Other

- *NAIC Financial Condition Examiners Handbook*
- Actuarial Standards Board *Actuarial Standards of Practice*

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Relevant Issue Papers

- *Issue Paper No. 89—Separate Accounts*
- *Issue Paper No. 110—Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts, and SSAP No. 56—Separate Accounts*

GLOSSARY

Guarantee represents an insurance company's general account contractual obligation to reimburse life insurance and annuity policyholders for their separate account investment losses including the return of principal, minimum crediting rates, minimum death, withdrawal, accumulation of income benefits and no-lapse guarantees, and for separate account mortality losses.

Insulation is the legal protection of separate account assets equal to the reserves and supporting contract liabilities from the general account liabilities of the insurance enterprise ensuring that the separate account contract holder is not subjected to insurer default risk to the extent of their assets held in the separate account.

Risk Charge is the contractual amount the general account charges the separate account policyholders' account for compensation relating to the general account's guarantee on separate account assets or contract performance.

Total Maximum Guarantee is the difference between the total amount of liability the general account is subject to reimbursing as at the balance sheet date and the policyholder's contract value referenced by the guarantee (e.g., account value). For guarantees in the event of death, it is the minimum guaranteed amount available to the contractholder upon death in excess of the contractholder's contract value referenced by the guarantee (e.g., account balance) at the balance sheet date. For guarantees of amounts at annuitization, it is the present value of the minimum guaranteed annuity payments available to the contractholder determined in accordance with the terms of the contract in excess of the contract value referenced by the guarantee (e.g., account balance).

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Statement of Statutory Accounting Principles No. 57

Title Insurance

STATUS

Type of Issue	Property and Casualty
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-628

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. Title insurance insures that the policyholder has title to the property on the subject real estate as of the date of policy issuance, subject to exceptions and exclusions in the policy. When issued, a title policy has a one-time premium and reserves are established by the title insurance company. Title insurance differs from other lines of property and casualty insurance because its basic goal is risk elimination.

2. This statement establishes statutory accounting principles for title insurance and addresses areas where title insurance accounting differs from other lines of insurance. To the extent a topic is not covered by this statement, title insurance accounting shall comply with statutory accounting guidance for other lines of property and casualty insurance.

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SUMMARY CONCLUSION

General

3. Title insurers perform many services in connection with the transfer of real estate; however, their principal function involves insuring, guaranteeing, or indemnifying owners of real property or the holders of liens or encumbrances thereon against loss or damage due to defective titles, liens, or encumbrances or, in most states, the unmarketability of the title.

4. In addition to insuring against defective records or examination of those records, an insurer insures against "non-record defects" such as:

a. Forgeries;

b. Fraud;

c. Confusion of name in change of title;

d. Incompetence (minors or persons of unsound mind);

e. Mistakes in public records;

f. Undisclosed or missing heirs;

g. Instruments executed under a fabricated or expired power of attorney;

h. Deeds delivered after death of grantor or grantee or without the consent of the grantor;

i. Deeds by persons supposedly single but actually married;

j. Wills not probated;

k. Liens against property (e.g., mechanics liens and tax liens);

l. Falsified records.

5. Before a title insurance policy is issued, the title insurer, or its agent, must search and examine public records concerning the ownership, liens, and encumbrances on the subject real estate together with information relating to persons having an interest in the real property as well as maps and other records to determine that title to the property is insurable, or defects can be overcome.

Premium Revenue and Loss Reserve Recognition

6. A variety of services are generally provided (either by the title insurance underwriter, its agent, or others) in connection with the transfer of title to real estate. Title insurance premiums frequently are determined in the rate-making process based on the bundle of services provided, including some or all of title search and examination and closing or escrow fees. By statute or custom, certain states exclude a combination of title search, examination and closing or escrow fees from the rate-making process for title insurance premiums. Premiums shall be recorded at the date of policy issuance, on a gross premium basis, consistent with the rate-making method used. The premium related to a title insurance policy is due upon the effective date of the insurance and is not refundable. The term of a title insurance policy is indefinite because the policyholder is insured for as long as he or his heirs or devisees have an interest in the property.

7. Amounts paid to or retained by agents shall be reported as an expense.

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8. A liability shall be established for all known unpaid claims and loss adjustment expenses (known claims reserve) with a corresponding charge to income. The known claim reserve is further detailed in the Title Annual Statement Operations and Investment Exhibit on Unpaid Losses and Loss Adjustment Expenses. The known claims reserve should be the estimated costs to settle reported claims based upon the most current information available to the company as of the balance sheet date. This amount cannot be less than the aggregate of the individual case reserves.

9. Premium revenue shall be deferred to the extent necessary to maintain a Statutory or Unearned Premium Reserve (SPR or UPR) determined in accordance with the reserve section of Appendix A-628.

10. If the actuarially determined liability (the sum of the known claims reserve, IBNR claims reserve, and loss adjustment expense reserve) exceeds the sum of the known claims reserve and SPR or UPR, a supplemental reserve shall be established that is equal to the difference between these sums. This calculation is explicitly detailed in the Title Annual Statement Operations and Investment Exhibit for Unpaid Losses and Loss Adjustment Expenses.

11. The actuarially determined liability for the sum of known claims reserve required in paragraph 8 and the IBNR claims and loss adjustment expenses required in paragraph 10 of this statement shall be determined consistently with the guidance detailed in *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* and consistent with paragraph 13 of this statement.

12. Assets acquired in settlement of claims (e.g., mortgages and real estate) shall be accounted for consistent with the guidance related to the asset acquired. For example, an impaired loan shall be accounted for in accordance with *SSAP No. 37—Mortgage Loans*, and real estate acquired in foreclosure shall be accounted for in accordance with *SSAP No. 40R—Real Estate Investments*.

Salvage and Subrogation

13. Salvage and subrogation shall be reflected as follows:

a. Paid losses shall be reported net of realized, but not anticipated, salvage and subrogation. Case basis loss and loss adjustment expense reserves shall not be reduced for anticipated salvage and subrogation, nor shall an asset be established;

b. Paid salvage and subrogation is not realized until a salvage asset or an actual payment pursuant to a subrogation right is in the direct control of the insurer and admissible as an asset for statutory reporting purposes in its own right;

c. Salvage assets and payments pursuant to a subrogation right shall be recorded at current fair value. Current fair value of real estate shall be established through an appraisal conducted by a qualified independent appraiser;

d. If a salvage asset is sold or revalued by the insurer within twelve months of realization for an amount less than the value at which it was originally placed on the books of the insurer, then the loss on disposition shall be treated as a decrease in paid salvage (same effect as an addition to the paid loss) on the corresponding claim. After twelve months, such salvage revaluation will be treated as a loss on disposition or change in value of an asset, and shall not be deducted from the salvage on the corresponding claim;

e. If a salvage asset is sold or revalued by the insurer within twelve months of realization for an amount greater than the value at which it was originally placed on the books of the insurer, then the gain on disposition shall be treated as an increase in paid salvage (same effect as a deduction to the paid loss) on the corresponding claim. After twelve months, such salvage revaluation shall be treated as a gain on disposition or change in value of an asset and shall not be added to the salvage on the corresponding claim;

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f. In completing Schedule P and Part 3B, IBNR reserves may make an actuarially determined provision for the expected value of future salvage and subrogation on open claims and IBNR claims.

Reinsurance

14. Although by their nature, title claims relate to errors or omissions that occurred prior to the inception of the reinsurance agreement, title reinsurance contracts shall be accounted for as prospective reinsurance agreements if they meet all of the other criteria established in *SSAP No. 62R—Property and Casualty Reinsurance*.

Allocation of Expenses

15. This statement establishes uniform allocation rules to classify title insurance expenses within prescribed principal groupings. It is necessary to allocate those expenses which may contain characteristics of more than one classification, which this statement will refer to as allocable expenses.

16. Allocable expenses for title insurance companies shall be classified into the following categories on the expense section of the Operations and Investment Exhibit of the annual statement.

a. Title and Escrow Operating Expenses—Title and escrow operating expenses consist of all expenses incurred in relation to engaging in the business of title insurance, including costs associated with the following: (i) issuing or offering to issue a title insurance policy; (ii) soliciting or negotiating the issuance of a title insurance policy; (iii) guaranteeing, warranting or otherwise insuring the correctness of title searches affecting title to real property; (iv) handling of escrows, settlements or closings; (v) executing title insurance policies, effecting contracts of reinsurance, and abstracting, searching or examining titles. Also included are specifically identifiable and allocated expenses relating to the following activities; (i) supervision and training of employees and agents; (ii) operating costs for branch offices or agencies; (iii) underwriting activities; (iv) receiving and paying of premiums and commissions; (v) maintaining general and detailed records; (vi) data processing, advertising, and publicity, clerical, secretarial, office maintenance, supervisory, and executive duties; (vii) postage and delivery; and (viii) all other functions reasonably associated with the business of title insurance. Title and escrow operating expenses do not include losses, loss adjustment expenses (allocated or unallocated), expense of other operations, or investment expenses. The expenses include only amounts incurred directly by the insurer and do not include expenses incurred by any agents (regardless of ownership interest).

b. Title and Escrow Operating Expenses are further broken down in the annual statement by the distribution network that gives rise to the expense incurrence. Accordingly, expenses are specifically identified or allocated (in accordance with reasonable allocation procedures consistently applied) to either Direct Operations, Non-affiliated Agency Operations, or Affiliated Agency Operations.

c. Unallocated Loss Adjustment Expenses (ULAE)—ULAE are those indirect costs incurred by a title insurer, typically internal to the company, which are necessary to process claims or manage the claims settlement function and which are not incurred on a claim-specific basis. ULAE shall include all costs of outside parties involved in claims adjusting services, but shall not include any costs incurred by agents in settlement of title or other claims.

d. Investment Expenses—Investment expenses are those expenses incurred in the investing of funds and the pursuit of investment income, including specifically identifiable and

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allocated expenses related to such activities as: (i) initiating or handling orders and recommendations for investments; (ii) research, pricing, appraising, and valuing; (iii) disbursing funds and collecting income; (iv) safekeeping of securities and valuable papers; (v) maintaining general and detailed records; (vi) data processing; (vii) general clerical, secretarial, office maintenance, supervisory, and executive duties; (viii) supplies, postage, and the like; and (ix) all other functions reasonably attributable to the investment of funds. Real estate expenses and real estate taxes are attributable to the Investment Expenses group.

e. Other Operations—The amounts shown for this category represent the allocable expenses incurred by the company in operations other than title and escrow, unallocated loss adjustment, or investment activities.

17. Allocation to the above categories should be based on a method that yields the most accurate results. Specific identification of an expense with an activity that is represented by one of the categories above will generally be the most accurate method. Where specific identification is not feasible, allocation of expenses should be based upon pertinent factors or ratios such as studies of employee activities, salary ratios, or similar analyses.

18. Many companies operate within a group where personnel and facilities are shared. Shared expenses, including expenses under the terms of a management contract, shall be apportioned to the companies incurring the expense as if the expense had been paid solely by the incurring company. The apportionment shall be completed based upon specific identification to the company incurring the expense. Where specific identification is not feasible, apportionment shall be based upon pertinent factors or ratios. Any basis adopted to apportion expenses shall be that which yields the most accurate results and may result from special studies of employee activities, salary ratios, premium ratios or similar analyses. Expenses that relate solely to the operations of an insurance company, such as personnel costs associated with the adjusting and paying of claims, must be borne solely by the insurance company and are not to be apportioned to other companies within a group. Pertinent factors in making this determination shall include which entity has the ultimate obligation to pay the expense. Apportioned expenses are subject to presentation and allocation as provided in paragraphs 16 and 17.

Title Plant

19. Title plants are an integrated and indexed collection of title records consisting of documents, maps, surveys, or entries affecting title to real property or any interest in or encumbrance on the property, which have been filed or recorded in the jurisdiction for which the title plant is established or maintained. They are tangible assets unique to the title insurance industry and are the principal productive asset used to generate title insurance revenue and to mitigate the risk of claims. Title plant shall be reported as an admitted asset, subject to the following valuation restrictions:

a. Costs incurred to construct a title plant, including the costs incurred to obtain, organize, and summarize historical information in an efficient and useful manner, shall be capitalized until the title plant can be used by the company to conduct title searches and issue title insurance policies. The capitalized costs shall be directly related to, and properly identified with, the activities necessary to construct the title plant;

b. Purchased title plants, including a purchased undivided interest in a title plant, shall be recorded at cost at the date of acquisition. For a title plant acquired separately, cost shall be measured by the fair value of the consideration given. For title plant acquired as part of a group of assets, cost shall be measured by the fair value of the consideration given and then cost shall be allocated to the title plant based on its fair value in relation to the total fair value of the group of assets acquired. For title plants acquired as part of a

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purchase of assets or in a business combination, cost shall be determined in accordance with *SSAP No. 68—Business Combinations and Goodwill*;

c. A backplant, i.e., a title plant that antedates the period of time covered by the existing title plant may be purchased or constructed. Costs to construct a backplant must be properly identifiable to qualify for capitalization;

d. Costs incurred after a title plant is operational to (i) convert the information from one storage and retrieval system to another, or (ii) modify or modernize the storage and retrieval system shall not be capitalized;

e. Costs incurred to maintain a title plant shall be expensed as incurred;

f. Costs incurred to perform title searches shall be expensed as incurred;

g. An investment in a title plant or plants in an amount equal to the actual cost shall be allowed as an admitted asset for title insurers. The aggregate carrying value of an investment in a title plant or plants shall not exceed the lesser of 20% of admitted assets or ~~forty percent (~~40%~~)~~ of surplus to policyholders, both as required to be shown on the statutory balance sheet of the insurer for its most recently filed statement with the domiciliary state commissioner; if the amount of the investment exceeds the above limits, the excess amount shall be recorded as a nonadmitted asset.

20. Certain circumstances may indicate that the value of the title plant may be impaired and, thus, the carrying value of the asset may not be recoverable. If there is an indication of possible impairment of value, the title plant shall be evaluated for impairment and recorded in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. The following are examples of circumstances that may indicate impairment:

a. Effects of obsolescence, demand, and other economic factors;

b. A significant change in legal requirements or statutory practices in the jurisdiction for which the title plant is established and maintained;

c. A current period operating or cash flow loss combined with a history of such losses or projections that indicate continued losses associated with the revenue produced by the title plant;

d. Failure to maintain the title plant on a current basis and/or lack of appropriate maintenance to keep the title plant up to date; or,

e. Abandonment of a title plant.

21. A properly maintained title plant has an indeterminate life and does not diminish in value with the passage of time, and accordingly, shall not be depreciated.

22. A title insurer may (a) sell its title plant and relinquish all rights to its future use, (b) sell an undivided ownership interest in its title plant, or (c) sell a copy of its title plant or the right to use it. Accounting and presentation for each type of sale noted shall be as follows:

a. When a title insurer sells its title plant and relinquishes all rights to its future use, consideration received shall be presented as a separate component of revenue net of the carrying value of the title plant sold;

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b. When a title insurer sells an undivided ownership interest in its title plant, consideration received shall be presented as a separate component of revenue net of the pro rata portion of the carrying value of the title plant;

c. When a title insurer sells a copy of its title plant or the right to use it, consideration received shall be presented as a separate component of revenue and the carrying value of the title plant shall not be reduced.

Disclosures

23. The financial statements shall disclose the following for each period presented:

a. The amount of the known claims reserve, SPR/UPR, and the supplemental reserve;

b. Whether the insurer uses discounting in the calculation of its supplemental reserve, the method and rate used to determine the discount, and the amount of such discount.

24. Any material individual component of the reported expense categories shall be presented either on the face of the Summary of Operations or within the footnotes or related exhibits to the financial statements.

25. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

26. This statement rejects *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises* (FAS 60); however, it is considered appropriate to use the factors to be considered in the determination of the ultimate cost of settling claims included in FAS 60 when establishing the reserves in accordance with paragraphs 8 and 10 of this statement.

27. This statement adopts *FASB Statement No. 61, Accounting for Title Plant*, with modification for carrying value restrictions. Restrictions on the total carrying value of an investment in a title plant or plants are determined by paragraph 19.g.

Effective Date and Transition

28. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

29. Additions to the SPR or UPR as a result of the provisions of paragraph 17.b.v. of Appendix A-628 shall be phased in pursuant to the provisions of paragraph 17.b.iv. of Appendix A-628.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 57—Title Insurance*

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Statement of Statutory Accounting Principles No. 58

Mortgage Guaranty Insurance

STATUS

Type of Issue	Property and Casualty
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-630

STATUS **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for mortgage guaranty insurance and addresses areas where mortgage guaranty insurance accounting differs from other lines of insurance. To the extent a topic is not covered by this statement and Appendix A-630, mortgage guaranty insurance accounting shall comply with statutory accounting guidance for other lines of property and casualty insurance.

2. Mortgage guaranty insurance protects a lender against loss of all or a portion of the principal amount of a mortgage loan upon default of the mortgagor. Mortgage guaranty insurance differs from other types of property and casualty insurance in that coverage is long-term, and in most cases premiums are level and paid monthly. Most states require issuers of mortgage guaranty contracts to be monoline insurers and impose limitations on the aggregate amount of risk insured based on geographic territories. Additionally, states may require mortgage guaranty insurers to reinsure with only selected reinsurers.

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SUMMARY CONCLUSION

General

3. Mortgage guaranty insurance is provided on residential loans (one to four family residences, including condominiums and townhouses). Coverage can range from as little as 5% on pool insurance to as much as 100% of the outstanding loan amount on individual policies. Most policies cover 10% to 30% of the loan amount and are written on first mortgage loans where the loan amount is a high percentage (generally 80% to 95%) of the value of the mortgaged property.

4. Lenders obtain mortgage guaranty insurance to facilitate sales of mortgage loans in secondary markets. It also enables lenders to make a greater number of high ratio (above 80%) loans and allows them to diversify their portfolio of loans.

5. Mortgage guaranty insurers market directly to mortgage lenders. Individual mortgage loans or pools of mortgage loans are insured under individual insurance certificates or policies; each loan, however, is separately underwritten.

6. Mortgage guaranty insurance companies generally offer the following premium payment plans: (a) monthly premiums, (b) a single premium which provides coverage for periods ranging from three to 15 years, (c) nonlevel annual premiums, and (d) level annual premiums. All policies are renewable at the discretion of the lender. The mortgage guaranty insurer does not have an option to cancel or nonrenew the policy, except for fraud or nonpayment of the premium.

7. Premiums are based upon: (a) the percentage of insurance coverage provided, (b) the ratio of the insured mortgage loan to the property value or sales price, and (c) the term and/or premium payment method selected by the lender. Premiums are quoted as a percentage of the total mortgage loan insured and increase as insurance coverage and loan-to-value ratio increases.

8. If a default occurs, the mortgage guaranty insurer generally requires the lender to foreclose and tender merchantable title to the mortgaged property in order to make a claim. The insurer may then, at its option: (a) purchase the property for the lender's cost (generally the entire remaining principal loan balance plus accumulated interest and allowable expenses), (b) pay the percentage of the lender's cost specified by the policy, or (c) arrange for the lender to sell the property and reimburse the lender for any loss up to an agreed amount. Under settlement option (a), the insurer intends to resell the property with the expectation of reducing the amount of loss which would have resulted if option (b) had been elected.

Insured Risk

9. The nature of the insured risk is influenced by certain factors which set mortgage guaranty insurance apart from other types of insurance. These factors are addressed in paragraphs 10-12.

Exposure Period

10. The exposure period is significantly longer for mortgage insurance than for most other property and casualty insurance products. The exposure period can run for the term of the mortgage; however, the average policy life is seven years. The policy is terminated when the mortgage obligation is satisfied or the lender elects to cancel or not renew the policy. In contrast to mortgage guaranty insurance, most property and casualty products need not be renewed by the insurer at the expiration of the policy. Mortgage insurance is renewable at the option of the insured at the renewal rate quoted when the policy commitment was issued.

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Losses

11. Losses are affected by the following factors specific to mortgage guaranty insurance:

a. The insured peril—the default of a borrower arises from the credit risk associated with mortgage loans. The frequency of loss is strongly influenced by economic conditions. The likelihood of individual default is further increased if the property has deteriorated since a borrower in financial difficulty will be less able to sell the property at a price sufficient to discharge the mortgage;

b. Mortgage insurance losses can be divided into three categories:

i. Normal losses associated with regular business cycles, interruptions in the borrower's earning power, and errors made in evaluating the borrower's willingness or ability to meet mortgage obligations;

ii. Defaults caused by adverse local economic conditions;

iii. Widespread defaults caused by a severe depression in the U.S. economy.

Loss Incidence

12. Losses are incurred over the exposure period which runs for the term of the mortgage. However, loss incidence peaks in the earlier years. When a loan has been delinquent two to four months, the policy requires the lender to notify the insurer. The lender generally agrees to institute foreclosure proceedings six to nine months from the date of delinquency. Foreclosure can require an additional 18 months which means a considerable delay between the delinquency and the presentation of the claim. Without adverse economic conditions, most delinquencies do not result in a loss payment. Once a claim is presented, payment normally is made within one or two months and ultimate loss costs can be known relatively quickly.

Pool Insurance

13. Mortgage guaranty insurance may be provided on pools of mortgage loans. Typically, pool insurance supports mortgage-backed securities or group sales. Unlike other pool or group products, each loan is individually underwritten.

14. Pool insurance may be provided on loans that are already insured by primary insurance, in which case the pool insurance provides an additional level of coverage, or it may be provided on loans without primary insurance (usually loans with loan-to-value ratios below 80%). Generally, pool insurance provides 100% coverage and includes a stop-loss limit of liability which may range from 5% to 20% of the initial aggregate principal balance. Because of regulatory requirements in some states, pool insurance usually uses participating reinsurance arrangements to limit the exposure of any one mortgage insurer of a pool of loans to 25% of each mortgage insured.

15. Pool insurance policies are not cancelable by the insurer except for nonpayment of premium. These policies may be written on mortgage pools having terms of up to 30 years. However, the average policy life is 8 to 12 years.

16. Upon default, the insurer has the same options as with individual insured mortgage loans. However, pool insurance loss payments are reduced by settlements under primary insurance and subject to the stop-loss limit.

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17. Three kinds of mortgage-backed securities which use pool insurance are:

a. Mortgage-backed bonds—Issued by banks, savings and loan associations and other mortgage lenders as a general obligation of the issuing institution. These bonds are collateralized by a pool of mortgages and have a stated rate of return and maturity date;

b. Mortgage revenue bonds—Issued by state and local housing authorities to support housing affordability for targeted income groups;

c. Mortgage pass-through certificates—Issued by banks, savings and loan associations, mortgage bankers, and others providing an undivided interest in a pool of mortgages with principal and interest payment passed to the certificate holder as received.

Premium Revenue Recognition

18. Written premium shall be recorded in accordance with *SSAP No. 53—Property and Casualty Contracts—Premiums*. Premium revenue shall be earned as follows:

a. For monthly premium plans, revenues shall be earned in the month to which they relate;

b. For annual premium plans, revenues shall be earned on a pro rata basis over the applicable year;

c. For single premium plans, revenues shall be earned over the policy life in relation to the expiration of risk;

d. Additional first year premiums or initial renewal premiums on nonlevel policies shall be deferred and amortized to income over the anticipated premium paying period of the policy in relation to the expiration of risk.

Unpaid Losses and Loss Adjustment Expense Recognition

19. Unpaid losses and loss adjustment expenses shall be recognized in accordance with *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*. For mortgage guaranty insurance contracts, the default shall be considered the incident that gives rise to a claim as discussed in SSAP No. 55. If a claim is ultimately presented, the date of default shall be considered the loss incurred date.

20. The process for estimating the liability shall include projections for losses that have been reported as well as those that have been incurred but not reported. The estimates shall be made based on historical data, trends, economic factors, and other statistical information including paid claims, reported losses, insurance in force statistics, and risk statistics.

21. Real estate and mortgages are acquired by mortgage guaranty insurers to mitigate losses. These assets shall be shown on the balance sheet at the lower of cost or net realizable value, net of encumbrances. Gains or losses from the holding or disposition of these assets shall be recorded as a component of losses incurred. Rental income or holding expenses shall be included in loss adjustment expenses.

Contingency Reserve

22. In addition to the unearned premium reserve, mortgage guaranty insurers shall maintain a liability referred to as a statutory contingency reserve. The purpose of this reserve is to protect policyholders against loss during periods of extreme economic contraction. The annual addition to the liability shall equal 50% of the earned premium from mortgage guaranty insurance contracts and shall be maintained for ten years regardless of the coverage period for which premiums were paid. With commissioner

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approval, when required by statute, the contingency reserve may be released in any year in which actual incurred losses exceed 35% of the corresponding earned premiums. Any such reductions shall be made on a first-in, first-out basis. Changes in the reserve shall be recorded directly to unassigned funds (surplus).

Premium Deficiency Reserve

23. When the anticipated losses, loss adjustment expenses, commissions and other acquisition costs, and maintenance costs exceed the recorded unearned premium reserve, contingency reserve, and the estimated future renewal premium on existing policies, a premium deficiency reserve shall be recognized by recording an additional liability for the deficiency with a corresponding charge to operations. Commissions and other acquisition costs need not be considered in the premium deficiency analysis to the extent they have been expensed. If an insurer utilizes anticipated investment income as a factor in the premium deficiency calculation, disclosure of such shall be made in the financial statements.

U.S. Mortgage Guaranty Tax and Loss Bonds

24. To obtain a current federal income tax benefit derived from annual additions to the statutory contingency reserve (for tax purposes, the mortgage guaranty account), mortgage guaranty insurers must purchase tax and loss bonds to the extent of the tax benefits. These bonds are noninterest bearing obligations of the U.S. Treasury and mature 10 years after issue. The usual purpose of tax and loss bonds is to satisfy taxes that will be due in 10 years when the tax benefit is reversed; however, the bonds may be redeemed earlier in the event of excess underwriting losses. These bonds are reported as admitted assets allowing mortgage insurers to conserve capital. In accordance with *SSAP No. 101—Income Taxes*, temporary differences (as defined in that statement) do not include amounts attributable to the statutory contingency reserve to the extent that "tax and loss" bonds have been purchased.

Contingency Reserve (for Tax Purposes, the Mortgage Guaranty Account)

25. Under IRS Code Section 832(e), mortgage guaranty insurers are permitted to deduct the annual addition to the contingency reserve from gross income. The tax deduction is generally an amount equal to (a) 50% of earned premium, or (b) taxable income as computed prior to this special deduction if less than 50% of earned premium. Annual deductions not utilized for tax purposes during the current period may be carried forward for eight years on a basis similar to net operating losses. The amount deducted must be restored to gross income after ten years; however, it may be restored to gross income at an earlier date in the event of a taxable net operating loss.

26. The tax deduction is permitted only if special U.S. Mortgage Guaranty Tax and Loss Bonds are purchased in an amount equal to the tax benefit derived from the deduction. Upon redemption the tax and loss bonds can be used to satisfy the additional tax liability that arises when the deduction is restored to income.

Disclosures

27. Mortgage guaranty insurers shall make all disclosures required by other statements within the *Accounting Practices and Procedures Manual*, including but not limited to the requirements of SSAP No. 55, and *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*.

28. Refer to the Preamble for further discussion regarding disclosure requirements.

Effective Date and Transition

29. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 88—Mortgage Guaranty Insurance*

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Statement of Statutory Accounting Principles No. 59

Credit Life and Accident and Health Insurance Contracts

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 01-29
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-010; A-225; A-812; A-818; A-820; A-822

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for income recognition and policy reserves for all contracts classified as credit life and credit accident and health contracts defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*.

SUMMARY CONCLUSION

Definitions

2. Credit life and accident and health insurance contracts will be referred to collectively as "credit insurance" for purposes of this statement. Credit insurance is generally issued in connection with the issuance of credit to an individual by a bank, retailer, finance company, or other similar organization. This type of insurance most often protects the creditor to the extent of the unpaid balance of the loan. Contracts sold in connection with loans or other credit transactions not exceeding a stated duration shall be reported as credit insurance. Mortgage guaranty insurance is addressed in *SSAP No. 58—Mortgage Guaranty Insurance*. Credit policies are generally limited to issues of 120 months or less in most states. Credit insurance is sold as either an individual or group policy and may provide for single or joint life coverage.

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3. Credit life insurance, generally in the form of decreasing term insurance, is issued on the lives of debtors to cover payment of loan balances in case of death. Credit accident and health insurance is insurance on a debtor to either provide indemnity for payments becoming due on a specific loan or other credit transaction while the debtor is disabled.

4. Premiums for credit insurance contracts shall be defined as the contractually determined amount charged by the reporting entity to the policyholder for the effective period of the contract.

Income Recognition

5. Consistent with *SSAP No. 51R—Life Contracts*, premiums shall be recognized in the summary of operations as income on the gross basis (amount charged to the policyholder) when due from policyholders under the terms of the insurance contract.

Policy Reserves

6. Statutory policy reserves shall be established for all unmatured contractual obligations of the reporting entity arising out of the provisions of the insurance contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. The statutory policy reserves for credit life contracts are generally calculated as the excess of the present value of future benefits to be paid to or on behalf of policyholders less the present value of future net premiums. The statutory policy reserves for credit accident and health contracts generally consist of an unearned premium reserve, and other reserves, as required, as further discussed in paragraphs 11-14. Statutory policy reserves meet the definition of liabilities as defined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. The actuarial methodologies referred to in the following paragraph meet the criteria required for reasonable estimates in SSAP No. 5R.

7. The reserving methodologies and assumptions used in computation of policy reserves shall meet the provisions of Appendices A-010, A-820 and A-822, and the actuarial guidelines found in Appendix C of this Manual. Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

8. Policy reserves are established through either a gross unearned premium reserve or a mortality/morbidity reserve. The gross unearned premium reserve represents the estimated amount of premium for insurance coverage that has not yet expired. The mortality/morbidity reserve represents the estimated amount of future anticipated benefits, discounted at valuation interest and mortality/morbidity, to be incurred on policies in force.

9. When the level of insurance risk is constant during the contract period, policy reserves shall be recognized over the period of risk using either the daily pro-rata or monthly pro-rata methods as described in *SSAP No. 53—Property and Casualty Contracts—Premiums*. Policy reserves for contracts where the level of insurance risk is not constant throughout the contract period shall be recognized over the period of risk in proportion to the amount of insurance protection provided. Various methods may be used to accomplish this as described below. The reporting entity shall select the method that most closely reflects the pattern of insurance protection provided. To the extent that these methods do not reflect the pattern of insurance protection provided, the reporting entity shall modify or develop, if necessary, a method that recognizes net income from the policy over the exposure period of the contract in proportion to the amount of insurance protection provided.

10. Single premium credit life policy reserves shall be based on either a gross unearned premium reserve based on a refund formula, or a reserve based on assumed risks using mortality factors. In practice, various methods exist and are currently used to estimate the amount of gross unearned premiums applicable to the unexpired portion of the policies in force. For decreasing gross coverage, the gross unearned premium may be estimated using a Rule of 78's method; for decreasing net payoff coverage,

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either the Rule of 78's or the single-premium method is used; and for level coverage, the pro-rata method is generally used. The reporting entity shall select a method that reflects the pattern of insurance protection provided.

11. Except as noted in paragraph 12, policy reserves for credit A&H policies shall be based on either a gross unearned premium reserve using the pro rata, Rule of 78's, mean of pro rata and Rule of 78's, or actuarial methods. The gross unearned premium reserve is a measure of the single premium for the debt's remaining term and amount. Most states required reporting entities to record a gross unearned premium reserve using the Rule of 78's method. In practice, such a gross unearned premium reserve has been the average of the Rule of 78's and the pro rata methods. The reporting entity shall select a method that reflects the pattern of insurance protection provided. Also, the method should be consistent with the refund method actually used or required in the state.

12. For single premium credit disability policies issued on or after January 1, 2002, Appendix A-010 requires that a contract reserve be established using a standardized morbidity table. For single premium credit disability policies issued prior to January 1, 2002, reserves may be established either according to the standards in Appendix A-010 or paragraph 11. Once an insurer elects to calculate reserves for all contracts on the standard in Appendix A-010, all future valuations must be on that basis.

13. For all credit contracts in the aggregate, if the premium refund liability exceeds the aggregate recorded reserve, an additional liability shall be established. This premium refund (excess) liability may include consideration of commission, premium tax, and other expenses recoverable. The excess reserve shall be established for the surrender values (premium refund) in excess of the mortality reserves. As such, the surrender values may be net of commissions, premium taxes, etc. Additionally, the excess reserve is calculated on an aggregated basis by combining all credit life and accident and health policies and certificates.

14. When the anticipated benefits, expected dividends to policyholders and maintenance cost exceed the recorded policy reserve, a premium deficiency reserve shall be recognized by recording an additional liability for the excess deficiency with a corresponding charge to operations. Commission and other acquisition costs need not be considered in the premium deficiency analysis since they have previously been expensed.

15. The difference between the policy reserves at the beginning and end of the reporting period shall be reflected as the change in reserves or change in unearned premium, as appropriate, in the summary of operations, except for any difference due to a change in valuation basis as discussed in paragraph 16.

Change In Valuation Basis

16. A change in valuation basis shall be defined as a change in the interest rate, mortality assumption, or reserving method (e.g., net level, preliminary term, etc.) or other factors affecting the reserve computation of policies in force and meets the definition of an accounting change as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors*. Consistent with SSAP No. 3, any increase (strengthening) or decrease (destrengthening) in policy reserves resulting from such a change in valuation basis shall be recorded directly to surplus rather than as a part of the reserve change recognized in the Summary of Operations. The impact on surplus is based on the difference between the reserve under the old and new methods as of the beginning of the year. This difference shall not be graded in over time unless an actuarial guideline adopted by the NAIC prescribes a new method and a specific transition that allows for grading.

Disclosures

17. For life reserves the financial statements shall disclose the following:

a. A description of reserve practices concerning the following:

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i. Waiver of deduction of deferred fractional premiums upon death of insured;

ii. Return of portion of final premium for periods beyond the date of death;

b. The methods employed in the valuation of substandard policies;

c. The amount of insurance, if any, for which the gross premiums are less than the net premiums according to the valuation standards;

d. The method used to determine tabular interest, tabular less actual reserves released, and tabular cost (by formula or from the basic data for such items);

e. The nature of significant other reserve changes.

18. If the company has reported life insurance premiums deferred and uncollected on policies in force as of the financial statement date, disclose separately the amounts and the loading excluded for credit life business.

19. Disclose the aggregate amount of direct premiums written through managing general agents or third party administrators. For purposes of this disclosure, a managing general agent means the same as in Appendix A-225. If this amount is equal to or greater than 5% of surplus, provide the following information for each managing general agent and third party administrator:

a. Name and address of managing general agent or third party administrator;

b. Federal Employer Identification Number;

c. Whether such person holds an exclusive contract;

d. Types of business written;

e. Type of authority granted (i.e., underwriting, claims payment, etc.);

f. Total premium written.

20. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

21. This statement incorporates the requirements of Appendices A-010, A-225, A-812, A-818, A-820 and A-822, the Actuarial Standards Board *Actuarial Standards of Practice* and the actuarial guidelines found in Appendix C of this Manual.

22. This statement rejects *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises* relating to accounting and reporting for credit life and accident and health insurance contracts.

Effective Date and Transition

23. This statement is effective for years beginning January 1, 2001. Contracts issued prior to January 1, 2001 shall be accounted for based on the laws and regulations of the domiciliary state. State laws and regulations shall be understood to include anything considered authoritative by the domiciliary state under the individual state's statutory authority and due process procedures. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance in paragraph 13 pertaining to establishing the excess reserve for surrender

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values was originally contained within *INT 01-29: SSAP No. 59 and Application to Credit Life* and was effective December 10, 2001.

REFERENCES

Other

- NAIC *Financial Condition Examiners Handbook*
- Actuarial Standards Board *Actuarial Standards of Practice*

Relevant Issue Papers

- *Issue Paper No. 59—Credit Life and Accident and Health Insurance Contracts*

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Statement of Statutory Accounting Principles No. 60

Financial Guaranty Insurance

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 00-04
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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EXHIBIT A – DISCLOSURE ILLUSTRATION **8**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for financial guaranty insurance and addresses areas where financial guaranty insurance accounting differs from other lines of insurance. To the extent a topic is not covered by this statement, financial guaranty insurance accounting shall comply with statutory accounting guidance for other lines of property and casualty insurance.

SUMMARY CONCLUSION

2. Financial guaranty insurance provides protection against financial loss as a result of default, changes in interest rate levels, differentials in interest rate levels between markets or products, fluctuations in exchange rates between currencies, inconvertibility of one currency into another, inability to withdraw funds held in a foreign country resulting from restrictions imposed by a governmental body, changes in the value of specific assets or commodities, financial or commodity indices, or price levels in general. Financial guaranty insurance does not provide protection from losses which occur due to fortuitous physical events, failure or deficiency in the operation of equipment, or the inability to extract natural resources. Additionally, it does not provide coverage from losses related to various types of bonds (e.g., individual or schedule public official bond; a contract bond; a court bond), credit insurance, guaranteed investment contracts, and residual value insurance.

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3. Included in the definition of financial guaranty insurance is student loan insurance. Student loan insurance includes financial guarantees issued as a surety bond or financial guarantee policies issued to a bank or other lending financial institution, under which the insurer agrees to provide financial guaranty of each student loan made by the bank within specified underwriting criteria. As each loan is made, the premium for that loan is paid to the insurer by the bank from the proceeds of the loan that are retained by the bank at issuance. Usually repayment of the loan is expected to commence six months after graduation. If and when there is a default in repayment of the loan by the graduate, the insurer pays the bank or lending institution the unpaid principal and interest on the loan, takes possession of the loan, and initiates recovery efforts. Student loan insurance is subject to the provisions of this statement and the statutory contingency reserve.

Premium Revenue Recognition

4. Written premium shall be recorded in accordance with *SSAP No. 53—Property and Casualty Contracts—Premiums* except that installment premiums, which may vary substantially over the term of the contract since the total amount insured and the premium rate are contingent upon the performance of the insured obligations, shall be recorded when received.

5. When premiums are paid on the installment basis, premium revenue shall be recognized in the statement of operations using the monthly pro-rata method. Premiums not paid on the installment basis shall be recognized in the statement of operations in proportion with the amount and expected coverage period of the insured risk.

6. When the anticipated losses, loss adjustment expenses, and maintenance cost exceed the recorded unearned premium reserve and contingency reserve, a premium deficiency reserve shall be recognized by recording an additional liability for the deficiency with a corresponding charge to operations. Commission and other acquisition costs need not be considered in the premium deficiency analysis since they have previously been expensed. If a reporting entity utilizes anticipated investment income as a factor in the premium deficiency calculation, disclosure of such shall be made in the financial statements.

Unpaid Losses and Loss Adjustment Expense Recognition

7. Unpaid losses and loss adjustment expenses shall be recognized in accordance with *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*. Each financial guaranty insurer shall establish and maintain reserves for unpaid losses and loss adjustment expenses. The initial date of default shall be considered the incident which gives rise to a claim. Loss reserves shall include a reserve for claims reported and unpaid net of collateral.

8. A deduction from loss reserves shall be allowed for the time value of money by application of a discount rate equal to the average rate of return on the admitted assets of the financial guaranty insurer as of the date of the computation of the reserve. The discount rate shall be adjusted at the end of each calendar year. In addition, a reserve component for incurred but not reported claims shall be reasonably estimated, if deemed necessary by the financial guaranty insurer or required by the commissioner following an examination or actuarial analysis.

Contingency Reserve

9. In addition to the unearned premium reserve and the liability established for unpaid losses and loss adjustment expenses, financial guaranty insurers shall maintain a liability referred to as a statutory contingency reserve. The purpose of this reserve is to protect policyholders against loss during periods of extreme economic contraction.

10. The contingency reserve shall be the greater of 50%~~fifty percent~~ of premiums written for each category or the amount provided by applying the following percentages to the principal guaranteed in

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each calendar year. The premiums written shall be net of reinsurance if the reinsurer has established a contingency reserve.

a.	Municipal obligation bonds	0.55% ~~percent~~
b.	Special revenue bonds	0.85% ~~percent~~
c.	Investment grade Industrial Development Bonds (IDBs) secured by collateral or having a term of seven years or less, and utility first mortgage obligations	1.00% ~~percent~~
d.	Other investment grade IDBs	1.50% ~~percent~~
e.	Other IDBs	2.50% ~~percent~~
f.	Investment grade obligations, secured by collateral or having a term of seven years or less	1.00% ~~percent~~
g.	Other investment grade obligations not secured	1.50% ~~percent~~
h.	Non-investment grade consumer debt obligations	2.00% ~~percent~~
i.	Non-investment grade asset backed securities	2.00% ~~percent~~
j.	All other non-investment grade obligations	2.50% ~~percent~~

11. Additions to the reserve for items a. through e. in paragraph 10, equal to one-eightieth of the amounts derived by applying the appropriate contribution specified above, shall be made each quarter for a period of twenty (20) years. Additions to the reserve for items f. through j. in paragraph 10, equal to one-sixtieth of the amounts derived by applying the appropriate contribution specified above, shall be made each quarter for a period of fifteen (15) years.

12. For contingency reserves required to be maintained for 20 years, contributions may be discontinued if the total reserve established for all categories in paragraphs 10.a. through 10.e. exceeds the sum of the percentages contained therein multiplied by the unpaid principal guaranteed. For contingency reserves required to be maintained for 15 years, contributions may be discontinued if the total reserve established for all categories in paragraphs 10.f. through 10.j. exceeds the sum of the percentages contained therein multiplied by the unpaid principal guaranteed.

13. The contingency reserve may also be released in the following circumstances:

a. For contingency reserves required to be maintained for 20 years:

i. In any year in which actual incurred losses exceed 35% of the corresponding earned premiums, with commissioner approval;

ii. If the reserve has been in existence less than 40 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, with commissioner approval;

iii. If the reserve has been in existence more than 40 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, upon 30 days prior written notice to the commissioner.

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b. For contingency reserves required to be maintained for 15 years:

i. In any year in which actual incurred losses exceed 65% of the corresponding earned premiums, with commissioner approval;

ii. If the reserve has been in existence less than 30 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, with commissioner approval;

iii. If the reserve has been in existence more than 30 quarters, upon demonstration that the amount is excessive in relation to the outstanding obligations under the insurer's financial guarantees, upon 30 days prior written notice to the commissioner.

Any reductions shall be made on a first-in first-out basis. Changes in the reserve shall be recorded through unassigned funds (surplus).

Disclosures

14. Financial guaranty insurers shall make all disclosures required by paragraphs 15-17 as well as other statements within the *Accounting Practices and Procedures Manual*, including but not limited to the requirements of SSAP No. 55 and *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*. (For disclosures within paragraph 16 and 17, all "expected" amounts and terms should be determined in accordance with management estimates.) In all instances, the insurer shall disclose when they elect to reflect timeframes or recognition principles from *FASB Statement No. 163*, *Accounting for Financial Guarantee Insurance Contracts—an interpretation of FASB Statement No. 60* (FAS 163) as permitted within the disclosure requirements.

15. An insurance enterprise shall disclose information that enables users of its financial statements to understand the factors affecting the present and future recognition and measurement of financial guarantee insurance contracts.

16. To meet the disclosure objective in paragraph 15, an insurance enterprise shall disclose the following information for each annual reporting statement, and in any interim period if a significant change has occurred in that interim period:

a. For financial guarantee insurance contracts where premiums are received as installment payments over the period of the contract, rather than at inception:

i. The unearned premium revenue as of the reporting date, in proportion with the amount and expected coverage period of the insured risk, which would have been reflected if the premium had been received at inception[1].

b. A schedule of premiums (undiscounted) expected to be collected under all installment contracts detailing the following:

i. The four quarters of the subsequent annual period and each of the next four annual periods;

ii. The remaining periods aggregated in five-year increments;

[1] If desired, a reporting entity that follows FAS 163 for GAAP may elect to report this disclosure in accordance with the revenue recognition principles of FAS 163.

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c. A rollforward of the expected future premiums (undiscounted), including:

i. Expected future premiums – Beginning of Year;

ii. Less - Premium payments received for existing installment contracts;

iii. Add – Expected premium payments for new installment contracts;

iv. Adjustments to the expected future premium payments;

v. Expected future premiums – End of Year.

d. For non-installment contracts for which premium revenue recognition has been accelerated, the amount and reasons for acceleration.

e. A schedule of the future expected earned premium revenue on non-installment contracts as of the latest date of the statement of financial position detailing the following:

i. The four quarters of the subsequent annual period and each of the next four annual periods;

ii. The remaining periods aggregated in five year increments.

f. For the claim liability:[2]

i. The rate used to discount the claim liability. This rate[3] shall equal the average rate of return on the admitted assets of the financial guaranty insurer as of the annual date of the computation of the reserve.

ii. The significant component(s) of the change in the claim liability for the period (the accretion of the discount on the claim liability, changes in the timing, establishment of new reserves for defaults of insured contracts, changes or establishment of deficiency reserves, and changes or establishment of reserves for incurred but not reported claims), and the amount relating to each component(s).

g. A description of the insurance enterprise's risk management activities used to track and monitor deteriorating insured financial obligations, including the following:

i. A description of each grouping or category used to track and monitor deteriorating insured financial obligations;

ii. The insurance enterprise's policies for placing an insured financial obligation in, and monitoring, each grouping or category;

iii. The insurance enterprise's policies for avoiding or mitigating claim liabilities, the related expense and liability reported during the period for those risk mitigation activities (not including reinsurance), and a description of where that expense and

[2] The reference to "claim liability" throughout the disclosure requirements shall reflect the "reserves for unpaid losses and loss adjustment expenses" from paragraphs 7 and 8 of this statement.

[3] The annual discount rate calculated pursuant to this paragraph shall be utilized for the subsequent year's quarterly financial statements. Per paragraph 8, the discount rate shall be adjusted at the end of each year.

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that liability are reported in the statement of income and the statement of financial position, respectively.

17. An insurance enterprise shall disclose the following information for each annual and interim period related to the claim liability:

a. A schedule of insured financial obligations at the end of each interim period detailing, at a minimum, the following for each category or grouping of these financial obligations (see Exhibit A):

i. Number of issued and outstanding financial guarantee insurance contracts;

ii. Remaining weighted-average[4] contract period;

iii. Insured contractual payments outstanding[5], segregating principal and interest;

iv. Gross claim liability;[6]

v. Gross potential recoveries;[7]

vi. Discount, net (both claim liability and potential recoveries;[8]

vii. Net claim liability;[9]

viii. Reinsurance recoverables;[10]

ix. Unearned premium revenue;[11]

18. Refer to the Preamble for further discussion regarding disclosure requirements.

[4] Weighted average contract period shall be based on management's estimate of the weighted average life of the contracts. If desired, a reporting entity that follows FAS 163 for GAAP may elect to mirror the time period calculated under FAS 163.

[5] Contractual payments outstanding shall be based on management's estimates of receivables. If desired, a reporting entity that follows FAS 163 for GAAP may elect to mirror the time period calculated under FAS 163.

[6] Represents the unpaid losses and loss adjustment expenses calculated in accordance with SSAP No. 55 and SSAP No. 60, but excluding the effects of subrogation recoveries, ceded reinsurance and discounting.

[7] Includes (a) subrogation recoveries, which are deducted from the gross claim liabilities in accordance with paragraph 15 of SSAP No. 55 and (b) ceded reinsurance recoveries on unpaid losses, which are deducted from the gross claim liability in accordance with paragraph 126.a. of SSAP No. 62R.

[8] Represents the discounting effect of the gross claim liability, subrogation recoveries, and reinsurance recoveries.

[9] Represents the gross claim liability less gross potential recoveries and the net discount. This line should reconcile to the sum of line 10, column 8 and column 9 (financial guaranty net unpaid losses and net unpaid loss adjustment expenses) of the Underwriting and Investment Exhibit, Part 2a – Unpaid Losses and Loss Adjustment Expenses.

[10] Represents reinsurance recoverables on paid losses which is reported as an asset with paragraph 24 of SSAP No. 62R. This line should reconcile to "Amounts recoverable from reinsurers" on the balance sheet.

[11] Unearned premium revenue (UPR) should be consistent with the UPR measurement principles of SSAP No. 60. UPR reported in this schedule may not reconcile to line 10, column 5 of the Underwriting and Investment Exhibit, Part 1a – Recapitulation of all Premiums. To the extent that this amount does not reconcile to line 10, column 5 of the Underwriting and Investment Exhibit, Part 1a – Recapitulation of Premiums, provide an additional reconciliation to line 10, column 5 of the Underwriting and Investment Exhibit, Part 1a in a footnote to the tabular disclosures required in paragraph 17.

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Effective Date and Transition

19. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in paragraph 3 was originally contained within *INT 00-04: Student Loan Insurance* and was effective June 12, 2000.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 69—Financial Guaranty Insurance*

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EXHIBIT A – DISCLOSURE ILLUSTRATION

A1. The example below assumes the insurance enterprise uses a surveillance list with four surveillance categories to track and monitor its insured financial obligations. The surveillance list and four surveillance categories are used for illustrative purposes only. The surveillance categories shown below describe the claim liability before the mitigating effects of potential recoveries. The following are brief descriptions of each surveillance category to provide context to the example:

a. Category A includes insured financial obligations that are still currently performing (that is, insured contractual payments are made on time but the likelihood of an event of default has increased since the financial guarantee insurance contract was first issued), but if economic conditions persist for an extended period of time, they may not be performing in the future. The issuer of the insured financial obligation may have experienced credit deterioration as a result of a general economic downturn. As a result, the present value of expected net cash outflows may exceed the unearned premium revenue of the financial guarantee insurance contract some time in the future.

b. Category B includes insured financial obligations that are currently characterized as potentially nonperforming and may require action by the insurance enterprise to avoid or mitigate an event of default.

c. Category C includes insured financial obligations that are characterized as nonperforming and for which actions to date by the insurance enterprise have not been successful in avoiding or mitigating an event of default. The insurance enterprise continues its efforts to cure the claim, but an event of default is imminent.

d. Category D includes insured financial obligations where an event of default has occurred.

	Surveillance Categories				
	A	B	C	D	Total
Number of policies	37	16	5	4	62
Remaining weighted-average contract period (in years)	16	14	11	12	
Insured contractual payments outstanding:					
Principal	$ 656,000,000	$ 409,000,000	$ 196,000,000	$ 111,000,000	$ 1,372,000,000
Interest	478,000,000	298,000,000	150,000,000	73,000,000	999,000,000
Total	$ 1,134,000,000	$ 707,000,000	$ 346,000,000	$ 184,000,000	$ 2,371,000,000
Gross claim liability	$ 1,045,000,000	$ 690,000,000	$ 330,000,000	$ 184,000,000	$ 2,249,000,000
Less:					
Gross potential recoveries	752,000,000	381,000,000	29,000,000	7,000,000	1,169,000,000
Discount, net	159,000,000	153,000,000	125,000,000	78,000,000	515,000,000
Net claim liability	$ 134,000,000	$ 156,000,000	$ 176,000,000	$ 99,000,000	565,000,000
Unearned premium revenue	$ 7,000,000	$ 4,000,000	$ 2,000,000	$ - (a)	$ 13,000,000
Reinsurance recoverables	$ 10,000,000	$ 19,000,000	$ 25,000,000	$ 27,000,000	$ 81,000,000

(a) In this instance, it is assumed that once an insured financial obligation is in Category D, the only remaining obligation of the insurance enterprise is making claim payments. As such, all related balances of the insured financial obligation are written off, including the unearned premium revenue.

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Statement of Statutory Accounting Principles No. 61 – Revised

Life, Deposit-Type and Accident and Health Reinsurance

STATUS

Type of Issue	Life, Accident and Health
Issued	Initial Draft; Substantively revised December 18, 2012
Effective Date	January 1, 2001; Certified reinsurer changes effective December 31, 2012
Affects	Nullifies and incorporates INT 02-04, INT 02-08 and INT 02-09; Nullifies INT 00-23
Affected by	No other pronouncements
Interpreted by	INT 03-02; INT 23-04
Relevant Appendix A Guidance	A-785; A-791

STATUS **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for life, deposit-type and accident and health reinsurance. This statement applies to life, deposit-type and accident and health contracts as defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*.

SUMMARY CONCLUSION

Indemnity Reinsurance

2. Reinsurance is an agreement by which a reporting entity transfers all or part of its risk under a contract to another reporting entity. The entity that issued the policy is called the primary insurer, direct writer, or ceding entity and the entity to which the risk is transferred is called the reinsurer or assuming entity. The process of transferring the risk from the ceding entity to the reinsurer is known as a cession. If an assuming entity, in turn, transfers a portion of this risk, the process is called a retrocession. A retrocession is customarily made when the amount assumed is beyond the reinsurer's limits of retention.

3. There is no direct relationship between the reinsurer or the retrocessionaire and the ceding entity's policyholder unless there is a "cut-through endorsement." In the event of the ceding entity's insolvency, except in the case of a "cut-through endorsement," the policyholder or beneficiary under a contract that is reinsured has the same status as a policyholder or beneficiary of a policy that was not reinsured. An entity may not need to be licensed, have accredited reinsurer status or other means of authorization in a state in order to act as a reinsurer of a domestic entity. However, the domestic entity is not permitted to take reserve credits on the business ceded to any unauthorized reinsurers or certified reinsurers to the extent that they are not properly securitized by means of a trust, letter of credit or funds withheld or other acceptable forms of collateral.

4. Fronting arrangements, pools and association business are often accomplished using reinsurance contracts.(INT 03-02) The guidance included in this statement also applies to these types of contracts except as specifically exempted.

Retention

5. In formulating its rules for accepting applications for insurance, an entity must decide upon three areas of action—retaining, reinsuring, or declining the risks presented. Entities of various sizes have different desired capacities to write insurance on a single life and/or entire blocks of business or portfolios. An entity determines the amount of risk exposure it is able to accept and retain as its own insurance business. Having made this determination, the entity then decides what to do with any risks presented that exceed the maximum amount it is willing to retain. It has two choices—accept the additional risk and reinsure it, or decline the extra risk.

6. Business to be written is expected to be profitable, so the direct writing entity will generally want to retain as much of the risk as possible, consistent with its overall objectives. The entity also will want to avoid exposure to large losses that could jeopardize its financial condition and the policy values of its policyholders. Consequently, a common practice in the life insurance industry is for a reporting entity to establish a schedule for maximum amounts of insurance, called retention limits, which it will retain at its

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own risk on individual lives in various categories of insurance. By adopting a suitably chosen schedule of retention, the reporting entity eliminates exposure to large losses and reduces fluctuations in the cost of death claims from year to year, which could adversely affect the reporting entity's surplus position. In addition, the reporting entity can utilize aggregate stop loss reinsurance to protect it from aggregate claims exceeding a specific threshold.

7. There are also reasons why a reporting entity might retain less than its defined maximum. One is to transfer from the ceding entity to the reinsurer the part of the surplus strain that results from writing new life insurance. The ceding entity may wish to limit the risk of loss on substandard business. Testing new coverages or new classes of lives may lead to reinsurance.

Reinsurance Arrangements

8. Reinsurance can be on a facultative or an automatic basis. For facultative, each risk is handled separately at the time it is written. When the direct writing entity receives an application for a policy and it wishes to reinsure some or all of the risk, it negotiates with another entity for a transfer of all or a portion of that risk. For purely facultative cessions, the assuming entity is not obligated to assume any of the risk until its offer to reinsure is accepted. For facultative obligatory reinsurance, the assuming entity is obligated to reinsure the risk subject to its having sufficient available capacity.

9. For automatic reinsurance, the ceding entity agrees to reinsure with the reinsurance entity all cases which meet certain defined conditions for amounts as defined in the reinsurance agreement. The reinsurance entity is bound to accept all such amounts, up to a predetermined maximum. Amounts in excess of automatic limits set out in the reinsurance agreement may be handled as facultative cessions. When the amount lies within the automatic maximum limit, called the binding authority, the ceding entity issues its policy upon completion of its underwriting procedures and without securing the prior approval of the reinsurance entity. Notification of automatic reinsurance is sent to the reinsurer within a specified period after the ceding entity issues its policy.

10. By agreeing to accept all business automatically ceded to it, the reinsurer is relying on the underwriting judgment of the ceding entity and is bound to accept the case even when it, the reinsurer, may not agree with the underwriting action. The reinsurer is protected by the requirement that the ceding entity retains at its own risk its defined retention limit for the class of business that is involved and by the maximum which may be ceded automatically.

Types of Reinsurance Arrangements

11. Once an entity has decided to reinsure amounts in excess of its desired retention, it may proceed in one of several basic arrangements—coinsurance, modified coinsurance, yearly renewable term or non-proportional. Such contracts may have funds withheld.

Coinsurance

12. In this arrangement, the risks are reinsured on the same plan as that of the original policy. The direct writer and the reinsurer share in the risk in the same manner. The ceding entity pays the reinsurer a proportional part of the premiums collected from the insured. In return, the reinsurer reimburses the ceding entity for the proportional part of the death or accident and health claim payments and other benefits provided by the policy, including nonforfeiture values, policy dividends, experience rating refunds, commissions, premium taxes, and other direct expenses agreed to in the contract. The reinsurer must also establish the required reserves for the portion of the policy it has assumed. A single policy can be coinsured with more than one entity or under more than one reinsurance contract with the same entity as long as the combined total of reinsurance and the retention of the ceding entity is not more than 100% of the risk.

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13. In coinsurance of participating policies, the reinsurer may reimburse the ceding entity for its portion of the dividends paid to the policyholder. In determining its schedule of dividends, the ceding entity takes into account the experience on the business as written. If the reinsurer reimburses dividends it will typically accept the ceding entity's schedule but may require input into the schedule. Changes to the schedule may have to be agreed to by the reinsurer. Coinsurance of all or a portion of a block of business also is used in situations where a severe strain is placed on the direct writing entity's surplus in the first policy year. For example, the premium received by the direct writer during the first policy year usually is insufficient to pay the high first-year commissions and other costs of issue and to establish the initial reserve. In such an example, coinsurance relieves some of the surplus strain of adding large amounts of new insurance.

Modified Coinsurance

14. The "modified coinsurance" or "modco" arrangement is a variation of coinsurance. The ceding entity has transferred all or a portion of the net policy liabilities on the reinsured policies to the reinsurer, and the reinsurer is required to indemnify the ceding entity for the same amount. The assets necessary to support the reserves for the original policies are maintained by the ceding entity instead of the reinsurer. This is accomplished by designating in the contract the transfer of the net policy liabilities to the assuming entity and an immediate transfer back to the extent of the modco deposit. Under modified coinsurance, the assuming entity shall transfer to the ceding entity the increase in the reserve on the reinsured portion. This transaction reflects the reinsurer's risk with respect to the reinsured business and its obligation to maintain the reserves supporting such obligation. In some cases, a policy may be reinsured partially on a coinsurance arrangement and partially on a modified coinsurance arrangement. This may be accomplished through the use of two contracts or in a single contract.

Yearly Renewable Term (YRT)

15. Under this arrangement of reinsurance, the ceding entity transfers the net amount at risk on the portion reinsured to the reinsurer and pays a one-year term premium. The "net amount at risk"—as defined in the contract—is usually the amount of insurance provided by the policy in excess of the ceding entity's reserve on it.

Non-Proportional

16. Other forms of reinsurance are also available, such as catastrophe and stop loss coverage. These arrangements provide for financial protection to the ceding entity for aggregate losses rather than providing indemnification for an individual policy basis as described in the preceding three reinsurance arrangements. Catastrophic and stop loss reinsurance are written on an annual basis to protect the ceding entity from excessive aggregate losses. Usually, the coverage does not extend over the life of the underlying policy nor is there any requirement on the ceding entity to renew the arrangement.

Transfer of Risk

17. Reinsurance agreements must transfer risk from the ceding entity to the reinsurer in order to receive the reinsurance accounting treatment discussed in this statement. If the terms of the agreement violate the risk transfer criteria contained herein, (i.e., limits or diminishes the transfer of risk by the ceding entity to the reinsurer), the agreement shall follow the guidance for Deposit Accounting. In addition, any contractual feature that delays timely reimbursement violates the conditions of reinsurance accounting.

18. This paragraph applies to all life, deposit-type and accident and health reinsurance agreements except for yearly renewable term reinsurance agreements and non-proportional reinsurance agreements such as stop loss and catastrophe reinsurance. All reinsurance agreements covering products that transfer significant risk shall follow the guidance for reinsurance accounting contained in this statement. All

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reinsurance contracts covering products that do not provide for sufficient transfer of risk shall follow the guidance for Deposit Accounting.

19. Yearly renewable term (YRT) reinsurance agreements that transfer a proportionate share of mortality or morbidity risk inherent in the business being reinsured and do not contain any of the conditions described in Appendix A-791, paragraphs 2.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k., shall follow the guidance for reinsurance accounting, including paragraphs 55-57 of this statement that apply to indemnity reinsurance. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit Accounting. For all treaties entered into on or after January 1, 2003, the deferral guidance in paragraph 3 of A-791 shall also apply to YRT agreements. Since YRT agreements only transfer the mortality or morbidity risks to the reinsurer, the recognition of income shall be reflected on a net of tax basis, as gains emerge based on the mortality or morbidity experience.

20. For non-proportional reinsurance agreements such as stop loss and catastrophe reinsurance agreements, contract terms shall be evaluated to assess whether they transfer significant risk to the reinsurer. For example, prepayment schedules and accumulating retentions from multiple years are contractual features inherently designed to delay the timing of reimbursement to the ceding entity limits the risk to the reinsurer. Regardless of what a particular feature might be called, any feature that can delay timely reimbursement violates the conditions for reinsurance accounting. Transfer of insurance risk requires that the reinsurer's payment to the ceding entity depend on and directly vary with the amount and timing of claims settled under the reinsured contracts. Contractual features that can delay timely reimbursement prevent this condition from being met. Reinsurance accounting shall apply to all non-proportional agreements that transfer significant risk and do not contain any provisions that protect the reinsurer from incurring a loss. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit Accounting.

Accounting and Reporting of Reinsurance

21. The obligation of reporting reinsurance in force and of determining unpaid premiums and incurred claims and other balances is generally on the ceding entity because it knows the current status of the policies it has written directly and reinsured. A lag will develop between the time of the entry of the underlying policy transaction on the books of the ceding entity and the transmittal of information and its entry on the books of the assuming entity. The assuming entity shall estimate any material unreported premiums and related costs.

22. The ceding entity must report these items in its balance sheet:

a. Credits (deductions) to its policy and claim reserves and unpaid claims;

b. Premiums or other amounts payable on reinsured risks;

c. Amounts recoverable on claims, surrender values, dividends, experience rating refunds, taxes, commissions, and other expenses;

d. Modified coinsurance reserves; and,

e. Amounts receivable or payable for funds withheld.

23. Similarly, in its balance sheet, the assuming entity must report:

a. Reserves for reinsurance assumed reduced by any modified coinsurance reserves;

b. Reinsurance premiums receivable or other amounts receivable;

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c. Amounts payable for claims, surrender values, dividends, experience rating refunds, taxes, commissions, and other expenses; and,

d. Amounts receivable or payable for funds withheld by the ceding entity.

24. While the premiums, commissions, expense allowances, reserves, claims, etc. will result in a net amount, the proper way to report them is in their separate classifications on the balance sheet. Each reinsurance agreement must be accounted for separately. Certain assets and liabilities are created by entities when they engage in reinsurance contracts. Reinsurance assets meet the definition of assets as defined by *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted to the extent they conform to the requirements of this statement.

Reinsurance Premiums

25. For all reinsurance arrangements, the assuming entity must report premiums under the terms of the reinsurance contract as income and establish any asset or liability consistent with the methods and assumptions used to establish its policy reserves and guidance contained in *SSAP No. 51R—Life Contracts*, *SSAP No. 54R—Individual and Group Accident and Health Contracts*, and *SSAP No. 59—Credit Life and Accident and Health Insurance Contracts*. The ceding entity shall reduce premium income by the amounts paid or payable to the reinsurers. The ceding entity shall reduce its deferred and uncollected premiums reported as an asset by the corresponding proportionate amount of any deferred and uncollected premium attributable to those insurance policies reinsured. When the ceding entity has collected the premium but has not remitted the proportionate share to the reinsurer, the ceding entity shall establish a liability for the amount due the reinsurer. The assuming entity shall record an asset for premiums receivable from the ceding entity.

26. If the assuming entity receives reinsurance premium prior to the due date, consistent with SSAP No. 51R paragraph 7 and SSAP No. 54R, paragraph 6, advance premiums are reported as a liability for the reinsurer in the statutory financial statement and not considered income until due. Such amounts are not included in premium or the unearned premium reserve (if applicable) until the due date. If the ceding entity pays reinsurance premium prior to the due date, the amount of the prepaid item shall be reflected as a write-in admitted asset and it should not be recognized in the income statement until due. Such amounts are not included in ceded premiums or ceded unearned premium but should be subject to impairment analysis.

Reinsurance Benefit Payments

27. Policy benefit payments paid or payable by the reinsurer shall be reported in the summary of operations and reduces the ceding entity's reported benefit payments. The reinsurer shall establish a liability for its share of any unpaid claim payments and the ceding entity shall reduce any policy and contract claim liability with respect to the reinsured policies or establish a receivable for the amount due from the reinsurer for claims paid.

Reinsurance of Deposit-Type Contracts

28. At the outset of a reinsurance contract covering deposit-type contracts as defined in *SSAP No. 52—Deposit-Type Contracts*, the net consideration exchanged between the parties shall be recorded as a contra-liability (reduction of reserve) by the payer of the net considerations and as a liability (reserve) by the receiver. Throughout the life of the contract, receipts and disbursements shall be recorded through the asset/liability accounts.

Expenses

29. It is common for the assuming entity to provide an expense allowance to cover expenses of the ceding entity. The allowance is frequently nonspecific with respect to premium taxes and other general

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expenses of the ceding entity and it is usually combined with and accounted for as part of the commissions on reinsurance assumed or ceded.

30. Commissions on direct business, commissions and expense allowances on reinsurance assumed, and commissions and expense allowances on reinsurance ceded are each accounted for separately in the summary of operations and on the balance sheet. Accordingly, for entities reporting on the Life, Accident and Health Annual Statement, commissions and expense allowances on reinsurance ceded are reported as income in the summary of operations and the balance sheet provision for due and accrued amounts is reported as an asset. For entities reporting on the Health Annual Statement commissions and expense allowance on reinsurance ceded are reported as an offset to administrative expenses.

31. The taxes, commissions, and other expenses that will be paid by the assuming entity to the ceding entity are agreed upon when the reinsurance agreement is negotiated. These items are calculated in accordance with the reinsurance agreement and usually relate to premiums or claims or both. At the statement date, the amount of unpaid expenses is generally based upon the amount of premiums and claims unpaid at that date.

32. Some coinsurance contracts provide that the assuming entity pay to the ceding entity a commission that exceeds the first-year premium. In the absence of any guarantees for payment of future premiums, or other similar persistency guarantees, these commissions are accounted for on the cash basis. If, however, the contract contains a persistency guarantee which provides for return of the excess commission, the ceding entity must record the excess commission as a liability. This liability is then released as future premiums are paid to the assuming entity or the persistency guarantee otherwise expires. The rate of release is determined in accordance with the anticipated experience and reasonable commission rate for first-year and renewal premiums. Excess commissions such as these are a means of financing for the ceding entity.

33. If renewal expense allowances in any accounting period are not sufficient to cover anticipated allocable renewal expenses of the ceding entity on the portion of the business reinsured, a liability is to be established by the ceding entity for the present value of the shortfall. In establishing this liability, assumptions are to be used equal to the applicable statutory reserve basis on the business reinsured. Anticipated allocable expenses include commissions, premium taxes and direct expenses including, but not limited to, billing, valuation, claims and maintenance expected by the entity at the time the business is reinsured.

Experience Refunds

34. Some reinsurance contracts, generally proportional reinsurance, provide that the reinsurer will refund an agreed upon portion of its profit to the ceding entity. The reinsurance contract will provide the calculation and the factors to be included.

35. If the contract provides for experience refunds, the ceding entity must record, as an asset, the amount of the refund receivable as of the statement date, but reduced by any amount that is contingent upon future experience. The assuming entity is also required to record, as a liability, the amount of the refund calculated at the statement date, but without regard to any effects that future experience might have.

Credits for Ceded Reinsurance

36. The credit taken by the ceding entity under the coinsurance arrangement is calculated using the same methodology and assumptions used in determining its policy and claim reserves. It is, of course, only for the percentage of the risk that was reinsured. Under modified coinsurance, the reserve credit is reduced by the modco deposit retained by the ceding entity. If the entity reinsures on a yearly renewable term basis, it is itself buying insurance for the portion of the ceded amount at risk. The amount of yearly

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renewable term reinsurance that is required on a given policy generally decreases each year as the entity's reserve increases. The net amount at risk may increase, however, on interest sensitive products such as universal life. The amount at risk on accident and health yearly renewal term reinsurance will remain level and the reinsurance premium will increase each year.

37. The reserve credit taken by the ceding entity is reported as a reduction to the reserves and not as an asset of the entity. The ceding entity's reserve credit and assuming entity's reserve for yearly renewable term reinsurance shall be computed as the one year term mean reserve on the amount of insurance ceded. The ceding entity must use the same mortality and interest bases which were used for valuing the original policy before reinsurance. The credit may also be computed on a pro rata basis if the result is not materially different from the credit computed on the mean reserve basis. For all types of reinsurance, the ceding entity also takes credit for other amounts due from the reinsurer such as unpaid claims and claims incurred but not reported. If contemplated by the reinsurance contract, recognition of related assets and liabilities must occur (policy loans, due and deferred premiums, etc.).

38. Non-proportional reinsurance is entered into on an annual basis to limit the claims experience of the ceding entity and thereby protect its financial integrity. When the period of the arrangement exceeds one year, the contract must be carefully reviewed to determine if the end result more closely follows proportional reinsurance. No reserve credit is taken for non-proportional reinsurance unless the aggregate attachment point has in fact been penetrated. In order for an entity to reflect reserve credits on a prospective basis, the entity will need to demonstrate that the present value of expected recoveries using realistic assumptions, to be realized from the reinsurer are in excess of the present value of the reinsurance premiums guaranteed to be paid by the ceding entity under the terms of the contract. Because non-proportional reinsurance aggregates experience, and does not indemnify the ceding entity for each policy loss, the use of statutory assumptions underlying the insured policies is inappropriate for determining any reserve credit to be taken by the ceding entity. Historical experience, pricing assumptions and asset shares shall be considered in determining if the reinsurer may be reasonably expected to pay any claims. The reserve credit taken shall only reflect these reasonable expectations. This treatment of non-proportional reinsurance is similar to the way property and casualty (P&C) reinsurance is considered. This is because these modes of reinsurance more closely follow P&C indemnification principles than life insurance formula basis, and because these coverages are very similar to excess insurance on P&C products. In determining the appropriate reserve credit, the probability of a loss penetrating to the reinsurer's level of coverage (using reasonable assumptions) must be multiplied by the expected amount of recovery. This is the same as reserve credits on coinsurance where the probability of a claim (i.e., mortality) is multiplied by the expected return (i.e., death benefit). In that the coverage is for aggregate experience, the mortality assumptions underlying any one policy risk are inappropriate to analyze the appropriate credits for non-proportional coverage.

Reserves for Reinsurance Assumed

39. In assuming any insurance risks, the assuming entity is required to establish policy reserves that are consistent with its obligations. The reserves it must establish, therefore, are also dependent upon the arrangement of reinsurance that is used. For risks transferred under the reinsurance arrangement, policy and claim reserves must be at least equal to the required reserves calculated using the same methodology and assumptions that would be used if the reinsurer had written the risk directly.

Accounting for Modified Coinsurance Arrangements

40. The following accounting applies to modified coinsurance arrangements:

a. Ceding Entity—In a modified coinsurance arrangement, the ceding entity retains the assets equal to the modified coinsurance reserve. This reserve represents a prepayment of the reinsurer's future obligation. Premiums paid or payable to the reinsurer net of any experience refunds shall result in the reduction of premium income. Policy benefit

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payments paid by the reinsurer shall reduce the ceding entity's reported policy benefits. Expense allowances paid by the reinsurer shall be reported separately in the summary of operations as they are earned. The modified coinsurance reserve is included in the category of policy reserves. The modified coinsurance reserve adjustment from period-to-period shall be reported separately in the summary of operations;

b. Assuming Entity (Reinsurer)—Premiums received or receivable by the reinsurer shall increase premium income net of any experience refunds and policy benefit payments paid by the reinsurer shall increase the reported policy benefits. Expense allowances paid by the reinsurer shall be reported separately in the summary of operations when payable. The statutory policy reserves exclude the modified coinsurance reserve. The modified coinsurance reserve adjustment from period-to-period shall be reported separately in the summary of operations. The reinsurer's accounting of its obligations shall be consistent with the ceding entity's accounting for the transfer of the obligations.

For separate accounts: The assuming reinsurer should account for the CRVM/CARVM expense allowances belonging to the assuming company when the ceding company holds the assets supporting the full account balance (prior to modification for CRVM/CARVM expense allowances) in its separate accounts as follows:

i. The assuming company records the CRVM/CARVM expense allowances in the Liabilities line, "Transfers to Separate Accounts due or accrued (net)" and includes them in the caption disclosure: "Including $_____, accrued for expense allowances recognized in reserves net of reinsurance"

ii. Period changes are recorded in the Summary of Operations Line, "Net transfers to or (from) Separate Accounts"

Accounting for Coinsurance With Funds Withheld Arrangements

41. The following accounting applies to coinsurance arrangements with funds withheld:

a. Ceding Entity—Premiums paid or payable to the reinsurer net of any experience refunds shall reduce premium income. Policy benefit payments paid by the reinsurer shall reduce the ceding entity's reported policy benefits. Expense allowances paid by the reinsurer shall be reported separately in the summary of operations as they are earned. A net reduction to policy reserves shall be taken for the portion of the obligation assumed by the reinsurer. Any amounts withheld by the ceding entity shall be recorded as a separate liability. Reporting entities filing the annual statement for life and accident and health insurers shall record any interest due or payable on the amounts withheld as a component of aggregate write-ins for miscellaneous deductions. Reporting entities filing the health annual statement shall record any interest due or payable on the amounts withheld as a component of aggregate write-ins for other income or expense.

b. Assuming Entity (Reinsurer)—Premiums received or receivable by the reinsurer net of any experience refunds shall increase premium income and policy benefit payments paid by the reinsurer shall increase the reported policy benefits. Expense allowances paid by the reinsurer shall be reported separately in the summary of operations when payable. The reinsurer shall record its share of the statutory policy reserves attributable to the business identified in the contract. Any funds withheld by the ceding entity shall be recorded as an accounts receivable. For reporting entities filing the annual statement for life and accident and health insurers shall record any interest earned or receivable on the funds withheld as a component of aggregate write-ins for miscellaneous income. Reporting entities filing the health annual statement shall record any interest earned or

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receivable on the funds withheld as a component of aggregate write-ins for other income or expense.

Uncollectible Reinsurance

42. The ceding and assuming companies must determine if reinsurance recoverables are collectible. If it is probable that reinsurance recoverables on paid or unpaid claim or benefit payments will be uncollectible, consistent with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, these amounts shall be written off through a charge to the Statement of Operations utilizing the same accounts which established the reinsurance recoverables.

Reinsurance Ceded to a Certified Reinsurer

43. A certified reinsurer is an assuming insurance entity that does not meet the requirements to be considered an authorized reinsurer in the domestic state of the ceding insurance entity, but has been certified by such state and is required to provide collateral as security for its reinsurance obligations incurred under contracts entered into or renewed on or after the effective date of certification.

44. Credit for reinsurance ceded to a certified reinsurer is permitted if security is held by or on behalf of the ceding entity in accordance with the certified reinsurer's rating assigned by the domestic state of the ceding insurance entity, and in accordance with requirements of Appendix A-785 of this manual. Such deposits are to be held under the control of the ceding entity. Additionally, any securities held under such an arrangement must be investments that the ceding entity is allowed to make under the provision of the investment sections of the insurance statutes of its domiciliary state. Other permissible arrangements include irrevocable trusts or "clean" letters of credit.

45. An upgrade in a certified reinsurer's assigned rating applies on a prospective basis, i.e., the revised collateral requirement applies only to contracts entered into or renewed on or after the effective date of the new rating (see A-785). A downgrade in a certified reinsurer's rating applies on a retroactive basis, i.e., the revised collateral requirement applies to all reinsurance obligations incurred by the assuming insurer under its certified reinsurer status. Notwithstanding a change in a certified reinsurer's rating or revocation of its certification, a reporting entity that has ceded reinsurance to such certified reinsurer is allowed a three (3)-month grace period before recording a provision for reinsurance due to collateral deficiency associated with such rating downgrade and increased collateral requirement for all reinsurance ceded to such assuming insurer under its certified reinsurer status, unless the reinsurance is found by the commissioner of the reporting entity's domestic state to be at high risk of uncollectibility.

46. With respect to reinsurance contracts involving a certified reinsurer, the contract must include a proper funding clause, which requires the certified reinsurer to provide and maintain security in an amount sufficient to avoid the imposition of any financial statement penalty on the ceding insurance entity for reinsurance ceded to the certified reinsurer. However, this does not preclude negotiation for higher contractual collateral amounts.

47. A liability is established by the ceding entity to offset credit taken in various balance sheet accounts for reinsurance ceded to a certified reinsurer in an amount proportionate to any deficiency in the amount of acceptable security that is provided by the certified reinsurer as compared to the amount of security that is required to be provided in accordance with the certified reinsurer's rating. In determining the amount of this liability, the ceding insurance entity must first determine the net obligations subject to collateral from the certified reinsurer, which is equal to the following:

a. Reserve credits taken including any Interest Maintenance Reserve (IMR) liability adjustment; plus

b. Claim liability credits taken on paid and unpaid (in course of settlement) claims recoverable; plus

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c. Other asset increases or liability reductions resulting from amounts recoverable from the assuming entity including commissions, expense allowances, modified coinsurance reserve adjustments, experience rating refunds, and estimated incurred but not reported claim liabilities; less

d. Amounts contractually due the assuming entity.

48. The liability for reinsurance with certified reinsurers due to collateral deficiency is then determined as follows:

a. The net obligations subject to collateral from the certified reinsurer as calculated in paragraph 47; less

b. The net obligations subject to collateral from the certified reinsurer as calculated in paragraph 47 multiplied by the ratio of the amount of collateral provided by the certified reinsurer to the amount of collateral required to be provided by the certified reinsurer in accordance with its rating assigned by the domestic state of the ceding entity.

49. The net liability defined in paragraphs 47 and 48 shall never be less than zero for any particular certified reinsurer. The change in liability for reinsurance with certified reinsurers is a direct charge or credit to surplus.

Unauthorized Reinsurance

50. If the reinsurer is not authorized, otherwise approved or certified to do business, the reinsurance is considered to be unauthorized. A liability is established to offset credit taken in various balance sheet accounts for reinsurance ceded to unauthorized reinsurers. Credit for reinsurance with unauthorized companies shall be permitted if the ceding entity holds securities or cash of the assuming entity equal to the reserve credit taken. Such deposits are to be held under the control of the ceding entity. Additionally, any securities held under such an arrangement must be investments that the ceding entity is allowed to make under the provision of the investment sections of the insurance statutes. Other permissible arrangements include irrevocable trusts or "clean" letters of credit. If the assuming entity is not licensed or is not an authorized reinsurer in the domiciliary state of the ceding entity or if the reinsurance does not meet required standards, the ceding entity must set up a net liability equal to the following:

a. Reserve credits taken including any IMR liability adjustment; plus

b. Claim liability credits taken on paid and unpaid (in course of settlement) claims recoverable; plus

c. Other asset increases or liability reductions resulting from amounts recoverable from the assuming entity including commissions, expense allowances, modified coinsurance reserve adjustments, experience rating refunds, and estimated incurred but not reported claim liabilities; less

d. Deposits by or funds withheld from the reinsurer, as provided for in the reinsurance treaty and in compliance with the security requirements of Appendix A-785, pledged as security for the payment of reinsurance obligations. Such deposits or funds are typically held by the ceding entity or are placed in a trust or custodial account. Amounts placed in trust or custodial accounts are held subject to withdrawal by, and under the control of, the ceding entity; less

e. Amounts of reinsurance recoverables covered by a clean, irrevocable letter of credit issued by a qualified U.S. financial institution as defined in Appendix A-785; less

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f. Amounts contractually due the assuming entity.

51. The net liability defined in paragraph 50 shall never be less than zero for any particular reinsurer. The change in liability for unauthorized reinsurance is a direct charge or credit to surplus.

Syndicated Letters of Credit

52. With a Syndicated Letter of Credit (Syndicated LC), the reinsurer enters into an agreement with a group of banks (the "Issuing Banks") and an agent bank (the "Agent"). Each Issuing Bank and the Agent is an NAIC-approved bank and a "qualified bank". This agreement requires the Agent to issue, on behalf of the each of the Issuing Banks, letters of credit in favor of the ceding insurer. The credit is issued (as an administrative matter) only through the Agent's letter of credit department. Each issuing bank signs the Syndicated LC through the Agent, as its attorney-in-fact. Syndicated LCs are consistent with A-785, in that the Syndicated LC is the legal equivalent of multiple letters of credit separately issued by each of the issuing banks. Reporting entities shall take a reduction in the liability on account of reinsurance recoverables secured by the Syndicated LC if all of the following conditions are met:

a. All listed banks on the letter of credit are qualified and meet the criteria of the NAIC SVO approved bank listing;

b. Banks are severally and not jointly liable; and

c. Specific percentages for each assuming bank are listed in the letter of credit.

Funds Held Under Reinsurance Treaties with Unauthorized Reinsurers or Certified Reinsurers

53. This liability is established for funds deposited by or contractually withheld from unauthorized reinsurers or certified reinsurers.

Accounting for Interest Maintenance Reserve (IMR)

54. The interest-related gain or loss (net of taxes) associated with the sale, transfer or reinsurance of a block of liabilities must be credited or charged to the IMR in accordance with the IMR instructions contained in the NAIC Annual Statement Instructions for Life and Accident and Health Insurance Companies.

Gains and Losses on Indemnity Reinsurance

55. Under an indemnity reinsurance arrangement the ceding entity continues to be liable to the policyholders and the reinsurer has no obligations to them except in the case of cut-through agreements. Typically the ceding entity will continue to perform all functions in connection with claims and other policyholder services. Gains and losses on indemnity reinsurance are defined as the net experience under the reinsurance contract within a calendar year. Net experience (underwriting gains or loss) includes ceded premiums, claims, expense allowances, reserve adjustments, any IMR liability adjustment, and experience refunds and dividends.

56. Losses that occur in any year of an indemnity reinsurance contract are immediately recognized. For reinsurance of in-force blocks of business, gains that occur in the initial calendar year are accounted for in accordance with Appendix A-791, paragraph 3. If a retrocession of all or a portion of an in-force block of assumed business occurs contemporaneously with assuming the in-force block of business, any resulting net gain from assuming the in-force block of business and the retrocession shall be accounted for in accordance with Appendix A-791. Any resulting net loss shall be recognized immediately in earnings.

57. For indemnity reinsurance agreements entered into for other than in-force blocks of business, the gains and losses are immediately recognized by the ceding and assuming entity.

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Recaptures and Commutations

58. A recapture or a commutation of a reinsurance agreement is a transaction which results in the complete and final settlement and discharge of all present and future obligations between the parties arising out of the agreement or a portion of the agreement. Commuted and recaptured balances shall be accounted for by writing them off through the accounts, exhibits and schedules in which they were originally recorded. The assumed reserves and reserve credits taken are eliminated by the reinsurer and ceding entity, respectively. The reinsurer and ceding entity must also make any required IMR liability adjustment changes. Any net gain or loss is reported in the summary of operations.

Deposit Accounting

59. To the extent that a reinsurance contract does not, despite its form, provide for sufficient transfer of risk amounts exchanged between the parties are to be accounted for and reported as follows:

a. At the outset of the reinsurance contract, the net consideration exchanged between the parties shall be recorded as an asset by the payer of the net considerations and as a liability by the receiver. The amount to be admitted as an asset is subject to the limitations for transactions with unauthorized reinsurers described in Appendix A-785. Throughout the life of the contract, receipts and disbursements shall be recorded through the asset/liability accounts. Income and losses shall be recognized by a party when, according to the terms of the contract, it has earned the amount and the other party has no recourse to repayment of such amount in future periods. When the contract is completed, or when there is a loss payment in excess of the deposit, any difference between consideration and recoveries shall be recorded as other miscellaneous insurance income or miscellaneous insurance loss;

b. No deduction shall be made from the policy or claim reserves on the balance sheet, schedules and exhibits.

Assumption Reinsurance

60. An entity may sell all or part of a block of insurance business through an assumption reinsurance agreement. Typically, under an assumption reinsurance arrangement, the reinsurance contract is intended to effect a novation, thereby to extinguish the ceding entity's liability to the policyholder. Assumption reinsurance requires that the reinsurer issue assumption certificates to the existing policyholders and take over responsibility for policyholder services. On occasion, the reinsurer will contract with the original entity to continue to provide such services on a fee basis or may contract with a third party. Regulatory approval of assumption reinsurance arrangements is usually required. Approval is also usually required from the policyholders, who have a predetermined time period in which to accept or reject the reinsurance transfer. After the deadline has passed, approval is considered implied for all outstanding responses. For those policyholders that reject the transfer, the reinsurance agreement typically converts to an indemnity arrangement. Under this circumstance, reinsurance accounting, as defined earlier in this statement, is to be followed.

Accounting for Assumption Reinsurance Transactions

61. Accounting for assumption reinsurance transactions involves all existing assets and liabilities with respect to the assumed policies. This involves policy reserves, policy loans, net due and deferred premiums, dividend accumulations, dividend liability, policy claims, advance premiums, unearned interest on policy loans, etc. The total effect of all of these assets and liabilities is collectively referred to as net policy liabilities.

62. Typically, because a block of in-force business has value, the sale transaction will result in a gain to the ceding entity. If the policies are somewhat mature and have reasonably large net policy liabilities,

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the transaction probably will result in a transfer of cash or other assets by the ceding entity. In this case, the net policy liabilities released by the ceding entity will be greater than the value of the assets transferred. If the policies are young and have very small net policy liabilities, the assuming entity may pay some amount in the purchase. The ceding entity is to follow accounting for indemnity reinsurance for the policies sold until it has been formally relieved of the legal liability by either consent from the policyholders or when the expiration period for objecting to the transfer has expired. Upon release of the liability or risk, the ceding entity shall recognize any gain or loss immediately. The gain or loss shall be the difference between the book value of the assets and liabilities including any unamortized IMR allocated or related to the block of business transferred. Direct and ceded balances are to be eliminated and gains are to be taken into income proportionally as the policyholders approve the transfer or at the end of the response period.

63. The assuming entity is to value the assets acquired at the date of acquisition at their fair values, and the reserves are to be established according to statutory requirements based on the benefits in the individual policies reinsured. If the liabilities exceed the assets, the difference represents goodwill that must be amortized into operations using the interest method over the life of the policies, but for a period not to exceed 10 years. Goodwill resulting from assumption reinsurance transactions shall be included in the total goodwill of an entity when calculating the amount of goodwill that is a nonadmitted asset pursuant to *SSAP No. 68—Business Combinations and Goodwill*. If the assets exceed the liabilities, the assuming entity shall record a deferred liability and amortize the amount into operations using the interest method over the expected life of the business but not to exceed ten years.

64. Upon initiation of the assumption reinsurance contract, the ceding and assuming companies are to report all balances reinsured as direct adjustments to the balance sheet. Any net gain or loss is reported as miscellaneous income when recognized.

Accounting for Non-Economic Assumption Reinsurance Transactions

65. When the sale, transfer, or reinsurance of an in-force block of business occurs between affiliated companies that is not an economic transaction, the ceding and assuming entity shall not recognize any gain or loss. The statutory liabilities and any unamortized IMR shall be transferred from the ceding entity to the assuming entity without adjustment. The assuming entity shall amortize any transferred IMR at the same rate or amount that would have occurred for the ceding entity. To the extent that the value of the assets transferred by the ceding entity or the net asset value recorded by the assuming entity differs from the liabilities including any unamortized IMR, the ceding and assuming entity shall defer and amortize their respective differences consistent with the interest method described for non-affiliated transactions.

Disclosures

66. For life and annuity reserves the financial statements shall disclose the following:

a. A description of reserve practices concerning the following:

i. Waiver of deduction of deferred fractional premiums upon death of insured;

ii. Return of portion of final premium for periods beyond the date of death;

iii. Amount of any surrender value promised in excess of the reserve as legally computed;

b. The methods employed in the valuation of substandard policies;

c. The amount of insurance, if any, for which the gross premiums are less than the net premiums according to the valuation standards;

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d. The method used to determine tabular interest, tabular less actual reserves released, and tabular cost (by formula or from the basic data for such items);

e. The method of determination of tabular interest on funds not involving life contingencies; and

f. The nature of significant other reserve changes.

67. For reinsurance of variable annuity contracts/certificates with an affiliated captive reinsurer[1], the reporting entity shall disclose the following for each transaction in the annual financial statements:

a. The type of benefits being reinsured (e.g., GMDB, GLIB and other guaranteed benefits);

b. A description that accurately conveys the purpose[2] of the transaction and significant terms of the reinsurance agreement;

c. A description of any risks retroceded to a third party as well as the ultimate risks retained by the reporting entity and its parent, subsidiaries and affiliates;

d. Whether the reporting entity reinsures variable annuities in a stand-alone captive arrangement, or a multi-product captive arrangement;

e. The amount of reserves held by the affiliated captive reinsurer, the reserve methodology for the affiliated captive reinsurer's financial statements, a brief description of the hedge target and how the reserve methodology differs from the requirements of *Actuarial Guideline XLIII—CARVM For Variable Annuities* (AG 43).

f. Identify any permitted or prescribed practices that apply to the affiliated captive reinsurer, in substance and form, following the guidance in *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*.

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[1] The purpose of this disclosure is to capture all cessions to affiliated insurance/reinsurance entities that are subject to a financial solvency regulatory system separate from that generally applicable to traditional insurers and/or reinsurers in the ceding entity's domestic jurisdiction. Given this purpose, an affiliated captive reinsurer is any entity that meets the definition of "affiliate" as established in the NAIC Model Holding Company Act. An affiliated non-traditional insurer/reinsurer is an insurance or reinsurance company that reinsures risks only from its parent or affiliates, and is subject to a financial solvency regulatory system separate from that generally applicable to traditional insurers and/or reinsurers in the ceding entity's domestic jurisdiction. For the purpose of annual statement reporting, this definition shall be presumed to include the following, subject to the cedant's rebuttal to its domicile:

a. An affiliated insurance or reinsurance company licensed, authorized or otherwise granted the authority to operate in a single United States jurisdiction under any captive insurer law, special purpose insurer law, or other similar law separate from those applicable to traditional insurers and/or reinsurers.

b. An affiliated insurance or reinsurance company licensed, authorized or otherwise granted the authority to operate in any jurisdiction outside the United States under any captive insurer law, special purpose insurer law, or other similar law separate from those applicable to traditional insurers and/or reinsurers in that non-United States jurisdiction.

c. Any other affiliated insurance or reinsurance company that by law, regulation, or order, or contract is authorized to insure or reinsure only risks from its parent or affiliate.

[2] For purposes of this disclosure, "purpose" includes, but is not limited to, the following:

a. Providing financing for the business outside of the company capital structure.

b. Managing volatility of financial results.

c. Managing risk mitigations by isolating risks in a legal entity.

d. Enhancing the ability to align hedging activity with economic results.

e. Any other sound business rationale, identified and justified.

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68. For each reinsurance agreement with an affiliated captive reinsurer (same definition as paragraph 67), provide the following information in the annual financial statements:

a. Reserve credit taken by the reporting entity for variable annuities.

b. The total amount of collateral supporting any reserve credit taken, if applicable.

c. A description of the nature of the collateral (funds withheld by the reporting entity, assets placed in trust for the benefit of the cedent, letters of credit (LOC), etc.), if applicable as well as a tabular presentation[3] of the value[4] of all assets held by or on behalf of the captive reinsurer that back the variable annuities liabilities (including capital).

69. For the disclosures noted below, disclose the amount of annuity actuarial reserves and deposit liabilities by withdrawal characteristics for the categories of general account, separate account with guarantees, separate account nonguaranteed as well as the total and percentage of the total, include a separate section for Individual Annuities, Group Annuities, and Deposit-Type Contracts (with no life contingencies). Supplementary contracts with life contingencies are reported in the appropriate Annuities section (Individual or Group).

a. Subject to discretionary withdrawal:

i. With market value adjustment, where withdrawal of funds is payable at all times, or prior to specified maturity dates where such dates are more than one year after the statement date and;

(a) In a lump sum with adjustments to reflect general changes in interest rates, or asset values since receipt of funds by the entity;

(b) In installments over five years or more, with or without a reduction in the interest rate during the installment period.

ii. At book value less current surrender charge, where the withdrawal of funds is payable at all times, or at any time within one year from the statement date in a lump sum subject to a current fixed surrender charge of 5% or more and it does not contain a meaningful bail out rate as described in paragraph 69.a.v.(d) below;

iii. At fair value, where the withdrawal of funds is payable at current market value of the assets supporting the liabilities, the assets are stated at current fair value, and the liabilities are stated at the current fair value or per unit value of the assets supporting the liabilities. These liabilities are for contracts where the customer bears the entire investment risk;

iv. Total with adjustment or at fair value;

v. At book value without adjustment (minimal or no charge or adjustment), where the withdrawal of funds is either payable at all times, or at any time (including a withdrawal on a scheduled payment date) within one year from the statement date and:

[3] List the major asset classes, such as bonds, unconditional LOC's, conditional LOC's and LOC-like instruments, parental guarantees, etc. Note which assets would not normally meet the definition of an admitted asset under SSAP No. 4.

[4] Indicate the basis of the valuation of the assets (carrying value, fair value, statutory, etc.).

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(a) In a lump sum without adjustment;

(b) In installments over less than five years, with or without a reduction in interest rate during the installment period;

(c) In a lump sum subject to a fixed surrender charge of less than 5%;

(d) In a lump sum subject to surrender charge, but such charge is waived if the credited rate falls below a specified "bail out" rate and the "bail out" rate is more than the maximum statutory valuation rate for life insurance policies for more than 20 years for new issues.

b. Not subject to discretionary withdrawal;

c. Total gross (Direct + Assumed);

d. Reinsurance ceded;

e. Total net (Net: Total gross (paragraph 69.c.) less Reinsurance ceded (paragraph 69.d.)); and

f. Amount with current surrender charge of 5% or more included in the current year in paragraph 69.a.ii. that will have less than a 5% surrender charge (and thus be reported with the amounts at book value with minimal or no charge or adjustment noted in paragraph 69.a.v.) for the first time within the year subsequent to the balance sheet year. (Note that percentage of total is not required for this item.)

70. Reconcile the total annuity reserves and deposit fund liabilities amount disclosed in the (non-life reserves) annual statement Aggregate Reserve for Life Contracts Exhibit 5 and the deposit-type contract fund liabilities from the Deposit-Type Contracts Exhibit 7 of the Life, Accident & Health Annual Statement and the corresponding lines in the Separate Accounts Statement. The reconciliation is a single presentation including all amounts from the sections on Individual Annuities, Group Annuities and Deposit-Type Contracts.

71. Reconcile total life insurance reserves amount disclosed to the appropriate sections of the Aggregate Reserves for Life Policies and Contracts Exhibit 5 of the Life, Accident and Health Annual Statement and the corresponding lines in the Separate Accounts Statement. The reconciliation is a single presentation including all amounts from the sections on Individual Life Insurance and Group Life Insurance.

72. Disclosures shall be made consistent with the interrogatories made under the "Ceded Reinsurance Report" detailed in the NAIC *Annual Statement Instructions For Life, Accident and Health Insurance Companies* in the Notes to the Financial Statements section.

73. Describe uncollectible reinsurance written off during the year reported in the following annual statement classifications, including the name or names of the reinsurer(s):

a. Claims incurred;

b. Claim adjustment expenses incurred;

c. Premiums earned; and

d. Other.

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74. Describe commutation of ceded reinsurance during the year reported in the following annual statement classifications, including the name or names of the reinsurer(s):

a. Claims incurred;

b. Claim adjustment expenses incurred;

c. Premiums earned; and

d. Other.

75. The financial statements shall disclose the impact on any reporting period in which a certified reinsurer's rating has been downgraded or its certified reinsurer status is subject to revocation and additional collateral has not been received as of the filing date. The disclosure should include the following:

a. Name of certified reinsurer downgraded or subject to revocation of certified reinsurer status and relationship to the reporting entity;

b. Date of downgrade or revocation and jurisdiction of action;

c. Collateral percentage requirements pre and post downgrade or revocation;

d. Net obligation subject to collateral;

e. As of the end of the current quarter, the estimated impact of the collateral deficiency to the reporting entity as a result of the assuming entity's downgrade or revocation of certified reinsurer status, (At year-end the actual impact of the collateral deficiency on the provision for reinsurance shall be disclosed).

f. U.S. domiciled reinsurers are eligible for certified reinsurer status. If the reporting entity is a certified reinsurer, the financial statements shall disclose the impact on any reporting period in which its certified reinsurer rating is downgraded or status as a certified reinsurer is subject to revocation. Such disclosure shall include information similar to paragraphs 75.b., 75.c. and 75.d. and the expectation of its ability to meet the increased requirements.

76. The annual audited financial statements shall:

a. Identify the applicable standard for the disclosure requirement set forth in paragraph 76.b. The applicable standard shall be (1) the Term and Universal Life Insurance Reserve Financing Model Regulation (Model #787), if such regulation has been adopted and is effective for the reporting period in the reporting entity's state of domicile; or (2) in all other cases, *Actuarial Guideline XLVIII—Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued Under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation* (AG 48). Capitalized terms used herein shall have the meanings ascribed to them in the applicable standard. The disclosures in paragraph 76.b. apply to all XXX/AXXX risks ceded under Covered Policies unless an exemption set forth in the applicable standard exempts the insurer or transaction from its scope. For example, if no exemption is available under the terms of the applicable standard for XXX/AXXX risks ceded under Covered Policies, but a state nevertheless determines that the insurer or transaction will not be required to comply in full with all aspects of the applicable standard, then the disclosures in paragraph 76.b. will still apply.

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b. Disclose the number of reinsurance contracts in which risks under Covered Policies have been ceded by the reporting entity and the following details for each such contract:

i. Whether funds consisting of Primary Security, in an amount at least equal to the Required Level of Primary Security, are held by or on behalf of the reporting entity as security under the reinsurance contract within the meaning of paragraph 19 of *Appendix A-785—Credit for Reinsurance* on a funds withheld, Trust, or modified coinsurance basis, and, if not, the amount of the shortfall;

ii. Whether funds consisting of Other Security, in an amount at least equal to any portion of the statutory reserves as to which Primary Security is not held pursuant to paragraph 76.b.i., are held by or on behalf of the reporting entity as security under the reinsurance contract within the meaning of paragraph 19 of *Appendix A-785—Credit for Reinsurance*, and, if not, the amount of the shortfall;

iii. For any contract as to which a shortfall exists and is required to be disclosed under paragraphs 76.b.i. and 76.b.ii., identify all of the following:

(a) The assuming insurer by name and NAIC code (if any);

(b) The name and effective date of the contract;

(c) The total amount of XXX/AXXX statutory reserves ceded under the contract;

(d) The Required Level of Primary Security;

(e) The actual amount of Primary Security;

(f) The actual amount of Other Security; and

(g) The amount of the shortfall(s) in Primary Security and/or Other Security required to be disclosed under paragraphs 76.b.i. and 76.b.ii.

77. The disclosures in this paragraph are for ceding entities that utilize captives to assume reserves subject to the XXX/AXXX Captive framework and should be disclosed in the annual financial statements.

a. For each captive in which a risk-based capital shortfall exists per the XXX/AXXX Captive Reinsurance Consolidated Exhibit:

i. List the name of the captive and the dollar amount of the risk-based capital shortfall.

ii. List the total adjusted capital (TAC) for the current year as reported in the Five-Year Historical Data page of the annual statement, along with the quantity of the sum of the total adjusted capital (TAC) and the total of the risk-based capital shortfalls shown in paragraph 77.a.i.

b. For each reinsurer for which a non-zero primary security shortfall is shown on the XXX/AXXX Reinsurance Primary Security Shortfall by Cession exhibit, list the name of the reinsurer and the amount of primary security shortfall. Also show the total shortfall from that exhibit across all reinsurers.

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78. Disclosures for paragraphs 79-84 apply to reinsurance contracts in effect for the current period covered by the statement and are required to be included with the annual audit report financial statements beginning with the period ended December 31, 2020, regarding reinsurance contracts. The disclosures required within paragraphs 79-84 shall be included in accompanying supplemental schedules of the annual audit report beginning in year-end 2020. If the disclosures are not applicable, an affirmative statement that no such contracts were identified is acceptable in the notes to the financial statements or the supplemental schedules. These disclosures shall be limited to reinsurance contracts entered into, renewed or amended on or after January 1, 1996. This limitation applies to the annual audit report only and does not apply to the statutory annual statement interrogatories and the property and casualty reinsurance summary supplemental filing.

79. Disclose any ceded reinsurance contracts (or multiple contracts with the same reinsurer or its affiliates) subject to A-791 that includes a provision, which limits the reinsurer's assumption of significant risks identified as in A-791. Examples of risk-limiting features include provisions such as a deductible, a loss ratio corridor, a loss cap, an aggregate limit or similar effect. If true, indicate the number of reinsurance contracts to which such provisions apply. For contracts subject to A-791, indicate if deposit accounting was applied for all contracts, which limit significant risks.

80. Disclose any ceded reinsurance contracts (or multiple contracts with the same reinsurer or its affiliates) not subject to A-791, for which reinsurance accounting was applied and includes a provision that limits the reinsurer's assumption of risk. Examples of risk-limiting features include provisions such as a deductible, a loss ratio corridor, a loss cap, an aggregate limit or similar effect. Note that a stop loss or excess of loss reinsurance agreement with deductibles or loss caps, which apply to the entire contract and are not adjustable based on other features, do not require disclosure under this paragraph. If true, indicate the number of reinsurance contracts to which such provisions apply. If affirmative, indicate if the reinsurance credit was reduced for the risk-limiting features.

81. Disclose if any ceded reinsurance contracts contain features (except reinsurance contracts with a federal or state facility) described below which result in delays in payment in form or in fact:

a. Provisions which permit the reporting of losses, or settlements are made, less frequently than quarterly or payments due from the reinsurer are not made in cash within ninety (90) days of the settlement date (unless there is no activity during the period).

b. Payment schedule, accumulating retentions from multiple years or any features inherently designed to delay timing of the reimbursement to the ceding entity.

82. Disclose if the reporting entity has reflected reinsurance accounting credit for any contracts not subject to Appendix A-791 and not yearly renewable term, which meet the risk-transfer requirements of SSAP No. 61R and identify the type of contracts and the reinsurance contracts.

a. Assumption Reinsurance – As discussed in paragraph 60, which are new for the reporting period.

83. Disclose if the reporting entity ceded any risk which is not subject to A-791 and not yearly renewable term reinsurance, under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:

a. Accounted for that contract as reinsurance under statutory accounting principles (SAP) and as a deposit under U.S. generally accepted accounting principles (GAAP); or

b. Accounted for that contract as reinsurance under U.S. GAAP and as a deposit under SAP.

If the reporting entity does not prepare U.S. GAAP financial statements or its financial statements are not part of upstream U.S. GAAP financial statements, this disclosure can be answered not applicable.

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84. If affirmative disclosure is required for paragraph 83, explain why the contract(s) is treated differently for GAAP and SAP.

85. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

86. This statement adopts with modification *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*. The statutory accounting principles established by this statement differ substantially from GAAP, reflecting much more detailed guidance, as follows:

a. Reserve credits taken by ceding companies as a result of reinsurance contracts are netted against the ceding entity's policy and claim reserves and unpaid claims;

b. First year and renewal ceding commissions on indemnity reinsurance of new business are recognized as income. Ceding commissions on ceded in-force business are included in the calculation of initial gain or loss;

c. As discussed in SSAP No. 50, statutory accounting defines deposit-type contracts as those contracts which do not include any mortality or morbidity risk. GAAP defines investment contracts as those that do not subject the insurance enterprise to significant policyholder mortality or morbidity risk. (The distinction is any mortality or morbidity risk for statutory purposes vs. significant mortality or morbidity risk for GAAP purposes.) Therefore, a contract may be considered an investment contract for GAAP purposes, and that same contract may be considered other than deposit-type for statutory purposes. A reinsurance treaty covering contracts that have insignificant mortality or morbidity risk (i.e., contracts classified as other than deposit-type contracts for statutory purposes, but investment contracts for GAAP purposes) that does not transfer that mortality or morbidity risk, but does transfer all of the significant risk inherent in the business being reinsured (e.g., lapse, credit quality, reinvestment or disintermediation risk) qualifies for reinsurance accounting for statutory reporting purposes, but would not qualify for reinsurance accounting treatment for GAAP purposes;

d. Initial gains on indemnity reinsurance of in-force blocks of business have unique accounting treatment. A portion of the initial gain (equal to the tax effect of the initial gain in surplus) is reported as commissions and expense allowances on reinsurance ceded in the statement of operations. The remainder of the initial gain is reported on a net-of-tax basis as a write-in for gain or loss in surplus in the Capital and Surplus Account. In subsequent years, the ceding entity recognizes income on the reinsurance ceded line for the net-of-tax profits that emerged on the reinsured block of business with a corresponding decrease in the write-in for gain or loss in surplus;

e. This statement prohibits recognition of a gain or loss in connection with the sale, transfer or reinsurance of an in-force block of business between affiliated entities in a non-economic transaction. Any difference between the assets transferred by the ceding entity and the liabilities, including unamortized IMR, shall be deferred and amortized under the interest method;

f. This statement requires that a liability be established through a provision reducing surplus for unsecured reinsurance recoverables from unauthorized reinsurers;

g. This statement prescribes offsetting certain reinsurance premiums.

87. This statement incorporates Appendices A-785 and A-791.

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88. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~88.~~89. This statement is effective for years beginning January 1, 2001, and, except as noted in paragraphs 89-92, applies to all reinsurance contracts entered into or amended subsequent to January 1, 1996. Changes resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

~~89.~~90. The accounting and reporting practices revised by this statement shall not apply to reinsurance agreements in force on January 1, 1996.

~~90.~~91. The requirements of paragraph 18 relating to reinsurance of deposit-type contracts shall be effective for all accounting periods beginning on or after January 1, 2001. The guidance in paragraph 19 pertaining to applying deferral guidance to YRT treaties was originally contained within *INT 02-08: Application of A-791 to YRT Reinsurance of a Block of Business* and was effective January 1, 2003. The guidance in paragraph 40 related to separate accounts was originally contained within *INT 02-04: Recognition of CARVM and CRVM Expense Allowances by the Assuming Reinsurer in a Modified Coinsurance Agreement* and was effective March 18, 2002. The guidance in paragraph 52 was originally contained within *INT 02-09: A-785 and Syndicated Letters of Credit* and was effective September 12, 2004.

~~91.~~92. Agreements which were: a) entered into on or after January 1, 1996, and which do not transfer risk shall be accounted for as deposits; b) amended on or after January 1, 1996, and which do not transfer risk shall be accounted for prospectively as deposits with the appropriate reclassification of outstanding reinsurance balances as deposits with no surplus impact. For arrangements which were amended on or after January 1, 1996, a change in accounting principle associated with the revised accounting in this statement shall be applied prospectively with no adjustment to surplus as required by SSAP No. 3.

~~92.~~93. The guidance related to certified reinsurers is applicable only to cedants domiciled in states that have enacted/promulgated the certified reinsurer collateral framework, and only for their cessions to reinsurers certified under that domestic law/rule, and shall be effective for all reporting periods beginning on or after December 31, 2012.

~~93.~~94. The disclosure for compliance with Model #787 or AG 48 shall be effective for reporting periods ending on or after December 31, 2015. The revisions adopted in November 2018 to expand liquidity disclosures are effective year-end 2019, concurrent with the inclusion of data-captured financial statement disclosures. The disclosures captured in paragraphs 78-84 which help to identify certain reinsurance contract features are effective for reporting periods ending on or after December 31, 2020.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 74—Life, Deposit-Type and Accident and Health Reinsurance*

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GLOSSARY[5]

Assume

To accept or take over an insurance risk; the reverse of cede.

Assumption Reinsurance

The form of reinsurance that extinguishes the ceding entity's liability to the policyholder. The reinsurer directly assumes all the service and financial obligations of the original entity on the block of business being assumed. Unlike indemnity reinsurance, assumption reinsurance makes the assuming entity (reinsurer) directly liable to the policyholders. In some instances, the original entity may continue to administer and service the business but, if it does so, it does it as the agent of the reinsurer.

Automatic Maximum Limit

The amount of risk which can be automatically ceded if all other conditions are met. Also called the binding authority.

Authorized Reinsurer

An assuming entity is considered an authorized reinsurer if either: 1) it is licensed in the domiciliary state of the ceding entity; 2) it is an accredited reinsurer in the domiciliary state of the ceding entity; 3) it is domiciled and licensed in a state which employs standards regarding credit for reinsurance substantially similar to those of the domiciliary state of the ceding entity and maintains surplus of at least $20 million; 4) it maintains a trust for the benefit of all its U.S. policyholders and ceding entities equal to its U.S. liabilities plus a level of surplus prescribed in the NAIC model law on credit for reinsurance; or 5) it is a reinsurer accepting risks located in jurisdictions where the laws require reinsurance to be ceded to such entity.

Automatic Reinsurance

A reinsurance agreement under which the reinsurer is obligated to accept or assume risks which meet certain specific criteria based on the ceding entity's underwriting. The reinsurance is ceded on the underwriting judgment of the ceding entity without a case by case concurrence of the reinsurer, up to a specified amount, the automatic maximum limit. The ceding entity normally is required to keep its full stipulated retention for the class of business involved on any case ceded automatically. Often certain defined types of cases are not eligible for automatic treatment. Cases in excess of the automatic maximum limits or otherwise ineligible for automatic cover can usually be submitted for facultative consideration.

Binding Authority

The amount of risk over the ceding entity's retention which can be automatically ceded if all other conditions are met. Also called the automatic maximum limit.

Catastrophe Reinsurance

A form of non-proportional reinsurance offering the ceding entity protection against excess losses from multiple claims arising out of a single event or a single large loss. Typically, reinsurance benefits will be paid if at least a specified minimum number of claims exceeding a minimum threshold amount of benefits

[5] Definitions in this glossary are adapted from the Society of Actuaries' Reinsurance Section Treaty Committee paper, "Discussion of Reinsurance Provisions in a Life Reinsurance Agreements," dated August 1, 1994, and the glossary contained in *Life, Health, and Annuity Reinsurance*, by John E. Tiller, Jr., FSA, and Denise Fagerbert, FSA (ACTEX Publications, Inc.).

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arises out of a single event. When these conditions are met, the ceding entity is reimbursed for a percentage (often 100%) of the claims over the threshold attachment point up to the maximum reinsurance benefit specified in the treaty.

Cede

To transfer an insurance risk from the entity originally issuing the policy to another insurance entity known as the reinsurer; the reverse of assume.

Certified Reinsurer

A certified reinsurer is an assuming insurance entity that does not meet the requirements to be considered authorized in the domestic state of the ceding insurer, but has been certified by such state and is required to provide collateral as security for its reinsurance obligations incurred under contracts entered into or renewed on or after the effective date of certification. The amount of security required to be provided by the certified reinsurer in order for a domestic ceding insurer to be eligible to receive financial statement credit for the reinsurance ceded is determined by an evaluation and rating that is assigned to the certified reinsurer by the domestic state of the ceding insurance entity.

Cession

The process of transferring risk from the ceding entity to the reinsurer.

Coinsurance

Indemnity life reinsurance in which the reinsurer participates in the risks and rewards of the policy provisions; the ceding entity retains its liability to the contractual relationship with the insured. The reinsurer is liable not only for its portion of the death benefit, but also all the nonforfeiture values. The reinsurer receives its proportionate share of the ceding entity's gross premium less a coinsurance allowance for commissions and other expenses. The reinsurer holds the reserve on its portion of the policy and usually retains any excess investment earnings.

Commutation

The termination of all obligations between the parties to a reinsurance agreement, normally accompanied by a final cash settlement. Commutation may be required by the reinsurance agreement or may be effected by mutual agreement.

Credit for Reinsurance

Negative entries (i.e., reductions) to the ceding entity's policy reserves and positive entries (i.e., increases) to the ceding entity's assets (amounts recoverable from reinsurers). In the context of reinsurance, the term "credit" is the opposite of its meaning in pure accounting terminology. In balance sheet accounting, a credit is a positive entry to a liability (reserve).

Cut Through Endorsement

An endorsement to a policy and referred to in a reinsurance agreement which requires that, in the event of the ceding entity's insolvency, any loss covered under the reinsurance agreement will be paid by the reinsurer directly to the insured (or a third party beneficiary).

Experience Rating Refund

A part of the profits under a reinsurance agreement which is returned to the ceding entity, allowing the ceding entity to share in a portion of profits realized on the reinsurance.

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Facultative Reinsurance

Reinsurance under which the ceding entity has the option (faculty) of submitting and the reinsurer has the option of accepting or declining individual risks. Thus it is reinsurance that the ceding entity chooses to submit to a reinsurer for its consideration and which may be ceded to the reinsurer only if the reinsurer makes an offer to reinsure. The underwriting classification assigned to the risk for purposes of the reinsurance is determined by the reinsurer. Facultative reinsurance may be ceded under the facultative terms of an automatic treaty for risks that the ceding entity cannot or does not wish to cede automatically, or it may be ceded under a purely facultative treaty.

Facultative Obligatory Reinsurance

A form of reinsurance that shares aspects of both facultative and automatic reinsurance. As with facultative reinsurance, the ceding entity has no obligation to offer specific cases to the reinsurer. However, once a case is offered to the facultative obligatory reinsurer, the case is treated largely as if it were automatic. The reinsurer receives no underwriting information and is offered the case at the ceding entity's rating with the option to accept or reject the case. While not always stated in the treaty, it is usually understood that the case will be rejected by the reinsurer only if the reinsurer does not have available capacity (i.e., its own retention and automatic retrocession facilities).

Fronting Arrangement

A situation where one insurance entity issues policies to specified applicants and reinsures all or substantially all of the risks on the insurance to another insurance entity for a fee or portion of the profits. Fronting typically is used in jurisdictions where the reinsuring entity is not licensed to do business.

Funds Withheld

Assets that would normally be paid over to a reinsurer but are withheld by the ceding entity to permit statutory credit for nonadmitted reinsurance, to reduce a potential credit risk, or to retain control over investments. Under certain conditions, the reinsurer may withhold funds from the ceding entity.

Indemnity Reinsurance

The form of reinsurance under which the ceding entity secures reinsurance as a partial or total reimbursement on the risks assumed on policies it has issued or reinsured. Under indemnity reinsurance, the reinsurer has no relationship with the original policyholders; the ceding entity continues to administer and service the insurance on which it has secured reinsurance and remains fully responsible for all the interests of the policyholders. If the reinsurer cannot or does not honor its obligations to the ceding entity, the ceding entity would still be fully liable to its policyholders.

Indemnity reinsurance may be employed, not only between a direct writing entity and a reinsurer, but also between two reinsurers when retrocession of risks is being implemented.

Mod-Co Reserve Adjustment

The net of two modified coinsurance items: the interest on reserves (payable by the ceding entity to the reinsurer) and the increase in the reserve (payable by the reinsurer to the ceding entity) or decrease in the reserve (payable by the ceding entity to the reinsurer).

Modified Coinsurance

Indemnity life insurance that differs from coinsurance only in that the reserves are retained by the ceding entity, which represents a prepayment of all or a portion of the reinsurer's future obligation. Periodically an adjustment is made to the mean reserve on deposit with the ceding entity. This is usually done

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quarterly but may be done more frequently. If the reserve increases, the increase in mean reserve less interest on the mean reserve held at the end of the previous accounting period is paid by the reinsurer to the ceding entity. If the mean reserve decreases, the decrease and interest are paid by the ceding entity to the reinsurer. The appropriate interest rate is defined in the treaty.

Net Amount at Risk

The excess of the death benefit of a policy over the policy reserve. It is the amount which must come from surplus in the event of a death claim.

Non-Proportional Reinsurance

Reinsurance that is not secured on individual lives for specific individual amounts of reinsurance, but rather reinsurance that protects the ceding entity's overall experience on its entire portfolio of business, or at least a broad segment of it. The most common forms of non-proportional reinsurance are stop loss reinsurance and catastrophe reinsurance.

Non-proportional reinsurance is a form of casualty insurance. Usually neither the premium nor continuance of coverage is guaranteed beyond a specified term.

Pool

A method of allocating reinsurance among several reinsurers. Using this method, each reinsurer receives a specified percentage of risk ceded into the pool. Percentages may vary by reinsurer.

Proportional Reinsurance

Reinsurance on a particular life for a specified amount or share generally, though not necessarily, secured at the time the policy is issued to the insured. The continuation of coverage guarantees for the reinsurance generally parallel those in the life insurance coverage reinsured. Most life reinsurance conducted in the United States is done so on a proportional basis.

Recapture

The process by which the ceding entity recovers the liabilities transferred to a reinsurer. Reinsurance treaties often provide that if a ceding entity increases its retention, the ceding entity can, under previously agreed upon terms, take back (recapture) amounts of insurance previously ceded to fill up its new retention.

Reinsurer

An insurance entity to which another insurance entity can transfer, through the mechanism of reinsurance, part or all of its risk under a policy or policies it has issued or reinsured. If the transfer of risk is secured through indemnity reinsurance, the reinsurer becomes liable to the ceding entity for the reinsured benefits while the original entity, the ceding entity, remains fully liable to its insured policyholders. If the transfer of risk is secured through assumption reinsurance, the original entity steps out of the picture and transfers all of its liabilities and responsibilities to the reinsurer, who then is henceforth directly responsible to the original policyholders.

Retention

The portion of a policy which the ceding entity retains for its own liability on life insurance. It is normally expressed in terms of face amount of insurance, especially if more than the mortality risk is reinsured. It is sometimes expressed in terms of risk amount, particularly with single premium products.

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An entity's retention is often graded by age and/or underwriting classification. Less frequently, special reduced retentions apply to specified risks, such as those engaging in aviation activities or with histories of coronary artery disease.

Retrocession

A form of reinsurance under which a reinsurer cedes to another insurer (the retrocessionaire) part or all of the reinsurance it has assumed from another entity. The original ceding entity has no relationship or recourse to the retrocessionaire and the original reinsurer remains fully liable to its client, the original ceding entity.

Retrocession provides a reinsurer with a method of accommodating its clients with respect to larger risks while still managing its own risk exposure.

Stop Loss Reinsurance

A form of non-proportional reinsurance under which the reinsurer pays some or all of a ceding entity's aggregate retained losses in excess of a predetermined dollar amount or in excess of a percentage of premium. Stop loss coverage provides protection against an excessive number or amount of claims in any given contract period.

Unauthorized Reinsurer

A reinsurer that is neither authorized, certified nor accredited (see "Authorized Reinsurer" and "Certified Reinsurer"). The ceding entity still may be able to take credit in its financial statements for reinsurance ceded to an unauthorized reinsurer if the reinsurer provides sufficient security for amounts due under the reinsurance treaty. This can usually be accomplished by permitting the ceding entity to withhold funds due the reinsurer (funds withheld approach) or by the reinsurer providing the ceding entity with a letter of credit, in a form acceptable to the state in question, or by the reinsurer establishing a trust agreement for the benefit of the ceding entity.

Yearly Renewable Term (YRT)

A form of life reinsurance under which the mortality or morbidity risks, but not the permanent plan reserves, are transferred to the reinsurer for a premium that varies each year with the amount at risk and the ages of the insureds. The amount of reinsurance, which may change annually, is generally the amount of insurance provided by the policy in excess of the primary insurer's reserve.

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Statement of Statutory Accounting Principles No. 62 – Revised

Property and Casualty Reinsurance

STATUS

Type of Issue	Common Area
Issued	Finalized March 13, 2000; Substantively revised December 5, 2009, and December 18, 2012; November 15, 2018
Effective Date	January 1, 2001; Substantive revisions in paragraphs 36.e., 102-105 and 120 (detailed in Issue Paper No. 137) effective January 1, 2010; Certified reinsurer changes effective December 31, 2012; Substantive revisions adopted November 2018 are effective January 1, 2019
Affects	Supersedes SSAP No. 75 with guidance incorporated August 2011; Nullifies and incorporates INT 02-06 and INT 02-09
Affected by	No other pronouncements
Interpreted by	INT 02-22; INT 03-02
Relevant Appendix A Guidance	A-440; A-785

STATUS **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for property and casualty reinsurance. A wide range of methods for structuring reinsurance arrangements can be employed depending on the requirements of individual companies. This statement deals with the more commonly employed methods.

SUMMARY CONCLUSION

General

2. Reinsurance is the assumption by an insurer of all or part of a risk undertaken originally by another insurer. The transaction whereby a reinsurer cedes all or part of the reinsurance it has assumed to another reinsurer is known as a retrocession.

3. Reinsurance has many beneficial purposes. Among them are that it enables an insurance entity to (a) expand its capacity, (b) share large risks with other insurers, (c) spread the risk of potential catastrophes and stabilize its underwriting results, (d) finance expanding volume by sharing the financial burden of reserves, (e) withdraw from a line or class of business, and (f) reduce its net liability to amounts appropriate to its financial resources.

4. Reinsurance agreements are generally classified as treaty or facultative. Treaty reinsurance refers to an arrangement involving a class or type of business written, while facultative reinsurance involves individual risks offered and accepted.

5. Reinsurance coverage can be pro rata (i.e., proportional reinsurance) where the reinsurer shares a pro rata portion of the losses and in the same proportion as it shares premium of the ceding entity or excess of loss (i.e., non-proportional) where the reinsurer, subject to a specified limit, indemnifies the ceding entity against the amount of loss in excess of a specified retention. Most reinsurance agreements fall into one of the following categories:

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a. Treaty Reinsurance Contracts—Pro Rata:

i. Quota Share Reinsurance—The ceding entity is indemnified against a fixed percentage of loss on each risk covered in the agreement;

ii. Surplus Share Reinsurance—The ceding entity establishes a retention or "line" on the risks to be covered and cedes a fraction or a multiple of that line on each policy subject to a specified maximum cession;

b. Treaty Reinsurance Contracts—Excess of Loss:

i. Excess Per Risk Reinsurance—The ceding entity is indemnified, subject to a specified limit, against the amount of loss in excess of a specified retention with respect to each risk covered by a treaty;

ii. Aggregate Excess of Loss Reinsurance—The ceding entity is indemnified against the amount by which the ceding entity's net retained losses incurred during a specific period exceed either a predetermined dollar amount or a percentage of the entity's subject premiums for the specific period subject to a specified limit;

c. Treaty Reinsurance Contracts—Catastrophe: The ceding entity is indemnified, subject to a specified limit, against the amount of loss in excess of a specified retention with respect to an accumulation of losses resulting from a catastrophic event or series of events;

d. Facultative Reinsurance Contracts—Pro Rata: The ceding entity is indemnified for a specified percentage of losses and loss expenses arising under a specific insurance policy in exchange for that percentage of the policy's premium;

e. Facultative Reinsurance Contracts—Excess of Loss: The ceding entity is indemnified, subject to a specified limit, for losses in excess of its retention with respect to a particular risk.

Characteristics of Reinsurance Agreements

6. Common contract provisions that may affect accounting practices include:

a. Reporting responsibility of the ceding entity—Details required and time schedules shall be established;

b. Payment terms—Time schedules, currencies intended, and the rights of the parties to withhold funds shall be established;

c. Payment of premium taxes—Customarily the responsibility of the ceding entity, a recital of nonliability of the reinsurer may be found;

d. Termination—May be on a cut-off or run-off basis. A cut-off provision stipulates that the reinsurer shall not be liable for loss as a result of occurrences taking place after the date of termination. A run-off provision stipulates that the reinsurer shall remain liable for loss under reinsured policies in force at the date of termination as a result of occurrences taking place after the date of termination until such time as the policies expire or are canceled; and

e. Insolvency clause—Provides for the survival of the reinsurer's obligations in the event of insolvency of the ceding entity, without diminution because of the insolvency.

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7. Reinsurance contracts shall not permit entry of an order of rehabilitation or liquidation to constitute an anticipatory breach by the reporting entity, nor grounds for retroactive revocation or retroactive cancellation of any contracts of the reporting entity.

Required Terms for Reinsurance Agreements

8. In addition to credit for reinsurance requirements applicable to reinsurance transactions generally, no credit or deduction from liabilities shall be allowed by the ceding entity for reinsurance recoverable where the agreement was entered into after the effective date of these requirements (see paragraphs ~~129~~130 and ~~130~~131) unless each of the following conditions is satisfied:

a. The agreement must contain an acceptable insolvency clause;

b. Recoveries due the ceding entity must be available without delay for payment of losses and claim obligations incurred under the agreement, in a manner consistent with orderly payment of incurred policy obligations by the ceding entity;

c. The agreement shall constitute the entire contract between the parties and must provide no guarantee of profit, directly or indirectly, from the reinsurer to the ceding entity or from the ceding entity to the reinsurer;

d. The agreement must provide for reports of premiums and losses, and payment of losses, no less frequently than on a quarterly basis, unless there is no activity during the period. The report of premiums and losses shall set forth the ceding entity's total loss and loss expense reserves on the policy obligations subject to the agreement, so that the respective obligations of the ceding entity and reinsurer will be recorded and reported on a basis consistent with this statement;

e. The agreement must include a proper reinsurance intermediary clause, if applicable, which stipulates that the credit risk for the intermediary is carried by the assuming insurance entity;

f. With respect to reinsurance contracts involving a certified reinsurer, the agreement must include a proper funding clause, which requires the certified reinsurer to provide and maintain security in an amount sufficient to avoid the imposition of any financial statement penalty on the ceding insurance entity for reinsurance ceded to the certified reinsurer. However, this does not preclude negotiation for higher contractual collateral amounts; and

g. With respect to retroactive reinsurance agreements, the following additional conditions apply:

i. The consideration to be paid by the ceding entity for the retroactive reinsurance must be a sum certain stated in the agreement;

ii. Direct or indirect compensation to the ceding entity or reinsurer is prohibited;

iii. Any provision for subsequent adjustment on the basis of actual experience in regard to policy obligations transferred, or on the basis of any other formula, is prohibited in connection with a retroactive reinsurance transaction, except that provision may be made for the ceding entity's participation in the reinsurer's ultimate profit, if any, under the agreement;

iv. A retroactive reinsurance agreement shall not be canceled or rescinded without the approval of the commissioner of the domiciliary state of the ceding entity.

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Reinsurance Agreements with Multiple Cedents

9. Reinsurance agreements with multiple cedents require allocation agreements. The allocation agreement can be part of the reinsurance agreement or a separate agreement. If the agreement has multiple cedents:

a. The allocation must be in writing and

b. The terms of the allocation agreement must be fair and equitable.

Reinsurance Contracts Must Include Transfer of Risk

10. The essential ingredient of a reinsurance contract is the transfer of risk[1]. The essential element of every true reinsurance agreement is the undertaking by the reinsurer to indemnify the ceding entity, i.e., reinsured entity, not only in form but in fact, against loss or liability by reason of the original insurance. Unless the agreement contains this essential element of risk transfer, no credit shall be recorded.(INT 02-22)

11. Insurance risk involves uncertainties about both (a) the ultimate amount of net cash flows from premiums, commissions, claims, and claims settlement expenses (underwriting risk) and (b) the timing of the receipt and payment of those cash flows (timing risk). Actual or imputed investment returns are not an element of insurance risk. Insurance risk is fortuitous—the possibility of adverse events occurring is outside the control of the insured.

12. Determining whether an agreement with a reinsurer provides indemnification against loss or liability (transfer of risk) relating to insurance risk requires a complete understanding of that contract and other contracts or agreements between the ceding entity and related reinsurers. A complete understanding includes an evaluation of all contractual features that (a) limit the amount of insurance risk to which the reinsurer is subject (e.g., experience refunds, cancellation provisions, adjustable features, or additions of profitable lines of business to the reinsurance contract) or (b) delay the timely reimbursement of claims by the reinsurer (e.g., payment schedules or accumulating retentions from multiple years).

13. Indemnification of the ceding entity against loss or liability relating to insurance risk in reinsurance requires both of the following:

a. The reinsurer assumes significant insurance risk under the reinsured portions of the underlying insurance agreements; and

b. It is reasonably possible that the reinsurer may realize a significant loss from the transaction.

The conditions are independent and the ability to meet one does not mean that the other has been met. A substantive demonstration that both conditions have been met is required to transfer risk.

14. The reference in paragraph 13.a. acknowledges that a ceding entity may reinsure only part of the risks associated with the underlying contracts. For example, a proportionate share of all risks or only specified risks may be reinsured. The conditions for reinsurance accounting are evaluated in relation to the reinsured portions of the underlying insurance contracts, rather than all aspects of those contracts.

15. The word “timely” is used in paragraph 12 in the ordinary temporal sense to refer to the length of time between payment of the underlying reinsured claims and reimbursement by the reinsurer. While the test for reasonable possibility of significant loss to the reinsurer provides for a present-value-based assessment of the economic characteristics of the reinsurance contract, the concept of timely reimbursement

[1] Exhibit A Questions and Answers, questions 6-19 provide additional risk transfer implementation guidance.

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relates to the transfer of insurance risk (the condition in paragraph 13.a.), not the reasonable possibility of significant loss (the condition in paragraph 13.b.). Accordingly, timely reimbursement shall be evaluated based solely on the length of time between payment of the underlying reinsured claims and reimbursement by the reinsurer.

16. Whether underwriting risk has transferred to the reinsurer depends on how much uncertainty about the ultimate amount of net cash flows from premiums, commissions, claims, and claim settlement expenses paid under a contract has been transferred to the reinsurer. A reinsurer shall not have assumed significant insurance risk under the reinsured contracts if the probability of a significant variation in either the amount or timing of payments by the reinsurer is remote. Implicit in this condition is the requirement that both the amount and timing of the reinsurer's payments depend on and directly vary with the amount and timing of claims settled by the ceding entity. Accordingly, the significance of the amount of underwriting risk transferred shall be evaluated in relation to the ceding entity's claims payments. Contractual provisions that delay timely reimbursement to the ceding entity prevent this condition from being met.

17. The ceding entity's evaluation of whether it is reasonably possible for a reinsurer to realize a significant loss from the transaction shall be based on the present value of all cash flows between the ceding and assuming companies under reasonably possible outcomes, without regard to how the individual cash flows are described or characterized. An outcome is reasonably possible if its probability is more than remote. The same interest rate shall be used to compute the present value of cash flows for each reasonably possible outcome tested. A constant interest rate shall be used in determining those present values because the possibility of investment income varying from expectations is not an element of insurance risk. Judgment is required to identify a reasonable and appropriate interest rate. To be reasonable and appropriate, that interest rate shall reflect both of the following:

a. The expected timing of payments to the reinsurer; and

b. The duration over which those cash flows are expected to be invested by the reinsurer.

18. Significance of loss shall be evaluated by comparing the present value of all cash flows, determined as described in paragraph 17, with the present value of the amounts paid or deemed to have been paid to the reinsurer. If, based on this comparison, the reinsurer is not exposed to the reasonable possibility of significant loss, the ceding entity shall be considered indemnified against loss or liability relating to insurance risk only if substantially all of the insurance risk relating to the reinsured portions of the underlying insurance agreements has been assumed by the reinsurer. In this narrow circumstance, the reinsurer's economic position is virtually equivalent to having written the insurance contract directly. This condition is met only if insignificant insurance risk is retained by the ceding entity on the retained portions of the underlying insurance contracts, so that the reinsurer's exposure to loss is essentially the same as that of the reporting entity. The assessment of that condition shall be made by comparing both of the following:

a. The net cash flows of the reinsurer under the reinsurance contract; and

b. The net cash flows of the ceding entity on the reinsured portions of the underlying insurance contracts.

If the economic position of the reinsurer relative to the insurer cannot be determined, the contract shall not qualify under the exception in this paragraph[2].

19. An extremely narrow and limited exemption is provided for contracts that reinsure either an individual risk or an underlying book of business that is inherently profitable. When substantially all of the insurance risk relating to the reinsured portions of the underlying insurance contracts has been assumed by the reinsurer, the contract meets the conditions for reinsurance accounting. To qualify under this exception,

[2] See additional detail on this topic in Exhibit A, question 19.

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no more than insignificant insurance risk on the reinsured portions of the underlying insurance contracts may be retained by the ceding entity.

20. Payment schedules and accumulating retentions from multiple years are contractual features inherently designed to delay the timing of reimbursement to the ceding entity. Regardless of what a particular feature might be called, any feature that can delay timely reimbursement violates the conditions for reinsurance accounting. Transfer of insurance risk requires that the reinsurer's payment to the ceding entity depend on and directly vary with the amount and timing of claims settled under the reinsured contracts. Contractual features that can delay timely reimbursement prevent this condition from being met. Therefore, any feature that may affect the timing of the reinsurer's reimbursement to the ceding entity shall be closely scrutinized.

21. Contracts that reinsure insurance risks over a significantly longer period than the underlying insurance contract are, in substance, financing transactions, if any of the following conditions exist:

a. Premiums are deferred over a period beyond the term of the underlying insurance contracts;

b. Losses are recognized in a different period than the period in which the event causing the loss takes place; or

c. Both events, 21.a. and 21.b., occur at different points in time.

Contracts that are in substance financing receive deposit accounting treatment.

Accounting for Reinsurance

22. Reinsurance recoverables shall be recognized in a manner consistent with the liabilities (including estimated amounts for claims incurred but not reported) relating to the underlying reinsured contracts. Assumptions used in estimating reinsurance recoverables shall be consistent with those used in estimating the related liabilities. Certain assets and liabilities are created by entities when they engage in reinsurance contracts. Reinsurance assets meet the definition of assets as defined by *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted to the extent they conform to the requirements of this statement.

23. Accounting for members of a reinsurance pool shall follow the accounting for the pool member which issued the underlying policy.(INT 03-02) Specific accounting rules for underwriting pools and associations are addressed in *SSAP No. 63—Underwriting Pools*.

24. Reinsurance recoverable on loss payments is an admitted asset. Notwithstanding the fact that reinsurance recoverables on paid losses may meet the criteria for offsetting under the provisions of *SSAP No. 64—Offsetting and Netting of Assets and Liabilities*, reinsurance recoverables on paid losses shall be reported as an asset without any available offset. Unauthorized reinsurance and reinsurance ceded to certified reinsurers is included in this asset and reflected separately as a liability to the extent required. Penalty for overdue authorized reinsurance shall be reflected as a liability.

25. Funds held or deposited with reinsured companies, whether premiums withheld as security for unearned premium and outstanding loss reserves or advances for loss payments, are admitted assets provided they do not exceed the liabilities they secure and provided the reinsured is solvent. Those funds which are in excess of the liabilities, and any funds held by an insolvent reinsured shall be nonadmitted.

26. Prospective reinsurance is defined as reinsurance in which a reinsurer agrees to reimburse a ceding entity for losses that may be incurred as a result of future insurable events covered under contracts subject to the reinsurance. Retroactive reinsurance is defined as reinsurance in which a reinsurer agrees to reimburse a ceding entity for liabilities incurred as a result of past insurable events covered under contracts subject to

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the reinsurance. A reinsurance agreement may include both prospective and retroactive reinsurance provisions.

27. The distinction between prospective and retroactive reinsurance agreements is based on whether the agreement reinsures future or past insured events covered by the underlying insurance policies. For example, in occurrence-based insurance, the insured event is the occurrence of a loss covered by the insurance contract. In claims-made insurance, the insured event is the reporting to the insurer, within the period specified by the policy, of a claim for a loss covered by the insurance agreement. A claims-made reinsurance contract that reinsures claims asserted to the reinsurer in a future period as a result of insured events that occurred prior to entering into the reinsurance agreement is a retroactive agreement. (However, a reinsurance agreement that reinsures claims reported to an insurer that are covered under currently effective claims-made insurance policies is a prospective reinsurance agreement.)

28. It is not uncommon for a reinsurance arrangement to be initiated before the beginning of a policy period but not finalized until after the policy period begins. Whether there was agreement in principle at the beginning of the policy period and, therefore, the agreement is substantively prospective shall be determined based on the facts and circumstances. However, except as respects business assumed by a U.S. reinsurer from ceding companies domiciled outside the U.S. and not affiliated with such reinsurer, or business assumed by a U.S. reinsurer where either the lead reinsurer or a majority of the capacity on the agreement is domiciled outside the U.S. and is not affiliated with such reinsurer, if an agreement entered into, renewed or amended on or after January 1, 1994 has not been finalized, reduced to a written form and signed by the parties within nine months after the commencement of the policy period covered by the reinsurance arrangement, then the arrangement is presumed to be retroactive and shall be accounted for as a retroactive reinsurance agreement. This presumption shall not apply to: (a) facultative reinsurance contracts, nor to (b) reinsurance agreements with more than one reinsurer which are signed by the lead reinsurer (i.e., the reinsurer setting the terms of the agreement for the reinsurers) within nine months after the commencement of the policy period covered by the reinsurance agreement, nor to (c) reinsurance agreements with more than one reinsurer (whether signed by the lead reinsurer or not) which were entered into, renewed or amended on or before December 31, 1996, (and which were not renewed or amended after that date) if reinsurers representing more than 50% of the capacity on the agreement have signed cover notes, placement slips or similar documents describing the essential terms of coverage and exclusions within nine months after the commencement of the policy period covered by the reinsurance arrangement. Also exempt from this presumption are reinsurance agreements where one of the parties is in conservation, rehabilitation, receivership or liquidation proceedings.

29. Prospective and retroactive provisions included within a single agreement shall be accounted for separately. If separate accounting for prospective and retroactive provisions included within a single agreement is impracticable, the agreement shall be accounted for as a retroactive agreement provided the conditions for reinsurance accounting are met.

Accounting for Prospective Reinsurance Agreements

30. Amounts paid for prospective reinsurance that meet the conditions for reinsurance accounting shall be reported as a reduction of written and earned premiums by the ceding entity and shall be earned over the remaining contract period in proportion to the amount of reinsurance protection provided or, if applicable, until the reinsurer's maximum liability under the agreement has been exhausted. If the amounts paid are subject to adjustment and can be reasonably estimated, the basis for amortization shall be the estimated ultimate amount to be paid. Reinstatement premium, if any, shall be earned over the period from the reinstatement of the limit to the expiration of the agreement.

31. Changes in amounts of estimated reinsurance recoverables shall be recognized as a reduction of gross losses and loss expenses incurred in the current period statement of income. Reinsurance recoverables on paid losses shall be reported as an asset, reinsurance recoverables on loss and loss adjustment expense payments, in the balance sheet. Reinsurance recoverables on unpaid case-basis and incurred but not reported

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losses and loss adjustment expenses shall be netted against the liability for gross losses and loss adjustment expenses.

32. Prospective reinsurance agreements that meet the conditions for reinsurance accounting shall only reflect reinsurance credit for the portion of risk which is ceded. Provisions that would limit the reinsurer's losses (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions) caused by any applicable risk limiting provision(s) shall be reflected adjustments to ceded premiums, commissions or losses. Reporting entities shall only take credit for reinsurance, i.e., record a reinsurance recoverable, for non-proportional reinsurance when and to the extent that incurred losses on the underlying subject business exceed the attachment point of the applicable reinsurance contract(s).

Accounting for Retroactive Reinsurance Agreements

33. Certain reinsurance agreements which transfer both components of insurance risk cover liabilities which occurred prior to the effective date of the agreement. Due to potential abuses involving the creation of surplus to policyholders and the distortion of underwriting results, special accounting treatment for these agreements is warranted.

34. All retroactive reinsurance agreements entered into, renewed or amended on or after January 1, 1994 (including subsequent development of such transactions) shall be accounted for and reported in the following manner:

a. The ceding entity shall record, without recognition of the retroactive reinsurance, loss and loss expense reserves on a gross basis on the balance sheet and in all schedules and exhibits;

b. The assuming entity shall exclude the retroactive reinsurance from loss and loss expense reserves and from all schedules and exhibits;

c. The ceding entity and the assuming entity shall report by write-in item on the balance sheet, the total amount of all retroactive reinsurance, identified as retroactive reinsurance reserve ceded or assumed, recorded as a contra-liability by the ceding entity and as a liability by the assuming entity;

d. The ceding entity shall, by write-in item on the balance sheet, restrict surplus resulting from any retroactive reinsurance as a special surplus fund, designated as special surplus from retroactive reinsurance account;

e. The surplus gain from any retroactive reinsurance shall not be classified as unassigned funds (surplus) until the actual retroactive reinsurance recovered exceeds the consideration paid;

f. The special surplus from retroactive reinsurance account for each respective retroactive reinsurance agreement shall be reduced at the time the ceding entity begins to recover funds from the assuming entity in amounts exceeding the consideration paid by the ceding entity under such agreement, or adjusted as provided in paragraph 34.j.;

g. For each agreement, the reduction in the special surplus from retroactive reinsurance account shall be limited to the lesser of (i) the actual amount recovered in excess of consideration paid or (ii) the initial surplus gain resulting from the respective retroactive reinsurance agreement. Any remaining balance in the special surplus from retroactive reinsurance account derived from any such agreement shall be returned to unassigned funds (surplus) upon elimination of all policy obligations subject to the retroactive reinsurance agreement;

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h. The ceding entity shall report the initial gain arising from a retroactive reinsurance transaction (i.e., the difference between the consideration paid to the reinsurer and the total reserves ceded to the reinsurer) as a write-in item on the statement of income, to be identified as Retroactive Reinsurance Gain and included under Other Income;

i. The assuming entity shall report the initial loss arising from a retroactive reinsurance transaction, as defined in the preceding paragraph 34.g., as a write-in item on the statement of income, to be identified as Retroactive Reinsurance Loss and included under Other Income;

j. Any subsequent increase or reduction in the total reserves ceded under a retroactive reinsurance agreement shall be reported in the manner described in the preceding paragraphs 34.h. and 34.i., in order to recognize the gain or loss arising from such increase or reduction in reserves ceded. The Special Surplus from Retroactive Reinsurance Account write-in entry on the balance sheet shall be adjusted, upward or downward, to reflect such increase or reduction in reserves ceded. The Special Surplus from Retroactive Reinsurance Account write-in entry shall be equal to or less than the total ceded reserves under all retroactive reinsurance agreements in-force as of the date of the financial statement. Special surplus arising from a retroactive reinsurance transaction shall be considered to be earned surplus (i.e., transferred to unassigned funds (surplus)) only when cash recoveries from the assuming entity exceed the consideration paid by the ceding entity as respects such retroactive reinsurance transaction; and

k. The consideration paid for a retroactive reinsurance agreement shall be reported as a decrease in ledger assets by the ceding entity and as an increase in ledger assets by the assuming entity.

(For an illustration of ceding entity accounting entries see question 31 in Exhibit A.)

35. Portfolio reinsurance is the transfer of an insurer's entire liability for in force policies or outstanding losses, or both, of a segment of the insurer's business. Loss portfolio transactions are to be accounted for as retroactive reinsurance.

36. The accounting principles for retroactive reinsurance agreements in paragraph 34 shall not apply to the following types of agreements (which shall be accounted for as prospective reinsurance agreements unless otherwise provided in this statement):

a. Structured settlement annuities for individual claims purchased to implement settlements of policy obligations;

b. Novations, (i.e., (i) transactions in which the original direct insurer's obligations are completely extinguished, resulting in no further exposure to loss arising on the business novated or (ii) transactions in which the original assuming entity's obligations are completely extinguished) resulting in no further exposure to loss arising on the business novated, provided that (1) the parties to the transaction are not affiliates (or if affiliates, that the transaction has the prior approval of the domiciliary regulators of the parties) and (2) the accounting for the original reinsurance agreement will not be altered from retroactive to prospective;

c. The termination of, or reduction in participation in, reinsurance treaties entered into in the ordinary course of business;

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d. Intercompany reinsurance agreements, and any amendments thereto, among companies 100% owned by a common parent or ultimate controlling person provided there is no gain in surplus as a result of the transaction; or

e. Reinsurance/retrocession agreements that meet the criteria of property/casualty run-off agreements described in paragraphs 102-105.

37. Retroactive reinsurance agreements resulting in surplus gain to the ceding entity (with or without risk transfer) entered into between affiliates or between insurers under common control (as those terms are defined in Appendix A-440) shall be reported as follows:

a. The consideration paid by the ceding entity shall be recorded as a deposit and reported as a nonadmitted asset; and

b. No deduction shall be made from loss and loss adjustment expense reserves on the ceding entity's balance sheet, schedules, and exhibits.

38. The accounting and reporting provisions applicable to retroactive reinsurance apply to all transactions transferring liabilities in connection with a court-ordered rehabilitation, liquidation, or receivership. The requirement to include stipulated contract provisions in the reinsurance agreements shall not apply to these transactions, with written approval of the ceding entity's domiciliary commissioner.

39. Novations meeting the requirements of paragraph 36.b. shall be accounted for as prospective reinsurance agreements. The original direct insurer, or the original assuming insurer, shall report amounts paid as a reduction of written and earned premiums, and unearned premiums to the extent that premiums have not been earned. Novated balances (e.g., loss and loss adjustment expense reserves) shall be written off through the accounts, exhibits, and schedules in which they were originally recorded. The assuming insurer shall report amounts received as written and earned premiums, and obligations assumed as incurred losses in the statement of income.

Deposit Accounting

40. To the extent that a reinsurance agreement does not, despite its form, transfer both components of insurance risk, all or part of the agreement shall be accounted for and reported as deposits in the following manner:

a. At the outset of the reinsurance agreement, the net consideration paid by the ceding entity (premiums less commissions or other allowances) shall be recorded as a deposit by the ceding company and as a liability by the assuming entity. The deposit shall be reported as an admitted asset by the ceding company if (i) the assuming company is licensed, accredited or otherwise qualified in the ceding company's state of domicile as described in Appendix A-785 or (ii) there are funds held by or on behalf of the ceding company which meet the requirements of paragraph 19 of Appendix A-785;

b. At subsequent reporting dates, the amount of the deposit/liability shall be adjusted by calculating the effective yield on the deposit agreement to reflect actual payments to date (receipts and disbursements shall be recorded through the deposit/liability accounts) and expected future payments (as discussed below), with a corresponding credit or charge to interest income or interest expense;

c. The calculation of the effective yield shall use the estimated amount and timing of cash flows. If a change in the actual or estimated timing or amount of cash flows occurs, the effective yield shall be recalculated to reflect the revised actual or estimated cash flows. The deposit shall be adjusted to the amount that would have existed at the reporting date

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had the new effective yield been applied since the inception of the reinsurance agreement. Changes in the carrying amount of the deposit asset/liability resulting from changes in the effective yield shall be recorded as interest income or interest expense;

d. It shall be assumed that any cash transactions for the settlement of losses will reduce the asset/liability accounts by the amount of the cash transferred. When the remaining losses are revalued upward, an increase in the deposit liability shall be recorded as interest expense – by the assuming company. Conversely, the ceding company shall increase its deposit (asset) with an offsetting credit to interest income; and increase its outstanding loss liability with an offsetting charge to incurred losses;

e. No deduction shall be made from the loss and loss adjustment expense reserves on the ceding company's Statement of Financial Position, schedules, and exhibits;

f. The assuming company shall record net consideration to be returned to the ceding company as a liability.

(For an illustration of the provisions of paragraph 40, see Exhibit C)

41. Deposit accounting shall not be used to avoid loss recognition that would otherwise be required. For example, if the ceding entity has no future coverage relating to the deposit with the reinsurer, the deposit is not recoverable.

Assumed Reinsurance

42. Reinsurance premiums receivable at the end of the accounting period are combined with direct business receivables and reported as agents' balances or uncollected premiums. Where the ceding entity withholds premium funds pursuant to the terms of the reinsurance agreement, such assets shall be shown by the assuming entity as funds held by or deposited with reinsured companies. Reporting entities shall record any interest earned or receivable on the funds withheld as a component of aggregate write-ins for miscellaneous income.

43. If the assuming entity receives reinsurance premium prior to the effective date of the reinsurance contract, consistent with *SSAP No. 53—Property and Casualty Contracts-Premiums*, paragraph 15, advance premiums shall be reported as a liability in the statutory financial statement and not considered income until the effective date of the coverage. Such amounts are not included in written premium or the unearned premium reserve. If the assuming entity receives reinsurance premium after the effective date of the reinsurance contract but prior to the due date, the amount received shall be reported as a reduction of the asset for deferred but not yet due (earned but unbilled premiums).

44. Reinsurance premiums more than 90 days overdue shall be nonadmitted except (a) to the extent the assuming entity maintains unearned premium and loss reserves as to the ceding entity, under principles of offset accounting as discussed in SSAP No. 64, or (b) where the ceding entity is licensed and in good standing in assuming entity's state of domicile. Reinsurance premiums are due pursuant to the original contract terms (as the agreement stood on the date of execution). In the absence of a specific contract date, reinsurance premiums will be deemed due thirty (30) days after the date on which (i) notice or demand of premium due is provided to the ceding entity or (ii) the assuming entity books the premium (see *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*).

45. A lag will develop between the time of the entry of the underlying policy transaction on the books of the ceding entity and the transmittal of information and entry on the books of the assuming entity. Assuming companies shall estimate unreported premiums and related costs to the extent necessary to

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prevent material distortions in the loss development contained in the assuming entity's annual statement schedules where calendar year premiums are compared to accident year losses.

46. Proportional reinsurance (i.e., first dollar pro rata reinsurance) premiums shall be allocated to the appropriate annual statement lines of business in the Underwriting and Investment exhibits. Non-proportional assumed reinsurance premiums shall be classified as reinsurance under the appropriate subcategories.

47. Assumed retroactive reinsurance premiums shall be excluded from all schedules and exhibits as addressed in paragraph 34.

48. Amounts payable by reinsurers on losses shall be classified as unpaid losses. Assumed reinsurance payable on paid losses shall be classified as a separate liability item on the balance sheet. IBNR losses on assumed reinsurance business shall be netted with ceded losses on the balance sheet and listed separately by annual statement line of business in the Underwriting and Investment exhibits.

Ceded Reinsurance

49. Ceded reinsurance premiums payable (net of ceding commission) shall be classified as a liability. Consistent with SSAP No. 64, ceded reinsurance premiums payable may be deducted from amounts due from the reinsurer, such as amounts due on assumed reinsurance, when a legal right of offset exists.

50. With regard to reinsurance premium paid prior to the effective date of the contract, the ceding entity shall reflect the prepaid item as a write-in admitted asset and it should not be recognized in the income statement until the effective date of the coverage. Such amounts are not included in ceded written premiums or ceded unearned premium but should be subject to impairment analysis. With regard to reinsurance premium paid by ceding entity after the reinsurance contract is in effect but prior to the due date, the ceding entity shall treat this item as a reduction to the liability for ceded reinsurance premiums payable. That liability reflects not only premiums unpaid but also amounts booked but deferred and not yet due.

51. Amounts withheld by the ceding entity that would otherwise be payable under the reinsurance agreement shall be reported as funds held by entity under reinsurance treaties. Reporting entities shall record any interest due or payable on the amounts withheld as a component of aggregate write-ins for miscellaneous income.

52. Ceded reinsurance transactions shall be classified in the annual statement line of business which relates to the direct or assumed transactions creating the cession or retrocession.

53. Ceded retroactive reinsurance premiums shall be excluded from all schedules and exhibits as addressed in paragraph 34.

54. Reinsurance accounting shall not be allowed for modeled trigger securitizations. Modeled trigger securitization transactions do not result in the kind of indemnification (in form and in fact) required by this SSAP, and are therefore not eligible for reinsurance accounting. Modeled trigger transactions should be evaluated as securitization transactions rather than as reinsurance transactions and should receive the accounting treatment recommended for securitization transactions.

Adjustable Features/Retrospective Rating

55. Reinsurance treaties may provide for adjustment of commission, premium, or amount of coverage, based on loss experience. The accounting for common examples is outlined in the following paragraphs:

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Commission Adjustments

56. An accrual shall be maintained for the following adjustable features based upon the experience recorded for the accounting period:

a. Contingent or Straight Profit—The reinsurer returns to the ceding entity a stipulated percentage of the profit produced by the business assumed from the ceding entity. Profit may be calculated for any specified period of time, but the calculation is often based on an average over a period of years; and

b. Sliding Scale—A provisional rate of commission is paid over the course of the agreement, with a final adjustment based on the experience of the business ceded under the agreement.

Premium Adjustments

57. If the reinsurance agreement incorporates an obligation on the part of the ceding entity to pay additional premium to the assuming entity based upon loss experience under the agreement, a liability in the amount of such additional premium shall be recognized by the ceding entity during the accounting period in which the loss event(s) giving rise to the obligation to pay such additional premium occur(s). The assuming entity shall recognize an asset in a consistent manner. If the reinsurance agreement incorporates an obligation on the part of the assuming entity to refund to the ceding entity any portion of the consideration received by the assuming entity based upon loss experience under the agreement, an asset in the amount of any such refund shall be recognized by the ceding entity during the accounting period in which the loss event(s) giving rise to the obligation to make such refund occur(s). The initial provisional or deposit premium is recalculated retrospectively, based on loss experience under the agreement during a specified period of time; the calculation is often based on an average over a period of years. The assuming entity shall recognize a liability in a consistent manner.

Adjustments in the Amount of Coverage

58. The amount of coverage available for future periods is adjusted, upward or downward, based on loss experience under the agreement during a specified period of time. If the reinsurance agreement incorporates a provision under which the reinsurance coverage afforded to the ceding entity may be increased or reduced based upon loss experience under the agreement, an asset or a liability shall be recognized by the ceding entity in an amount equal to that percentage of the consideration received by the assuming entity which the increase or reduction in coverage represents of the amount of coverage originally afforded. The asset or liability shall be recognized during the accounting period in which the loss event(s) (or absence thereof) giving rise to the increase or decrease in reinsurance coverage occur(s), and shall be amortized over all accounting periods for which the increased or reduced coverage is applicable. The term "consideration" shall mean, for this purpose, the annualized deposit premium for the period used as the basis for calculating the adjustment in the amount of coverage to be afforded thereafter under the agreement.

59. The ceding entity and the assuming entity shall account for changes in coverage in the same manner as changes in other contract costs. For example, the effects of decreases in coverage without a commensurate reduction in premium shall be recognized as a loss by the ceding entity and as a gain by the assuming entity when the event causing the decrease in coverage takes place.

60. Changes in either the probability or amount of potential future recoveries are considered a change in coverage. For example, if the contract limit stayed the same but the ceding entity could not receive any recoveries unless losses forthe industry as a whole reached a certain level, coverage has been reduced. What matters is not the specific contract provisions regarding coverage, but whether the probability or amount of potential future recoveries has increased or decreased as a result of those provisions.

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Multiple-Year Retrospectively-Rated Contracts

61. Many short-duration insurance and reinsurance contracts have retrospective rating provisions. A retrospectively-rated contract is a multiple-year contract in which events in one period of the contract create rights and obligations in another. For example, if losses above a certain level occur in one contract year, premiums increase in future years unless the ceding entity compensates the reinsurer through a settlement adjustment. The ceding entity has an obligation because it must pay either the settlement adjustment or the higher future premiums.

62. An insurer (ceding entity) may enter into a multiple-year retrospectively-rated reinsurance contract with a reinsurer (assuming entity). Examples of these contracts may include transactions referred to as funded catastrophe covers. These contracts include a retrospective rating provision that provides for at least one of the following based on contract experience:

a. Changes in the amount or timing of future contractual cash flows, including premium adjustments, settlement adjustments, or refunds to the ceding entity; or

b. Changes in the contract's future coverage.

63. A critical distinguishing feature of these contracts is that part or all of the retrospective rating provision is obligatory such that the retrospective rating provision creates future rights and obligations as a result of past events. Therefore, a retrospectively-rated contract that could be cancelled without further obligation (because it does not create rights and obligations that will be realized in a future period) is excluded.

64. The principal issues in accounting for a multiple-year retrospectively-rated contract involve how to recognize and measure assets and liabilities resulting from the obligatory retrospective rating provisions. While it may be difficult for some types of multiple–year retrospectively-rated contracts to pass the risk transfer test, the recognition and measurement questions are present regardless of whether the contract transfers risk. In fact, the questions become clearly evident with contracts that meet the risk transfer test and are accounted for as reinsurance.

Multiple-Year Retrospectively-Rated Contracts by Ceding and Assuming Entities

65. To be accounted for as reinsurance, a reinsurance contract must meet all of the following conditions:

a. The contract shall not contain features that prevent the risk transfer criteria from being reasonably applied and the risk transfer criteria shall be met.

b. The ultimate premium expected to be paid or received under the contract shall be reasonably estimable and allocable in proportion to the reinsurance protection provided.

If any of these conditions are not met, a deposit method of accounting shall be applied by the ceding and assuming entities.

66. The condition in paragraph 65.a. applies to a contract and determining the substance of a contract is a judgmental matter. If an agreement with a reinsurer consists of both risk transfer and non-risk transfer coverages that have been combined into a single legal document, those coverages must be considered separately for accounting purposes. This statement does not intend for different kinds of exposures combined in a program of reinsurance to be evaluated for risk transfer and accounted for together because that would allow contracts that do not meet the conditions for reinsurance accounting to be accounted for as reinsurance by being designated as part of a program that in total meets the conditions for reinsurance accounting.

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67. Recognizing a smaller asset based on potential unfavorable loss development implies that claim liabilities are understated at the financial reporting date. Accordingly, changes in estimates of claim liabilities shall not be recognized in measuring the related asset until the change in estimate takes place.

Obligatory Retrospective Rating Provisions

68. This guidance discusses how the guidance on multiple-year retrospectively-rated contracts is based on the concept that there is a substantive difference between a contract that contains an obligatory retrospective rating provision and one that does not. This distinction is derived from *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, which requires recognition of liabilities (which are defined as present obligations) as of a financial reporting date but prohibits recognition of losses and expenses that will result from future events. For example, it may be a virtual certainty that an entity will pay employee salaries next year. But because there is no present obligation to pay those salaries, they are not recognized today.

69. Similarly, under SSAP No. 5R even if there is a high probability that an asset will be impaired in the future or a liability incurred in the future, the conditions for accrual have not been met because there is no present impairment or obligation to be recognized. Consistent with this principle, the guidance on multiple-year retrospectively rated contracts does not permit recognition of the effects of retrospective rating provisions unless those provisions are obligatory.

Allocation of Certain Payments Between Coverage and Past Losses

70. This guidance addresses a circumstance in which, under a multiple-year retrospectively rated reinsurance contract, the ceding entity has to make additional payments to the reinsurer but the ceding entity also receives expanded coverage. The single payment is allocated to the two separate transactions. In one transaction, the ceding entity has acquired an asset by making a payment to the reinsurer in exchange for expanded coverage. In the other, the ceding entity has incurred a loss or liability to the extent that it is reimbursing the reinsurer for past losses. Because a variety of factors may affect the value of reinsurance coverage at any point in time, the most appropriate measure of the value of additional coverage generally is the price of the initial coverage. For example, if coverage of $6.00 was acquired for a $1.00 premium, and the ceding entity would pay $4.00 more for another $6.00 of coverage if a loss occurs, the most relevant measure of the amount of premium that relates to the new coverage would be $1.00. The other $3.00 presumably is a reimbursement for the loss that has been incurred.

Contractual Termination Features

71. In some circumstances, the ceding entity will be relieved of its obligation if the reinsurer cancels the contract and only has to pay additional amounts if either:

a. The contract remains in force; or

b. The ceding entity cancels before the end of the contract term.

Unless the reinsurer has terminated the contract, the ceding entity has an obligation for the additional amounts and must recognize the related liability. The effect of termination, which is to relieve the ceding entity of its liability, shall not be recognized until termination takes place.

72. If either party entering into a new contract in consideration for canceling a retrospectively-rated contract would not have agreed to cancel the existing retrospectively-rated contract unless a new contract were entered into, the two contracts are, in effect, the same contract for purposes of measuring assets and liabilities and shall be accounted for in that way.

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Impairment

73. Include as a nonadmitted asset, amounts accrued for premium adjustments on retrospectively rated reinsurance agreements with respect to which all uncollected balances due from the ceding company have been classified as nonadmitted.

74. The amount of the asset to be recognized may be affected by credit risk, and appropriate impairment shall be recognized for any amounts deemed uncollectible. The relevant recorded claim liability at that date represents the ceding entity's best estimate of the expected ultimate claim liability and is the liability that must be used in measuring the refundable amount based on contract experience to date.

Commissions

75. Commissions payable on reinsurance assumed business shall be included as an offset to Agents' Balances or Uncollected Premiums. Commissions receivable on reinsurance ceded business shall be included as an offset to Ceded Reinsurance Balances Payable.

76. If the ceding commission paid under a reinsurance agreement exceeds the anticipated acquisition cost of the business ceded, the ceding entity shall establish a liability, equal to the difference between the anticipated acquisition cost and the reinsurance commissions received, to be amortized pro rata over the effective period of the reinsurance agreement in proportion to the amount of coverage provided under the reinsurance contract.

Unauthorized Reinsurance

77. If the assuming reinsurer is not authorized, otherwise approved or certified to do business in the ceding entity's domiciliary state, the assumed reinsurance is considered to be unauthorized. A provision is established to offset credit taken in various balance sheet accounts for reinsurance ceded to unauthorized reinsurers. Credit for reinsurance with unauthorized reinsurers shall be permitted to the extent the ceding entity holds collateral in accordance with Appendix A-785. If the assuming reinsurer is not licensed or is not an authorized reinsurer in the domiciliary state of the ceding entity or if the reinsurance does not meet required standards, the ceding entity must set up a provision for reinsurance liability in accordance with the NAIC Annual Statement Instructions for Property and Casualty Insurance Companies Schedule F.

78. The provision defined in paragraph 77 shall never be less than zero for any particular reinsurer. The change in liability for unauthorized reinsurance is a direct charge or credit to surplus.

Reinsurance Ceded to a Certified Reinsurer

79. The term certified reinsurer shall have the same meaning as set forth in the Appendix A-785.

80. Credit for reinsurance ceded to a certified reinsurer is permitted if security is held by or on behalf of the ceding entity in accordance with the certified reinsurer's rating assigned by the domestic state of the ceding insurance entity, and in accordance with Appendix A-785 of this manual. However, nothing in this guidance would prohibit the parties to a reinsurance agreement from agreeing to provisions establishing security requirements that exceed the minimum security requirements established for certified reinsurers.

81. An upgrade in a certified reinsurer's assigned rating applies on a prospective basis, i.e., the revised collateral requirement applies only to contracts entered into or renewed on or after the effective date of the new rating (see A-785). A downgrade in a certified reinsurer's rating applies on a retroactive basis, i.e., the revised collateral requirement applies to all reinsurance obligations incurred by the assuming insurer under its certified reinsurer status. Notwithstanding a change in a certified reinsurer's rating or revocation of its certification, a reporting entity that has ceded reinsurance to such certified reinsurer is allowed a three (3)-month grace period before recording a provision for reinsurance due to collateral deficiency associated with

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such rating downgrade and increased collateral requirement for all reinsurance ceded to such assuming insurer under its certified reinsurer status, unless the reinsurance is found by the commissioner of the reporting entity's domestic state to be at high risk of uncollectibility.

82. A provision is established by the ceding entity to offset credit taken in various balance sheet accounts for reinsurance ceded to a certified reinsurer in an amount proportionate to any deficiency in the amount of acceptable security that is provided by the certified reinsurer as compared to the amount of security that is required to be provided in accordance with the certified reinsurer's rating. The calculation of the provision for a collateral shortfall is separate from the calculation of the provision for overdue reinsurance ceded to certified reinsurers and shall be calculated in accordance with the NAIC Annual Statement Instructions for Property and Casualty Insurance Companies.

83. The provision defined in paragraph 82 shall never be less than zero for any particular certified reinsurer. The change in liability for reinsurance with certified reinsurers is a direct charge or credit to surplus.

Funds Held Under Reinsurance Treaties

84. This liability is established for funds deposited by or contractually withheld from reinsurers or reinsurers.

Provision for Reinsurance

85. The NAIC Property/Casualty Annual Statement Instructions, Schedule F, Part 3 – Ceded Reinsurance, references the provision for overdue reinsurance, which provides for a minimum reserve for uncollectible reinsurance with an additional reserve required if an entity's experience indicates that a higher amount should be provided. The minimum reserve provision for reinsurance is recorded as a liability and the change between years is recorded as a gain or loss directly to unassigned funds (surplus). Any reserve over the minimum amount shall be recorded on the statement of income by reversing the accounts previously utilized to establish the reinsurance recoverable.

86. The provision for reinsurance is calculated separately for unauthorized, authorized and certified reinsurers. An authorized reinsurer is licensed, accredited or approved by the ceding entity's state of domicile; a certified reinsurer is certified by the ceding entity's state of domicile; an unauthorized reinsurer is not so licensed, accredited, approved or certified.

Asbestos and Pollution Contracts – Counterparty Reporting Exception

87. Upon approval by the domiciliary regulator(s) of the ceding entity (either the original direct insurer in the case of a reinsurance agreement or the original assuming reinsurer in the case of a retrocession agreement), an exception may be allowed with respect to a retroactive reinsurance agreement providing substantially duplicate coverage as prior reinsurance agreements on asbestos and/or pollution exposures, including reinsurance provided through an affiliated reinsurer that retrocedes to the retroactive reinsurance counterparty. Under this exception, a reporting entity may aggregate reinsurers into one line item in Schedule F reflecting the counterparty under the retroactive agreement for the purposes of determining the Provision for Reinsurance regarding overdue amounts paid by the retroactive counterparty (both authorized and unauthorized). This exception would allow the Provision for Reinsurance to be reduced by reflecting that amounts have been recovered by the reporting entity under the duplicate coverage provided by the retroactive contract, and that inuring balances from the original contract(s) are payable to the retroactive counterparty. In addition, such approval would also permit the substitution of the retroactive counterparty for authorized original reinsurers without overdue balances for purposes of reporting on the primary section of the annual statement Schedule F. An agreement must meet all of the requirements in paragraphs 87.a. through 87.e. in order to be considered for this exception.

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a. The underlying agreement clearly indicates the credit risk associated with the collection of the reporting entity's inuring reinsurance recoverables and losses related to the credit risk will be covered by the retroactive reinsurance counterparty.

b. The retroactive reinsurance agreement must transfer significant risk of loss.

c. The assuming retroactive reinsurance counterparty must have a financial strength rating from at least two nationally recognized statistical rating organizations (NRSRO), the lowest of which is higher than or equal to the NRSRO ratings of the underlying third-party reinsurers.

d. The transaction is limited to reinsurance recoverables attributable to asbestos, and/or pollution.

e. The recoverables from the inuring reinsurers remain subject to credit analysis and contingent liability analysis.

88. With the approval of the reporting entity's domestic state commissioner pursuant to the applicable state credit for reinsurance law regarding the use of other forms of collateral acceptable to the commissioner, the reporting entity shall present the amount of other approved security related to the retroactive reinsurance agreement as an "Other Allowed Offset Item" with respect to the uncollateralized amounts recoverable from unauthorized reinsurers for paid and unpaid losses and loss adjustment expenses under the original reinsurance contracts. Amounts approved as "Other Allowed Offset Items" shall be reflected as amounts recoverable from the retroactive counterparty and aggregated reporting described in paragraph 87 shall also be applied for unpaid losses and loss adjustment expenses under the original reinsurance contracts. The security applied as an "Other Allowed Offset Item" shall also be reflected in the designated sub-schedule and disclosed as a prescribed or permitted practice. (See Exhibit D of this statement.)

89. The reporting entity will continue to detail the reporting of original reinsurers that were aggregated for one-line reporting per paragraph 87 as provided in the annual statement instructions. The aggregation reporting in schedule F applies only to the extent that inuring balances currently receivable under original reinsurance contracts are also payable to the retroactive reinsurance counterparty, and additionally to reinsurance recoverable on unpaid losses if the domestic state commissioner has approved amounts related to the retroactive reinsurance contract as any other form of security acceptable under the applicable provisions of the state's credit for reinsurance law. This guidance is not intended to otherwise change the application of retroactive accounting guidance for the retroactive portions of the contract that are not duplicative of the original reinsurance. Other than measurement of the provision for reinsurance and presentation in Schedule F, the retroactive contracts should continue to follow guidance applicable to retroactive accounting and reporting.

Syndicated Letters of Credit

90. With a Syndicated Letter of Credit (Syndicated LC), the reinsurer enters into an agreement with a group of banks (the "Issuing Banks") and an agent bank (the "Agent"). Each Issuing Bank and the Agent is an NAIC-approved bank and a "qualified bank". This agreement requires the Agent to issue, on behalf of the each of the Issuing Banks, letters of credit in favor of the ceding insurer. The credit is issued (as an administrative matter) only through the Agent's letter of credit department. Each issuing bank signs the Syndicated LC through the Agent, as its attorney-in-fact. Syndicated LCs are consistent with A-785, in that the Syndicated LC is the legal equivalent of multiple letters of credit separately issued by each of the issuing banks. Reporting entities shall take a reduction in the liability on account of reinsurance recoverables secured by the Syndicated LC if all of the following conditions are met:

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a. All listed banks on the letter of credit are qualified and meet the criteria of the NAIC SVO approved bank listing;

b. Banks are severally and not jointly liable; and

c. Specific percentages for each assuming bank are listed in the letter of credit.

Disputed Items

91. Occasionally a reinsurer will question whether an individual claim is covered under a reinsurance agreement or may even attempt to nullify an entire agreement. A ceding entity, depending upon the individual facts, may or may not choose to continue to take credit for such disputed balances. A ceding entity shall take no credit whatsoever for reinsurance recoverables in dispute with an affiliate.

92. Items in dispute are those claims with respect to which the ceding entity has received formal written communication from the reinsurer denying the validity of coverage.

Uncollectible Reinsurance

93. Uncollectible reinsurance balances shall be written off through the accounts, exhibits, and schedules in which they were originally recorded.

Commutations

94. A commutation of a reinsurance agreement, or any portion thereof, is a transaction which results in the complete and final settlement and discharge of all, or the commuted portion thereof, present and future obligations between the parties arising out of the reinsurance agreement.

95. In commutation agreements, an agreed upon amount determined by the parties is paid by the reinsurer to the ceding entity. The ceding entity immediately eliminates the reinsurance recoverable recorded against the ultimate loss reserve and records the cash received as a negative paid loss. Any net gain or loss shall be reported in underwriting income in the statement of income.

96. The reinsurer eliminates a loss reserve carried at ultimate cost for a cash payout calculated at present value. Any net gain or loss shall be reported in underwriting income in the statement of income.

97. Commuted balances shall be written off through the accounts, exhibits, and schedules in which they were originally recorded.

National Flood Insurance Program

98. The National Flood Insurance Program was created by the Federal Emergency Management Agency (FEMA) and is designed to involve private insurers in a write-your-own (WYO) flood insurance program financially backed by FEMA at no risk to the insurer. To become a participating WYO entity, the entity signs a document with the Federal Insurance Administration (FIA) of the Federal Emergency Management Agency known as the Financial Assistance/Subsidy Arrangement.

99. Premium rates are set by FEMA. The WYO participating companies write the flood insurance coverage qualifying for the program on their own policies, perform their own underwriting, premium collections, claim payments, administration, and premium tax payments for policies written under the program.

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100. Monthly accountings are made to FIA and participants draw upon FEMA letters of credit for deficiencies of losses, loss expenses, and administrative expenses in excess of premiums, subject to certain percentage limitations on expenses.

101. Policies written by the reporting entity under the National Flood Insurance Program are considered insurance policies issued by the reporting entity, with reinsurance ceded to FEMA. (Such policies are not considered uninsured plans under *SSAP No. 47—Uninsured Plans*.) Balances due from or to FEMA shall be reported as ceded reinsurance balances receivable or payable. The commission and fee allowances received from FEMA shall be reported consistent with reinsurance ceding commission.

Accounting for the Transfer of Property and Casualty Run-Off Agreements

102. Property and casualty run-off agreements are reinsurance or retrocession agreements that are intended to transfer essentially all of the risks and benefits of a specific line of business or market segment that is no longer actively marketed by the transferring insurer or reinsurer. A property and casualty run-off agreement is not a novation as the transferring insurer or reinsurer remains primarily liable to the policyholder or ceding entity under the original contracts of insurance or reinsurance. Reinsurance agreements between affiliates or between insurers under common control (as those terms are defined in Appendix A-440) are not eligible for the exception for property and casualty run-off agreements in paragraph 36.e.

Criteria

103. The accounting treatment for property and casualty run-off agreements must be approved by the domiciliary regulators of the transferring entity (either the original direct insurer in the case of a reinsurance agreement or the original assuming reinsurer in the case of a retrocession agreement) and the assuming entity. If the transferring entity and assuming entity are domiciled in the same state, then the regulator of the state where the majority of the transferred liabilities is located shall be asked to approve the accounting treatment. In determining whether to approve an agreement for this accounting treatment, the regulators shall require the following:

a. Assuming Entity Properly Licensed – The entity assuming the run-off agreement must have the appropriate authority or license to write the business being assumed.

b. Limits and Coverages – The reinsurance or retrocession agreement shall provide the same limits and coverages that were afforded in the original insurance or reinsurance agreement.

c. Non-recourse – The reinsurance or retrocession agreement shall not contain any adjustable features or profit share or retrospective rating, and there shall be no recourse (other than normal representations and warranties that would be associated with a purchase and sale agreement) directly or indirectly against the transferring entity.

d. Risk Transfer – The reinsurance or retrocession agreement must meet the requirements of risk transfer as described in this statement.

e. Financial Strength of Reinsurer – The assuming reinsurer shall have a financial strength rating from at least two independent rating agencies (from NAIC credit rating providers (CRP)) which is equal to or greater than the current ratings of the transferring entity. The lowest financial strength rating received from an NAIC acceptable rating organization rating agency will be used to compare the financial strength ratings of the transferring and assuming entities.

f. Assessments – The assuming reinsurer or retrocessionaire (if required in the original reinsurance contract) shall be financially responsible for any and all assessments, including

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guaranty fund assessments, that are assessed against the transferring entity related to the insurance business being assumed.

g. Applicable Only to "Run-off" Business – The reinsurance or retrocession agreement shall only cover liabilities relating to a line(s) of business or specific market segments no longer actively marketed by the transferring entity.

h. Non-cancelable Reinsurance – The reinsurance or retrocession agreement shall provide that the reinsurance or retrocessional coverage provided by the proposed agreement cannot be cancelable by either party for any reason. (However, this provision will not override standard contracts law and principles and will not prevent any remedies, including rescission or termination that might be available for breach, misrepresentation, etc.)

Statutory Schedules and Exhibits

104. At the inception of the transaction, the transferring entity shall record the consideration paid to the assuming entity as a paid loss. If the consideration paid by the transferring entity is less than the loss reserves transferred, the difference shall be recorded by the ceding entity as a decrease in losses incurred. The assuming entity shall record the consideration received as a negative paid loss. In addition, the transferring entity shall record an increase to ceded reinsurance recoverable for the amount of the transferred reserve. Journal entries illustrating these transactions, including situations in which the transaction includes an unearned premium reserve, are included in Exhibit B of this statement.

105. The assuming entity will report the business in the same line of business as reported by the original insurer or reinsurer. The assuming entity will report the business at the same level of detail using the appropriate statutory schedules and exhibits.

Disclosures

106. Unsecured Reinsurance Recoverables:

a. If the entity has with any individual reinsurers, authorized, reciprocal jurisdiction, unauthorized, or certified an unsecured aggregate recoverable for losses, paid and unpaid including IBNR, loss adjustment expenses, and unearned premium, that exceeds 3% of the entity's policyholder surplus, list each individual reinsurer and the unsecured aggregate recoverable pertaining to that reinsurer; and

b. If the individual reinsurer is part of a group, list the individual reinsurers, each of its related group members having reinsurance with the reporting entity, and the total unsecured aggregate recoverables for the entire group.

107. Reinsurance Recoverables in Dispute—Reinsurance recoverable on paid and unpaid (including IBNR) losses in dispute by reason of notification, arbitration or litigation shall be identified if the amounts in dispute from any entity (and/or affiliate) exceed 5% of the ceding entity's policyholders surplus or if the aggregate of all disputed items exceeds 10% of the ceding entity's policyholders surplus. Notification means a formal written communication from a reinsurer denying the validity of coverage.

108. Uncollectible Reinsurance—Describe uncollectible reinsurance written off during the year reported in the following annual statement classifications, including the name(s) of the reinsurer(s):

a. Losses incurred;

b. Loss adjustment expenses incurred;

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c. Premiums earned; and

d. Other.

109. Commutation of Ceded Reinsurance—Describe commutation of ceded reinsurance during the year reported in the following annual statement classifications, including the name(s) of the reinsurer(s):

a. Losses incurred;

b. Loss adjustment expenses incurred;

c. Premiums earned; and

d. Other.

110. Retroactive Reinsurance—The table illustrated in the NAIC Annual Statement Instructions for Property and Casualty Companies under Retroactive Reinsurance in the Notes to Financial Statements section shall be completed for all retroactive reinsurance agreements that transfer liabilities for losses that have already occurred and that will generate special surplus transactions. The insurer (assuming or ceding) shall assign a unique number to each retroactive reinsurance agreement and shall utilize this number for as long as the agreement exists. Transactions utilizing deposit accounting shall not be reported in this note.

111. Reinsurance Assumed and Ceded—The tables illustrated in the NAIC Annual Statement Instructions for Property and Casualty Companies under "Reinsurance Assumed and Ceded in the Notes to Financial Statements" section shall be completed as follows:

a. The financial statements shall disclose the maximum amount of return commission which would have been due reinsurers if all reinsurance were canceled with the return of the unearned premium reserve; and

b. The financial statements shall disclose the accrual of additional or return commission, predicated on loss experience or on any other form of profit sharing arrangements as a result of existing contractual arrangements.

112. A specific interrogatory requires information on reinsurance of risk accompanied by an agreement to release the reinsurer from liability, in whole or in part, from any loss that may occur on the risk or portion thereof.

113. Disclosures for paragraphs 114-119 represent annual statement interrogatories, which are required to be included with the annual audit report beginning with audit reports on financial statements as of and for the period ended December 31, 2006. The disclosures required within paragraphs 114-119 shall be included in accompanying supplemental schedules of the annual audit report beginning in year-end 2006. These disclosures shall be limited to reinsurance contracts entered into, renewed or amended on or after January 1, 1994. This limitation applies to the annual audit report only and does not apply to the statutory annual statement interrogatories and the reinsurance summary supplemental filing.

114. Disclose if any risks are reinsured under a quota share reinsurance contract with any other entity that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g. a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)? If yes, indicate the number of reinsurance contracts containing such provisions and if the amount of reinsurance credit taken reflects the reduction in quota share coverage caused by any applicable limiting provision(s).

115. Disclose if the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards

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policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:

a. A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;

b. A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;

c. Aggregate stop loss reinsurance coverage;

d. A unilateral right by either party (or both parties) to commute the reinsurance contract, whether conditional or not, except for such provisions which are only triggered by a decline in the credit status of the other party;

e. A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or

f. Payment schedule, accumulating retentions from multiple years or any features inherently designed to delay timing of the reimbursement to the ceding entity.

116. Disclose if the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders. This disclosure is limited to reinsurance contracts with written premium cessions or loss and loss expense reserve cessions described in this paragraph that meet the criteria of paragraph 116.a. or paragraph 116.b. This disclosure excludes cessions to approved pooling arrangements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member.

a. The written premium ceded to the reinsurer by the reporting entity or its affiliates represents ~~fifty percent (~~50%~~)~~ or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or

b. Twenty–five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates in separate reinsurance contract.

117. If affirmative disclosure is required for paragraph 115 or 116, provide the following information:

a. A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting paragraph 115 or 116;

b. A brief discussion of management's principal objectives in entering into the reinsurance contract including the economic purpose to be achieved; and

c. The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income.

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118. Except for transactions meeting the requirements of paragraph 36, disclose if the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:

a. Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or

b. Accounted for that contract as reinsurance under GAAP and as a deposit under SAP.

119. If affirmative disclosure is required for paragraph 118, explain in a supplemental filing why the contract(s) is treated differently for GAAP and SAP.

120. Disclosures for the Transfer of Property and Casualty Run-off Agreements

a. Disclose if the reporting entity has entered into any agreements which have been approved by their domiciliary regulator and have qualified pursuant to paragraph 36.e. (also see paragraphs 102-105).

b. If affirmative, provide a description of the agreement and the amount of consideration paid and liabilities transferred.

121. The financial statements shall disclose the following with respect to reinsurance agreements which qualify for reinsurer aggregation in accordance with paragraphs 87-89:

a. A description of the significant terms of the reinsurance agreement, including established limits and collateral, and

b. The amount of unexhausted limit as of the reporting date.

c. To the extent that the domestic state insurance department approves the use of the retroactive contract as an acceptable form of security related to the original reinsurers under the applicable provisions of the state's credit for reinsurance law, the use of such discretion shall be disclosed in the annual statement Note 1 as a prescribed or permitted practice. In addition, Note 1 shall disclose as part of the total impact on the provision for reinsurance the impact on the overdue aspects of the calculation if the reporting entity also receives commissioner approval pursuant to paragraph 87 related to overdue paid amounts (both authorized and unauthorized).

122. The financial statements shall disclose the following with respect to reinsurance agreements that have been accounted for as deposits:

a. A description of the reinsurance agreements.

b. Any adjustment of the amounts initially recognized for expected recoveries. The individual components of the adjustment (e.g., interest accrual, change due to a change in estimated or actual cash flow) shall be disclosed separately.

123. The financial statements shall disclose the impact on any reporting period in which a certified reinsurer's rating has been downgraded or its certified reinsurer status is subject to revocation and additional collateral has not been received as of the filing date. The disclosure should include the following:

a. Name of certified reinsurer downgraded or subject to revocation of certified reinsurer status and relationship to the reporting entity;

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b. Date of downgrade or revocation and jurisdiction of action;

c. Collateral percentage requirements pre and post downgrade or revocation;

d. Net ceded recoverable subject to collateral;

e. As of the end of the current quarter, the estimated impact of the collateral deficiency to the reporting entity as a result of the assuming entity's downgrade or revocation of certified reinsurer status. (At year-end the actual impact of the collateral deficiency on the provision for reinsurance shall be disclosed.)

124. U.S. domiciled reinsurers are eligible for certified reinsurer status. If the reporting entity is a certified reinsurer, the financial statements shall disclose the impact on any reporting period in which its certified reinsurer rating is downgraded or status as a certified reinsurer is subject to revocation. Such disclosure shall include information similar to paragraphs 123.b., 123.c. and 123.d. and the expectation of its certified reinsurer's ability to meet the increased requirements.

125. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

126. This statement adopts with modification *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts* (FAS 113) and FASB *Emerging Issues Task Force No. 93-6, Accounting for Multiple-Year Retrospectively Rated Contracts by Ceding and Assuming Enterprises* for the following:

a. Reinsurance recoverables on unpaid case-basis and incurred but not reported losses and loss adjustment expenses shall be reported as a contra-liability netted against the liability for gross losses and loss adjustment expenses;

b. Amounts paid for prospective reinsurance that meet the conditions for reinsurance accounting shall be reported as a reduction of unearned premiums;

c. The gain created by a retroactive reinsurance agreement because the amount paid to the reinsurer is less than the gross liabilities for losses and loss adjustment expenses ceded to the reinsurer is reported in the statement of income as a write-in gain in other income by the ceding entity and a write-in loss by the assuming entity. The gain created by a retroactive reinsurance agreement is restricted as a special surplus account until the actual retroactive reinsurance recovered is in excess of the consideration paid;

d. This statement requires that a liability (provision for reinsurance) be established through a provision reducing unassigned funds (surplus) for unsecured reinsurance recoverables from unauthorized or certified reinsurers and for certain overdue balances due from authorized reinsurers;

e. Some reinsurance agreements contain adjustable features that provide for adjustment of commission, premium or amount of coverage, based on loss experience. This statement requires that the asset or liability arising from the adjustable feature be computed based on experience to date under the agreement, and the impact of early termination may only be considered at the time the agreement has actually been terminated;

f. Structured settlements are addressed in *SSAP No. 65—Property and Casualty Contracts*. Statutory accounting and FAS 113 are consistent in accounting for structured settlement annuities where the reporting entity is the owner and payee and where the claimant is the payee and the reporting entity has been released from its obligation. FAS 113 distinguishes

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structured settlement annuities where the claimant is the payee and a legally enforceable release from the reporting entity's liability is obtained from those where the claimant is the payee but the reporting entity has not been released from its obligation. GAAP requires the deferral of any gain resulting from the purchase of a structured settlement annuity where the reporting entity has not been released from its obligation; and

g. This statement requires that reinsurance recoverables on unpaid losses and loss adjustment expenses be presented as a contra-liability. Requirements for offsetting and netting are addressed in SSAP No. 64.

127. This statement adopts American Institute of Certified Public Accountants (AICPA) *Statement of Position 98-7, Deposit Accounting: Accounting for Insurance and Reinsurance Contracts That Do Not Transfer Insurance Risk* (SOP 98-7) paragraphs 10-12 and 19 (subsection b only). This statement rejects AICPA SOP 98-7 paragraphs 13-17 and 19 (subsections a and c).

128. This statement rejects AICPA *Statement of Position No. 92-5, Accounting for Foreign Property and Liability Reinsurance*. This statement incorporates Appendix A-785 as applicable.

129. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~129.~~130. This statement shall apply to:

a. Reinsurance agreements entered into, renewed, or amended on or after January 1, 1994. An amendment is any revision or adjustment of contractual terms. The payment of premiums or reimbursement of losses recoverable under the agreement shall not constitute an amendment; and

b. Reinsurance agreements in force on January 1, 1995, which cover losses occurring or claims made on or after that date on policies reinsured under such agreements.

~~130.~~131. The guidance shall not apply to:

a. Reinsurance agreements which cover only losses occurring or claims made before January 1, 1994, and which were entered into before January 1, 1994, and were not subsequently renewed or amended; and

b. Reinsurance agreements that expired before and were not renewed or amended after January 1, 1995.

~~131.~~132. The guidance in paragraphs 55-74 shall be effective for all accounting periods beginning on or after January 1, 1996, and shall apply to reinsurance agreements entered into, renewed or amended on or after January 1, 1994.

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~~132.~~133. This statement, including the guidance in paragraph 40 incorporated from SSAP No. 75, is effective for years beginning January 1, 2001. Changes resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

a. Revisions to paragraph 36.e., related to paragraphs 102-105, and disclosures in paragraph 120 documented in *Issue Paper No. 137—Transfer of Property and Casualty Reinsurance Run-off Agreements* are effective for contracts entered on or after January 1, 2010.

b. The guidance in paragraphs 40, 122 and 127 was previously included within *SSAP No. 75—Reinsurance Deposit Accounting—An Amendment to SSAP No. 62R, Property and Casualty Reinsurance* and was also effective for years beginning January. 1, 2001. In 2011, the guidance from SSAP No. 75 was incorporated within this statement, with SSAP No. 75 nullified. The original guidance included in this statement for deposit accounting, as well as the original guidance adopted in SSAP No. 75, are retained for historical purposes in Issue Paper No. 104. The guidance in paragraph 54 was originally contained within *INT 02-06: Indemnification in Modeled Trigger Transactions* and was effective June 9, 2002. The guidance in paragraph 90 was originally contained within *INT 02-09: A-785 and Syndicated Letters of Credit* and was effective September 12, 2004.

c. The guidance related to certified reinsurers is applicable only to cedents domiciled in states that have enacted/promulgated the new collateral framework and only for their cessions to reinsurers certified under that domestic law/rule. The requirements applicable to contracts with certified reinsurers shall be effective for all reporting periods beginning on or after December 31, 2012.

~~133.~~134. The guidance in paragraphs 87-89 and 121 which allowed retroactive reinsurance exceptions for asbestos and pollution contracts was effective for all accounting periods beginning on or after January 1, 2014, for paid losses. This guidance was revised to also allow for unpaid losses effective for reporting periods ending on and after December 31, 2015.

~~134.~~135. The substantive revisions adopted November 15, 2018, which primarily incorporated guidance originally from *EITF 93-6, Accounting for Multiple-Year Retrospectively-Rated Contracts by Ceding and Assuming Enterprises,* and from *EITF Topic D-35, FASB Staff Views on Issue No. 93-6, Accounting for Multiple-Year Retrospectively Rated Contracts by Ceding and Assuming Enterprises,* are effective for contracts in effect on or after January 1, 2019. These revisions are required for contracts in effect as EITF 93-6 had been adopted with modification in this statement from its original 2001 effective date. The revisions adopted in November 2018 primarily added clarification and implementation guidance. (Companies that have previously been following the original intent, as clarified in the revisions, should not be impacted by the November 2018 revisions.) However, if a reporting entity becomes aware that the prior application of reinsurance credit guidance was not consistent with the adopted guidance, the updates should be applied as a change in accounting principle to contracts in effect as of January 1, 2019.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 75—Property and Casualty Reinsurance*
- *Issue Paper No. 104—Reinsurance Deposit Accounting – An Amendment to SSAP No. 62R—Property and Casualty Reinsurance*
- *Issue Paper No. 137—Transfer of Property and Casualty Reinsurance Run-off Agreements*

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- *Issue Paper No. 153—Counterparty Reporting Exception for Asbestos and Pollution Contracts*

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CLASSIFYING REINSURANCE CONTRACTS

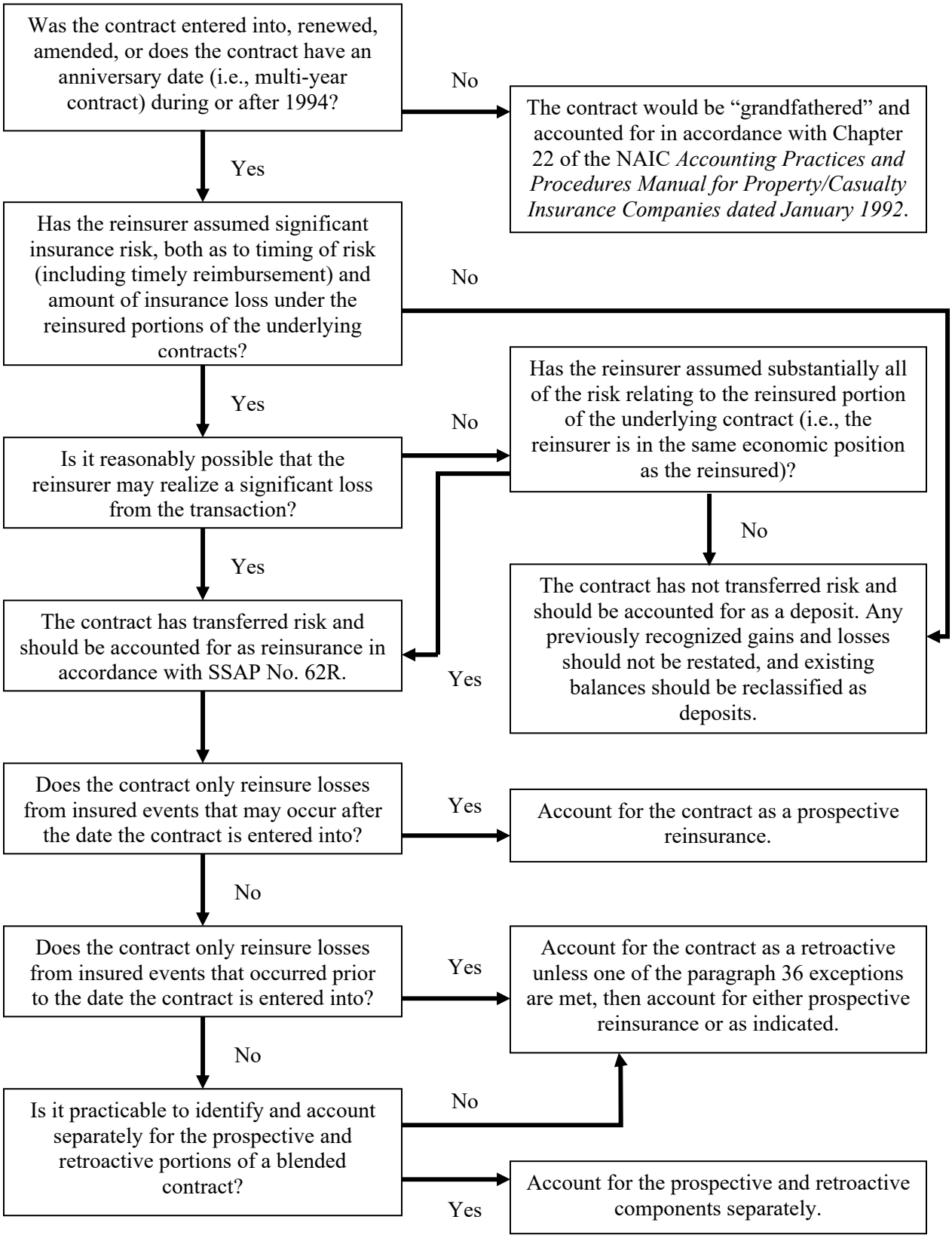

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EXHIBIT A – IMPLEMENTATION QUESTIONS AND ANSWERS

This exhibit addresses common questions regarding implementation of the property and casualty reinsurance accounting standards.

Index to Questions

No.	Question
Applicability	
1	The accounting practices in SSAP No. 62R specify the accounting and reporting for reinsurance contracts. What contracts are considered reinsurance contracts for purposes of applying these accounting practices?
2	The provisions of this statement will apply to (a) reinsurance contracts entered into, renewed or amended on or after January 1, 1994, and (b) any other reinsurance contracts that are in force on January 1, 1995, and cover insurable events on the underlying insurance policies that occur on or after that date. What contracts would be exempt from the accounting rules included in SSAP No. 62R?
3	This statement is to be applied to contracts which are amended on or after January 1, 1994. What if the change in terms is not significant, or the terms changed have no financial effect on the contract?
4	Must the accounting provisions of SSAP No. 62R be applied to an *otherwise exempt* contract if the ceding entity pays additional premiums under the contract on or after January 1, 1994?
5	Prospective and retroactive portions of a reinsurance contract are allowed to be accounted for separately, if practicable. Can the retroactive portion of an existing contract be segregated and, therefore, exempted with other retroactive contracts covering insured events occurring prior to January 1, 1994?
Risk Transfer	
6	Do the risk transfer provisions apply to existing contracts?
7	How does the effective date affect the assessment of whether a significant loss to the reinsurer was reasonably possible?
8	Should risk transfer be reassessed if contractual terms are subsequently amended?
9	How should the risk transfer assessment be made when a contract has been amended?
10	For purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract?
11	If the assessment of risk transfer changes after the initial assessment at contract inception, how should the ceding entity account for the change?
12	SSAP No. 62R requires that reasonably possible outcomes be evaluated to determine the reinsurer's exposure to significant loss. What factors should be considered in determining whether a scenario being evaluated is reasonably possible?

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No.	Question
13	In determining the amount of the reinsurer's loss under reasonably possible outcomes, may cash flows directly related to the contract other than those between the ceding and assuming companies, such as taxes and operating expenses of the reinsurer, be considered in the calculation?
14	In evaluating the significance of a reasonably possible loss, should the reasonably possible loss be compared to gross or net premiums?
15	How does a commutation clause affect the period of time over which cash flows are evaluated for reasonable possibility of significant loss to the reinsurer?
16	SSAP No. 62R refers to payment schedules and accumulating retentions from multiple years as features that delay timely reimbursement of claims. Does the presence of those features generally prevent a contract from meeting the conditions for reinsurance accounting?
17	What if a contract contains a feature such as a payment schedule or accumulating retention but could still result in the reasonable possibility of significant loss to the reinsurer?
18	Can a reinsurance agreement compensate a reinsurer for losses?
19	In determining whether a reinsurance contract qualifies under the exception referred to in paragraph 18 of SSAP No. 62R, how should the economic position of the reinsurer be assessed in relation to that of the ceding entity?
Accounting Provisions	
20	An existing contract that was accounted for as reinsurance no longer qualifies for reinsurance accounting under the accounting rules included in SSAP No. 62R. How should the ceding and assuming companies account for the contract in future periods?
21	What is the definition of past insurable events that governs whether reinsurance coverage is prospective or retroactive? For example, could a reinsurance contract that covers losses from asbestos and pollution claims on occurrence-based insurance policies effective during previous periods be considered prospective if the reinsurance coverage is triggered by a court interpretation that a loss is covered within the terms of the underlying insurance policies?
22	Would the answer to the above question change if the reinsurance were written on a claims-made basis?
23	What is the effect of adjustments to future premiums or coverage in determining whether reinsurance is prospective or retroactive?
24	A reinsurance contract is entered into after the contract's effective date. Is the coverage between the contract's effective date and the date the contract was entered into prospective or retroactive?
25	How is the date the reinsurance contract was entered into determined?
26	Are contracts to reinsure calendar-year incurred losses considered blended contracts that have both prospective and retroactive elements?
27	When the prospective and retroactive portions of a contract are being accounted for separately, how should premiums be allocated to each portion of the contract?

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No.	Question
28	A retroactive reinsurance contract contains a cut-through provision that provides the ceding entity's policyholders and claimants with the right to recover their claims directly from the reinsurer. May the ceding entity immediately recognize earned surplus associated with this type of contract?
29	A ceding entity enters into a retroactive reinsurance agreement that gives rise to segregated surplus. If the reinsurer prepays its obligation under the contract, may the ceding entity recognize earned surplus at the time the prepayment is received?
30	If the ceding entity does not expect to receive any recoveries because the reinsurer has agreed to reimburse claimants under the reinsured contracts directly, would the ceding entity be considered to have recovered or terminated its transferred liabilities?
31	What accounting entries would a ceding entity make to report a retroactive reinsurance contract?
32	How should the parties account for an adverse loss development reinsurance contract where, as of the statement date, the attachment level of the contract exceeds the ceding company's current case and IBNR reserves for the covered accident years (i.e., no surplus gain and no reinsurance recoverable as of the statement date), and the ceding company transferred cash to the reinsurer at the inception of the contract?
33	How should a ceding company account for payment of the premium for a retroactive reinsurance contract by the ceding company's parent company or some other person not a party to the reinsurance contract (for example, adverse loss development reinsurance contracts purchased by the parent company in the context of the purchase or sale of the ceding company)?

Applicability

1. Q: The accounting practices in SSAP No. 62R specify the accounting and reporting for reinsurance contracts. What contracts are considered reinsurance contracts for purposes of applying these accounting practices?

   A: Any transaction that indemnifies an insurer against loss or liability relating to insurance risk shall be accounted for in accordance with the accounting practices included in SSAP No. 62R. Therefore, all contracts, including contracts that may not be structured or described as reinsurance, shall be accounted for as reinsurance when those conditions are met.

2. Q: The provisions of this statement will apply to (a) reinsurance contracts entered into, renewed or amended on or after January 1, 1994, and (b) any other reinsurance contracts that are in force on January 1, 1995 and cover insurable events on the underlying insurance policies that occur on or after that date. What contracts would be exempt from the accounting rules included in SSAP No. 62R?

   A: The only exempt contracts are:

      1) Purely retroactive reinsurance contracts that cover only insured events occurring before January 1, 1994, provided those contracts were entered into before that date and are not subsequently amended and

      2) Contracts that expired before January 1, 1995 and are not amended after that date.

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3. Q: This statement is to be applied to contracts which are amended on or after January 1, 1994. What if the change in terms is not significant, or the terms changed have no financial effect on the contract?

   A: In general, the term amendment should be viewed broadly to include all but the most trivial changes. Examples of amendments include, but are not limited to, replacing one assuming entity with another (including an affiliated entity), or modifying the contract's limit, coverage, premiums, commissions, or experience-related adjustable features. No distinction is made between financial and non-financial terms.

4. Q: Must the accounting provisions of SSAP No. 62R be applied to an *otherwise exempt* contract if the ceding entity pays additional premiums under the contract on or after January 1, 1994?

   A: The answer depends on why the additional premiums are paid. If the additional premiums are the result of a renegotiation, adjustment, or extension of terms, the contract is subject to the accounting provisions of SSAP No. 62R. However, additional premiums paid without renegotiation, adjustment, or extension of terms would not make an otherwise exempt contract subject to those provisions.

5. Q: Prospective and retroactive portions of a reinsurance contract are allowed to be accounted for separately, if practicable. Can the retroactive portion of an existing contract be segregated and, therefore, exempted with other retroactive contracts covering insured events occurring prior to January 1, 1994?

   A: No. The transition provisions apply to an entire contract, which is either subject to or exempt from the provisions of SSAP No. 62R. A ceding entity may bifurcate a contract already subject to the accounting rules in SSAP No. 62R and then account for both the prospective and retroactive portions in accordance with the accounting standard.

Risk Transfer

6. Q: Do the risk transfer provisions apply to existing contracts?

   A: Yes, the risk transfer provisions apply to some existing contracts. SSAP No. 62R applies in its entirety only to existing contracts which were renewed or amended on or after January 1, 1994, or which cover losses occurring or claims made after that date. Therefore, those contracts must be evaluated to determine whether they transfer risk and qualify for reinsurance accounting. For accounting periods commencing on or after January 1, 1995, balances relating to such contracts which do not transfer insurance risk shall be reclassified as deposits and shall be accounted for and reported in the manner described under the caption Reinsurance Contracts Must Include Transfer of Risk.

   SSAP No. 62R does not apply to existing contracts which were entered into before, and were not renewed or amended on or after, January 1, 1994, and which cover only losses occurring or claims made before that date, nor to contracts which expired before, and were not renewed or amended on or after, January 1, 1995. Those contracts will continue to be accounted for in the manner provided by SSAP No. 62R before these revisions.

7. Q: How does the effective date affect the assessment of whether a significant loss to the reinsurer was reasonably possible?

   A: The risk transfer assessment is made at contract inception, based on facts and circumstances known at the time. Because that point in time has passed for existing contracts, some have suggested that the risk transfer provisions be applied as of the effective date. However, that approach to the risk transfer assessment would violate the requirement to consider all cash flows from the contract.

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Therefore, the test must be applied from contract inception, considering the effect of any subsequent contract amendments. Careful evaluation and considered judgment will be required to determine whether a significant loss to the reinsurer was reasonably possible at inception.

8. Q: Should risk transfer be reassessed if contractual terms are subsequently amended?

   A: Yes. When contractual terms are amended, risk transfer should be reassessed. For example, a contract that upon inception met the conditions for reinsurance accounting could later be amended so that it no longer meets those conditions. The contract should then be reclassified and accounted for as a deposit.

9. Q: How should the risk transfer assessment be made when a contract has been amended?

   A: No particular method is prescribed for assessing risk transfer in light of a contract amendment. Whether an amended contract in substance transfers risk must be determined considering all of the facts and circumstances in light of the risk transfer requirements. Judgment also will be required to determine whether an amendment in effect creates a new contract.

10. Q: For purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract?

    A: A contract is not defined, but is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract. For example, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist.

    The inconsistency that could result from varying interpretations of the term *contract* is limited by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers, in the aggregate, do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

11. Q: If the assessment of risk transfer changes after the initial assessment at contract inception, how should the ceding entity account for the change?

    A: The status of a contract should be determinable at inception and, absent amendment, subsequent changes should be very rare. If the risk of significant loss was not deemed reasonably possible at inception, and a significant loss subsequently occurred, the initial assessment was not necessarily wrong, because remote events do occur. Likewise, once a reasonable possibility of significant loss has been established, such loss need not occur in order to maintain the contract's status as reinsurance.

12. Q: SSAP No. 62R requires that reasonably possible outcomes be evaluated to determine the reinsurer's exposure to significant loss. What factors should be considered in determining whether a scenario being evaluated is reasonably possible?

    A: The term *reasonably possible* means that the probability is more than remote. The test is applied to a particular scenario, not to the individual assumptions used in the scenario. Therefore, a scenario is not reasonably possible unless the likelihood of the entire set of assumptions used in the scenario occurring together is reasonably possible.

13. Q: In determining the amount of the reinsurer's loss under reasonably possible outcomes, may cash flows directly related to the contract other than those between the ceding and assuming companies, such as taxes and operating expenses of the reinsurer, be considered in the calculation?

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A: No. The evaluation is based on the present value of all cash flows *between the ceding and assuming enterprises* under reasonably possible outcomes and, therefore, precludes considering other expenses of the reinsurer in the calculation.

14. Q: In evaluating the significance of a reasonably possible loss, should the reasonably possible loss be compared to gross or net premiums?

A: Gross premiums should be used.

15. Q: How does a commutation clause affect the period of time over which cash flows are evaluated for reasonable possibility of significant loss to the reinsurer?

A: All cash flows are to be assessed under reasonably possible outcomes. Therefore, unless commutation is expected in the scenario being evaluated, it should not be assumed in the calculation. Further, the assumptions used in a scenario must be internally consistent and economically rational in order for that scenario's outcome to be considered reasonably possible.

16. Q: SSAP No. 62R refers to payment schedules and accumulating retentions from multiple years as features that delay timely reimbursement of claims. Does the presence of those features generally prevent a contract from meeting the conditions for reinsurance accounting?

A: Yes. Payment schedules and accumulating retentions from multiple years are contractual features inherently designed to delay the timing of reimbursement to the ceding entity. Regardless of what a particular feature might be called, any feature that can delay timely reimbursement violates the conditions for reinsurance accounting. Transfer of insurance risk requires that the reinsurer's payments to the ceding entity depend on and directly vary with the amount and timing of claims settled under the reinsured contracts. Contractual features that can delay timely reimbursement prevent this condition from being met. Therefore, any feature that may affect the timing of the reinsurer's reimbursement to the ceding entity should be closely scrutinized.

17. Q: What if a contract contains a feature such as a payment schedule or accumulating retention but could still result in the reasonable possibility of significant loss to the reinsurer?

A: Both of the following conditions are required for reinsurance accounting:

a. Transfer of significant risk arising from uncertainties about both (i) the ultimate amount of net cash flows from premiums, commission, claims, and claim settlement expenses paid under a contract (underwriting risk) and (ii) the timing of the receipt and payment of those cash flows (timing risk); and

b. Reasonable possibility of significant loss to the reinsurer.

Because both condition (a) and condition (b) must be met, failure to transfer significant timing and underwriting risk is not overcome by the possibility of significant loss to the reinsurer.

18. Q: Can a reinsurance agreement compensate a reinsurer for losses?

A: A contract does not meet the conditions for reinsurance accounting if features of the reinsurance contract or other contracts or agreements directly or indirectly compensate the reinsurer or related reinsurers for losses to an extent that risk-transfer criteria is violated. That compensation may take many forms, and an understanding of the substance of the contracts or agreements is required to determine whether the ceding entity has been indemnified against loss or liability relating to insurance risk. For example, contractual features may limit the reinsurer's exposure to insurance risk or delay the reimbursement of claims so that investment income mitigates exposure to insurance risk. Examples of those contractual features noted in paragraph 12 are not all-inclusive.

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19. Q: In determining whether a reinsurance contract qualifies under the exception referred to in paragraph 18, how should the economic position of the reinsurer be assessed in relation to that of the ceding entity?

A: The assessment should be made by comparing the net cash flows of the reinsurer under the reinsurance contract with the net cash flows of ceding entity on the reinsured portions of the underlying insurance contracts. This may be relatively easy for reinsurance of individual risks or for unlimited-risk quota-share reinsurance, because the premiums and losses on these types of reinsurance generally are the same as the premiums and losses on the reinsured portions of the underlying insurance policies.

In other types of reinsurance, determining the reinsurer's net cash flows relative to the insurer is likely to be substantially more difficult. For example, it generally would be difficult to demonstrate that the ceding entity's premiums and losses for a particular layer of insurance are the same as the reinsurer's premiums and losses related to that layer. If the economic position of the reinsurer relative to the insurer cannot be determined, the contract would not qualify under the exception.

Accounting Provisions

20. Q: An existing contract that was accounted for as reinsurance no longer qualifies for reinsurance accounting under the accounting rules included in SSAP No. 62R. How should the ceding and assuming companies account for the contract in future periods?

A: Because the statement of income cannot be restated, previously recognized gains and losses are not revised. If the contract was entered into before, and not renewed or amended on or after, January 1, 1994 and covers only losses occurring or claims made before that date, or the contract expired before January 1, 1995 and was not renewed or amended on or after that date, it would continue to be accounted for in the manner provided before these revisions.

For accounting periods commencing on or after January 1, 1995, existing balances relating to contracts which do not transfer insurance risk and which were entered into on or after January 1, 1994 (covering losses occurring or claims made after that date) would be reclassified as deposits.

Premium payments to a reinsurer would be recorded as deposits. Likewise, losses recoverable from a reinsurer would not be recognized as receivables. Rather, any reimbursement for losses would be accounted for upon receipt as a refund of a deposit.

21. Q: What is the definition of past insurable events that governs whether reinsurance coverage is prospective or retroactive? For example, could a reinsurance contract that covers losses from asbestos and pollution claims on occurrence-based insurance policies effective during previous periods be considered prospective if the reinsurance coverage is triggered by a court interpretation that a loss is covered within the terms of the underlying insurance policies?

A: The distinction between prospective and retroactive reinsurance is based on whether a contract reinsures future or past insured events covered by the underlying reinsurance contracts. In the example above, the insured event is the occurrence of loss within the coverage of the underlying insurance contracts, not the finding of a court. Therefore, the fact that the asbestos exposure or pollution is covered under insurance policies effective during prior periods makes the reinsurance coverage in this example retroactive.

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22. Q: Would the answer to the above question change if the reinsurance were written on a claims-made basis?

    A: No. The form of the reinsurance—whether claims-made or occurrence-based—does not determine whether the reinsurance is prospective or retroactive. A claims-made reinsurance contract that reinsures claims asserted to the reinsurer in a future period as a result of insured events that occurred prior to entering into the reinsurance contract is a retroactive contract.

23. Q: What is the effect of adjustments to future premiums or coverage in determining whether reinsurance is prospective or retroactive?

    A: Adjustments to future premiums or coverage may affect the accounting for a reinsurance contract. Whenever an adjustment results in a reinsurer providing new or additional coverage for past insurable events, that coverage is retroactive. For example, if subsequent years' premiums under a multiple accident year contract create additional coverage for previous accident years, the additional coverage is retroactive, even if the original coverage provided in the contract for those accident years was prospective. Likewise, if current losses under a multiple-year contract eliminate coverage in future periods, some or all of the premiums to be paid in those future periods should be charged to the current period.

24. Q: A reinsurance contract is entered into after the contract's effective date. Is the coverage between the contract's effective date and the date the contract was entered into prospective or retroactive?

    A: The portion of the contract related to the period of time between the effective date of the contract and the date the contract was entered into is retroactive because it covers insured events that occurred prior to entering into the reinsurance contract.

25. Q: How is the date the reinsurance contract was entered into determined?

    A: It is not uncommon for a reinsurance arrangement to be initiated before the beginning of a policy period but not finalized until after the policy period begins. Whether there was agreement in principle at the beginning of the policy period and, therefore, the contract is substantively prospective must be determined based on the facts and circumstances. For example, a contract may be considered to have been substantively entered into even though regulatory approval of that contract has not taken place.

    The absence of agreement on significant terms, or the intention to establish or amend those terms at a later date based on experience or other factors, generally indicates that the parties to the contract have not entered into a reinsurance contact, but rather have agreed to enter into a reinsurance contract at a future date. If contractual provisions under a contract substantively entered into at a future date covered insurable events prior to that date, that coverage is retroactive.

    In any event, SSAP No. 62R provides that if a contract (except facultative contracts and contracts signed by the lead reinsurer and certain cover notes or similar documents signed by reinsurers representing more than 50% of the capacity on the contract) has not been finalized, reduced to written form and signed by the parties within 9 months after its effective date, it is presumed to be retroactive.

26. Q: Are contracts to reinsure calendar-year incurred losses considered blended contracts that have both prospective and retroactive elements?

    A: Yes. Most reinsurance contracts covering calendar-year incurred losses combine coverage for insured events that occurred prior to entering into the reinsurance contract with coverage for future insured events and, therefore, include both prospective and retroactive elements.

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In any event, SSAP No. 62R provides that if a contract (except facultative contracts, contracts signed by the lead reinsurer and certain cover notes or similar documents signed by reinsurers representing more than 50% of the capacity on the contract) has not been finalized, reduced to written form and signed by the parties within 9 months after its effective date it is presumed retroactive.

27. Q: When the prospective and retroactive portions of a contract are being accounted for separately, how should premiums be allocated to each portion of the contract?

A: No specific method for allocating the reinsurance premiums to the risks covered by the prospective and retroactive portions of a contract is required. However, separate accounting for the prospective and retroactive portions of a contract may take place only when an allocation is practicable.

Practicability requires a reasonable basis for allocating the reinsurance premiums to the risks covered by the prospective and retroactive portions of the contract, considering all amounts paid or deemed to have been paid regardless of the timing of payment. If a reasonable basis for allocating the premiums between the prospective and retroactive coverage does not exist, the entire contract must be accounted for as a retroactive contract.

28. Q: A retroactive reinsurance contract contains a cut-through provision that provides the ceding entity's policyholders and claimants with the right to recover their claims directly from the reinsurer. May the ceding entity immediately recognize earned surplus associated with this type of contract?

A: No. SSAP No. 62R states that earned surplus may not be recognized "until the actual retroactive reinsurance recovered exceeds the consideration paid."

29. Q: A ceding entity enters into a retroactive reinsurance agreement that gives rise to segregated surplus. If the reinsurer prepays its obligation under the contract, may the ceding entity recognize earned surplus at the time the prepayment is received?

A: Segregated surplus arising from retroactive reinsurance transactions is earned as actual liabilities that have been transferred are recovered or terminated. Therefore, earned surplus is based on when the reinsurer settles its obligations to the ceding entity, and it may be appropriate to recognize earned surplus at the time the prepayment is received.

However, all of the facts and circumstances must be considered to determine whether the ceding entity has substantively recovered the liabilities transferred to the reinsurer. For example, if the ceding entity agrees to compensate the reinsurer for the prepayment, such as by crediting the reinsurer with investment income on prepaid amounts or balances held, the ceding entity has not, in substance, recovered its transferred liabilities but rather has received a deposit from the reinsurer that should be accounted for accordingly.

30. Q: If the ceding entity does not expect to receive any recoveries because the reinsurer has agreed to reimburse claimants under the reinsured contracts directly, would the ceding entity be considered to have recovered or terminated its transferred liabilities?

A: No. In the example given, the reinsurer is substantively acting as disbursing agent for the ceding entity. Therefore, the ceding entity cannot be said to have recovered amounts due from the reinsurer before payment is made to the claimant.

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31. Q: What accounting entries would a ceding entity make to report a retroactive reinsurance contract?

A: Accounting Entries for a Ceding Entity to Report a Retroactive Reinsurance Contract:

Entry 1		
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)	10,000	
Retroactive Reinsurance Gain (I/S)		2,000
Cash		8,000

To record initial portfolio transfer, see paragraph 34.c. and paragraph 34.h. The ceding entity must establish the segregated surplus per paragraph 34.d.

Entry 1A		
Retro. Reins. Gain	2,000	
Profit/Loss Account		2,000

To close gain from retroactive transaction.

Entry 1B		
Profit/Loss Account	2,000	
Special Surplus from Retro. Reins.		2,000

To close profit from retroactive reinsurance to special surplus.

Entry 2		
Cash	2,000	
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)		2,000

To record recovery of paid losses from the reinsurer. Outstanding ceded reserves after this recovery equals $8,000, and special surplus from retroactive reinsurance account equals $2,000; therefore, segregated surplus account is not changed per paragraph 34.j.

Entry 3		
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)	3,000	
Retroactive Reinsurance Gain (I/S)		3,000

To record subsequent revision of the initial reserves ceded per paragraph 34.j. The segregated surplus account is increased to $5,000 as a result of this upward development.

Entry 3A		
Retro. Reinsurance Gain	3,000	
Profit/Loss Account		3,000

To close profit from retroactive reinsurance.

Entry 3B		
Profit/Loss (I/S)	3,000	
Special Surplus from Retro. Reins.		3,000

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To close profit and loss account to special surplus. (Retroactive reinsurance reserves ceded or assumed account balance equals $11,000. Special Surplus from retroactive reinsurance balance equals $5,000.)

Entry 4		
Cash	4,000	
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)		4,000

To record recovery of paid losses from the reinsurer. Outstanding ceded reserves after this recovery equals $7,000, therefore segregated surplus account is not changed per paragraph 34.j.

Entry 5		
Cash	3,000	
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)		3,000

To record recovery of paid losses from reinsurer. Outstanding ceded reserves after recovery equals $4,000, therefore the following entry is needed per paragraph 34.f. and paragraph 34.j.

Entry 5A		
Special Surplus—Retro. Reins.	1,000	
Unassigned Funds		1,000

Retroactive Reinsurance reserves ceded or assumed after this entry equals $4,000.

Entry 6		
Retroactive Reinsurance Loss (I/S)	1,000	
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)		1,000

To record subsequent revision of the initial reserves ceded per paragraph 34.j. The segregated surplus account is decreased as a result of this downward development to $3,000. The following entry is needed per paragraph 34.f. and paragraph 34.j.

Entry 6A		
Profit/Loss Account	1,000	
Retro. Reins. Loss		1,000

To close loss to profit and loss account.

Entry 6B		
Special Surplus from Retro. Reins.	1,000	
Profit/Loss Account		1,000

To close profit and loss account to special surplus. (Remaining balance of retroactive reinsurance reserve ceded or assumed account equals $3,000.) (Special surplus from retro. reins. account balance equals $3,000.)

Entry 7		
Cash	2,500	
Retroactive Reinsurance Gain (I/S)	500	
Retroactive Reinsurance Reserves Ceded or Assumed (B/S)		3,000

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Entry 7A		
Profit and Loss Account	500	
Retro. Reins. Gain		500

To close other income to profit and loss account.

Entry 7B		
Special Surplus from Retro. Reins.	500	
Profit/Loss Account		500

To close profit and loss account to special surplus. (Remaining balance of special surplus from retro. reins. account equals $2,500.) (Remaining balance of retroactive reinsurance reserve ceded or assumed account -0-.)

Entry 7C		
Special Surplus from Retro. Reins.	2,500	
Unassigned Funds		2,500

To close remaining special surplus account to unassigned surplus.

32. Q: How should the parties account for an adverse loss development reinsurance contract where, as of the statement date, the attachment level of the contract exceeds the ceding company's current case and IBNR reserves for the covered accident years (i.e. no surplus gain and no reinsurance recoverable as of the statement date), and the ceding company transferred cash to the reinsurer at the inception of the contract?

A: An adverse loss development reinsurance contract covering prior accident years meets the definition of "retroactive reinsurance" set forth in paragraph 26 of SSAP No. 62R:

> ….reinsurance in which a reinsurer agrees to reimburse a ceding entity for liabilities incurred as a result of past insurable events covered under contracts subject to the reinsurance….

Paragraph 34.k. of SSAP No. 62R specifically provides that the consideration paid for a retroactive reinsurance contract is to be recorded as a decrease in ledger assets by the ceding entity and an increase in ledger assets by the assuming entity.

Question 31 illustrates the accounting entries for retroactive reinsurance contracts.

If the retroactive reinsurance contract transfers both components of insurance risk then, pursuant to paragraph 34 of SSAP No. 62R, the ceding company would record the consideration paid as a decrease in ledger assets, recognize an expense for the reinsurance ceded through Other Income or Loss accounts as a write-in item identified as "Retroactive Reinsurance Ceded", and record the recoverable from the reinsurer as a contra liability.

No contra liability is established until and unless (and then only to the extent that) the ceding company establishes reserves which exceed the attachment point.

For the contract described, at inception no contra liability is recorded to offset current liability for the business ceded, since the ceded retroactive reinsurance premium relates to coverage in excess of the current liabilities recorded by the ceding company.

Once the ceding company's recorded liabilities exceed the attachment point of the adverse loss development reinsurance contract and triggers reinsurance recoverable from the reinsurer, a contra

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liability is established by the ceding company for the amount of the reinsurance recoverable. Any surplus resulting from the retroactive reinsurance is carried as a write-in item on the balance sheet designated as "Special Surplus from Retroactive Reinsurance Account." The surplus gain may not be classified as unassigned funds (surplus) until the actual retroactive reinsurance recovered exceeds the consideration paid.

If any portion of a retroactive reinsurance contract does not transfer insurance risk, then the portion which does not transfer risk is accounted for as a deposit pursuant to paragraph 40. The deposit is reported as an admitted asset of the ceding company if the reinsurer is licensed, accredited, certified or otherwise qualified in the ceding company's state of domicile as described in Appendix A-785, or if there are funds held by or on behalf of the ceding company as described in that appendix. Receipts and disbursements under the contract are recorded through the deposit/liability accounts. Amounts received in excess of the deposit made are recognized as a gain in the Other Income or Loss account.

Accounting entries for a ceding entity to report a retroactive reinsurance contract at the inception of which the cedent's reserves are lower than the attachment point of the reinsurance coverage:

Assume the company pays $16m to purchase adverse development coverage of $50m, above an attachment point.

Entry 1: Payment of Retrospective Reinsurance Premium

Retrospective Reinsurance Expense*	$16m	
Cash		$16m

The company pays $16m premium for the retrospective reinsurance contract.
*This is an Other Expense item, it does not flow through Schedule F or Schedule P.

Entry 2: Adverse Development Reaches the Attachment Point

Losses Incurred	$25m	
Gross Loss Reserve		$25m
Recoverable on Retro Reinsurance Contract**	$25m	
Other Income*		$9m
Contra – Retro Reinsurance Expense*		$16m
Surplus***	$9m	
Segregated Surplus***		$9m

The company incurs $25m development on reserves related to the contract.
*These are Other Income/Expense items do not flow through Schedule F or Schedule P.
**A contra-liability write-in item, not netted against loss reserves.
***Surplus is segregated in the amount of [$25m - $16m = $9m] recoverables less consideration paid.

Entry 3: Cash is Recovered on Paid Losses

Cash	$20m	
Recoverable on Retrospective Reinsurance Contract		$20m
Segregated Surplus	$4m	
Surplus		$4m

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The company recovers $20m cash from reinsurer on this retro contract. Segregated Surplus decreases in the amount of [$20m - $16m = $4m] (decreases for amount recovered in excess of consideration paid).

33. Q: How should a ceding company account for payment of the premium for a retroactive reinsurance contract by the ceding company's parent company or some other person not a party to the reinsurance contract (for example, adverse loss development reinsurance contracts purchased by the parent company in the context of the purchase or sale of the ceding company)?

A: If the reinsurance premium is not paid directly by the ceding company but is instead paid on behalf of the ceding company by the ceding company's parent company or some other entity not a party to the reinsurance contract, then the ceding company should (1) record an increase in gross paid in and contributed surplus in the amount of the reinsurance premium to reflect the contribution to surplus by the parent or third party payor, and (2) record an expense in the amount of the reinsurance premium and account for the contract as provided in questions 31 and 32.

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EXHIBIT B – P&C RUNOFF REINSURANCE TRANSACTIONS

The following provides illustrative journal entries for P&C Runoff Reinsurance Transactions.

Example 1: Transfer of existing block of runoff business **with no residual UPR** on books of Transferor

Cedent/Transferor		**DR**	**CR**
Day 1 – Cedent transfers 50,000 in reserves for 50,000			
Ceded Reinsurance Recoverable (U&I Part 2A & Sch. F)	Contra Liab ↑	50,000	
Cash	Asset ↓		50,000
Losses Paid (U/W Part 2 & Sch. P)	I/S ↓	50,000	
Change in Reserves - Incurred Losses (U&I Part 2)	I/S ↑		50,000
Unlike novation, gross reserves stay on books of transferor			
Day 360 – Negative Development on Transferred Business - 3,000			
Reinsurance Recoverable on Unpaid Losses (Sch. F)	Contra Liab ↑	3,000	
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↑		3,000
Day 540 – Reinsurer Pays the Loss @ Reported Reserve			
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↓	53,000	
Ceded Reinsurance Recoverable (U&I Part 2A & Sch. F)	Contra Liab ↓		53,000
Reinsurer/ Transferee			
Day 1 – Cedent transfers 50,000 in reserves for 50,000			
Cash	Asset ↑	50,000	
Reported Losses on Reins. Assumed (U&I Part 2A & Sch. P)	Liab ↑		50,000
Change In Reserves – Incurred Losses (U&I Part 2)	I/S ↓	50,000	
Losses Paid or Incurred (negative) (U&I Part 2 & Sch. P)	I/S ↑		50,000
Day 360 – Negative Development on Transferred Business - 3,000:			
Change in Reserves – Incurred Losses (U&I Part 2)	I/S↓	3,000	
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↑		3,000
Day 540 – Reinsurer Pays the Loss			
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↓	53,000	
Cash	Asset ↓		53,000

Comments:
Since the Transferor is ceding incurred losses neither party should have premium impacted. To do that would distort many financial ratios.

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Example 2: Transfer of existing block of runoff business **with some residual UPR** of 10,000 on books of Transferor (this should be less common).

Cedent/Transferor		**DR**	**CR**
Day 1 – Cedent transfers 50k in reserves & 10k UPR for 60,000			
Ceded Reinsurance Recoverable (U&I Part 2A & Sch. F)	Contra Liab ↑	50,000	
Unearned Premium Reserve (U&I Part 1 & 1A)	Liab ↓	10,000	
Cash	Asset ↓		60,000
Ceded Premium Written (U&I Part 1B)	I/S ↓	10,000	
Losses Paid (U&I Part 2 & Sch. P)	I/S ↓	50,000	
Change in Reserves - Incurred Losses (U&I Part 2)	I/S ↑		50,000
Change in UPR (U&I Part 1 & 1A)	I/S ↑		10,000
Unlike novation, gross reserves stay on books of transferor			
Day 180 – Premium is Fully Earned (Assumes 80% Loss Ratio)			
Ceded Reinsurance Recoverable (U&I Part 2A & Sch. F)	Contra Liab ↑	8,000	
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↑		8,000
To mirror the increase in unpaid losses by the transferee			
Day 360 – Negative Development on Transferred Business - 3,000:			
Reinsurance Recoverable on Unpaid Losses (Sch. F)	Contra Liab ↑	3,000	
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↑		3,000
Day 540 – Reinsurer Pays the Loss @ Reported Reserves (50+8+3)			
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↓	61,000	
Ceded Reinsurance Recoverable (U&I Part 2A & Sch. F)	Contra Liab ↓		61,000

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Reinsurer/Transferee			
Day 1 – Cedent transfers 50k in reserves & 10k UPR for 60,000			
Cash	Asset ↑	60,000	
Reported Losses on Reins. Assumed (U&I Part 2A & Sch. P)	Liab ↑		50,000
Unearned Premium Reserve (U&I Part 1 & 1A)	Liab ↑		10,000
Assumed Premium Written (U&I Part 1B)	I/S ↑		10,000
Change In Reserves – Incurred Losses (U&I Part 2)	I/S ↓	50,000	
Change in UPR (U&I Part 1 & 1A)	I/S ↓	10,000	
Losses Paid or Incurred (negative) (U&I Part 2 & Sch. P)	I/S ↑		50,000
Day 180 – Premium is Fully Earned (Assumes 80% Loss Ratio)			
Unearned Premium Reserve (U&I Part 1 & 1A)	Liab ↓	10,000	
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↑		8,000
Change In Reserves – Incurred Losses (U&I Part 2)	I/S↓	8,000	
Change in UPR (U&I Part 1 & 1A)	I/S ↑		10,000
To record the increase in unpaid losses by the transferee			
Day 360 – Negative Development on Transferred Business -3,000:			
Change In Reserves – Incurred Losses (U&I Part 2)	I/S↓	3,000	
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↑		3,000
Day 540 – Reinsurer Pays the Loss @ Reported Reserves (50+8+3)			
Reserves for Unpaid Losses (U&I Part 2A & Sch. P)	Liab ↓	61,000	
Cash	Asset ↓		61,000

Comments:
In this second example, the portion of the runoff business that has an UPR associated with it is essentially booked as prospective reinsurance. Other elements of the example are the same except that we assumed an 80% loss ratio on the unearned portion of the business.

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EXHIBIT C – ILLUSTRATION OF A REINSURANCE CONTRACT THAT IS ACCOUNTED FOR AS A DEPOSIT USING THE INTEREST METHOD

Assumptions:

Premium = $1,000 (assumes no commissions or allowances)
Coverage Period = 1 year
Initial expected recoveries = $225 per year (at end of year) for five years
Initial Implicit rate = 4% ~~percent~~*

*Present value of $225 per year for five years at 4% ~~percent~~ = $1,000

At the end of Year 2, the timing of anticipated recoveries under the reinsurance contract changes. A reevaluation of the implicit interest rate produces a rate of 3.63% ~~percent~~ and an asset of $640 at the end of the year.

Description	Interest Income	Cash Recoveries	Deposit Balance
Initial payment			$1,000
Year 1 (4%)	$ 40		$1,040
End of Year 1		$ (225)	$ 815
Year 2 (4%)	$ 33		$ 848
End of Year 2		$ (200)	$ 648
Yield Adjustment	$ (8)		$ 640
Year 3 (3.63%)	$ 23		$ 663
End of Year 3		$ (175)	$ 488
Year 4 (3.63%)	$ 18		$ 506
End of Year 4		$ (175)	$ 331
Year 5 (3.63%)	$ 12		$ 343
End of Year 5		$ (175)	$ 168
Year 6 (3.63%)	$ 7		$ 175
End of Year 6		$ (175)	$ 0

At the inception of the contract, the ceding insurer records a deposit asset of $ 1,000 and the assuming company, a $1,000 deposit liability. The asset is admitted providing the conditions for credit for reinsurance are met.

At subsequent reporting dates, the deposit asset is adjusted by calculating the effective yield on the reinsurance agreement to reflect actual payments to date and expected future payments with a corresponding credit to interest income by the ceding company and interest expense by the assuming company.

At the end of year two, it is determined that the expected cash flows will differ from previous estimates, resulting in a lower effective yield on the deposit asset. The deposit asset is adjusted to the amount that would have existed at the reporting date had the new effective yield been applied from the inception of the reinsurance agreement. The adjustment is charged to interest income, i.e., as a reduction of interest income. Interest income during the remaining term of the agreement is reduced accordingly (i.e., the yield is reduced from 4.0% to 3.63%).

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EXHIBIT D – ILLUSTRATION OF ASBESTOS AND POLLUTION COUNTERPARTY REPORTING EXCEPTION

SCHEDULE F – PART 3[3]
Aging of Ceded Reinsurance as of December 31, Current Year
(000 Omitted)

1	2	3	4	5	6	Reinsurance Recoverable On		
						7	8	9
ID Number	NAIC Company Code	Name of Reinsurer	Domiciliary Jurisdiction	Special Code	Reinsurance Premiums Ceded	Paid Losses	Paid LAE	Known Case Loss Reserves
FEIN	####	Retroactive Reinsurer X	NE	3		3,000	3,000	15,000
FEIN	####	Original Company A	US	3				5,000
Subtotal Other U.S. Authorized						**3,000**	**3,000**	**20,000**
AA-	####	Original Company B	UK	3		12,000	9,000	2,500
AA-	####	Original Company C	UK	3		6,000	3,000	7,500
Subtotal Other Non-U.S. Unauthorized						**18,000**	**12,000**	**10,000**
999999 Totals						**21,000**	**15,000**	**30,000**

Reinsurance Recoverable On				16	Reinsurance Payable		19	Collateral	
10	11	12	15		17	18		24	25
Known Case LAE Reserves	IBNR Loss Reserves	IBNR LAE Reserves	Cols. 7 through 14 Totals	Amount in Dispute Included in Column 15	Ceded Balances Payable	Other Amounts Due to Reinsurers	Net Amount Recoverable from Reinsurers Cols. 15 – [17 + 18]	Single Beneficiary Trusts Other Allowable Collateral	Total Funds Held Payables and Collateral
15,000	25,000[4]	37,500	98,500		6,000		92,500		
2,500	10,000	15,000	32,500				32,500		
17,500	**35,000**	**52,500**	**131,000**		**6,000**		**125,000**		
7,500	12,500	5,000	48,500				48,500	48,500	48,500
5,000	2,500	17,500	41,500				41,500	41,500	41,500
12,500	**15,000**	**22,500**	**90,000**				**90,000**	**90,000**	**90,000**
30,000	**50,000**	**75,000**	**221,000**		**6,000**		**215,000**	**90,000**	**90,000**

Reinsurance Recoverable on Paid Losses and Paid Loss Adjustment Expenses						
	Overdue					
37	38	39	40	41	42	43
Current Reinsurance Recoverable on Paid Losses and Paid LAE	1 to 29 days Reinsurance Recoverable on Paid Losses and Paid LAE	30 to 90 days Reinsurance Recoverable on Paid Losses and Paid LAE	91 to 120 days Reinsurance Recoverable on Paid Losses and Paid LAE	Over 120 days Reinsurance Recoverable on Paid Losses and Paid LAE	Total Overdue Reinsurance Recoverable on Paid Losses and Paid LAE	Total Due Reinsurance Recoverable on Paid Losses and Paid LAE Cols. 37 + 42 (In total should equal Cols. 7 + 8)
6,000						6,000
6,000						**6,000**
21,000						21,000
9,000						9,000
30,000						**30,000**
36,000						**36,000**

[3] Note that unused columns have been removed for this exhibit.

[4] This example assumes 1/2 of the original company reinsurers' unpaid recoverables are Asbestos and Pollution related.

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SUPPLEMENTAL SCHEDULE FOR REINSURANCE COUNTERPARTY REPORTING EXCEPTION – ASBESTOS AND POLLUTION CONTRACTS

For The Year Ended December 31, 20___ ($000 Omitted)

1 ID Number (Original Reinsurer)	2 NAIC Company Code (Original Reinsurer)	3 Name of Reinsurer (Original Reinsurer)	4 Domiciliary Jurisdiction (Original Reinsurer)	5 ID] Number (Retroactive Reinsurer)	6 Name of Retroactive Reinsurer Reported in Sch. F Part 3 (Retroactive Reinsurer)	Reinsurance Recoverable On				
						7 Paid Losses	8 Paid LAE	9 Unpaid Case Losses & LAE	10 IBNR Losses & LAE	11 Cols. 7+ 8+9+10 Totals
		Original Company A	US		Retroactive Reinsurer X	1,000	1,000	7,500	25,000	34,500
Subtotal Authorized						**1,000**	**1,000**	**7,500**	**25,000**	**34,500**
		Original Company B	UK		Retroactive Reinsurer X	1,000	1,000	10,000	17,500	29,500
		Original Company C	UK		Retroactive Reinsurer X	1,000	1,000	12,500	20,000	34,500
Subtotal Other Non-U.S. Unauthorized						**2,000**	**2,000**	**22,500**	**37,500**	**64,000**
9999999 Totals						**3,000**	**3,000**	**30,000**	**62,500**	**98,500**

Original Reinsurer Collateral			15	Reinsurance Recoverable On Paid Losses and Paid Loss Adjustment Expenses						23	24
12 Funds Held (Original Reinsurer)	13 Letters Of Credit (Original Reinsurer)	14 Trust Funds And Other Allowed Offset Items	Amounts Approved As Other Allowed Offset Items	16 Current	Overdue 17 1 – 29 Days	18 30 – 90 Days	19 91 – 120 Days	20 Over 120 Days	21 Total Overdue	22 Total Due	Percentage Overdue	Percentage More Than 90 Days Overdue
-	-	-	(a)	2,000	-	-	-	-	-	2,000	-	-
-	**-**	**-**	**-**	**2,000**						**2,000**		
-	-	-	29,500	2,000	-	-	-	-	-	2,000	-	-
-	-	-	34,500	2,000	-	-	-	-	-	2,000	-	-
-	**-**	**-**	**64,000**	**4,000**						**4,000**		
-	**-**	**-**	**64,000 (b)**	**6,000**	**-**	**-**	**-**	**-**	**-**	**6,000**		

(a) Amount is zero because available offsets are not applied for authorized reinsurers under the credit for reinsurance model.

(b) Annual statement Note 1 would disclose total impacts to the provision for reinsurance composed of 1) $64,000 (impact for unauthorized/uncollateralized) plus 2) reduction to the provision for overdue.

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Statement of Statutory Accounting Principles No. 63

Underwriting Pools

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 03-02
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 2

Effective Date and Transition 3

REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for underwriting pools and associations.

SUMMARY CONCLUSION

2. Underwriting pools and associations can be categorized as follows: (a) involuntary, (b) voluntary, and (c) intercompany.

3. Involuntary pools represent a mechanism employed by states to provide insurance coverage to those with higher than average probability of loss who otherwise would be excluded from obtaining coverage. Reporting entities are generally required to participate in the underwriting results, including premiums, losses, expenses, and other operations of involuntary pools, based on their proportionate share of similar business written in the state. Involuntary plans are also referred to as residual market plans, involuntary risk pools, and mandatory pools.

4. Voluntary pools are similar to involuntary pools except they are not state mandated and a reporting entity participates in the pool voluntarily. In addition, voluntary pools are not limited to the provision of insurance coverage to those with higher than average probability of loss, but often are used to provide greater capacity for risks with exceptionally high levels of insurable values (e.g., aircraft, nuclear power plants, refineries, and offshore drilling platforms).

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5. Intercompany pooling relates to business which is pooled among affiliated entities who are party to a pooling arrangement.(INT 03-02)

6. Participation in a pool may be on a joint and several basis, i.e., in addition to a proportional share of losses and expenses incurred by the pool, participants will be responsible for their share of any otherwise unrecoverable obligations of other pool participants. In certain instances, one or more entities may be designated as servicing carriers for purposes of policy issuance, claims handling, and general administration of the pooled business, while in other cases a pool manager or administrator performs all of these functions and simply bills pool participants for their respective shares of all losses and expenses incurred by the pool. In either case, liabilities arising from pooled business are generally incurred on a basis similar to those associated with non-pooled business, and should therefore be treated in a manner consistent with the guidelines set forth in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*.

7. Intercompany pooling arrangements involve establishment of a conventional quota share reinsurance agreement under which all of the pooled business is ceded to the lead entity and then retroceded back to the pool participants in accordance with their stipulated shares. Arrangements whereby there is one lead company that retains 100% of the pooled business and all or some of the affiliated companies have a 0% net share of the pool may qualify as intercompany pooling. In these arrangements, only the policy issuing entity has direct liability to its policyholders or claimants; other pool participants are liable as reinsurers for their share of the issuing entity's obligations. Although participants may use different assumptions (e.g., discount rates) in recording transactions, the timing of recording transactions shall be consistently applied by all participants.

8. Underwriting results relating to voluntary and involuntary pools shall be accounted for on a gross basis whereby the participant's portion of premiums, losses, expenses, and other operations of the pools are recorded separately in the financial statements rather than netted against each other. Premiums and losses shall be recorded as direct, assumed, and/or ceded as applicable. If the reporting entity is a direct writer of the business, premiums shall be recorded as directly written and accounted for in the same manner as other business which is directly written by the entity. To the extent that premium is ceded to a pool, premiums and losses shall be recorded in the same manner as any other reinsurance arrangement. A reporting entity who is a member of a pool shall record its participation in the pool as assumed business as in any other reinsurance arrangement.

9. Underwriting results relating to intercompany pools shall be accounted for and reported as described in paragraph 8. While it is acceptable that intercompany pooling transactions be settled through intercompany arrangements and accounts, intercompany pooling transactions shall be reported on a gross basis in the appropriate reinsurance accounts consistent with other direct, assumed and ceded business.

10. Equity interests in, or deposits receivable from, a pool represent cash advances to provide funding for operations of the pool. These are admitted assets and shall be recorded separately from receivables and payables related to a pool's underwriting results. Receivables and payables related to underwriting results shall be accounted for in accordance with the guidance in paragraphs 6-8. If it is probable that these receivables are uncollectible, any uncollectible amounts shall be written off against operations in the period such determination is made. If it is reasonably possible a portion of the balance is uncollectible but is not written off, disclosure requirements outlined in SSAP No. 5R shall be followed.

Disclosures

11. If a reporting entity is part of a group of affiliated entities which utilizes a pooling arrangement under which the pool participants cede substantially all of their direct and assumed business to the pool, the financial statements shall include:

a. A description of the basic terms of the arrangement and the related accounting;

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b. Identification of the lead entity and of all affiliated entities participating in the intercompany pool (include NAIC Company Codes) and indication of their respective percentage shares of the pooled business;

c. Description of the lines and types of business subject to the pooling agreement;

d. Description of cessions to non-affiliated reinsurers of business subject to the pooling agreement, and indication of whether such cessions were prior to or subsequent to the cession of pooled business from the affiliated pool members to the lead entity;

e. Identification of all pool members which are parties to reinsurance agreements with non-affiliated reinsurers covering business subject to the pooling agreement and which have a contractual right of direct recovery from the non-affiliated reinsurer per the terms of such reinsurance agreements;

f. Explanation of any discrepancies between entries regarding pooled business on the assumed and ceded reinsurance schedules of the lead entity and corresponding entries on the assumed and ceded reinsurance schedules of other pool participants;

g. Description of intercompany sharing, if other than in accordance with the pool participation percentage, of the Aging of Ceded Reinsurance (Schedule F, Part 3) and the write–off of uncollectible reinsurance;

h. Amounts due to/from the lead entity and all affiliated entities participating in the intercompany pool as of the balance sheet date.

12. Refer to the Preamble for further discussion regarding disclosure requirements.

Effective Date and Transition

13. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 97—Underwriting Pools and Associations Including Intercompany Pools*

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Statement of Statutory Accounting Principles No. 64

Offsetting and Netting of Assets and Liabilities

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 20-06
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 2
Relevant Literature 2
Effective Date and Transition 3

REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for offsetting and netting of assets and liabilities.

SUMMARY CONCLUSION

2. Assets and liabilities shall be offset and reported net only when a valid right of setoff exists except as provided for in paragraphs 3 and 4. A right of setoff is a reporting entity's legal right, by contract or otherwise, to discharge all or a portion of the debt owed to another party by applying an amount that the other party owes to the reporting entity against the debt. A valid right of setoff exists only when all the following conditions are met:

a. Each of the two parties owes the other determinable amounts. An amount shall be considered determinable for purposes of this provision when it is reliably estimable by both parties to the agreement;

b. The reporting party has the right to set off the amount owed with the amount owed by the other party;

c. The reporting party intends to setoff; and

d. The right of setoff is enforceable at law.

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3. Assets and liabilities that meet the criteria for offset shall not be netted when prohibited by specific statements of statutory accounting principles. An example of such is in the case of reinsurance recoverables on paid losses and ceded premiums payable as provided for in *SSAP No. 62R—Property and Casualty Reinsurance*.

4. Netting of assets and liabilities for reporting purposes when no valid right of setoff exists shall be allowed only when provided for by specific statements of statutory accounting principles. An example of such is in the case of real estate investments required to be shown net of encumbrances as provided for in *SSAP No. 40R—Real Estate Investments.*

5. Amounts due to or from affiliates shall be offset and reported net only when the provisions of paragraph 2 are met.

Disclosures

6. The following quantitative information shall be disclosed (separately for assets and liabilities) at the end of each reporting period (interim and annual) when derivative, repurchase and reverse repurchase, and securities borrowing and securities lending assets and liabilities are offset and reported net in accordance with paragraph 2 (valid right to offset):

a. The gross amounts of recognized assets and recognized liabilities

b. The amounts offset in accordance with paragraph 2 (valid right to offset)

c. The net amounts presented in the statement of financial positions.

7. Assets and liabilities that have a valid right to offset under paragraph 2, but are not netted as they are prohibited under paragraph 3, are not required to be captured in the disclosures in paragraph 6.

Relevant Literature

8. This statement adopts paragraphs 1, 7 and 13 of *APB Opinion No. 10, Omnibus Opinion—1966* and *FASB Interpretation No. 39, Offsetting of Amounts Related to Certain Contracts* with modifications (1) to prohibit offsetting as provided in specific statements and require netting when provided in specific statements, and (2) to reject guidance in paragraphs 10, 10A, and 10B of FIN 39, as amended by FSP FIN 39-1, that permits a reporting entity election to offset fair value amounts recognized for derivative instruments and fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral arising from the derivative instruments with the same counterparty under a master netting agreement. Offsetting for statutory accounting purposes is limited to situations meeting the conditions in paragraph 2 and 4 of this SSAP. This statement adopts *FASB Emerging Issues Task Force No. 86-25, Offsetting Foreign Currency Swaps.*

9. This statement rejects *FSP FIN 39-1, Amendment of FASB Interpretation 39*. This statement rejects *FASB Interpretation No. 41, Offsetting of Amounts Related to Certain Repurchase and Reverse Repurchase Agreements.* FIN 41 has an offsetting exception for repurchase and reverse repurchase agreements and permits offsetting when the reporting parties do not intend to set off. This guidance is rejected for statutory accounting, and payables under repurchase agreements may only be offset against amounts recognized as receivables under reverse repurchase agreements if there is a valid right to offset meeting all the conditions, including the intent to offset, detailed in paragraph 2. This statement rejects *ASU 2011-11, Disclosures about Offsetting Assets and Liabilities* and *ASU 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*. Statutory disclosure requirements for assets and liabilities reported net under a valid right to offset are detailed in paragraph 6.

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Effective Date and Transition

10. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The revisions to paragraphs 8-9 are effective January 1, 2013. The revisions to paragraph 9 rejecting FIN 41 reflects a reversal of a prior decision to adopt FIN 41.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 76—Offsetting and Netting of Assets and Liabilities*

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Statement of Statutory Accounting Principles No. 65

Property and Casualty Contracts

STATUS

Type of Issue	Property and Casualty
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 02-10
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

Claims-Made Policies 2
Discounting 3
Structured Settlements 4
Policies with Coverage Periods Equal to or in Excess of Thirteen Months 4
High Deductible Policies 6
Asbestos and Environmental Exposures 8
Excess Statutory Reserve 9
Policyholder Dividends 9
Relevant Literature 9
Effective Date and Transition 9

REFERENCES **9**

Other 9
Relevant Issue Papers 9

EXHIBIT A – GUIDELINES FOR STATES WHO PRESCRIBE OR PERMIT DISCOUNTING ON A NON-TABULAR BASIS **10**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for property and casualty insurance contracts. Topics not covered by this statement shall comply with the more general statutory accounting guidance.

2. Topics specific to title insurance, mortgage guaranty insurance, and financial guaranty insurance are not within the scope of this statement. These topics are addressed in *SSAP No. 57—Title Insurance*, *SSAP No. 58—Mortgage Guaranty Insurance*, and *SSAP No. 60—Financial Guaranty Insurance*.

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SUMMARY CONCLUSION

3. Property and casualty insurance contracts can be written to cover insured events on the following reporting bases:

a. Occurrence—These policies cover insured events that occur within the effective dates of the policy regardless of when they are reported to the reporting entity. Liabilities for losses on these policies shall be recorded when the insured event occurs;

b. Claims-made—These policies cover insured events that are reported (as defined in the policy) within the effective dates of the policy, subject to retroactive dates when applicable. Liabilities for losses on these policies shall be recorded when the event is reported to the reporting entity; and

c. Extended reporting—Endorsements to claims-made policies covering insured events reported after the termination of a claims-made contract but subject to the same retroactive dates where applicable. See paragraphs 7 and 8 for guidance for when premium shall be earned and losses shall be recorded.

Claims-Made Policies

4. Normally, when claims-made coverage is obtained, existing coverage is being replaced. The existing coverage may have been a claims-made policy or an occurrence policy. In either case, in an effort to reduce premium costs, the insured may request that the claims-made coverage cover only claims reported within the effective dates of the policy that occur after a specified date. This specified date is referred to as the retroactive date of the claims-made policy and eliminates duplicate coverage when converting from occurrence coverage to claims-made coverage.

5. The liability for an insured event shall be determined in accordance with *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*.

6. Extended reporting endorsements, commonly referred to as tail coverage, allow extended reporting of insured events after the termination of a claims-made contract. Extended reporting endorsements modify the exposure period of the underlying contract and can be for a defined period (e.g., six months, one year, five years) or can be for an indefinite period.

7. When a reporting entity issues an extended reporting endorsement or contract and the preceding claims-made policy terminates, the reporting entity assumes liability for unreported claims and expense. This extended reporting coverage can be issued for an indefinite period or a fixed period. For indefinite reporting periods, premium shall be fully earned and loss and expense liability associated with unreported claims shall be recognized immediately. For coverage for a fixed period, premium shall be earned over the term of the fixed period, the reporting entity shall establish an unearned premium reserve for the unexpired portion of the premium and shall record losses as reported.

8. Some claims-made policies provide extended reporting coverage at no additional charge in the event of death, disability, or retirement of a natural person insured. In such instance, a policy reserve is required to assure that premiums are not earned prematurely. The amount of the reserve should be adequate to pay for all future claims arising from these coverage features, after recognition of future premiums to be paid by current insureds for these benefits. The reserve, entitled “extended reporting endorsement policy reserve” shall be classified as a component part of the unearned premium reserve considered to run more than one year from the date of the policy.

9. When the anticipated losses, loss adjustment expenses, and maintenance costs anticipated to be reported during the extended reporting period exceed the recorded unearned premium reserve for a

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claims-made policy, a premium deficiency reserve shall be recognized in accordance with *SSAP No. 53—Property and Casualty Contracts—Premiums*.

Discounting

10. With the exception of fixed and reasonably determinable payments such as those emanating from workers' compensation tabular indemnity reserves and long-term disability claims, property and casualty loss reserves shall not be discounted. No loss adjustment expense reserves shall be discounted.

11. Tabular reserves are indemnity reserves that are calculated using discounts determined with reference to actuarial tables which incorporate interest and contingencies such as mortality, remarriage, inflation, or recovery from disability applied to a reasonably determinable payment stream. Tabular reserves shall not include medical loss reserves or loss adjustment expense reserves.

12. Due to several instances in which states have prescribed or permitted practices to allow discounting on a non-tabular basis, recommended guidelines for discounting non-tabular unpaid loss and LAE are provided within Exhibit A. If a state has a prescribed or permitted practice allowing the use of discounts, or if discounting is utilized in accordance with this SSAP, financial statement disclosures are required in accordance with paragraphs 13-16.

13. In accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*, a change in the discount rate used in discounting loss reserves shall be accounted for as a change in estimate. SSAP No. 3 requires changes in estimates to be included in the statement of income in the period the change becomes known.

14. The financial statements shall disclose whether or not any of the liabilities for unpaid losses or unpaid loss adjustment expenses are discounted, including liabilities for workers' compensation. The following disclosures, for each line of business, shall be made separately:

a. Table(s) used;

b. Rate(s) used;

c. The amount of discounted liability reported in the financial statement;

d. The amount of tabular discount, by the line of business and reserve category (i.e., case and Incurred But Not Reported (IBNR));

e. The amount of interest accretion recognized in the statement of income; and

f. The line item(s) in the statement of income in which the interest accretion is classified.

15. If the rate(s) used to discount prior accident years' liabilities have changed from the previous financial statement or if there have been changes in other key discount assumptions such as payout patterns, the financial statements shall disclose:

a. Amount of discounted current liabilities at current rate(s) and assumption(s) (exclude the current accident year);

b. Amount of discounted current liabilities at previous rate(s) and assumption(s) (exclude the current accident year);

c. Change in discounted liability due to change in interest rate(s) and assumption(s); and

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d. Amount of non-tabular discount, by line of business and reserve category (i.e., case, defense and cost containment, adjusting and other).

16. Refer to the Preamble for further discussion regarding disclosure requirements.

Structured Settlements

17. Structured settlements are periodic fixed payments to a claimant for a determinable period, or for life, for the settlement of a claim. Frequently a reporting entity will purchase an annuity to fund the future payments. Reporting entities may purchase an annuity in which the entity is the owner and payee, or an annuity in which the claimant is the payee. When annuities are purchased to fund periodic fixed payments, they shall be accounted for as follows:

a. When the reporting entity is the owner and payee, no reduction shall be made to loss reserves. The annuity shall be recorded at its present value and reported as an other-than-invested asset. Income from the annuities shall be recorded as miscellaneous income. The present value of the annuity and the related amortization schedule shall be obtained from the issuing life insurance company at the time the annuity is purchased; and

b. When the claimant is the payee, loss reserves shall be reduced to the extent that the annuity provides for funding of future payments. The cost of the annuities shall be recorded as paid losses.

18. Statutory accounting and Generally Accepted Accounting Principles (GAAP) are consistent for the accounting of structured settlement annuities where the reporting entity is the owner and payee, and where the claimant is the owner and payee and the reporting entity has been released from its obligation. GAAP distinguishes structured settlement annuities where the owner is the claimant and a legally enforceable release from the reporting entity's liability is obtained from those where the claimant is the owner and payee but the reporting entity has not been released from its obligation. GAAP requires the deferral of any gain resulting from the purchase of a structured settlement annuity where the claimant is the owner and payee yet the reporting entity has not been released from its obligation. Statutory accounting treats these settlements as completed transactions and considers the earnings process complete, thereby allowing for immediate gain recognition.

19. The following information regarding structured settlements shall be disclosed in the financial statements:

a. The amount of reserves no longer carried by the reporting entity because it has purchased annuities with the claimant as payee, and the extent to which the reporting entity is contingently liable for such amounts should the issuers of the annuities fail to perform under the terms of the annuities; and

b. The name, location, and aggregate statement value of annuities due from any life insurer to the extent that the aggregate value of those annuities equal or exceed 1% of policyholders' surplus. This disclosure shall only include those annuities for which the reporting entity has not obtained a release of liability from the claimant as a result of the purchase of an annuity. The reporting entity shall also disclose whether the life insurers are licensed in the reporting entity's state of domicile.

20. Refer to the Preamble for further discussion regarding disclosure requirements.

Policies with Coverage Periods Equal to or in Excess of Thirteen Months

21. Some property and casualty insurance contracts are written for coverage periods that equal or exceed thirteen months. These contracts may be single premium or fixed premium policies, and generally

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are not subject to cancellation or premium modification by the reporting entity. The most common policies with such coverage periods are home warranty and mechanical breakdown policies. Accordingly, this guidance is primarily focused on home warranty and mechanical breakdown policies and does not apply to multiple-year contracts comprised of single-year policies, each of which have separate premiums and annual aggregate deductibles.

22. Revenues are generally not received in proportion to the level of exposure or period of exposure. In order to recognize the economic results of the contract over the contract period, a liability shall be established for the estimated future policy benefits while taking into account estimated future premiums to be received. Unearned premiums shall be recorded in accordance with paragraphs 23-33 of this statement.

23. Paragraphs 24-33 shall apply to all direct and assumed contracts or policies ("contracts"), excluding financial guaranty contracts, mortgage guaranty contracts, and surety contracts, that fulfill both of the following conditions:

a. The policy or contract term is greater than or equal to 13 months; and

b. The reporting entity can neither cancel the contract, nor increase the premium during the policy or contract term.

24. At any reporting date prior to the expiration of the contracts, the reporting entity is required to establish an adequate unearned premium reserve, to be reported as the unearned premium reserve. For each of the three most recent policy years, the gross (i.e., direct plus assumed) unearned premium reserve shall be no less than the largest result of the three tests described in paragraphs 27-29. For years prior to the three most recent policy years, the gross unearned premium reserve shall be no less than the larger of the aggregate result of Test 1 or the aggregate result of Test 2 or the aggregate result of Test 3 taken over all of those policy years.

25. Any reserve credit applicable for reinsurance ceded shall be appropriately reflected in the financial statements with the resulting net unearned premium reserve being established by the reporting entity.

26. The projected losses and expenses may be reduced for expected salvage and subrogation recoveries, but may not be reduced for anticipated deductible recoveries, unless the deductibles are secured by a letter of credit (LOC) or like security. Projected salvage and subrogation recoveries (net of associated expenses) shall be established based on reporting entity experience, if credible; otherwise, based on industry experience.

27. Test 1 is management's best estimate of the amounts refundable to the contractholders at the reporting date.

28. Test 2 is the gross premium multiplied by the ratio of paragraph 28.a. to paragraph 28.b.:

a. Projected future gross losses and expenses to be incurred during the unexpired term of the contracts; and

b. Projected total gross losses and expenses under the contracts.

29. Test 3 is the projected future gross losses and expenses to be incurred during the unexpired term of the contracts as adjusted below, reduced by the present value of the future guaranteed gross premiums, if any.

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a. A provision for investment income is permitted in the unearned premium reserve only with respect to the projected future losses and expenses used to determine the unearned premium reserve, and not with respect to incurred but unpaid losses and expenses;

b. A provision for investment income on projected future losses and expenses may be calculated to the expected date the loss or expense is incurred, not from the expected date of payment;

c. The rate of interest used to calculate the provision for investment income shall be reviewed and changed as necessary at each reporting date and shall not exceed the lesser of the following two standards:

i. The reporting entity's future net yield to maturity on statutory invested assets as shown in Schedule D, less a 1.5% actuarial provision for adverse deviations; or

ii. The current yield to maturity on a United States Treasury debt instrument maturing in five (5) years as of the reporting date.

d. The reporting entity's statutory invested assets shall be reduced by the loss and loss adjustment expense reserves on unpaid losses and expenses to calculate "available invested assets." If the available invested assets are less than the result of Test 3, as calculated above, an "invested asset shortfall" exists. In this event, the Test 3 reserve shall be recalculated with the provision for investment income based on the restricted amount of available invested assets.

30. For the purposes of Tests 2 and 3 of paragraphs 28 and 29, "expenses" shall include all incurred and anticipated expenses related to the issuance and maintenance of the policy, including loss adjustment expenses, policy issuance and maintenance expenses, commissions, and premium taxes.

31. The projected future losses and expenses are to be re-estimated for each reporting date, and the most recent estimate of these projected losses and expenses is to be used in these Tests. If a range is selected and no single point in the range is identified as being the most likely, then the midpoint of management's estimate of the range shall be used. For purposes of this statement, it is assumed that management can quantify the high end of the range. If management determines that the high end of the range cannot be quantified, then a range does not exist, and management's best estimate shall be accrued.

32. The reporting entity shall provide an Actuarial Opinion and Report in conformity with the NAIC *Annual Statement Instructions for Property and Casualty Insurers*. Exhibit A of the actuarial opinion shall include the following three items: 1) the Reserve for Direct and Assumed Unearned Premiums; 2) the Reserve for Net Unearned Premiums; and 3) any other premium reserve items on which an opinion is being expressed. If any of these three items are material, the material item(s) must also be covered in the opinion and relevant comments of the actuarial opinion.

33. The actuarial report shall include a description of the manner in which the adequacy of the amount of security for deductibles and self-insured retentions is determined. The actuarial report need not assess the credit-worthiness of the specific securities (e.g. LOC's), but the actuarial opinion must report collectibility problems if known to the actuary.

High Deductible Policies

34. Certain policies, particularly workers' compensation coverage, are available under high deductible plans. High deductible plans differ from self insurance coupled with an excess of loss policy because state laws generally require the reporting entity to fund the deductible and to periodically review the financial viability of the insured and make an assessment of the suitability of the deductible plan to the insured.

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35. The liability for loss reserves shall be determined in accordance with SSAP No. 55. Because the risk of loss is present from the inception date, the reporting entity shall reserve losses throughout the policy period, not over the period after the deductible has been reached. Reserves for claims arising under high deductible plans shall be established net of the deductible, however, no reserve credit shall be permitted for any claim where any amount due from the insured has been determined to be uncollectible.

36. If the policy form requires the reporting entity to fund all claims including those under the deductible limit, the reporting entity is subject to credit risk, not underwriting risk. Reimbursement of the deductible shall be accrued and recorded as a reduction of paid losses simultaneously with the recording of the paid loss by the reporting entity.

37. If the reporting entity does not hold specific collateral for the policy, amounts accrued for reimbursement of the deductible shall be billed in accordance with the provisions of the policy or the contractual agreement and shall be aged according to the contractual due date. In the absence of a contractual due date, billing date shall be utilized for the aging requirement. Deductible recoverables that are greater than ninety days old shall be nonadmitted. However, if the reporting entity holds specific collateral for the high deductible policy, 10%~~ten percent~~ of deductible recoverable in excess of collateral specifically held and identifiable on a per policy basis, shall be reported as a nonadmitted asset in lieu of applying the aging requirement; however, to the extent that amounts in excess of the 10% are not anticipated to be collected they shall also be nonadmitted. The collateral requirements of this paragraph may be satisfied when an insured provides one collateral instrument to secure amounts owed under multiple policies, provided that the reporting entity has the contractual right to apply the collateral to the high deductible policy. Collateral obtained at a group level that is not supported by an existing pooling agreement requires a written allocation agreement among all collateral beneficiaries. The terms of such agreement must be fair and equitable. Documentation supporting any allocation of collateral among reporting entities must be maintained to allow proper calculation of the nonadmitted amounts and prohibit double counting of collateral.

38. The financial statements shall disclose the following related to high deductible policies:

a. Gross (of high deductible) amount of loss reserves, unpaid by line of business.

b. The amount of reserve credit that has been recorded for high deductibles on unpaid claims and the amounts that have been billed and are recoverable on paid claims, by line of business and the total of these two numbers.

c. Related to the amounts that have been billed and are recoverable on paid claims,

i. paid recoverable amounts that are over 90 days overdue, and

ii. the amounts nonadmitted (per paragraph 37).

d. Total collateral pledged to the reporting entity related to deductible and paid recoverables:

i. the amount of collateral on balance sheet, and

ii. the amount of collateral off balance sheet.

e. The total amount of unsecured high deductible amounts related to unpaid claims and for paid recoverables and the total percentage that is unsecured.

f. Highest ten unsecured high deductible amounts by counterparty ranking. Note that the counterparty does not have to be named, just amount by counterparty 1, counterparty 2,

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etc. For this purpose, a group of entities under common control shall be regarded as a single customer.

39. Unsecured High Deductible Recoverables: If the individual obligor is part of a group under the same management or control, such as a professional employer organization (PEO), list the individual obligors, each of its related group members, and the total unsecured aggregate recoverables on high deductible policies for the entire group, which are greater than 1% of capital and surplus. For this purpose, a group of entities under common control shall be regarded as a single customer.

40. Refer to the Preamble for further discussion regarding disclosure requirements.

Asbestos and Environmental Exposures

41. Asbestos exposures are defined as any loss or potential loss (including both first party and third party claims) related directly or indirectly to the manufacture, distribution, installation, use, and abatement of asbestos-containing material, excluding policies specifically written to cover these exposures. Environmental exposures are defined as any loss or potential loss, including third party claims, related directly or indirectly to the remediation of a site arising from past operations or waste disposal. Examples of environmental exposures include but are not limited to chemical waste, hazardous waste treatment, storage and disposal facilities, industrial waste disposal facilities, landfills, superfund sites, toxic waste pits, and underground storage tanks.

42. Reporting entities that are potentially exposed to asbestos and/or environmental claims shall record reserves consistently with SSAP No. 55.

43. The financial statements shall disclose the following if the reporting entity is potentially exposed to asbestos and/or environmental claims:

a. The reserving methodology for both case and IBNR reserves;

b. The amount paid and reserved for losses and loss adjustment expenses for asbestos and/or environmental claims, on a direct, assumed and net of reinsurance basis. Each company should report only its share of a group amount (after applying its respective pooling percentage) if the company is a member of an intercompany pooling agreement;

c. Description of the lines of business written for which there is potential exposure of a liability due to asbestos and/or environmental claims, and the nature of the exposure(s);

d. The following for each of the five most current calendar years[1] on both a gross and net of reinsurance basis, separately for asbestos and environmental losses (including coverage dispute costs):

Beginning reserves	$_____
Incurred losses and loss adjustment expenses	_____
Calendar year payments for losses and loss adjustment expenses	_____
Ending reserves	$_____

[1] The requirement for five years of data is only applicable to the annual statement blank. The audited statutory financial report is only required to report two years. Additionally, the audited statutory financial statement shall include items not included in the notes to the annual statement blank where the blank's schedules and exhibits satisfy disclosure requirements that are not included in the audited statutory financial statement (i.e., Since the audited financial statements do not include Schedule P, all of the SSAP No. 55 disclosures shall be included in the audited notes to financial statements).

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44. Refer to the Preamble for further discussion regarding disclosure requirements.

Excess Statutory Reserve

45. This statement eliminates the requirement to record excess statutory reserves. Excess statutory reserves do not meet the definition of a liability established in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets.*

Policyholder Dividends

46. Dividends to policyholders immediately become liabilities of the reporting entity when they are declared by the board of directors and shall be recorded as a liability. Incurred policyholder dividends are reported in the statement of income.

47. The financial statements shall disclose the terms of dividend restrictions, if any. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

48. Structured settlements are addressed in *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts* (FAS 113). FAS 113 is addressed in *SSAP No. 62R—Property and Casualty Reinsurance*. This statement rejects the AICPA *Audit and Accounting Guide—Audits of Property and Liability Insurance Companies.*

Effective Date and Transition

49. This statement is effective for years beginning January 1, 2001. To the extent that the requirements of paragraphs 23-33 produce a higher reserve than the reporting entity would have established through the use of their previous methodology, the reporting entity may phase in the additional reserve over a period not to exceed three years. Such a phase in period shall only be permitted if the reporting entity is able to demonstrate that it would not be operating in a hazardous financial condition and that there is not adverse risk to its insureds. The phase in shall be at least 60% of the difference between the reserve required by this statement and the reserve determined by the previous methodology during the first year, 80% in the second year, and 100% in the third year. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance in the footnote of paragraph 43.d. was originally contained within *INT 02-10: Statutory Audit Report Notes and the Reporting Requirements Related to Discosures Containing Multiple Year Information* and was effective June 9, 2002.

REFERENCES

Other

- *Actuarial Standard of Practice No. 20, Discounting of Property and Casualty Loss and Loss Adjustment Expense*
- NAIC *Annual Statement Instructions for Property and Casualty Insurers*

Relevant Issue Papers

- *Issue Paper No. 65—Property and Casualty Contracts*

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EXHIBIT A – GUIDELINES FOR STATES WHO PRESCRIBE OR PERMIT DISCOUNTING ON A NON-TABULAR BASIS

As discussed in paragraph 10 of this statement, with the exception of fixed and reasonably determinable payments such as those emanating from workers' compensation tabular indemnity reserves and long-term disability claims, property and casualty loss reserves shall not be discounted. However, one of the most common prescribed or permitted state practices is to allow discounting of unpaid losses and unpaid loss adjustment expenses on a non-tabular basis. The recommendations in this exhibit are not requirements and therefore should only be viewed as a recommendation to those states that prescribe or permit non-tabular discounting.

Recommended Prescribed or Permitted Practice Guidelines

The state of XYZ office will permit [insert domestic companies if prescribed or insert insurance company name if prescribed] to discount its December 20XX unpaid loss (i.e., reported losses and incurred but not reported losses) and unpaid loss adjustment expense (LAE) reserves on an non-tabular basis subject to the following conditions:

1. The unpaid loss and LAE reserves shall be determined in accordance with *Actuarial Standard of Practice No. 20, Discounting of Property and Casualty Loss and Loss Adjustment Expense* (and as agreed to by an actuary) but in no event shall the rate used exceed the lesser of the following two standards:

   a. If the reporting entity's statutory invested assets are at least equal to the total of all policyholder reserves, the reporting entity's net rate of return on statutory invested assets, less 1.5%, otherwise, the reporting entity's average net portfolio yield rate less 1.5% as indicated by dividing the net investment income earned by the average of the reporting entity's current and prior year total assets; or

   b. The current yield to maturity on a United States Treasury debt instrument with maturities consistent with the expected payout of the liabilities.

2. Disclosure of the [insert either prescribed or permitted practice] in compliance with the requirements of the NAIC *Accounting Practices and Procedures Manual* and the *NAIC Annual Statement Instructions – Property and Casualty*, including but not limited to:

   Note 1 – Summary of Significant Accounting Policies

   A. Disclosure of permitted practice

      a. Disclose that the reporting entity employs a prescribed or permitted accounting practice that departs from the *Accounting Practices and Procedures Manual*; and

      b. Disclose the monetary effect on net income and statutory surplus of using the practice of discounting on a non-tabular basis rather than the NAIC statutory accounting practice of discounting fixed and reasonably determinable payments such as those emanating from workers' compensation tabular indemnity reserves and long-term disability claims.

   Note 32 – Discounting of Liabilities for Unpaid Losses or Unpaid Loss Adjustment Expenses
   XX. Non-tabular discounting

      a. Disclosure of whether the reporting entity is applying non-tabular discounting based upon a state prescribed or permitted practice. If permitted, provide further disclosure as to the date domiciliary state issued permitted practice and the

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expiration date of such practice;

b. Rate(s) used and the basis for the rate(s) used;

c. Amount of non-tabular discount disclosed by line of business and reserve category (i.e., unpaid loss, incurred but not reported, defense and cost containment expense, and adjusting and other expense); and

d. The amount of non-tabular discount reported in the statement.

Non-tabular discounting illustration:

	(1) Case	(2) IBNR	(3) Defense & Cost Containment Expense	(4) Adjusting & Other Expense
1. Homeowners/Farmowners				
2. Private Passenger Auto Liability/Medical				
3. Commercial Auto/Truck Liability/Medical				
4. Workers' Compensation				
5. Commercial Multiple Peril				
6. Medical Malpractice – Occurrence				
7. Medical Malpractice – Claims-Made				
8. Special Liability				
9. Other Liability – Occurrence				
10. Other Liability – Claims-Made				
11. Special Property				
12. Auto Physical Damage				
13. Fidelity, Surety				
14. Other (including Credit, Accident & Health)				
15. International				
16. Reinsurance Nonproportional Assumed Property				
17. Reinsurance Nonproportional Assumed Liability				
18. Reinsurance Nonproportional Assumed Financial Lines				
19. Products Liability – Occurrence				
20. Products Liability – Claims-Made				
21. Financial Guaranty/Mortgage Guaranty				
22. Total				

The rates used to discount Medical Malpractice unpaid losses at December 31, 20X2 have changed from the rates used at December 31, 20X1. At December 31, 20X2, the amount of discounted Medical Malpractice unpaid losses, excluding the current accident year, is $_____. Had these unpaid losses been discounted at the rates used at December 31, 20X1 the amount of discounted liabilities would be $_____. The reduction in the discounted liability due to the change in rates is $_____.

This illustration neither regulates, permits, nor prohibits the practice of discounting liabilities for unpaid losses or unpaid loss adjustment expenses.

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Statement of Statutory Accounting Principles No. 66

Retrospectively Rated Contracts

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 05-05
Relevant Appendix A Guidance	A-785

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 5
Relevant Literature 5
Effective Date and Transition 5

REFERENCES **6**

Other 6
Relevant Issue Papers 6

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for retrospectively rated contracts. This statement applies to property and casualty contracts, life insurance contracts, and accident and health contracts.

2. Retrospective reinsurance contracts are not within the scope of this statement. They are addressed in *SSAP No. 62R—Property and Casualty Reinsurance*.

SUMMARY CONCLUSION

3. A retrospectively rated contract is one which has the final policy premium calculated based on the loss experience of the insured during the term of the policy (including loss development after the term of the policy) and the stipulated formula set forth in the policy or a formula required by law. The periodic adjustments may involve either the payment of return premium to the insured or payment of an additional premium by the insured, or both, depending on experience. Retrospective rating features are common in certain property and casualty contracts, group life, and group accident and health contracts. Some contracts have retrospective features required by law. Contracts with retrospective rating features are referred to as loss sensitive contracts.

4. Amounts due from insureds and amounts due to insureds under retrospectively rated contracts meet the definitions of assets and liabilities as set forth in *SSAP No. 4—Assets and Nonadmitted Assets*

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and *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets*, respectively. Amounts due from insureds and amounts due to insureds under retrospectively rated contracts are admitted assets to the extent they conform to the requirements of this statement.

5. Initial premiums shall be recognized in accordance with *SSAP No. 51R—Life Contracts, SSAP No. 53—Property and Casualty Contracts—Premiums,* and *SSAP No. 54R—Individual and Group Accident and Health Contracts*.

6. Specific funds received by the prescription drug plan sponsor from either the Medicare Part D enrollee or the government as payment for standard coverage that will be subject to retrospective premium adjustments should be accounted for under this statement. These funds include 'Direct Subsidy', 'Low-Income Subsidy (premium portion)', 'Beneficiary Premium (standard coverage portion)', 'Part D Payment Demonstration' and 'Risk Corridor Payment Adjustment'. The funds noted above have a final policy amount that is calculated based on the loss experience of the insured during the term of the policy, therefore should be treated as such. Refer to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* for additional information and definitions of terms specifically related to Medicare Part D business.

7. Because policy periods do not always correspond to reporting periods and because an insured's loss experience may not be known with certainty until sometime after the policy period expires, retrospective premium adjustments shall be estimated based on the experience to date using one of the following methods:

a. Property and Casualty Contracts:

i. Use of actuarially accepted methods in accordance with filed and approved retrospective rating plans. This includes but is not limited to the application of historical ratios of retrospective rated developments to earned standard premium to develop a ratio which is then applied to those policies for which no retrospective calculation has been recorded or for which no modification to the recorded calculation is needed. This method results in the calculation of one amount which is either a net asset or a net liability;

ii. Reviewing each individual retrospectively rated risk, comparing known loss development (including IBNR) with that anticipated in the policy contract to arrive at the best estimate of return or additional premium earned at that point in time. This method results in the calculation of an asset or a liability for each risk. The total of all receivables shall be recorded as an asset and the total of all return premiums shall be recorded as a liability.

b. Life and Accident & Health Contracts: Reporting entities offering group coverage have extensive underwriting procedures and complex individually negotiated benefits and contracts. Due to cost and reporting deadlines, these factors make it difficult to establish an exact valuation of retrospective premium adjustments. The method used to estimate the liability shall be reasonable based on the reporting entity's procedures and consistent among reporting periods. Common methods include a mathematical approach using a complex algorithm of the reporting entity's underwriting rules and experience rating practices, and an aggregate or group approach.

8. Assumptions used in estimating retrospective premium adjustments shall be consistent with the assumptions made in recording other assets and liabilities necessary to reflect the underwriting results of the reporting entity such as claim and loss reserves (including IBNR) and contingent commissions. Contingent commissions and other related expenses shall be adjusted in the same period the additional or return retrospective premiums are recorded.

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9. Retrospective premium adjustments are estimated for the portion of the policy period that has expired and shall be considered an immediate adjustment to premium. Additional retrospective premiums and return retrospective premiums shall be recorded as follows:

a. Property and Casualty Reporting Entities:

i. Accrued additional retrospective premiums shall be recorded as a receivable with a corresponding entry made either to written premiums or as an adjustment to earned premiums. Premiums not recorded through written premium when accrued shall be recorded through written premium when billed;

ii. Accrued return retrospective premiums shall be recorded as part of the change in unearned premium (detailed in the underwriting and investment exhibit) liability with a corresponding entry made either to written premiums or as an adjustment to earned premiums. Premiums not recorded through written premium when accrued shall be recorded through written premium when billed;

iii. Ceded retrospective premium balances payable shall be recorded as liabilities, consistent with SSAP No. 62R. Ceded retrospective premiums recoverable shall be recorded as an asset. Consistent with *SSAP No. 64—Offsetting and Netting of Assets and Liabilities*, ceded retrospective premium balances payable may be deducted from ceded retrospective premiums recoverable when a legal right of setoff exists.

b. Life and Accident and Health Reporting Entities:

i. Accrued additional retrospective premiums shall be recorded as an asset, accrued retrospective premiums, with a corresponding entry to premiums;

ii. Accrued return retrospective premiums shall be recorded as a liability, provision for experience rating refunds, with a corresponding entry to premiums.

c. Managed Care/Accident and Health Reporting Entities

i. Accrued additional retrospective premiums shall be recorded as an asset, accrued retrospective premiums with a corresponding entry to premiums;

ii. Accrued return retrospective premiums shall be recorded as a liability, as part of Accident and Health Reserves (reserve for rate credits or experience rating refunds), with a corresponding entry to premiums.

10. The amount of accrued estimated retrospective premiums to be recorded as a nonadmitted asset for property and casualty insurers shall be determined as follows:

a. 100% of the amount recoverable from any person for whom any agents' balances or uncollected premiums are classified as nonadmitted, and item (b), plus item (c) or (d) below. Once an insurer has elected either (c) or (d) below, a change from one to the other requires approval from the insurer's domiciliary state and such change must be disclosed in the financial statements.

b. Retrospective premium adjustments shall be determined and billed or refunded in accordance with the policy provisions or contract provisions. If accrued additional retrospective premiums are not billed in accordance with the policy provisions or contract provisions, the accrual shall be nonadmitted.

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c. 10% of any accrued retrospective premiums not offset by retrospective return premiums, other liabilities to the same party (other than loss and loss adjustment expense reserves), or collateral, not otherwise used. Collateral shall be of the same types and quality permitted for use in connection with reinsurance (types of acceptable collateral vary from state to state) or by financial guaranty coverage issued by an insurer having an "A" or better rating from a nationally recognized rating agency. The financial guaranty coverage must allow the insured under the financial guaranty policy the same degree of access to payments under that policy as a beneficiary has under a qualified letter of credit as described in Appendix A-785. Accrued retrospectively rated premiums relating to bulk IBNR must be allocated to individual policyholder accounts prior to applying collateral by account. If the insurer is unable to allocate amounts by account, no credit may be taken for collateral.

d. An amount calculated using the factors below for accrued retrospective premiums not offset by retrospective return premiums, other liabilities to the same party (other than loss and loss expense reserves), or collateral, not otherwise used. Collateral shall be of the same types and quality permitted for use in connection with reinsurance (types of acceptable collateral vary from state to state) or by financial guaranty coverage issued by an insurer having an "A" or better rating from a nationally recognized rating agency. The financial guaranty coverage must allow the insured under the financial guaranty policy the same degree of access to payments under that policy as a beneficiary has under a qualified letter of credit as described in Appendix A-785.

Accrued retrospectively rated premiums relating to bulk IBNR must be allocated to individual policyholder accounts prior to categorizing by Quality Rating.

Insured's Current Quality Rating*	Insured's Corporate Debt Equivalent to (S&P/Moody's)**	Percentage of Retro Premium to be Nonadmitted***
1	AAA, AA, A/Aaa, Aa, A	1%
2	BBB/Baa	2%
3	BB/Ba	5%
4	B/B	10%
5	CCC, CC, C/Caa, Ca	20%
6	CI, D/C, or insured in default on debt service payments, or insured's debt service payments are jeopardized upon filing of a bankruptcy petition	100%

* The Percentage of Retro Premium to be Nonadmitted is based upon the Insured's Current Quality Rating (i.e., if an insured's quality rating drops, the percentage relating to the lower quality rating is used in calculating the amount to be nonadmitted and vice versa).

** Insureds that do not have a debt rating issued by a publicly recognized rating agency are required to be rated by the NAIC's Securities Valuation Office (SVO).

*** In the event the insured has no debt rating (either from a publicly recognized rating agency or from the SVO) the insured's quality rating will be considered category 5 for purposes of this calculation (i.e., a factor of 20% shall be applied), unless the insurer is aware of conditions of the insured that would warrant a category 6 classification (i.e., a factor of 100%).

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11. Once accrued retrospective premium is billed, the due date is governed by *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*. Life and accident and health reporting entities shall nonadmit any accrued retrospective premium that is more than 90 days due. If a reporting entity has issued more than one policy to the same insured, retrospective balances shall be netted in accordance with SSAP No. 64.

12. If, in accordance with SSAP No. 5R, it is probable that the additional retrospective premium is uncollectible, any uncollectible additional retrospective premium shall be written off against operations in the period the determination is made. If it is reasonably possible a portion of the balance in excess of the nonadmitted portion determined in accordance with paragraph 10 is not anticipated to be collected, the disclosure requirements outlined in SSAP No. 5R shall be made.

Disclosures

13. The financial statements shall disclose the method used by the reporting entity to estimate retrospective premium adjustments. The amount of net premiums written that are subject to retrospective rating features, as well as the corresponding percentage to total net premiums written, shall be disclosed. In addition, disclose whether accrued retrospective premiums are recorded through written premium or as an adjustment to earned premium.

14. The financial statements shall disclose the calculation of nonadmitted retrospective premium. If a reporting entity chooses treatment described in paragraph 10.c. or 10.d., the appropriate exhibit must be included in the Notes to Financial Statements in the annual statement. Once a reporting entity has elected either 10.c. or 10.d., a change from one to the other requires approval from the reporting entity's domiciliary state and such change must be disclosed in the financial statements.

15. The financial statements shall disclose the following amounts for medical loss ratio rebates required pursuant to the Public Health Service Act for the current reporting period year-to-date and prior reporting period year: incurred rebates, amounts paid and unpaid liabilities segregated into the following categories: individual, small group employer, large group employer and other. In addition, the impact of reinsurance assumed, ceded and net on the total medical loss ratio rebate shall be disclosed.

16. Refer to the Preamble for further discussion of the disclosure requirements.

Relevant Literature

17. This statement rejects *FASB Emerging Issues Task Force No. 93-14, Accounting for Multiple Year Retrospectively Rated Insurance Contracts* (EITF 93-14) since it applies only to multiple-year retrospectively rated contracts. The statutory principles outlined in the conclusion above are consistent with the guidance provided for accounting and retrospectively rated contracts in *FASB Statement No. 60, Accounting and Reporting by Insurance Companies* (FAS 60) and EITF 93-14, with the exception of the requirement to record certain amounts as nonadmitted. Although FAS 60 is rejected in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts* and EITF 93-14 is rejected in this statement, it is considered appropriate that the accounting for retrospectively rated contracts be consistent with those provisions of both FAS 60 and EITF 93-14 as they are consistent with the Statement of Concepts.

Effective Date and Transition

18. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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REFERENCES

Other

- NAIC *Annual Statement Instructions for Property and Casualty Insurance Companies*

Relevant Issue Papers

- *Issue Paper No. 66—Accounting for Retrospectively Rated Contracts*

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Statement of Statutory Accounting Principles No. 67

Other Liabilities

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Self-Insurance 1
Amounts Withheld or Retained by Company as Agent or Trustee 2
Remittances and Items Not Allocated 2
Interest Payable 3
Payable to Parent, Subsidiaries and Affiliates 3
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REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for other liabilities.

SUMMARY CONCLUSION

2. For purposes of identifying other liabilities, the guidance outlined in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* must be considered. This statement is not an all-inclusive list of other liabilities. Certain other liabilities are covered in other statements. All other liabilities, whether or not specifically identified in this statement, shall be recorded and disclosed in accordance with SSAP No. 5R, which states that "Liabilities shall be recorded on a reporting entity's financial statements when incurred."

Self-Insurance

3. Self-insurance occurs when an entity retains insurance risks associated with the entity's day-to-day operations that are commonly transferred to an insurer through an insurance contract.

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4. The fact that a decision is made not to insure against losses that can reasonably be expected sometime in the future does not necessitate accrual by the entity if it is not probable that an asset has been impaired or a liability incurred at the date of the financial statements.

5. If an uninsured (self-insured) event occurs, which either creates a liability or impairs an asset, the entity shall either establish a liability or write-down the impaired asset. The liability shall be established using the same estimation methodology an insurance company uses when an insurance contract is issued for the type of insurance risk which is self-insured. *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* describes the specific reserving guidance which shall be followed.

6. The related costs shall be recorded based on the nature of the underlying expenses, and allocated in accordance with *SSAP No. 70—Allocation of Expenses*. Related costs shall be recorded based on the nature of the underlying expenses.

Amounts Withheld or Retained by Company as Agent or Trustee

7. A reporting entity may, in the normal course of its business, withhold funds as an agent or trustee which will ultimately be paid to others.

8. Amounts withheld or retained by an entity as trustee or agent shall be recorded as a liability when the salaries or other compensation are expensed (paragraphs 8.a. and 8.b.) or the funds are received (paragraphs 8.c. through 8.e.). Examples of such occurrences are:

a. As an employer, the reporting entity deducts and withholds federal and state income taxes, social security taxes, charitable contributions, savings plan deductions, garnishments, employee contributions to pension plans, employee share of group life and health insurance premiums, and other employee salary withholdings or deductions;

b. Amounts due under deferred compensation arrangements shall be accrued in accordance with the provisions of *SSAP No. 92—Postretirement Benefits Other Than Pensions*. Segregated funds (i.e., Rabbi trusts and similar arrangements) shall not be netted against the accrued liability unless the requirements of *SSAP No. 64—Offsetting and Netting of Assets and Liabilities* are met.

c. For a reporting entity that invests in commercial and residential mortgages, the entity may require the mortgagor to prepay real estate taxes and property insurance premiums which the entity will hold in escrow and pay when due;

d. The reporting entity holds deposits in connection with leases of investment property; and

e. The reporting entity may receive and hold other funds in a fiduciary capacity.

Remittances and Items Not Allocated

9. Cash receipts cannot always be identified for a specific purpose or, for other reasons, applied to a specific account when received. The reporting entity shall record a liability for these cash receipts when the funds are received. These liability accounts are generally referred to as suspense accounts. Examples include:

a. Premium payments received with the application for policies which have not yet been issued;

b. Premium payments in an amount different than the amount billed by the reporting entity; and

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c. Unidentified cash receipts.

Interest Payable

10. Interest payable includes interest on debt, interest on real estate obligations, and approved interest on surplus notes. It also includes interest on funds held as a deposit or security, such as those held by a ceding company against a reinsurer. The amount to be reported is the amount which has accrued and is unpaid at the balance sheet date.

Payable to Parent, Subsidiaries and Affiliates

11. A liability shall be recognized and identified as due to affiliates for expenditures incurred on behalf of the reporting entity by a parent, affiliates, or subsidiaries or for amounts owed through other intercompany transactions. Amounts due to or from affiliates shall be offset and reported net only when the provisions of SSAP No. 64 are met. Examples of these expenses are executive salaries, workers' compensation insurance premiums, and pension contributions.

12. Reinsurance transactions are not considered liabilities of this nature and are covered in *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* and *SSAP No. 62R—Property and Casualty Reinsurance.*

Relevant Literature

13. This statement adopts *FASB Statement No. 116, Accounting for Contributions Received and Contributions Made* and AICPA *Statement of Position 96-1, Environmental Remediation Liabilities*. This statement is consistent with *FASB Statement No. 5, Accounting for Contingencies* as discussed in SSAP No. 5R.

Effective Date and Transition

14. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 96—Other Liabilities*

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Statement of Statutory Accounting Principles No. 68

Business Combinations and Goodwill

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 99-10 and INT 03-16
Affected by	No other pronouncements
Interpreted by	INT 00-28; INT 01-18; INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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REFERENCES **8**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for business combinations. It addresses: (a) accounting for purchases of subsidiary, controlled and affiliated (SCA) investments (defined in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*); (b) accounting for purchases of partnerships, joint ventures, and limited liability companies (defined in *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*); (c) accounting for goodwill; and (d) accounting for mergers. This statement does not include guidance for stock of an affiliated company received as a capital contribution, rather than through a purchase. Stock received as a capital contribution is addressed by *SSAP No. 25—Affiliates and Other Related Parties*, *SSAP No. 95—Nonmonetary Transactions*, or SSAP No. 97, based on the details of each transaction. The statutory purchase method within this statement is not applicable for stock received as a capital contribution.

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SUMMARY CONCLUSION

Business Combinations

2. A business combination shall be accounted for as either a statutory purchase or a statutory merger. Business combinations that create a parent-subsidiary relationship shall be accounted for as a statutory purchase. Business combinations where equity of one entity is issued in exchange for the equity of another entity, which is then canceled, and prospectively only one entity exists, shall be accounted for as a statutory merger.

Statutory Purchases of SCA Investments

3. The statutory purchase method of accounting is defined as accounting for a business combination as the acquisition of one entity by another. It shall be used for all purchases of SCA entities including partnerships, joint ventures, and limited liability companies. The acquiring reporting entity shall record its investment at cost. Cost is defined as the sum of: (a) any cash payment, (b) the fair value of other assets distributed, (c) the fair value of any liabilities assumed, and (d) any direct costs of the acquisition.(INT 00-28) Contingent consideration issued in a purchase business combination that is embedded in a security or that is in the form of a separate financial instrument shall be recorded by the issuer at fair value at the acquisition date.

4. For those acquired SCA entities accounted for in accordance with paragraphs 8.b.i., 8.b.ii., 8.b.iii. or 8.b.iv. of SSAP No. 97, and joint venture, partnership or limited liability company entities accounted for in accordance with paragraph 8 of SSAP No. 48, goodwill is defined as the difference between the cost of acquiring the entity and the reporting entity's share of the book value of the acquired entity. When the cost of the acquired entity is greater than the reporting entity's share of the book value, positive goodwill exists. When the cost of the acquired entity is less than the reporting entity's share of the book value, negative goodwill exists. Goodwill resulting from assumption reinsurance shall be recorded as a separate write-in for other-than-invested assets. All other goodwill shall be reported in the carrying value of the investment.

5. A business combination accounted for under the statutory purchase method and in which the acquired entity is valued in accordance with paragraphs 8.b.ii., 8.b.iii. or, 8.b.iv. of SSAP No. 97 shall determine the amount of positive goodwill or negative goodwill created by the combination using the reporting entity's share of the GAAP net book value of the acquired entity, adjusted to a statutory basis of accounting in accordance with paragraph 9 of SSAP No. 97 in the case of acquired entities valued in accordance paragraphs 8.b.ii. or 8.b.iv. of SSAP No. 97. Business combinations accounted for under the statutory purchase method and in which the acquired entity is valued in accordance with, paragraph 8.b.i. of SSAP No. 97 shall determine the amount of positive or negative goodwill created by the business combination using the insurer's share of the statutory book value of the acquired entity.

6. For those acquired SCA entities accounted for in accordance with paragraph 8.b.i. of SSAP No. 97 under the statutory purchase method, the historical bases of the acquired entity shall continue to be used in preparing its statutory financial statements. Therefore, pushdown accounting is not permitted.

7. Positive goodwill recorded under the statutory purchase method of accounting shall be admitted subject to the following limitation: Positive goodwill from all sources, including life, accident and health, and deposit-type assumption reinsurance and goodwill resulting from the acquisition of an SCA by the insurance reporting entity that is reported on the SCA's financial statements (resulting from the application of pushdown accounting), is limited in the aggregate to 10% of the acquiring[1] entity's capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for its most

[1] The "acquiring" entity is intended to reflect the insurance reporting entity that reports the investment resulting in goodwill. The goodwill limitation test shall be completed at the individual reporting company level.

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recently filed statement with the domiciliary state commissioner adjusted to exclude any net positive goodwill, EDP equipment and operating system software, and net deferred tax assets. Additionally, all positive goodwill shall be nonadmitted when the underlying investment in the SCA or partnership, joint venture and limited liability company is nonadmitted[2]. When negative goodwill exists, it shall be recorded as a contra-asset.

8. Positive or negative goodwill resulting from the purchase of an SCA, joint venture, partnership or limited liability company shall be amortized to unrealized capital gains and losses on investments over the period in which the acquiring entity benefits economically, not to exceed 10 years. Positive or negative goodwill resulting from life, accident and health, and deposit-type assumption reinsurance shall be amortized to operations as a component of general insurance expenses over the period in which the assuming entity benefits economically, not to exceed 10 years. Goodwill shall be evaluated separately for each transaction.(INT 01-18)

Impairment

9. For any decline in the fair value of an entity, acquired through a purchase, that is other than temporary(INT 06-07), the investment shall be written down to fair value as the new cost basis and the amount of the write down shall be accounted for as a realized loss. The write down shall first be considered as an adjustment to any portion of the investment that is nonadmitted (e.g., nonadmitted goodwill). The new cost basis shall not be changed for subsequent recoveries in fair value. Future declines in fair value, which are determined to be other than temporary, shall be recorded as realized losses. A long-lived asset shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The following are examples of such triggering events or changes in circumstances:

a. A significant decrease in the fair value of a long-lived asset

b. A significant adverse change in the extent or manner in which a long-lived asset is being used or in its physical condition

c. A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset, including an adverse action or assessment by a regulator

d. An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset

e. A current period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset

f. A current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life

10. An impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to recover the carrying amount of the investment or there is evidence indicating inability of the investee to sustain earnings which would justify the carrying amount of the investment. A fair value of an investment that is below the carrying amount based on the statutory equity method or the existence of investee operating losses may indicate a loss in value; however, they are not necessarily indicative of a loss in value that is other than temporary.

[2] This includes, but is not limited to, situations in which the investment is nonadmitted as the audited financial statements for the SCA, joint venture, partnership or limited liability company includes substantial doubt on the entity's ability to continue as a going concern, or on the basis/contents of the audit opinion pursuant to paragraph 21 of SSAP No. 97.

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Statutory Mergers

11. The statutory merger method of accounting is defined as accounting for a business combination in which the original investors in the investee receive equity of the reporting entity for their interest in the investee and only one entity survives. It shall be used for all business combinations accomplished by (a) issuing equity of a newly formed entity for the equity of the merging entities; (b) one entity issuing equity in exchange for the equity of another entity and immediately canceling the equity of that entity; (c) cancelling equity of an owned entity, without issuance of new equity, and incorporating the assets and liabilities of the owned entity directly within the reporting entity's financial statements (e.g., dissolving the SCA entity and absorbing their assets and liabilities); or (d) the exchange of membership interest.

12. Under the statutory merger method, no acquisition shall be recognized because the combination is accomplished without disbursing resources of the constituents. Ownership interest continues and the former statutory bases of accounting shall be retained. However, if one of the merged entities did not employ the statutory basis of accounting, the accounts shall be adjusted to the statutory bases with an offsetting adjustment to beginning surplus of the earliest period presented. The recorded assets, liabilities, and related surplus accounts of the constituents shall be carried forward to the combined corporation at their recorded statutory amounts. The capital accounts of the entities shall be adjusted as necessary to reflect the appropriate par values of the capital stock of the new entity. Adjustments to the capital stock account shall be made to gross paid-in and contributed surplus, to the extent there is a balance in the account.

13. Income of the combined reporting entity shall include income of the constituents for the entire fiscal period in which the combination occurs and the balance sheet and the statement of operations for the two years presented shall be restated, as required by *SSAP No. 3—Accounting Changes and Corrections of Errors*. A reporting entity that merges with an entity which effectively is a shell company[3] (i.e., the reporting entity has no outstanding underwriting liabilities) shall be exempt from prior year restatement.

Treatment of Goodwill When Previously Purchased or Merged Entity Ceases to Exist

14. Goodwill carried by an entity related to a previous business combination shall be charged or credited to surplus immediately in the event that the investee or previous investor that the goodwill relates to ceases to exist (e.g., by merger or dissolution). This guidance is intended to prevent recognition of goodwill when the acquisition, merger or dissolution of the investor or investee would result with the remaining entity reporting goodwill in itself. Internally generated goodwill, or amounts that reflect the goodwill of the reporting entity are not permitted under statutory accounting principles.

Disclosures

15. For business combinations accounted for under the statutory purchase method, the financial statements shall disclose the following for as long as unamortized goodwill is reported as a component of the investment:

a. The name and brief description of the acquired entity;

b. Method of accounting, that is the statutory purchase method;

c. Acquisition date, cost of the acquired entity, the original amount of goodwill and the original amount of admitted goodwill;

[3] When one of the entities is a "shell company," the prior year amounts shall only consist of the "non-shell company." The merger with a shell entity shall be reflected as of January 1 of the current year.

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d. Each SCA's book value, the amount of amortization of goodwill recorded for the period; the SCA's admitted goodwill as of the reporting date;

e. Total admitted goodwill as of the reporting date; and

f. Admitted goodwill as a percentage of the SCA's book adjusted carrying value (gross of admitted goodwill).

16. For business combinations taking the form of a statutory merger, the financial statements shall disclose:

a. The names and brief description of the combined entities;

b. Method of accounting, that is the statutory merger method;

c. Description of the shares of stock issued or cancelled in the transaction;

d. Details of the results of operations of the previously separate entities for the period before the combination is consummated that are included in the current combined net income, including revenue, net income, and other changes in surplus; and

e. A description of any adjustments recorded directly to surplus for any entity that previously did not prepare statutory statements.

17. The financial statements shall disclose the following information regarding goodwill resulting from assumption reinsurance:

a. The name of the ceding entity;

b. The type of business assumed;

c. The cost of the acquired business and the amount of goodwill; and

d. The amount of amortization of goodwill recorded for the period.

18. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment charged to realized capital gains and losses and how fair value was determined.

19. A reporting entity shall disclose the subcomponents and calculation of adjusted surplus and total admitted goodwill as a percentage of adjusted surplus.

Relevant Literature

20. This statement adopts paragraph 12 of *FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* (FAS 121) to the extent that it addresses impairment of goodwill. Paragraphs 14.a. and 14.b. of FAS 121 are also adopted. Paragraphs 13, 14.c. and 14.d. of FAS 121 are rejected. *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets* (FAS 144) supersedes FAS 121, but specifically scopes out the concept of goodwill. Given the applicability of the guidance found in paragraph 12 of FAS 121 to statutory accounting principles, the impairment guidance found in FAS 121, paragraph 12 is retained.

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21. This statement adopts *FASB Emerging Issues Task Force No. 95-19, Determination of the Measurement Date for the Market Price of Securities Issued in a Purchase Business Combination* and *FASB Emerging Issues Task Force No. 97-8: Accounting for Contingent Consideration Issued in a Purchase Business Combination.*

22. This statement rejects *ASU 2021-08, Business Combinations, Accounting for Contract Assets and Contract Liabilities from Contracts with Customers;* however, the rejection of which shall not modify the U.S. GAAP accounting standards as required within this standard*, ASU 2021-03, Intangibles – Goodwill and Other – Accounting Alternative for Evaluating Triggering Events, ASU 2019-06, Intangibles—Goodwill and Other Business Combinations, and Non-for-Profit Entities, ASU 2017-04, Simplifying the Test for Goodwill Impairment*, *ASU 2016-03, Intangibles—Goodwill and Other, Business Combinations, Consolidation, Derivatives and Hedging*; *ASU 2014-02, Accounting for Goodwill (a consensus of the Private Company Council)*, *ASU 2012-02, Testing Indefinite-Lived Intangible Assets for Impairment*, *ASU 2011-08, Testing Goodwill for Impairment* and *ASU 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts*; *Accounting Principles Board Opinion No. 16, Business Combinations*; *FASB Statement No. 38, Accounting for Preacquisition Contingencies of Purchased Enterprises, an amendment of APB Opinion No. 16*; *Accounting Principles Board Opinion No. 17*, *Intangible Assets*; *FASB Statement No. 79, Elimination of Certain Disclosures for Business Combinations by Nonpublic Enterprises*; *FASB Statement No. 141, Business Combinations*; and *FASB Statement No. 142, Goodwill and Other Intangible Assets.* The following related interpretative pronouncements are also rejected*:*

a. *AICPA Accounting Interpretations, Business Combinations: Accounting Interpretations of APB Opinion No. 16*;

b. *FASB Statement No. 10, Extension of "Grandfather" Provisions for Business Combinations*;

c. *AICPA Accounting Interpretations, Intangible Assets: Unofficial Accounting Interpretations of APB Opinion No. 17*;

d. *FASB Emerging Issues Task Force No. 85-14, Securities That Can Be Acquired for Cash in a Pooling of Interests*;

e. *FASB Emerging Issues Task Force No. 86-9, IRC Section 338 and Push-Down Accounting*;

f. *FASB Emerging Issues Task Force No. 86-10, Pooling with 10 Percent Cash Payout Determined by Lottery*;

g. *FASB Emerging Issues Task Force No. 87-11, Allocation of Purchase Price to Assets to Be Sold*;

h. *FASB Emerging Issues Task Force No. 87-15, Effect of a Standstill Agreement on Pooling-of-Interests Accounting*;

i. *FASB Emerging Issues Task Force No. 87-16, Whether the 90 Percent Test for a Pooling of Interests Is Applied Separately to Each Company or on a Combined Basis*;

j. *FASB Emerging Issues Task Force No. 87-27, Poolings of Companies that Do Not Have a Controlling Class of Common Stock*;

k. *FASB Emerging Issues Task Force No. 88-26, Controlling Preferred Stock in a Pooling of Interests*;

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l. *FASB Emerging Issues Task Force No. 88-27, Effect of Unallocated Shares in an Employee Stock Ownership Plan on Accounting for Business Combinations*;

m. *FASB Emerging Issues Task Force No. 89-7, Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity*;

n. *FASB Emerging Issues Task Force No. 90-5, Exchanges of Ownership Interest between Entities under Common Control*;

o. *FASB Emerging Issues Task Force No. 90-6, Accounting for Certain Events Not Addressed in Issue No. 87-11 Relating to an Acquired Operating Unit to Be Sold*;

p. *FASB Emerging Issues Task Force No. 90-12, Allocating Basis to Individual Assets and Liabilities for Transactions within the Scope of Issue No. 88-16*;

q. *FASB Emerging Issues Task Force No. 90-13, Accounting for Simultaneous Common Control Mergers*;

r. *FASB Emerging Issues Task Force No. 91-5, Nonmonetary Exchange of Cost-Method Investments*;

s. *FASB Emerging Issues Task Force No. 92-9, Accounting for the Present Value of Future Profits Resulting from the Acquisition of a Life Insurance Company*;

t. *FASB Emerging Issues Task Force No. 93-7, Uncertainties Related to Income Taxes in a Purchase Business Combination*;

u. *FASB Emerging Issues Task Force No. 95-3, Recognition of Liabilities in Connection with a Purchase Business Combination*;

v. *FASB Emerging Issues Task Force No. 95-8, Accounting for Contingent Consideration Paid to the Shareholders of an Acquired Enterprise in a Purchase Business Combination*;

w. *FASB Emerging Issues Task Force No. 95-12, Pooling of Interests with a Common Interest in a Joint Venture*;

x. *FASB Emerging Issues Task Force No. 95-14, Recognition of Liabilities in Anticipation of a Business Combination*;

y. *FASB Emerging Issues Task Force No. 96-8, Accounting for a Business Combination When the Issuing Company Has Targeted Stock*;

z. *FASB Technical Bulletin 85-5, Issues Related to Accounting for Business Combinations*;

aa. *FASB Interpretations No. 4, Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method, an interpretation of FASB Statement No. 2*.

bb. *FASB Staff Position FAS 141/142-1: Interaction of FASB Statements No. 141 and No. 142 and EITF Issue No. 04-2.*

cc. *FASB Staff Position FAS 142-3, Determination of the Useful Life of Intangible Assets*

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Effective Date and Transition

23. This statement is effective for years beginning January 1, 2001. The provisions of this statement shall be applied to all business combinations entered into on or after January 1, 2001. Goodwill that had been written off prior to the effective date of this statement is prohibited from being restored for purposes of applying the provisions of this statement. The guidance in paragraphs 4-6 was previously included within *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* and was effective for reporting periods ending on and after December 31, 2007. In 2011, the guidance related to goodwill included in SSAP No. 97 was incorporated into this statement. The original guidance included in this standard, and the substantive revisions reflected in SSAP No. 97 are retained for historical purposes within Issue Paper No. 118. Guidance reflected in paragraph 1, incorporated from *INT 03-16: Contribution of Stock*, was effective December 7, 2003. Guidance reflected in paragraph 3 incorporated from *INT 99-10: EITF No. 97-8: Accounting for Contingent Consideration Issued in a Purchase Business Combination* was effective June 7, 1999. Disclosure modifications adopted in July 2020, reflected in agenda item 2020-03, are effective for the year-end 2021 financial statements.

REFERENCES

Other

- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*

Relevant Issue Papers

- *Issue Paper No. 68—Business Combinations and Goodwill*
- *Issue Paper No. 118—Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46*

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Statement of Statutory Accounting Principles No. 69

Statement of Cash Flow

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Disclosures 1
Relevant Literature 2
Effective Date and Transition 2

REFERENCES **3**

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the Statement of Cash Flow.

SUMMARY CONCLUSION

2. For purposes of the Statement of Cash Flow, cash shall include cash, cash equivalents[1] and short-term investments. The Statement of Cash Flow shall be prepared using the direct method and shall only include transactions involving cash. Cash from operations shall be reported consistent with the Statement of Income, excluding the effect of current and prior year accruals. Worksheets to facilitate completion of the cash flow statement, which necessitate adjustments for reporting entity-specific insurance operations and for non-cash transactions, are provided in the annual statement instructions.

Disclosures

3. The financial statements shall disclose the following:

   a. Transactions considered to be operating, investing and financing activities (consistent with the classifications in the annual statement) that affect recognized assets or liabilities

[1] Amounts generally described as restricted cash or restricted cash equivalents shall be included in the beginning and ending balance in the cash flow statement. Transfers between cash, cash equivalents, amounts generally described as restricted cash or restricted cash equivalents, and short-term investments are not part of the entity's operating, investing and financing activities, and details of those transfers are not reported as cash flow activities in the statement of cash flows.

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but do not result in cash receipts or cash payments in the period (in narrative or schedule form); and

b. The cash and noncash aspects of the above transactions identified as operating, investing or financing consistent with the classifications provided by the annual statement instructions. Examples of noncash operating, investing and financing transactions include:

i. Receiving non-cash financial assets from parent as a capital contribution;

ii. Settling reinsurance transactions with exchange of non-cash financial assets;

iii. Converting debt to equity;

iv. Acquiring assets by assuming directly related liabilities, such as purchasing a building by incurring a mortgage to the seller; and

v. Exchanging noncash assets or liabilities for other noncash assets or liabilities.

4. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

5. This statement adopts *ASU 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments*, including the related effective date and transition guidance of ASU 2016-15. This statement adopts *FASB Emerging Issues Task Force Issue No. 95-13*, *Classification of Debt Issue Costs in the Statement of Cash Flows* which requires that cash payments for debt issue costs shall be classified as a financing activity in the Statement of Cash Flow. This statement adopts with modification *ASU 2012-05, Not-For-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows* for all reporting entities. Donated assets with donor-restrictions as to the sale or use of the contributed financial assets, or cash receipts from the sale of donated assets that are restricted as to use are not considered available to meet policyholder obligations and are nonadmitted in accordance with *SSAP No. 4—Assets and Nonadmitted Assets*. This statement adopts *ASU 2016-18, Statement of Cash Flows: Restricted Cash* and requires restricted cash and restricted cash equivalents to be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows.

6. *FASB Statement No. 95, Statement of Cash Flows, FASB Statement No. 102, Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale, an amendment of FASB Statement No. 95*, and *FASB Statement No. 104, Statement of Cash Flows—Net Reporting of Certain Cash Receipts and Cash Payments and Classification of Cash Flows from Hedging Transactions, an amendment of FASB Statement No. 95*, are rejected in this statement.

Effective Date and Transition

7. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* Revisions incorporated to clarify that only transactions involving cash shall be included in the cash flow statement and to expand the disclosure to include non-cash operating transactions are effective December 31, 2015. Revisions to adopt ASU 2016-18 and include restricted cash and restricted cash equivalents with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows are effective December 31, 2019, with early adoption permitted. This revision shall be shown retrospectively, allowing for comparative cash flow statements.

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 92—Statement of Cash Flow*

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Statement of Statutory Accounting Principles No. 70

Allocation of Expenses

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Effective Date and Transition 2

REFERENCES **3**

Other 3

Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for presentation and allocation of certain expenses of reporting entities into general categories and the apportionment of shared expenses between members of a group of entities.

SUMMARY CONCLUSION

2. This statement establishes uniform expense allocation rules to classify expenses within prescribed principal groupings. It is necessary to allocate those expenses which may contain characteristics of more than one classification, which this statement will refer to as allocable expenses.

3. Allocable expenses for property and casualty insurance companies shall be classified into one of three categories on the Underwriting and Investment Exhibit as follows:

a. Loss adjustment expenses—Expenses incurred in the adjusting, recording and paying of claims (including expenses associated with commutations);

b. Investment expenses—Expenses incurred in the investing of funds and pursuit of investment income. Such expenses include those specifically identifiable and allocated costs related to activities such as initiating and handling orders, researching and recommending investments (i.e., investment strategy), appraising, valuing, disbursing funds and collecting income, securities safekeeping, real estate taxes, records maintenance, data processing, support personnel, postage and supplies, office overhead,

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management and executive duties and all other functions reasonably associated with the investment of funds; or

c. Other underwriting expenses—Allocable expenses other than loss adjustment expenses and investment related expenses.

4. Similarly for life and accident and health insurers allocable expenses shall be categorized as general insurance expenses; insurance taxes, licenses and fees; or investment expenses which are netted against investment income on the Summary of Operations.

5. Allocable expenses for health insurers shall be classified as claim adjustment expenses; general administrative expenses; or investment expenses which are netted against investment income on the Statement of Revenue and Expenses.

6. Allocation to the above categories should be based on a method that yields the most accurate results. Specific identification of an expense with an activity that is represented by one of the categories above will generally be the most accurate method. Where specific identification is not feasible allocation of expenses should be based upon pertinent factors or ratios such as studies of employee activities, salary ratios or similar analyses.

7. Allocation may be entirely to one expense category based upon the type of expense incurred, for example, premium taxes would be 100% allocated to Other Underwriting Expenses for property and casualty companies. Other expenses may be allocated across several categories, such as salaries, which may be allocated to both general insurance expenses and net investment income of a life and accident and health company.

8. Many entities operate within a group where personnel and facilities are shared. Shared expenses, including expenses under the terms of a management contract, shall be apportioned to the entities incurring the expense as if the expense had been paid solely by the incurring entity. The apportionment shall be completed based upon specific identification to the entity incurring the expense. Where specific identification is not feasible apportionment shall be based upon pertinent factors or ratios.

9. Any basis adopted to apportion expenses shall be that which yields the most accurate results and may result from special studies of employee activities, salary ratios, premium ratios or similar analyses. Expenses that relate solely to the operations of a reporting entity, such as personnel costs associated with the adjusting and paying of claims, must be borne solely by the reporting entity and are not to be apportioned to other entities within a group.

10. Apportioned expenses are subject to presentation and allocation as provided in paragraphs 3-6.

11. Any material individual component of the reported expense categories shall be presented either on the face of the Summary of Operations or within the footnotes or related Exhibits to the financial statements of the Life and Accident and Health annual statement, the Property and Casualty annual statement or the Health annual statement.

12. Refer to the Preamble for further discussion regarding disclosure requirements.

Effective Date and Transition

13. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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REFERENCES

Other

- NAIC *Annual Statement Instructions for Property and Casualty Insurance Companies, "Underwriting and Investment Exhibit"*
- NAIC *Annual Statement Instructions for Life and Accident and Health Insurance Companies*

Relevant Issue Papers

- *Issue Paper No. 94—Allocation of Expenses*

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Statement of Statutory Accounting Principles No. 71

Policy Acquisition Costs and Commissions

STATUS

Type of Issue..... Common Area
Issued ..... Initial Draft
Effective Date ..... January 1, 2001
Affects..... No other pronouncements
Affected by..... No other pronouncements
Interpreted by..... No other pronouncements
Relevant Appendix A Guidance ..... None

STATUS **1**
SCOPE OF STATEMENT **1**
SUMMARY CONCLUSION **1**
Relevant Literature 2
Effective Date and Transition 2
REFERENCES **3**
Relevant Issue Papers 3

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for policy acquisition costs and commissions.

SUMMARY CONCLUSION

2. Acquisition costs are those costs that are incurred in the acquisition of new and renewal insurance contracts and include those costs that vary with and are primarily related to the acquisition of insurance contracts (e.g., agent and broker commissions, certain underwriting and policy issue costs, and medical and inspection fees). Acquisition costs and commissions shall be expensed as incurred. Determination of when acquisition costs and commissions have been incurred shall be made in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*.

3. Contingent commission liabilities shall be determined in accordance with the terms of each individual commission agreement. Commission liabilities determined on the basis of a formula that relates to loss experience shall be established for the earned portion. Assumptions used to calculate the contingent commission liability shall be consistent with the terms of the policy contract and with the assumptions made in recording other assets and liabilities necessary to reflect underwriting results of the reporting entity such as retrospective premium adjustments and loss reserves, including incurred but not reported.

4. Levelized commissions occur in situations where agents receive normal (non-level) commissions with payments made by a third party. It is intended, but not necessarily guaranteed, that the amounts paid

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to the agents by the third party would ultimately be repaid (with interest explicit or implied) to the third party by levelized payments (which are less than the normal first year commissions but exceed the normal renewal commissions) from the reporting entity. These transactions are, in fact, funding agreements between a reporting entity and a third party, regardless of how the payment to the third party is characterized. The continuance of the stream of payments specified in the levelized commission contract is a mechanism which attempts to bypass recognition of those expenses which are ordinarily charged to expense in the first year of the contract. Consequently, the normal link between the persistency of the policy, the continuance of the premium payment or the maintenance of the agent's license with the reporting entity is not maintained with respect to the payment stream.

5. The use of an arrangement such as a levelized commission arrangement where commission payments are not linked to traditional elements such as premium payments and policy persistency, but rather are linked to the repayment of an advance amount paid by a third party to the direct selling agents requires the establishment of a liability by the reporting entity for the full amount of the unpaid principal and accrued interest which is payable to a third party related to levelized commissions. Arrangements that use a third party to pay agents who write policies for the reporting entity and the insured can be an attempt to de-link the relationship between the insurer and those agents and defer or levelize the acquisition commissions. The insurance reporting entity is required to recognize the full amount of earned commission costs to the direct policy writing agents even if those costs are paid indirectly to the agents by a third party through the use of levelized commission, or similar arrangement, which is in substance a funding arrangement. Having a third party pay commission costs to the selling agent is strong evidence of a potential funding arrangement which shall be recognized as a liability because the substance of the arrangement indicates that repayment is reasonable and probable, even if a contingency has been incorporated into the funding arrangement, until the underlying policy has been cancelled. A third-party structure cannot recharacterize (e.g., by referencing policy persistency) and delay recognition of liabilities for initial sales commission owed from the writing of policies regardless of how a third-party arrangement is structured with regard to the timing of payment from the insurer. The amount owed for full initial sales commission shall be recognized immediately as the writing of an insurance contract is the event that obligates the insurer, and such action shall occur consistently among insurers. As such, this recognition is required regardless of if the insurer owes a selling agent directly or if a third party has been contracted to provide payment to the selling agent.

Relevant Literature

6. This statement rejects *ASU 2022-05, Transition for Sold Contracts, ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts*, *ASU 2010-26, Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts, FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises, FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*, and *Statement of Position 05-1, Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts.*

Effective Date and Transition

7. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The nonsubstantive revisions adopted on March 15, 2021, regarding levelized commission are to clarify the original intent of this statement and apply to existing contracts in effect as of December 31, 2021, and new contracts thereafter.

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REFERENCES

Relevant Issue Papers

- *Issue Paper No. 71—Policy Acquisition Costs and Commissions*
- *Issue Paper 165—Levelized Commission*

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Statement of Statutory Accounting Principles No. 72

Surplus and Quasi-Reorganizations

STATUS

Type of Issue	Common Area
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Nullifies and incorporates INT 99-01 and INT 00-12
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-791

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

Capital Stock 2
Treasury Stock 2
Gross Paid-in and Contributed Surplus 2
Surplus Notes 3
Unassigned Funds (Surplus) 3
Special Surplus Funds 5
Other-Than-Special Surplus Funds 6
Quasi-Reorganizations 6
Demutualizations 7
Changes in Statutory Surplus 7
Disclosures 7
Relevant Literature 8
Effective Date and Transition 9

REFERENCES **9**

Relevant Issue Papers 9

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for statutory surplus and quasi-reorganizations.

SUMMARY CONCLUSION

2. Statutory surplus of a reporting entity consists of the following:

   a. Capital stock;

   b. Treasury stock;

   c. Gross paid-in and contributed surplus;

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d. Surplus notes;

e. Unassigned funds (surplus);

f. Special surplus funds; and

g. Other-than-special surplus funds.

Capital Stock

3. The articles of incorporation set forth the number of authorized shares of capital stock and the par value of each share. The capital stock account represents the number of shares issued times the par value of each share. When no par value is set forth, the reporting entity shall declare a "stated value" and record such amount in the capital stock account. Changes in the par value of a reporting entity's capital stock shall be reflected as a reclassification between the capital stock account and gross paid-in and contributed surplus. Issued, free-standing financial instruments with characteristics of both liability and equity shall be reported as a liability to the extent described in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*.

4. Notes or other receivables received for the issuance of capital stock which have been approved by the domiciliary commissioner and have been satisfied by receipt of cash or readily marketable securities prior to the filing of the statutory financial statement shall be treated as a Type I subsequent event in accordance with *SSAP No. 9—Subsequent Events* and as such shall be considered an admitted asset. To the extent that the notes or other receivables are not satisfied, they shall be nonadmitted.

5. Stock splits, similar to stock dividends, have no impact on the overall surplus of a reporting entity. The distinction between a stock split and a stock dividend shall be made in accordance with *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research* Bulletins, "Chapter 7, Capital Accounts, Section B-Stock Dividends and Split-ups*"* (ARB 43). Stock splits shall be recorded by adjusting the capital stock account to reflect the par value of the outstanding number of shares after the split. An offsetting entry shall be made to paid-in or contributed surplus. Stock dividends shall be recorded in a manner consistent with paragraph 13.i.

Treasury Stock

6. Treasury stock is capital stock that has been issued and subsequently reacquired by the reporting entity. It is held for either reissuance or cancellation in the future. When a reporting entity's stock is acquired for purposes other than retirement, or when ultimate disposition has not yet been decided, the cost of acquired stock shall be reported as treasury stock which reduces statutory surplus. The acquisition of treasury stock has no effect on either the number of shares issued or the amount of paid up capital shown in the capital stock account. Cancellation of treasury stock shall reduce the capital stock account by the par value and reduce paid-in or contributed surplus by the excess of cost over par value or stated value.

Gross Paid-in and Contributed Surplus

7. Gross paid-in and contributed surplus is the amount of capital received in excess of the par value of the stock issued. Changes in the par value of a reporting entity's capital stock shall be reflected as a reclassification between the capital stock account and gross paid-in and contributed surplus. Forgiveness of a reporting entity's obligations to its parent or other stockholders shall be accounted for as contributed surplus.

8. Notes or other receivables received as additional capital contributions satisfied by receipt of cash or readily marketable securities prior to the filing of the statutory financial statement shall be treated as a Type I subsequent event in accordance with SSAP No. 9 and as such shall be considered an admitted

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asset based on the evidence of collection and approval of the domiciliary commissioner. To the extent that the notes or other receivables are not satisfied, they shall be nonadmitted.

9. Bonds received as capital contributions, reflecting economic transactions, shall be recognized at fair value in accordance with *SSAP No. 25—Affiliates and Other Related Parties*. Real estate or other assets received as additional capital contributions shall be recognized in accordance with SSAP No. 25 or as nonreciprocal transfers as defined in *SSAP No. 95—Nonmonetary Transactions*, in accordance with the details of the transaction.

10. Stock purchase warrants issued in return for cash shall be credited to gross paid-in and contributed surplus. An entity shall treat a modification of the terms or conditions or an exchange of a freestanding equity-classified written call option as an exchange of the original instrument for a new instrument. In substance, the entity repurchases the original instrument by issuing a new instrument. The total effect of the modification or exchange shall be allocated to the respective elements in the transaction. When debt instruments are issued with conversion features, no value shall be assigned to the conversion features unless the conversion feature is clearly separable from the debt obligation in the form of a detachable stock purchase warrant. In such instances the relative fair value of the detachable stock purchase warrant at time of issue shall be credited to gross paid-in and contributed surplus. For instances in which a reporting entity has issued puttable warrants or mandatorily redeemable warrants, such items shall be reflected as liabilities as the warrants obligate the reporting entity to ultimately transfer cash or other assets to the holder in order to repurchase the shares.

11. Distributions that reflect a return of capital shall be charged directly to gross paid in and contributed surplus. (A return of capital will reduce the adjusted cost basis of the parent/stockholder in the reporting entity.)

Surplus Notes

12. Surplus notes are financial instruments that are subject to strict control by the commissioner of the reporting entity's state of domicile and have been approved by the commissioner as to form and content. These instruments are commonly referred to as surplus notes but are also referred to as surplus debentures or contribution certificates. *SSAP No. 41R—Surplus Notes* provides the specific characteristics of surplus notes and provides accounting guidance for surplus notes. Only notes meeting the requirements of SSAP No. 41R shall be accounted for as surplus notes.

Unassigned Funds (Surplus)

13. Unassigned funds (surplus) represents the undistributed and unappropriated amount of surplus at the balance sheet date. Certain components of unassigned funds (surplus) are addressed in more detail in other issue papers. Unassigned funds (surplus) is comprised of the cumulative effect of:

a. Net Income

Net income resulting from insurance and other operating activities of the reporting entity since its inception is a component of unassigned funds (surplus);

b. Unrealized Capital Gains and Losses on Investments

The cumulative unrealized capital gain or loss that results from differences between the prescribed statement value of investments carried at fair value and the cost of those investments is a component of unassigned funds (surplus). This component changes as periodic unrealized gains and losses are credited or charged directly to unassigned funds (surplus);

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c. Effect of Exchange Rate Fluctuations

The cumulative gain or loss due to translating foreign operations to U.S. dollars and changes in balance sheet asset and liability values due to foreign currency translation is recorded as an unrealized capital gain or and loss and therefore is a component of unassigned funds (surplus). This component changes as the exchange rates fluctuate;

d. Nonadmitted Assets

The nonadmitted values of assets owned by a reporting entity are a reduction of unassigned funds (surplus). This component of unassigned funds (surplus) changes as nonadmitted asset values change. Changes in nonadmitted asset values are charged or credited directly to unassigned funds (surplus);

e. Provision for Reinsurance

A reporting entity must establish a statutory liability, provision for reinsurance, for unsecured reinsurance recoverables from unauthorized reinsurers and certain overdue balances from authorized reinsurers. The liability is charged directly to unassigned funds (surplus). Therefore, at any point in time there is a reduction of unassigned funds (surplus) equal to a reporting entity's liability for unauthorized reinsurance;

f. Asset Valuation Reserves

Where an Asset Valuation Reserve is required to be recorded as a statutory liability, there is a reduction of unassigned funds (surplus) in an amount equal to the liability. Changes to the Asset Valuation Reserve are charged or credited directly to unassigned funds (surplus);

g. Separate Accounts

A life insurer's balance sheet includes the total assets and liabilities of any separate accounts business which it maintains and, therefore, the surplus, if any, of its separate accounts business. Changes in the surplus of the separate accounts business of an insurer are charged or credited directly to unassigned funds (surplus);

h. Subscribers Savings Accounts

Subscribers Savings Accounts (SSAs) are unique to reciprocals. SSAs represent a portion of a reciprocal insurance company's surplus that has been identified as subscribers (policyholders) accounts. When the source of amounts credited to the subscriber accounts is from the reciprocal's operations, the amounts are reported as unassigned funds (surplus);

i. Dividends to Stockholders

Dividends[1] declared are charged directly to unassigned funds (surplus) on the declaration date and are carried as a liability until paid. The amount of the dividend is the cash paid if

[1] As a dividend represents the distribution of earnings, in any event in which unassigned funds is negative or goes below zero as a result of a distribution to a parent or stockholder, the distribution (or portion thereof that does not reflect undistributed accumulated earnings in unassigned funds) shall be considered a return of capital and captured in paragraph 11. Determining whether a distribution is a dividend or a return of capital does not impact consideration of whether the distribution is "extraordinary" as both dividends and other distributions (e.g., return of capital) are subject to that assessment. (Reporting entities with positive unassigned funds may choose to make return of capital distributions. Those distributions are also captured in paragraph 11.)

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it is a cash dividend, the fair value of the assets distributed if it is property dividend, or the par value of the company's stock if it is a stock dividend. A stock dividend is recorded as a transfer from unassigned funds (surplus) to capital stock. Stock dividends have no effect on total capital and surplus while other forms of dividends reduce surplus. Forgiveness by a reporting entity of any debt, surplus note or other obligation of its parent or other stockholders shall be accounted for as a dividend. Dividends paid to related parties are subject to the requirements of SSAP No. 25;

j. Change in Accounting Principles

The effects of a change in accounting principle or the application of an accounting principle, such as a change in reserve account because of a change in valuation basis, are reported as a charge or credit to unassigned funds (surplus). The effect of these changes shall not be included in the determination of net income or loss;

k. Correction of an Error

Corrections of errors in previously issued financial statements are charged or credited directly to unassigned funds (surplus). The effect of corrections of errors shall not be included in the determination of net income or loss;

l. Stock Issuance Expenses

Expenses relating to the issuance of capital stock, for example underwriting commissions and filing fees are charged to unassigned funds (surplus);

m. Change in Surplus as a Result of Reinsurance

Life and accident and health insurers report increases in surplus that result from certain types of reinsurance transactions on a net of tax basis. As profits emerge from the ceded business the increase in surplus is amortized to income as provided for in Appendix A-791;

n. Changes in Deferred Tax Assets and Deferred Tax Liabilities

Consistent with the conclusions reached in *SSAP No. 101—Income Taxes*, changes in deferred tax assets and deferred tax liabilities, including changes attributable to changes in tax rates and changes in tax status, if any, shall be recognized as a separate component of unassigned funds (surplus);

o. Other

This category includes other gains and losses in surplus not specifically identified elsewhere in this statement including but not limited to net proceeds from life insurance on employees, changes in the additional minimum pension liability as discussed in *SSAP No. 102—Pensions* and unearned compensation relating to stock issuances made under compensatory Employee Stock Ownership Plans, Stock Option Plans and Stock Purchase Plans.

Special Surplus Funds

14. A company may establish a segregated surplus account to provide for contingencies. Surplus thus appropriated is called appropriated surplus or special surplus funds. Surplus resulting from any retroactive reinsurance transaction entered by a property and casualty insurer must be recorded as an appropriation of surplus by the ceding company (special surplus from retroactive reinsurance account). Voluntary and

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general contingency reserves which are not actual liabilities of the company are shown as appropriated surplus or special surplus funds.

Other-Than-Special Surplus Funds

15. Amounts provided to reporting entities, other than stock companies, in the organization stage to defray the expenses and meet initial minimum surplus requirements required to obtain a license to do the business of insurance or for the ongoing operations shall be reported as Other-Than-Special Surplus Funds. Examples of these types of deposits include but are not limited to: guaranty fund notes and subscriber accounts that represent individual subscriber contributions.

Quasi-Reorganizations

16. Restatement of gross paid-in and contributed surplus and unassigned funds (surplus) under a quasi-reorganization shall be permitted only if the criteria in both paragraphs 16.a. and 16.b. and either paragraph 16.c. or 16.d. are met:

a. The restatement is approved in writing by the domiciliary commissioner;

b. An 80% or greater change in the ultimate ownership of the reporting entity has occurred within six months prior to approval of the restatement;

c. A new business plan has been adopted that results in a substantive change in the operations and business mix of the reporting entity and the situation or circumstances that gave rise to the negative unassigned funds (surplus) will not be part of the ongoing operations;

d. The reporting entity is a shell company with no existing operations, in force policies or outstanding claims.

17. Restatement shall not result in the unassigned funds (surplus) account being greater than zero or the gross paid-in and contributed surplus account being less than zero immediately following the restatement. Total surplus as regards policyholders shall remain unchanged following restatement. The following components of unassigned funds (surplus) shall be considered in determining the amount available for restatement:

a. Net Income;

b. Effect of Exchange Rate Fluctuations;

c. Dividends to Stockholders;

d. Change in Accounting Principles;

e. Correction of an Error and

f. Stock Issuance Expenses.

18. The assets and liabilities of the reporting entity shall continue to be carried at historical cost or other value required by statutory accounting principles. No adjustments to assets or liabilities shall be made to reflect the effect of a quasi-reorganization.

19. The tax benefits of operating losses or tax credits existing at the date of a quasi-reorganization and subsequently recognized after the quasi-reorganization shall be recognized as an adjustment to gross paid-in and contributed surplus.

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Demutualizations

20. Mutual insurance companies may undergo demutualization transactions and convert to stock enterprises. In order to effect a demutualization, a company may be required to issue consideration, often in the form of stock, to existing participating policyholders in exchange for their current membership interests. The receipt of such stock has no direct effect on the policyholders' contractual interests of their insurance policies (for example, it does not alter the cash surrender value of their life insurance policies). However, the governance of the mutual insurance company and, in particular, the participating policyholders' interest in that governance are modified. Stock received from a demutualization shall be accounted for at fair value with a gain recognized in income from continuing operations.

Changes in Statutory Surplus

21. The components of the change in the capital and surplus accounts shall be presented for each year for which an income statement is presented.

Disclosures

22. The financial statements shall disclose the following:

a. The number of shares of each class of capital stock authorized, issued and outstanding as of the balance sheet date and the par value or stated value of each class;

b. The dividend rate, liquidation value and redemption schedule (including prices and dates) of any preferred stock issues;

c. Dividend restrictions, if any, and an indication if the dividends are cumulative;

d. The dates and amounts of dividends, or distributions paid. Note for each payment whether the dividend or distribution was ordinary or extraordinary.

e. The portion of the reporting entity profits that may be paid as ordinary dividends to stockholders;

f. A description of any restrictions placed on the unassigned funds (surplus) including for whom the surplus is being held;

g. For mutual reciprocals and similarly organized entities, the total amount of advances to surplus not repaid, if any;

h. The total amount of stock held by the reporting entity, including stock of affiliated entities, for special purposes such as conversion of preferred stock, employee stock options, and stock purchase warrants;

i. A description of the reasons for changes in the balances of any special surplus funds from the prior period;

j. The portion of unassigned funds (surplus) represented or reduced by each of the following items:

i. unrealized gains and losses;

ii. nonadmitted asset values;

iii. separate account business;

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iv. asset valuation reserves;

v. provision for reinsurance.

k. For reciprocal insurance companies only:

i. the amount of surplus identified as subscriber savings accounts;

ii. the source of the funds (either from the reciprocal's operations or contributed by the individual subscriber) and, the reporting location in surplus;

iii. the conditions upon which the balances are paid to the subscribers.

l. Disclosures required by SSAP No. 41R;

m. Disclosures required by SSAP No. 9;

n. The impact of the restatement in a quasi-reorganization as long as financial statements for the period of the reorganization are presented; and

o. The effective date of a quasi-reorganization for a period of ten years following the reorganization.

23. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

24. Paragraphs 9 and 10 of *Accounting Principles Board Opinion No. 12, Omnibus Opinion—1967,* are adopted with modification to eliminate the option of disclosing changes in the notes to the financial statements rather than in the Statement of Capital and Surplus. This statement originally adopted paragraphs 10 and 11 of *Accounting Principles Board Opinion No. 10, Omnibus Opinion—1966* (APB 10). However, for reporting periods ending after December 15, 1997, paragraphs 10 and 11 of APB 10 were deleted by paragraph 9, and replaced by paragraphs 6 and 7 of *FASB Statement No. 129, Disclosure of Information About Capital Structure* (FAS 129). As such, this statement adopts paragraphs 6, 7 and 9 of FAS 129. All other paragraphs of FAS 129 are rejected. This statement also adopts with modification paragraph 12 of *Accounting Principles Board Opinion No. 6* (APB 6), *Status of Accounting Research Bulletins,* to eliminate the option of recording treasury stock as an asset.

25. Paragraph 15 of *FASB Statement No. 5, Accounting For Contingencies*, is adopted by this statement. Paragraphs 1-4 and 10-16 of *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting* Research *Bulletins,* "Chapter 7, Capital Accounts, Section B—Stock Dividends and Stock Split-ups" are adopted by this statement.

26. This statement adopts with modification *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting* Research *Bulletins,* "Chapter 7, Capital Accounts, Section A—Quasi-Reorganization or Corporate Readjustment," to permit restatement of gross paid-in and contributed surplus and unassigned funds (surplus) only in certain limited circumstances. This statement adopts *FASB Emerging Issues Task Force 99-4, Accounting for Stock Received from the Demutualization of a Mutual Insurance Company*.

27. This statement adopts with modification *Accounting Research Bulletin No. 46, Discontinuance of Dating Earned Surplus,* to require disclosure of the impact of the restatement in the financial statements as long as financial statements for the period of reorganization are presented and paragraph 28 of *Accounting Principles Board Opinion No. 9, Reporting the Results of Operations.* This statement rejects *FASB Emerging Issues Task Force No. 88-9, Put Warrants, FAS 150, Accounting for Certain Financial*

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Instruments with Characteristics of both Liabilities and Equity (FAS 150), *FSP FAS 150-3, Effective Date, Disclosures and Transition for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests Under FASB Statement No. 150* (FSP FAS 150-3) and *FSP FAS 150-5, Issuer's Accounting Under FASB Statement No. 150 for Freestanding Warrants and Other Similar Instruments on Shares That Are Redeemable* (FSP FAS 150-5). FAS 150, and the corresponding FSPs are rejected as insurers do not prevalently issue financial instruments within the confines of these standards. However, guidance has been incorporated within this SSAP to ensure that puttable warrants and mandatorily redeemable warrants are reflected as liabilities, and not equity, within the financial statements.

28. This statement rejects paragraphs 1-11 and 13-24 of APB 6*, FASB Emerging Issue Task Force No. 85-1, Classifying Notes Received for Capital Stock,* and *FASB Emerging Issue Task Force No. 85-2, Classification of Costs Incurred in a Takeover Defense*.

29. This statement also rejects *Accounting Research Bulletin No. 43*, *Restatement and Revision of* Accounting Research *Bulletins,* "Chapter 1, Prior Opinions," paragraph 12 of APB 10*, FASB Technical Bulletin No. 85-6, Accounting for a Purchase of Treasury Shares at a Price Significantly in Excess of the Current Market Price of the Shares and the Income Statement Classification of Costs Incurred in Defending against a Takeover Attempt,* and *Accounting Standard Update (ASU) 2021-04, Earnings Per Share (Topic 260), Debt—Modifications and Extinguishments (Subtopic 470-50), Compensation—Stock Compensation (Topic 718), and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40)—Issuer's Accounting for Certain Modifications or Exchanges of Freestanding Equity-Classified Written Call Options*, while incorporating guidance that clarifies that an entity shall treat a modification of the terms or conditions or an exchange of a freestanding equity-classified written call option as an exchange of the original instrument for a new instrument.

30. This statement rejects *ASU 2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40), Accounting for Convertible Instruments and Contracts in an Entity's Own Equity.*

Effective Date and Transition

31. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. The guidance in paragraph 19 of this statement was originally contained within *INT 99-01: Accounting for Tax Benefits of Operating Losses and Tax Credit in Quasi-Reorganizations* and was effective March 8, 1999. The guidance in paragraph 20 of this statement was originally contained within *INT 00-12: EITF No. 99-4, Accounting for Stock Received from the Demutualization of a Mutual Insurance Company* and was effective June 12, 2000.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 72—Statutory Surplus*
- *Issue Paper No. 84—Quasi-Reorganizations*

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Statement of Statutory Accounting Principles No. 73

Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities

STATUS

Type of Issue	Health Entities
Issued	Initial Draft
Effective Date	January 1, 2001
Affects	Supersedes SSAP No. 87 with guidance incorporated August 2011
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for health care delivery assets - supplies, pharmaceuticals and surgical supplies, durable medical equipment, furniture, medical equipment and fixtures and leasehold improvements.

SUMMARY CONCLUSION

2. This statement applies only to reporting entities which directly provide health care services to subscribers, members or policyholders. Such providers acquire and retain assets commonly referred to as "health care delivery assets" used in connection with the direct delivery of health care services in facilities owned or operated by the reporting entity and include supplies, pharmaceuticals and surgical supplies, durable medical equipment, furniture, medical equipment and fixtures and leasehold improvements in health care facilities.

3. Furniture, medical equipment and fixtures used in connection with the direct provision of health care services include diagnostic equipment, laboratory equipment, patient monitoring equipment, hospital beds, examining tables, and operating room equipment.

4. Supplies, pharmaceuticals and surgical supplies, durable medical equipment, furniture, medical equipment and fixtures, and leasehold improvements in health care facilities owned or operated by the reporting entity meet the definition of assets established in *SSAP No. 4—Assets and Nonadmitted Assets*.

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Pharmaceuticals and surgical supplies, and durable medical equipment held by reporting entities and used for the direct delivery of health care services are assets which are used to fulfill policyholder obligations within the meaning of SSAP No. 4 and are admitted assets to the extent that they conform to the requirements of this statement. Furniture, medical equipment and fixtures, and leasehold improvements held by health reporting entities and used for the direct delivery of health care services are admitted assets to the extent that they conform to the requirements of this statement. Furniture, fixtures and equipment, and leasehold improvements which are not used in the direct delivery of health care (e.g., for administrative activities including claims processing, billing, and maintenance of medical records) are nonadmitted assets and are addressed in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*.

5. The reporting entity shall maintain a control system that provides for identification of quantities on hand and appropriate valuation (lower of cost or fair value) of supplies, pharmaceuticals and surgical supplies, and durable medical equipment.

6. Supplies except for pharmaceuticals and surgical supplies discussed in paragraph 7 (e.g., linens, uniforms and garments, food and other commodities, and housekeeping, maintenance, and office supplies) shall be nonadmitted assets.

7. Pharmaceutical and surgical supplies (e.g. drugs, surgical items (such as implants), and medical dressings) used directly in the treatment of medical conditions shall be admitted assets.

8. Durable medical equipment includes consumable or salable equipment such as wheelchairs, crutches, braces, that is generally classified as inventory, and is of a nature that it may be reused. Subscribers, members or policyholders may utilize durable medical equipment on a temporary basis and later return the equipment to the provider. The provider shall recognize the diminution in value, if any, as a result of use of such equipment.

9. Furniture, medical equipment and fixtures, and leasehold improvements shall be depreciated over their estimated useful lives but for a period not to exceed three years, except for a leasehold improvement which shall be amortized against net income over the shorter of its estimated useful life or the remaining lease term, using methods detailed in SSAP No. 19. The amortization of leasehold improvements (including property improvements and integral equipment) shall cease, with any remaining amount immediately expensed, in any event in which the lease is terminated in advance of the lease term. This includes situations in which leased real estate is acquired by the reporting entity lessee but excludes situations where the real estate lease agreement has a purchase option that contains language that allows leasehold improvements necessary for the functionality of specific health care delivery assets[1] to be excluded from the purchase cost of the real estate. Upon acquisition, such leasehold improvements necessary for the functionality of healthcare delivery assets shall follow the guidance for health care delivery assets in this statement. If leased real estate is acquired, recognition of the real estate shall follow the provisions in *SSAP No. 40R—Real Estate Investments.*

10. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of medical supplies, pharmaceuticals and surgical supplies, durable medical equipment, furniture, medical equipment and fixtures, and leasehold improvements shall be expensed when purchased. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

Disclosures

11. The financial statements shall disclose if the written capitalization policy and the resultant predefined thresholds changed from the prior period and the reason(s) for such change.

[1] The application of this exception is limited to leasehold improvements necessary for the functionality of health care delivery assets that qualified for admittance under SSAP No. 73.

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Relevant Literature

12. This statement rejects the *AICPA Audit and Accounting Guide: Health Care Organizations*.

Effective Date and Transition

13. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance reflected in paragraphs 10 and 11, incorporated from SSAP No. 87, was originally effective for years beginning on and after January 1, 2004.

14. Medical supplies, pharmaceuticals and surgical supplies, durable medical equipment, furniture, medical equipment and fixtures, and leasehold improvements capitalized prior to January 1, 2001 shall be depreciated over the shorter of its remaining useful life or three years.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 100—Health Care Delivery Assets—Supplies, Pharmaceuticals and Surgical Supplies, and Durable Medical Equipment*
- *Issue Paper No. 101—Health Care Delivery Assets—Furniture, Medical Equipment and Fixtures, and Leasehold Improvements in Health Care Facilities*
- *Issue Paper No. 119—Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29, 73, 79 and 82*

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Statement of Statutory Accounting Principles No. 74

Insurance-Linked Securities Issued Through a Protected Cell

STATUS

Type of Issue	Property and Casualty
Issued	Finalized September 12, 2000
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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GLOSSARY **5**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the issuance of insurance-linked securities issued by a property and casualty insurer through a protected cell. This statement applies to property and casualty contracts as defined in *SSAP No. 50—Classifications of Insurance or Managed Care Contracts*.

SUMMARY CONCLUSION

2. An insurance-linked security can be issued by the insurer through a protected cell for purchase by investors. A protected cell is retained within the insurance or reinsurance company and is used to insulate the proceeds of the securities offering from the general business risks of the insurer, granting an additional comfort level for investors of the securitized instrument. The insurance exposures that have been securitized by the insurance-linked security are attributed to the protected cell.

3. Under the terms of the security, the principal may be paid to the investor on a specified maturity date, with interest, unless a trigger event occurs. The proceeds of the security offering will collateralize (i)

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the issuer's obligation under an insurance or reinsurance agreement if a trigger event occurs and (ii) the issuer's obligation to repay the security if a trigger event does not occur.

4. If the trigger event takes place before a specified date, the issuer is relieved of some or its entire obligation to repay the securityholders, and the investor incurs a loss of some or all of its investment. The security must be issued with an indemnity trigger.

5. In an insurance-linked security, the insurer that originated the transaction has hedged its portfolio of insurance risks by transferring certain of those risks to the securityholders. Should the triggering event occur, the issuer would incur a loss that would be partly offset by the amount of liability to securityholders from which it is relieved. This statement provides statutory accounting guidance solely for indemnity triggered insurance securitization transactions conducted through a protected cell.

Accounting for Prefunded Insurance-Linked Securities for Business Attributed to the Protected Cell from the General Account

General Account Reporting

6. Activities such as sales, underwriting and contract administration, premium collection and payment of premium taxes, and claims processing are activities of the insurance company distinct from the protected cell and shall be accounted for as transactions of the general account.

7. Amounts paid to the protected cell for underwriting risks, which ultimately will be securitized by the protected cell, shall be reported separately as a reduction of written and earned premiums in the current period general account's statement of income. This premium is earned by the general account in accordance with *SSAP No. 53—Property and Casualty Contracts–Premiums*.

8. At the maturity of the protected cell all assets and liabilities of the protected cell are distributed based on the contractual agreement with the securityholders. If after this distribution assets still reside in the protected cell, these assets shall be attributed to the general account and recognized as an adjustment to surplus.

9. Insurance claim liabilities arising from past insurable events attributed to the protected cell account from the general account shall be accounted for as retroactive reinsurance as prescribed in *SSAP No. 62R—Property and Casualty Reinsurance*.

10. General account recoverables from the protected cell as a result of an indemnity based securitized event, shall be recognized separately as a reduction of gross losses and loss expenses incurred in the current period general account's statement of income. General account recoverables from the protected cell on unpaid reported and incurred but not reported losses and loss adjustment expenses shall be netted against the liability for gross losses and loss adjustment expenses in the general account's balance sheet. Recoverables from the protected cell shall not exceed the assets carried at fair value in the protected cell.

11. The general account shall include aggregate amounts on the designated lines in the balance sheet and income statement for any protected cell which it maintains. Transfers to the general account due or accrued shall be reported on a net basis so that the asset and the liability totals of the general account are not overstated.

Protected Cell Reporting

12. The protected cell annual statement is concerned with the investment activities and obligations relating to insurance-linked securities attributed to that protected cell. As a result, the protected cell statement shall report only the financial activities of the protected cell and shall not include general account expenses related to insurance activities which are recorded for in the general account.

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13. The protected cell shall record premium income for transactions attributed to it by the general account as income reported in the protected cell's statement of income. This premium attribution is earned by the protected cell in accordance with SSAP No. 53.

14. The obligation from the issuance of the insurance-linked security is recorded as Funds Held Under Securitization Agreement, a liability on the protected cell balance sheet which is reported at its contractual value which will be the lower of the scheduled amount to be repaid to investors or the fair value of the investments in the protected cell. All protected cell assets shall be reported at fair value. Interest expenses payable to securityholders associated with the protected cell investment operations shall be deducted in the determination of net operating income of the cell. Net investment income and realized capital gains and losses relating to the investment operations of the protected cell are recorded as net investment income. Payables to the general account shall not exceed the assets carried at fair value in the protected cell.

15. Changes in both (i) the fair value of the protected cell invested assets and (ii) the protected cell contractual value of liabilities to investors shall be reported as an unrealized gain/loss in the equity section of the protected cell balance sheet.

16. If the trigger event occurs with respect to the underlying exposures attributed to the protected cell, the protected cell shall record the appropriate incurred losses in its current period statement of income. Correspondingly, the Funds Held Under Securitization Agreement shall be reduced and offset by gross losses incurred in the current period Statement of Income. The applicable funds to cover the subject exposure are then attributed to the general account via a balance sheet account, “Due to/from the General Account.”

17. If the trigger event does not take place on or before the contractual maturity date, the protected cell repays the security as prescribed in the debt contract by reducing Funds Held Under Securitization Agreement.

Disclosures

General Account

18. The general account shall reflect all activities with its protected cells on the designated lines within its statutory balance sheet and income statement. The general account shall also disclose in its notes to the financial statements the types and amounts of exposures/risks attributed to each of its protected cells.

Protected Cells

19. Each protected cell of a protected cell company shall prepare and submit to all states where the protected cell company is licensed and the NAIC the following supplemental financial information:

a. Balance Sheet

b. Income Statement

c. Statement of Cash Flows

d. Investment Schedules as typically required for a property/casualty insurer

e. Schedule P

20. Refer to the Preamble for further discussion regarding disclosure requirements.

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Relevant Literature

21. This statement only contemplates transactions with an indemnity-based trigger, as such they would be excluded from *FAS No. 133, Accounting for Derivative Instruments and Hedging Activities*.

Effective Date and Transition

22. This statement is effective for years beginning January 1, 2001. Changes resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 103—Accounting for the Issuance of Insurance-Linked Securities Issued by a Property and Casualty Insurer through a Protected Cell*

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GLOSSARY [1]

Fair Value – See *SSAP No. 100R—Fair Value*

Fully Funded – With respect to any exposure attributed to a protected cell, the fair value of the protected cell assets, on the date on which the insurance securitization is effected, equals or exceeds the maximum possible exposure attributable to the protected cell with respect to such exposures.

General Account – The assets and liabilities of a protected cell company other than protected cell assets and protected cell liabilities.

Indemnity Trigger – A transaction term by which relief of the issuer's obligation to repay investors is triggered by its incurring a specified level of losses under its insurance or reinsurance contracts.

Protected Cell – An identified pool of assets and liabilities of a protected cell company segregated and insulated by means of this Act from the remainder of the protected cell company's assets and liabilities.

Protected Cell Account – A specifically identified bank or custodial account established by a protected cell company for the purpose of segregating the protected cell assets of one protected cell from the protected cell assets of other protected cells and from the assets of the protected cell company's general account.

Protected Cell Assets – All assets, contract rights and general intangibles, identified with and attributable to a specific protected cell of a protected cell company.

Protected Cell Company – A domestic insurer that has one or more protected cells.

Protected Cell Company Insurance Securitization – The issuance of debt instruments, the proceeds from which support the exposures attributed to the protected cell, by a protected cell company where repayment of principal or interest, or both, to investors pursuant to the transaction terms is contingent upon the occurrence or nonoccurrence of an event with respect to which the protected cell company is exposed to loss under insurance or reinsurance contracts it has issued.

Protected Cell Liabilities – All liabilities and other obligations identified with and attributable to a specific protected cell of a protected cell company.

[1] Definitions in this glossary were adapted from the Protected Cell Company Model Act as adopted by the Insurance Securitization Working Group of the Financial Condition (E) Committee in 1999. These definitions are not intended to change the meaning of any terms used elsewhere in the *Accounting Practices and Procedures Manual*, and should only be used in the context of SSAP No. 74.

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Statement of Statutory Accounting Principles No. 76

Start-Up Costs

STATUS

Type of Issue	Common Area
Issued	Finalized December 4, 2000
Effective Date	January 1, 2002
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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Effective Date and Transition 2

REFERENCES **2**

Relevant Issue Papers 2

SCOPE OF STATEMENT

1. This statement addresses start-up costs. In practice, various terms are used to refer to start-up costs, such as pre-opening, pre-operating, and organization costs. For purpose of this statement, these costs are referred to as start-up costs.

SUMMARY CONCLUSION

2. Costs of start-up activities, including activities related to organizing a new entity (commonly referred to as organization costs), shall be expensed as incurred. Start-up activities are defined broadly as those one-time activities related to: (1) opening a new facility; (2) introducing a new product or service; (3) conducting business in a new territory; (4) conducting business with a new class of customer or beneficiary; (5) initiating a new process in an existing facility; or (6) commencing some new operation.

Disclosures

3. Cost of start-up activities incurred in an accounting period shall be disclosed in the annual audited statutory financial report only.

4. Refer to the Preamble for further discussion regarding disclosure requirements.

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Relevant Literature

5. This statement adopts American Institute of Certified Public Accountants (AICPA) *Statement of Position SOP 98-5, Reporting on the Costs of Start-Up Activities* (SOP 98-5), which requires costs of start-up activities and organization costs to be expensed as incurred. This statement is consistent with *SSAP No. 17—Preoperating and Research and Development Costs*.

Effective Date and Transition

6. This statement is effective for years beginning January 1, 2002. Adoption as of January 1, 2001 is encouraged but not required. Changes resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 105—Reporting on the Costs of Start-Up Activities*

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Statement of Statutory Accounting Principles No. 78

Multiple Peril Crop Insurance

STATUS

Type of Issue	Property and Casualty
Issued	Finalized December 4, 2000
Effective Date	January 1, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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EXHIBIT A - ILLUSTRATION OF CEDED PREMIUMS AND LOSSES **5**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for Multiple Peril Crop Insurance (MPCI). This statement also establishes statutory accounting principles for the Aquatic Crop Reinsurance Agreement (hereinafter included in the term MPCI).

SUMMARY CONCLUSION

Introduction

2. Farming has always been an inherently risky enterprise because farmers operate at the mercy of nature and frequently are subjected to weather-related perils such as droughts, floods, hurricanes, and other natural disasters. Since the 1930s, many farmers have been able to transfer part of the risk of loss in production to the federal government through the subsidized MPCI program administered by the Federal Crop Insurance Corporation (FCIC), an agency of the United States Department of Agriculture. Major legislation enacted in 1980 and 1994 restructured the MPCI program. The 1980 legislation enlisted, for the first time, private insurance companies to sell, service, and share the risk of MPCI insurance policies.

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Subsequently, in 1994, the Federal Crop Insurance Reform and Department of Agriculture Reorganization Act revised the program to offer farmers two primary levels of insurance coverage, catastrophic and buy-up.

3. Catastrophic insurance is designed to provide farmers with protection against extreme crop losses for a small processing fee. Buy-up insurance provides protection against more typical and smaller crop losses in exchange for a policyholder-paid premium. The government subsidizes the total premium for catastrophic insurance and a portion of the premium for buy-up insurance. Farmers who purchase buy-up crop insurance must choose both the coverage level (the proportion of the crop to be insured) and the unit price (such as, per bushel) at which any loss is calculated. With respect to the coverage level of production, farmers can choose to insure as much as 85% ~~percent~~ of normal production or as little as 50% ~~percent~~ of normal production at different price levels. With respect to the unit price, farmers choose whether to value their insured production at FCICs full estimated market price or at a percentage of the full price.

4. In recent years, FCIC has introduced a new risk management tool called revenue insurance. Unlike traditional crop insurance, which insures against losses in the level of crop production, revenue insurance plans insure against losses in revenue. The plans protect the farmer from the effects of declines in crop prices or declines in crop yields, or both. Like traditional buy-up insurance, the government subsidizes a portion of the premiums. One of the plans, called Crop Revenue Coverage, is available in many states for major crops. Two other plans, called Income Protection and Revenue Assurance, are available to farmers in only limited areas.

5. Companies participate in the MPCI program with FCIC through the Standard Reinsurance Agreement (SRA) per the terms of which the insurance companies share in the underwriting results of each policy. The SRA reinsurance terms provide a company the flexibility to limit its exposure on a state-by-state basis. MPCI premium is not expense loaded, therefore FCIC pays the insurance companies, on behalf of the policyholder, a percent of premium for administrative expenses associated with selling and servicing crop insurance policies, including the expenses associated with adjusting claims.

6. The FCIC utilizes an escrow account to distribute or collect additional funds. Premium (collected from the policyholders and the federal government subsidy) is deposited in the escrow account and is available to pay the claims arising under the program.

Premium Recognition

7. MPCI gross premium is defined as the contractually determined amount specified by FCIC to the policyholder for the effective period of the contract based on the actuarially determined expectation of risk and policy benefits associated with the coverage provided by the terms of the insurance contract. In addition, gross premium shall also include the government premium subsidy paid on behalf of the policyholder.

8. MPCI ceded premium and losses are defined as the amount calculated by applying the proportional and non-proportional factors as stated in the SRA. An example of this application is shown in Exhibit A to this statement.

9. MPCI written premium shall be recorded as soon as an estimate can be made, but no later than the processing date. Upon recording written premium, a liability for the unearned premium reserve shall be established to reflect the amount of premium for the portion of the insurance coverage that has not yet expired. Premiums shall be recognized as revenue over the period of risk in proportion to the amount of insurance protection provided.

10. The company shall disclose the method used to compute the unearned premium reserve in the financial statements.

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Amounts Receivable or Payable

11. The company shares underwriting risk with FCIC and can earn or lose money according to the claims it must pay farmers for crop losses. The company earns underwriting profits when the net retained premiums exceed the net crop loss claims paid. The company incurs underwriting losses when the net claims paid for crop losses exceed the net retained premiums. These definitions do not consider underwriting expenses, which would be included for traditional statutory accounting underwriting gains and losses. The use of the terms underwriting gains and losses in this issue paper are unique to the MPCI program. As the premiums of the program are held by FCIC in escrow, the company shall recognize as a write-in asset a receivable from FCIC for the amount of the underwriting gain (as defined in this paragraph). Whereas, when the company is in an underwriting loss position, the company shall recognize a write-in liability to the FCIC for the amount of the underwriting loss (as defined in this paragraph), as the monies held in the escrow account are not sufficient to cover the company's claims. In accordance with the SRA, funds that remain in escrow will be distributed to the company at the conclusion of the contract period if the contract results in a gain to the company. If the company owes additional funds to the escrow (i.e., it is in a loss position), those funds are remitted on a periodic basis until the contract expires. These amounts shall be recorded net as the program meets the requirements of offsetting as defined in *SSAP No. 64—Offsetting and Netting of Assets and Liabilities*. In accordance with *SSAP No. 21R—Other Admitted Assets*, the amount receivable under the Federal Crop Insurance program shall be reported as an admitted asset.

12. Amounts receivable from policyholders meet the definition of an admitted asset as set forth in *SSAP No. 4—Assets and Nonadmitted Assets* and should be accounted for in accordance with *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*. The due date shall be governed by contractual due date of the premium billing, and not the effective date of the contract.

Unpaid Losses and Loss Adjustment Expenses

13. In accordance with *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*, losses and loss adjustment expenses shall be recognized as expense when a covered or insured event occurs.

14. The covered or insured event is the occurrence of an incident which gives rise to a claim or the incurring of costs. Claim payments and related expense payments are made subsequent to the occurrence of a covered or insured event and, in order to recognize the expense of a covered or insured event, it is necessary to establish a liability. The following are the types of future costs relating to the MPCI program:

a. Reported Losses: Expected payments for losses relating to insured events that have occurred and have been reported to, but not paid by, the insurer as of the statement date;

b. Incurred But Not Reported Losses, (IBNR): Expected payments for losses relating to insured events that have occurred but have not been reported to the insurer as of the statement date;

c. Loss Adjustment Expenses: Costs expected to be incurred in connection with the adjustment and recording of losses defined in paragraphs 14.a. and 14.b. of this statement.

Administrative Expense Payment

15. FCIC pays the insurance companies a percent of premium for administrative expenses associated with selling and servicing crop insurance policies, including the expenses associated with adjusting claims. The expense payment associated with the catastrophic coverage shall be recorded as a reduction

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of loss expenses whereas the expense payment for the buy-up coverage shall be recorded as a reduction of other underwriting expenses. The company shall disclose the total amounts received for each type of coverage.

Escrow Account

16. The escrow account shall not be recorded on the financial statements of the insurance company. This account is considered an FCIC account and as such is not owned by the insurance company, however, the company's underwriting gain is reflected as a receivable in accordance with paragraph 11.

Effective Date

17. This statement is effective for SRA contracts entered into on or after January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Correction of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 108—Multiple Peril Crop Insurance*

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EXHIBIT A - ILLUSTRATION OF CEDED PREMIUMS AND LOSSES

NOTES TO THE ILLUSTRATION

Fund	The reinsurance fund specified in the Standard Reinsurance Agreement (SRA).
Column 1	Reinsured Company proportional reinsurance retention percentage.
Column 2	Gross Written Premium equals the insured paid premium amount plus premium subsidy provided by FCIC.
Column 3	Net Retained Premium is the Reinsured Company retained premium after proportional reinsurance. Gross Written Premium (Column 2) times the Reinsured Company retention percentage (Column 1).
Column 4	Proportional Ceded Premium is the premium retained by FCIC after proportional reinsurance. Gross Written Premium (Column 2) minus the Reinsured Company Net Retained Premium (Column 3).
Column 5	Reinsured Company proportional reinsurance retention percentage (Column 1).
Column 6	Gross Losses equals total claim payments to insured.
Column 7	Net Retained Losses are the Reinsured Company retained losses after proportional reinsurance. Gross Losses (Column 6) times the Reinsured Company retention percentage (Column 5).
Column 8	Proportional Ceded Losses are the losses retained by FCIC after proportional reinsurance. Gross Losses (Column 6) minus the Reinsured Company Net Retained Losses (Column 7).
Column 9	Retained Loss Ratio is the Reinsured Company's Net Retained Losses (Column 7) divided by the Reinsured Company's Net Retained Premium (Column 3).
Column 10	Underwriting (Gain)/Loss is the Reinsured Company share of the MPCI program gain or loss after calculating the non-proportional reinsurance provided in the SRA.
Column 11	Non-Proportional Ceded Premium is equal to the Reinsured Company Net Retained Premium (Column 3) minus Net Retained Losses (Column 7) minus an Underwriting (Gain) (Column 10) if one exists. This is FCIC's share of the underwriting gain after proportional reinsurance, based on the non-proportional reinsurance gain sharing factors specified in the SRA.
Column 12	Non-Proportional Ceded Losses is equal to the Reinsured Company Net Retained Premium (Column 3) minus Net Retained Losses (Column 7) minus an Underwriting Loss (Column 10) if one exists. This is FCIC's share of the underwriting loss after proportional reinsurance, based on the non-proportional reinsurance loss sharing factors specified in the SRA.
Column 13	Final Retained Premium is equal to the Reinsured Company Net Retained Premium (Column 3) minus the Non-Proportional Ceded Premium (Column 11). The Reinsured Company Net Retained Premium after proportional reinsurance is reduced by the amount of FCIC's underwriting gain share after non-proportional reinsurance.

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Column 14 Final Retained Losses is equal to the Reinsured Company Net Retained Premium (Column 3) minus the Non-Proportional Ceded Losses (Column 12). The Reinsured Company Net Retained Losses after proportional reinsurance are reduced by the amount of FCIC's underwriting loss share after non-proportional reinsurance.

Column 15 Final Retained Loss Ratio is equal to Final Retained Losses divided by Final Retained Premium.

(a) Calculated based on the loss ratios for each fund by state. Net Retained Premium (Col 3) is applied to the percentages of Section II. C. and D. of the Standard Reinsurance Agreement.

(b) If the fund is in a GAIN position then there would be Non-proportional ceded premium. If the fund is in a LOSS position then there would be Non-proportional ceded losses.

Since each fund and state stands alone in the calculations, there is a possibility of Non-proportional ceded premium AND ceded losses within the same reinsurance year. There is also the possibility of this within the same fund (some states with a Gain and some states with a Loss).

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EXHIBIT A - ILLUSTRATION OF CEDED PREMIUMS AND LOSSES

Fund	(1) Retention %	(2) Gross Written Premium	(3) Net Retained Premium (Col 2 x Col 1)	(4) Proportional Ceded Premium (Col 2 - Col 3)
Assigned Risk	20%	20,000,000	4,000,000	16,000,000
Developmental	35%	10,000,000	3,500,000	6,500,000
Dev - CRC	35%	5,000,000	1,750,000	3,250,000
Dev - CAT	35%	5,000,000	1,750,000	3,250,000
Commercial	100%	100,000,000	100,000,000	0
Comm - CRC	100%	20,000,000	20,000,000	0
Comm - CAT	100%	40,000,000	40,000,000	0
Total Premium		200,000,000	171,000,000	29,000,000

Fund	(5) Retention %	(6) Gross Losses	(7) Net Retained Losses (Col 6 x Col 5)	(8) Proportional Ceded Losses (Col 6 - Col 7)	(9) Retained Loss Ratio (Col 7/Col 3)	(10) Underwriting (Gain)Loss (a)
Assigned Risk	20%	40,000,000	8,000,000	32,000,000	200.0%	184,000
Developmental	35%	16,000,000	5,600,000	10,400,000	160.0%	525,000
Dev - CRC	35%	7,000,000	2,450,000	4,550,000	140.0%	210,000
Dev - CAT	35%	4,000,000	1,400,000	2,600,000	80.0%	(157,500)
Commercial	100%	80,000,000	80,000,000	0	80.0%	(18,800,000)
Comm - CRC	100%	18,000,000	18,000,000	0	90.0%	(1,880,000)
Comm - CAT	100%	22,000,000	22,000,000	0	55.0%	(12,500,000)
Total Losses		187,000,000	137,450,000	49,550,000	80.4%	(32,418,500)

Fund	(11) Non-Proportional Ceded Premium (b) (Col 3 - Col 7 - Col 10 "Gain")	(12) Non-Proportional Ceded Losses (b) (Col 3 - Col 7 + Col 10 "Loss")	(13) Final Retained Premium (Col 3 - Col 11)	(14) Final Retained Losses (Col 7 - Col 12)	(15) Final Retained Loss Ratio (Col 14/Col 13)
Assigned Risk	0	3,816,000	4,000,000	4,184,000	104.6%
Developmental	0	1,575,000	3,500,000	4,025,000	115.0%
Dev - CRC	0	490,000	1,750,000	1,960,000	112.0%
Dev - CAT	192,500	0	1,557,500	1,400,000	89.9%
Commercial	1,200,000	0	98,800,000	80,000,000	81.0%
Comm - CRC	120,000	0	19,880,000	18,000,000	90.5%
Comm - CAT	5,500,000	0	34,500,000	22,000,000	63.8%
Total	7,012,500	5,881,000	163,987,500	131,569,000	80.2%

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Statement of Statutory Accounting Principles No. 83

Mezzanine Real Estate Loans

STATUS

Type of Issue	Common Area
Issued	Finalized October 16, 2001
Effective Date	December 31, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	A-001

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for Mezzanine Real Estate Loans (MREL). An MREL is a loan secured by a pledge of direct or indirect equity interests in an entity that owns real estate (the "real estate owner"). The real estate owner is typically the borrower under a mortgage loan secured by the same real estate. The MREL borrower (the "mezz borrower") may be the real estate owner or one or more of the holder(s) of the direct or indirect equity interest(s) in the real estate owner. As used herein, "direct equity interests" means the then issued and outstanding shares or units of partnership, membership or other beneficial interests in the real estate owner, and "indirect equity interests" means the then issued and outstanding shares or units of partnership, membership or other beneficial interests in a member, partner, shareholder or other holder of direct equity interests in the real estate owner.

SUMMARY CONCLUSION

2. For statutory accounting purposes, a MREL shall be defined as a debt obligation, that is not a security, which is secured by a pledge of equity interest in an entity that owns real estate. A security is a share, participation, or other interest in property or in an enterprise of the issuer or an obligation of the issuer that:

a. Either is represented by an instrument issued in bearer or registered form, or if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer;

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b. Is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment; and

c. Either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

3. MREL's meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

4. Reporting entities holding MREL's shall follow the accounting, reporting and disclosure requirements defined within *SSAP No. 37—Mortgage Loans*.

5. In order for a MREL to qualify as an admitted asset, the MREL agreement (the agreement) shall:

a. Require that each pledgor abstain from granting additional security interests in the equity interest pledged; and

b. In addition to satisfaction of the requirements set forth in paragraphs 5.c. and 5.d., the MREL lender shall employ techniques to minimize the likelihood or impact of a bankruptcy filing on the part of the real estate owner and, if different, on the part of the mezz borrower. These techniques may include (by way of example and not limitation) one or more of the following: (i) separateness covenants, (ii) cash management techniques, (iii) exceptions to the non-recourse provisions for damages arising out of the mezz borrower's failure to comply with covenants prohibiting additional debt, transfers of the real estate, transfers of pledged interests, and violation of the single asset/single purpose covenants, (iv) full recourse liability in the event of a bankruptcy filing on the part of the real estate owner and, if different, on the part of the mezz borrower, and (v) loan guaranties. The selection of techniques that are applied in the instance of any particular MREL to achieve said purposes requires an exercise of judgement by the MREL lender. The reasonableness of the techniques utilized in any particular MREL will be assessed in light of the credit characteristics of the MREL borrower, any guarantors and the underlying real estate at the time of origination. Utilizing this standard provides flexibility to the MREL lender and provides a basis for the regulator and auditor in analyzing the reasonableness of the judgement of the MREL lender; and

c. The real estate owner and, if different, the mezz borrower shall:

i. Hold no assets other than, in the case of the real estate owner, the real property, and in the case of the mezz borrower (if different), the equity interest in the real estate owner;

ii. Not engage in any business other than, in the case of the real estate owner, the ownership and operation of the real estate, and in the case of the mezz borrower (if different), holding an ownership interest in the real estate owner; and

iii. Not incur additional debt, other than limited trade payables, a first mortgage loan (in the case of the real estate owner), and the MREL (in the case of the mezz borrower, if different).

d. At the time of the initial investment, the MREL lender shall corroborate that the sum of the first mortgage and the MREL does not exceed 100% of the value of the real estate as evidenced by a current appraisal. Acceptable appraisal methods are described in paragraph 13 of *SSAP No. 40R—Real Estate Investments*.

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Disclosures

6. The financial statements shall disclose, as applicable, the requirements of SSAP No. 37, paragraphs 25-27. The MREL lender shall report in Appendix A-001 to its annual statement the amount and percentages of its total admitted assets held in MREL and the largest three investments held in MREL except that such detail shall not be required for assets held in MREL totaling less than 2.5% of its total admitted assets.

Effective Date and Transition

7. This statement is effective for years ending on and after December 31, 2001. Any change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 113—Mezzanine Real Estate Loans*

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Statement of Statutory Accounting Principles No. 84

Health Care and Government Insured Plan Receivables

STATUS

Type of Issue	Common Area
Issued	Finalized October 16, 2001
Effective Date	December 31, 2001
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 05-05
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for pharmaceutical rebate receivables, claim overpayment receivables, loans and advances to providers who do not meet the definition of related parties, capitation arrangement receivables, risk-sharing receivables, and amounts receivable under government insured plans.

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SUMMARY CONCLUSION

Overview

2. Pharmaceutical rebates are arrangements between pharmaceutical companies and reporting entities in which the reporting entities receive rebates based upon the drug utilization of its subscribers at participating pharmacies. These rebates are sometimes recorded as receivables by reporting entities using estimates based upon historical trends which should be adjusted to reflect significant variables involved in the calculation, such as number of prescriptions written/filled, type of drugs prescribed, use of generic vs. brand-name drugs, etc. In other cases, the reporting entity determines the amount of the rebate due based on the actual use of various prescription drugs during the accumulation period and then bills the pharmaceutical company. Oftentimes, a pharmacy benefits management company may determine the amount of the rebate based on a listing (of prescription drugs filled) prepared for the reporting entity's review. The reporting entity will confirm the listing and the pharmaceutical rebate receivable.

3. Claim overpayments may occur as a result of several events, including but not limited to claim payments made in error to a provider. Reporting entities often establish receivables for claim overpayments.

4. A health entity may make loans or advances to large hospitals or other providers. Such loans or advances are supported by legally enforceable contracts and are generally entered into at the request of the provider. In many cases, loans or advances are paid monthly and are intended to represent one month of fee-for-service claims activity with the respective provider.

5. A capitation arrangement is a compensation plan used in connection with some managed care contracts in which a physician or other medical provider is paid a flat amount, usually on a monthly basis, for each subscriber who has elected to use that physician or medical provider. In some instances, advances are made to a provider under a capitation arrangement in anticipation of future services.

6. Risk-sharing agreements are contracts between reporting entities and providers with a risk-sharing element based upon utilization. The compensation payments for risk-sharing agreements are typically estimated monthly and settled annually. These agreements can result in receivables due from the providers if annual utilization is different than that used in estimating the monthly compensation.

7. The definition and accounting treatment for nonadmitted assets is outlined in paragraph 3 of *SSAP No. 4—Assets and Nonadmitted Assets*. Pharmaceutical rebate receivables, claim overpayment receivables, loans and advances to providers, capitation arrangement receivables, risk-sharing receivables, and amounts receivable under government insured plans meet the definition of assets as set forth in SSAP No. 4, and are admitted assets to the extent that the requirements for admission defined in this statement are met.

8. This statement shall not be considered an all-inclusive list of health care receivables. Certain health care receivables are addressed in other statements. Health care receivable assets not addressed in other statements or this statement are nonadmitted assets.

Pharmaceutical Rebate Receivables

9. Pharmaceutical rebates receivables consist of reasonably estimated amounts and billed amounts. Both the billed amount and the estimated amount shall be admitted assets subject to the conditions specified below:

a. Estimated amounts shall be related solely to actual prescriptions filled during the 3 months immediately preceding the reporting date;

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b. Billed amounts represent pharmaceutical rebate receivables that have been invoiced or confirmed in writing but not collected as of the reporting date. Billed amounts for an estimated amount under paragraph 9.a. shall be admitted only if the determination of the rebate, based on actual prescriptions filled, occurs and is invoiced or confirmed in writing within the 2 months following the reporting date of the estimated amount. Adjustments to previously billed amounts related to prior periods shall be nonadmitted until invoiced or confirmed in writing. Pharmaceutical rebates that have not been collected within 90 days of the invoice date or confirmation date shall be nonadmitted. Furthermore, if accrued pharmaceutical rebate receivables are not invoiced or confirmed in writing in accordance with the contract provisions, the accrual shall be nonadmitted; and

c. Evaluation of the collectibility of pharmaceutical rebate receivables shall be made periodically. If in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

10. The method used to reasonably estimate the receivable shall be consistent from period to period and shall be adjusted periodically for any changes in the underlying pharmaceutical rebate contract provisions. The financial statements shall disclose information regarding the reporting entity's pharmaceutical rebates in accordance with paragraph 23 of this statement.

11. Income from pharmaceutical rebates of insured plans shall be reported as a reduction to claims expense on the summary of operations.

12. Receivable and payable balances related to uncollected pharmaceutical rebates of uninsured plans shall be recorded on the financial statements of the reporting entity. Any pharmaceutical rebates earned by the reporting entity that are in excess of the amounts to be remitted to the uninsured plan pursuant to an administrative services agreement shall be determined consistent with the requirements of paragraphs 9 and 10 and shall be reported on the balance sheet as an amount receivable relating to uninsured accident and health plans, and as a reduction to general expenses on the statement of operations.

Claim Overpayment Receivables

13. A claim overpayment shall not be recorded as a receivable until invoiced. To the extent that the claim overpayment meets the setoff conditions in *SSAP No. 64—Offsetting and Netting of Assets and Liabilities* and the overpayment is a specific identifiable payment and not an estimate, the receivable may be admitted up to the amount of the payable to the provider for reported claims (i.e., excluding incurred but not reported claims). The receivable and payable shall be reported gross rather than netted on the balance sheet. Evaluation of the collectibility of claim overpayment receivables shall be made periodically. If in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. Amounts in excess of that written off that do not meet the right of offset conditions shall be nonadmitted as they are not available to satisfy policyholder obligations.

Loans and Advances to Providers

14. Loans or advances to providers who meet the definition of related parties in *SSAP No. 25—Affiliates and Other Related Parties* shall follow the guidance in that statement. To the extent a loan or advance to a non-related party provider meets the setoff conditions in SSAP No. 64, the loan or advance may be admitted up to the amount of the payable to the provider for reported claims (i.e., excluding incurred but not reported claims).

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15. In addition, a loan or advance to a non-related party hospital shall be admitted up to the amount of claims incurred and payable to the hospital if all of the following conditions are met:

a. The loan or advance meets the setoff conditions in SSAP No. 64;

b. The loan or advance is supported by a legally enforceable contract;

c. The loan or advance is administered pursuant to contractual terms;

d. The contractual terms of the agreement provide for separate quarterly reconciliations;

e. Each quarterly reconciliation shall be completed within nine months of the end of such quarter; and

f. A quarterly reconciled difference shall be settled within 90 days of the date the reconciliation is completed.

16. If a quarterly reconciliation is not performed or settled in accordance with paragraphs 15.e. and 15.f., all assets for loans or advances to that hospital shall be nonadmitted.

17. The receivable and payable shall be reported gross rather than netted on the balance sheet. Evaluation of the collectibility of loans and advances to providers shall be made periodically. If in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. Amounts in excess of that written off that do not meet the right of offset conditions shall be nonadmitted as they are not available to satisfy policyholder obligations.

Capitation Arrangement Receivables

18. Advances to providers under capitation arrangements that are made under the terms of an approved provider services contract in anticipation of future services shall be admitted to the extent that the advanced amount does not exceed one month of average capitation payments for the subject provider during the preceding twelve months, and provided that the contract cannot be terminated before the end of the month for which the advanced amount was paid. Evaluation of the collectibility of capitation arrangement receivables shall be made periodically. If in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

Risk-Sharing Receivables

19. Risk-sharing receivables may consist of reasonably estimated amounts and billed amounts. Both the billed amount and the estimated amount shall be admitted assets subject to the conditions specified below:

a. Risk-sharing receivables and payables shall only be recorded when reasonably estimated. Estimates of risk-sharing receivables may be admitted if based on at least six months of actual claims experience for each risk-sharing contract. The contractual terms of any risk-sharing agreement shall provide for evaluation of the experience under the contract at least annually. The determination of the risk-sharing balance shall commence no later than 6 months following the close of such annual period, and the balance shall be invoiced no later than 8 months following close of the annual period;

b. Billed amounts represent risk-sharing receivables that have been invoiced but not collected as of the reporting date. Risk-sharing receivables and payables shall be invoiced or refunded in accordance with the contractual provisions of the risk-sharing agreement.

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Adjustments resulting in increases to previously billed amounts related to prior periods shall be nonadmitted until invoiced. Adjustments resulting in decreases to previously billed amounts shall be recognized immediately. Risk-sharing receivables that have not been collected within 90 days of the date of billing shall be nonadmitted;

c. Risk-sharing receivables and payables shall be reported gross rather than netted on the balance sheet. However, if a reporting entity has both a receivable and payable balance with the same provider and the balances meet the setoff conditions in SSAP No. 64, those balances shall be netted in accordance with SSAP No. 64; and

d. Evaluation of the collectibility of risk-sharing receivables shall be made quarterly. If in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

20. The method used to reasonably estimate the receivable shall be consistent from period to period and shall be adjusted periodically for any changes in the underlying risk-sharing contract. The financial statements shall disclose information regarding the reporting entity's risk-sharing receivables in accordance with paragraph 24 of this statement.

21. Income/expense from risk-sharing contracts shall be reported as a component of claims expense on the summary of operations.

Amounts Receivable Under Government Insured Plans

22. Amounts receivable that originate from the government, under government insured plans, including amounts over 90 days due, that qualify as accident and health contracts in accordance with *SSAP No. 50—Classifications of Insurance or Managed Care Contracts* shall be admitted assets. These receivables may include, but are not limited to, receivables due from the government under Medicare, Medicaid and similarly funded government insured plans. Evaluation of the collectibility of amounts receivable under government insured plans shall be made periodically. If in accordance with SSAP No. 5R, it is probable the balance is uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. The collectibility and any nonadmission of amounts receivable from the government insured or uninsured plans are addressed here and in *SSAP No. 47—Uninsured Plans*, paragraph 11.c. Refer to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* for additional information and definitions of terms specifically related to Medicare Part D business[1].

Disclosures

23. The financial statements shall disclose the method used by the reporting entity to estimate pharmaceutical rebate receivables. Furthermore, for the most recent three years and for each quarter therein, the reporting entity shall also disclose the following:

a. Estimated balance of pharmacy rebate receivable as reported on the financial statements;

b. Pharmacy rebates as invoiced or confirmed in writing; and

c. Pharmacy rebates collected.

An example of this disclosure is shown in Exhibit A to this statement.

[1] Although Medicare Part D business is considered a government plan, performance network rebate-based receivables under such plans may or may not originate from the government. Only receivables that originate from the government are captured within paragraph 22.

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24. The financial statements shall disclose the method used by the reporting entity to estimate its risk-sharing receivables. If any receivable and payable balances with the same provider are netted, the reporting entity shall disclose the gross receivable and payable balances in the notes to the financial statements. Furthermore, for the most recent three years, the reporting entity shall also disclose the following:

a. Risk-sharing receivables as estimated and reported on the prior year financial statements for annual periods ending in the current year;

b. Risk-sharing receivables as estimated and reported on the financial statements for annual periods ending in the current year and the following year;

c. Risk-sharing receivables invoiced as determined after the annual period;

d. Risk-sharing receivables not yet invoiced; and

e. Amounts collected from providers as payments under risk-sharing contracts.

An example of this disclosure is shown in Exhibit B to this statement.

Effective Date and Transition

25. This statement is effective for years ending on and after December 31, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

26. Prior to January 1, 2003, reporting entities may transition the invoicing provision outlined in paragraph 9 and shall invoice pharmaceutical rebates on no less than a semi-annual basis. Furthermore, prior to January 1, 2003, reporting entities may transition the 90 day admissibility provision outlined in paragraph 9 and shall nonadmit pharmaceutical rebates if such rebates have not been collected within 180 days of the billing date.

27. Prior to January 1, 2003, reporting entities may transition the invoicing provision outlined in paragraph 19 and shall invoice the risk-sharing balance no later than 11 months following the close of the annual period.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 107—Certain Health Care Receivables and Receivables Under Government Insured Plans*

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EXHIBIT A – ILLUSTRATION OF PHARMACEUTICAL REBATE RECEIVABLES

(000 omitted)

Quarter	Estimated Pharmacy Rebates as Reported on Financial Statements	Pharmacy Rebates as Invoiced/ Confirmed	Actual Rebates Collected Within 90 Days of Invoicing/ Confirmation	Actual Rebates Collected Within 91 to 180 Days of Invoicing/ Confirmation	Actual Rebates Collected More Than 180 Days After Invoicing/ Confirmation
12/31/2003	$150	$147			
9/30/2003	130	133	$62		
6/30/2003	142	143	70	$55	
3/30/2003	157	152	65	42	$20
12/31/2002	125	132	70	27	20
9/30/2002	123	129	62	31	14
6/30/2002	112	120	54	20	16
3/31/2002	110	118	57	39	20
12/31/2001	68	75	34	20	10
9/30/2001	60	59	27	17	10
6/30/2001	57	60	31	15	10
3/31/2001	45	50	25	18	7

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EXHIBIT B – ILLUSTRATION OF RISK-SHARING RECEIVABLES

(000 omitted)

Calendar Year	Evaluation Period Year Ending	Risk-Sharing Receivable as Estimated and Reported in the Prior Year	Risk-Sharing Receivable as Estimated and Reported in the Current Year	Risk-Sharing Receivable Invoiced	Risk-Sharing Receivable Not Invoiced	Actual Risk-Sharing Amounts Collected in Year Invoiced	Actual Risk-Sharing Amounts Collected First Year Subsequent	Actual Risk-Sharing Amounts Collected Second Year Subsequent	Actual Risk-Sharing Amounts Collected – All Other
2003	2003	$245	$232	$155	$77	$0			
	2004	XXX	$189	XXX	$189	XXX	XXX		
2002	2002	$223	$225	$203	$22	$0	$200		
	2003	XXX	$245	XXX	$245	XXX	XXX	XXX	XXX
2001	2001	$190	$178	$174	$4	$0	$170	$5	
	2002	XXX	$223	XXX	$223	$XXX	XXX	XXX	XXX

If there were only one contract or if all contracts have the same experience period, then there would only be an entry in either the "Invoiced" or "Not Invoiced" column for the current year. This example assumes varying dates on experience periods for multiple contracts. Assumptions: Two risk-sharing contracts are in place, one with an experience period that ends 3/31/03 and one with an experience period that ends 10/31/03.

The $155,000 receivable for the contract period that ends 3/31/03 would be invoiced no later than 11/30/03 (or 8 months following close of the contract period) and could be collected no later than 2/28/04. Therefore, the $155,000 would appear in the "Invoiced" column in 2003 but not shown as collected in 2003. Further, the $189,000 estimate for the experience period that ends 3/31/04 could be recorded on the December 31, 2003 financial statement, since there is more than six months of experience under the contract.

The contract with the experience period that ends 10/31/03 with an estimated $77,000 receivable would be invoiced by 6/30/04 and collected by 09/30/04. Therefore, it would appear in the "Not Invoiced" column and not shown as collected in 2003. However, no estimate could be reported on the December 31, 2003 financial statement for the experience period that ends 10/31/04, because there is less than six months of experience under the contract.

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EXHIBIT C – IMPLEMENTATION GUIDE

The purpose of this guide is to assist regulators as well as reporting entities in the practical application of SSAP No. 84.

Pharmaceutical Rebate Receivables

1. Q: What is a reasonable method of determining receivables for estimated amounts?

   A: At any one reporting date, a reporting entity's receivable for pharmaceutical rebates can consist of two distinct amounts: 1) an estimated amount, and 2) a billed amount (that can include adjustments to previously billed amounts). The estimated amount represents the reporting entity's best estimate of the rebates it expects to receive for those prescriptions drugs filled during the most recent quarter, i.e. at 12/31/20X1, the estimate would relate to those prescriptions filled during the fourth quarter of 20X1. Estimated rebate amounts for prescription drugs filled in any other quarter must be nonadmitted.

   When determining its estimate, the reporting entity should use the most accurate methods possible that utilize historical information relative to pharmaceutical rebates received. The reporting entity should use methods that consider contractual changes in rebate amounts, seasonality differences, changes in membership or premium revenue, changes in utilization of drugs with varying rebate levels, etc.

2. Q: Paragraph 9.b. states, "Billed amounts for an estimated amount under paragraph 9.a. shall be admitted only if the determination of the rebate, based on actual prescriptions filled, occurs and is invoiced or confirmed in writing within the 2 months following the reporting date of the estimated amount." What is meant by the phrase "within 2 months following the reporting date of the estimated amount?" Why does the SSAP make a distinction between those rebates that are invoiced and those that are confirmed in writing?

   A: This sentence is worded in this fashion in order to show the relationship between an estimated amount and the related billed amount. At any reporting date, a billed amount will qualify as an admitted asset only if it was invoiced or confirmed in writing within the two months following the most previously filed financial statement, or the financial statement in which the related estimate was reported. E.g., using the example in Q&A 1, the reporting entity could admit billed amounts for rebates attributable to prescriptions drugs filled in *third quarter* of 20X1, only if the rebates were invoiced or confirmed in writing no later than 11/30/20X1. Further, the billed amount must be collected by 2/28/20X2 or it will become a nonadmitted asset.

   Secondly, reporting entities typically administer their pharmaceutical benefit programs in one of two fashions, either directly or though a pharmaceutical benefit manager (PBM). The SSAP makes a distinction for these two instances. Entities that contract directly with the pharmaceutical company will invoice the pharmaceutical company for its rebates. However, for those entities that use a PBM, the SSAP requires that to admit billed amounts the reporting entity must receive reports from the PBM on a quarterly basis; the reports should provide fairly detailed information as to the number of each prescription drug filled, the rebate for each individual drug, the total amount of rebates to be received, any rebates to be received that relate to prior periods, etc. The reporting entity must then accept or "confirm" the report, and then communicate formal acceptance of the report to the PBM. Only after this occurs is the amount considered confirmed as required by the SSAP.

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3. Q: What is a reasonable method of confirming a report received from our PBM?

   A: The reporting entity should perform whatever verification procedures it deems necessary to provide adequate assurance that the report is accurate. These procedures might include, but are not limited to, reviewing the information required from the PBM as discussed in Q&A 2, verification of payments for prescription drug charges, trend testing, etc.

4. Q: Rebates relating to uninsured plans have been included in the gross receivable for pharmaceutical rebates. However, much of the amount was nonadmitted because of the requirement to bill within two months was not met. Is it still necessary to record the payable to the uninsured plan, even though the liability is essentially a pass-through?

   A: Yes, the liability must still be recorded, regardless of the fact that the related asset may be nonadmitted.

5. Q: Should the disclosure in Exhibit A include rebates for both insured and uninsured business?

   A: Yes, the disclosure to be included in the Notes to Financial Statements for pharmaceutical rebate receivables should include pharmaceutical rebates of insured and uninsured business. However, ultimately the reporting entity must have the ability to separately identify rebates for insured and uninsured business, given the distinct difference in treatment on the Statement of Revenue and Expenses.

6. Q: Please explain the transition period related to the invoicing of pharmaceutical rebate receivables.

   A: The transition applies to all reporting periods preceding January 1, 2003, and allows transition for the invoicing and collection provisions found in paragraph 9.b. Throughout the transition period, the reporting entity may invoice (or confirm in writing) its pharmaceutical rebates semi-annually, i.e. the receivable for the estimated or billed amount may include two quarters, depending upon the invoice dates elected. However, reporting entities must still invoice or confirm in writing their rebates within 2 months of the end of each semi-annual period for the billed amount to be admitted.

   For example, during the transition period B&P HMO elected to invoice its pharmaceutical rebates with semi-annual periods ending 12/31/2001 and 6/30/2002. B&Ps admitted asset for pharmaceutical rebate receivables for reporting periods ending 12/31/2001 through 3/31/2003 would be comprised of the following:

   <u>Transition period:</u>

12/31/2001	Estimated amounts: third and fourth quarters of 2001 Billed amounts: none
3/31/2002	Estimated amounts: first quarter of 2002 Billed amounts: third and fourth quarters of 2001 if billed by 2/28/2002 (note that these billed amounts must be collected by 8/31/2002)
6/30/2002	Estimated amounts: first and second quarters of 2002 Billed amounts: third and fourth quarters of 2001 if billed by 2/28/2002 (note that these billed amounts must be collected by 8/31/2002)

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9/30/2002 Estimated amounts: third quarter of 2002
Billed amounts: first and second quarters of 2002 if billed by 8/31/2002 (these billed amounts must be collected by 1/1/2003, the date of full implementation of SSAP No. 84)

12/31/2002 Estimated amounts: third and fourth quarters of 2002
Billed amounts: first and second quarters of 2002 if billed by 8/31/2002 (take note that these billed amounts must be collected by 1/1/2003, the date of full implementation of SSAP No. 84)

Full implementation of SSAP No. 84

3/31/2003 Estimated amounts: first quarter of 2003
Billed amounts: fourth quarter of 2002 if billed by 2/28/2003

Note that this situation will result in no admitted asset allowed for the billed amount related to the third quarter of 2002, given that the requirements of the SSAP are fully effective on 1/1/2003. B&P should consider invoicing its rebates as required by the SSAP prior to the close of the transition period to avoid this situation.

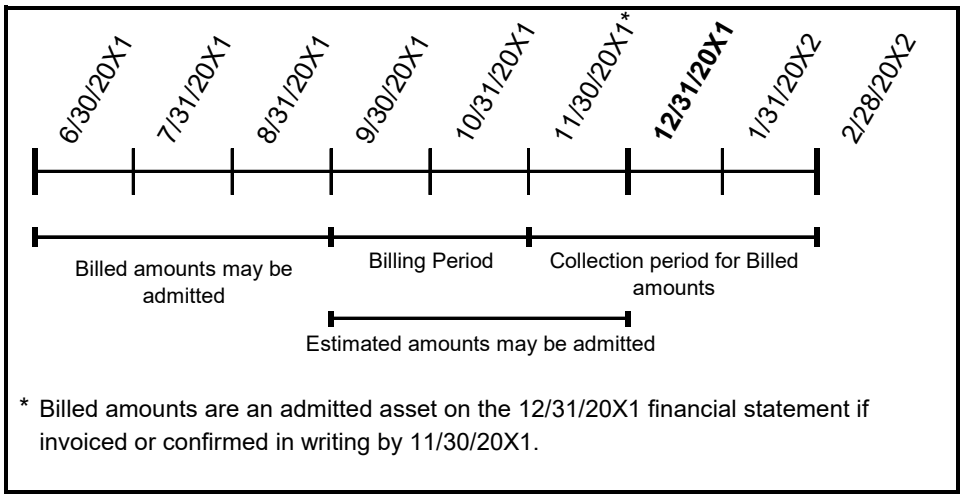
7. Q: How much historical data is required in the pharmaceutical rebates disclosure in 2001 and 2002?

A: Reporting entities should include as much information as possible when completing this disclosure in 2001 and 2002. Be aware that in 2001 and 2002, this disclosure will be included under Note 20, Other Items. In 2003, this disclosure will be a separate note.

8. Q: Should the disclosure include rebates invoiced or confirmed in writing that relate to prior periods?

A: Yes. The disclosure should include all rebates invoiced or confirmed in writing during the respective quarter, whether such rebates relate to the most recently invoiced quarter or any quarter preceding that.

Illustrative timeline of SSAP No. 84 requirements relative to pharmaceutical rebate receivables, assuming a financial statement date of 12/31/20X1:



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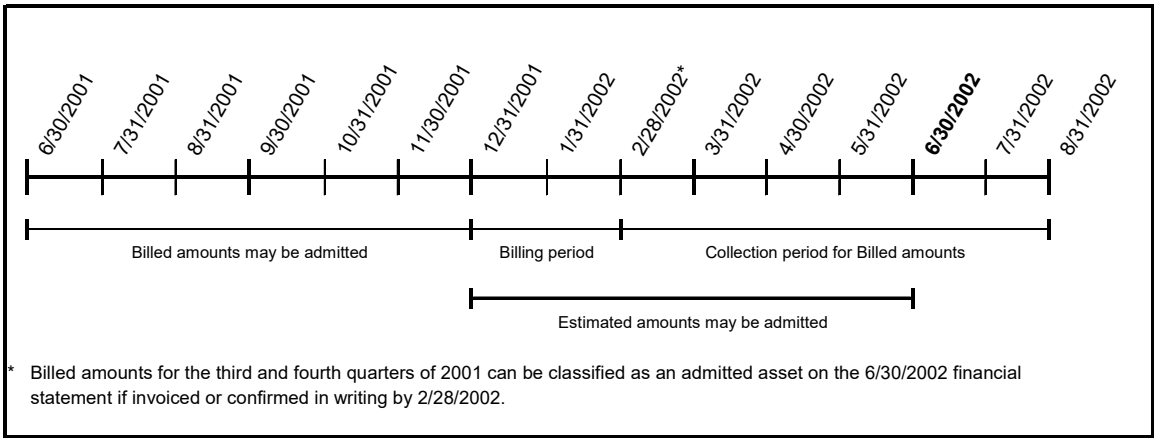
Illustrative timeline of SSAP No. 84 transition guidance as related to pharmaceutical rebate receivables, assuming a financial statement date of 6/30/2002 and that the reporting entity has elected to invoice/confirm in writing its rebates at 12/31/2001 and 6/30/2002:



Loans and Advances to Providers

9. Q: Why was a distinction made between loans and advances to providers and loans and advances to hospitals?

   A: This distinction was made to recognize the unique nature of certain arrangements between reporting entities and hospitals, whereby the participating hospitals are loaned and advanced amounts monthly or quarterly. Such arrangements oftentimes result in lower charges to the reporting entity and work to the benefit of the reporting entity.

10. Q: With regard to the phrase "a loan or advance to a non-related party hospital shall be admitted up to the amount of claims incurred and payable to the hospital," what does this mean? Does this require that the IBNR valuation be performed for each hospital in which funds are loaned or advanced?

    A: In a situation in which amounts are loaned/advanced to a hospital, as the hospital provides services and reports such to the reporting entity, the costs of such services are applied against the outstanding loan. Also applied against the loan is the reporting entity's estimate of the amount of services provided but not yet reported, i.e. IBNR. The remaining portion of the loan represents the receivable subject to the requirements of the SSAP.

    In determining the amount of claims incurred and payable to a particular hospital, the reporting entity should use the most accurate method available. In most instances an IBNR calculation would be the most accurate method of determining this amount.

11. Q: Please explain the reconciliation requirements in paragraph 15.d. and 15.e. related to loans and advances to hospitals.

    A: While loans and advances to hospitals are typically paid monthly, the SSAP requires that such balances be reconciled at least quarterly on a per-hospital basis. The SSAP further requires that each quarter's account be reconciled within nine months of the end of that quarter, i.e. the reconciliation for the quarter ending 3/31/20X1 must be completed by 12/31/20X1.

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Therefore, at 12/31/20X1, a reporting entity can have four quarters of loans and advances in its receivable: three quarters worth of unreconciled amounts and one quarter that has been reconciled but not settled.

12. Q: If amounts are loaned or advanced to a hospital but the reconciliation requirements of paragraph 15 are not met, must these amounts be nonadmitted?

A: Not necessarily. In this event, the guidance in paragraph 14 can be followed to determine admissibility, in that the loan or advance may be admitted up to the amount of the payable to the provider for reported claims.

Risk-Sharing Receivables

13. Q: The SSAP allows for the classification of certain estimates of risk-sharing receivables as admitted assets. In what instances may estimates be admitted, and what is a reasonable method of determining receivables for estimated amounts?

A: At any reporting date, a reporting entity's receivable for any one risk-sharing arrangement can consist of two amounts: 1) an estimated amount, and 2) a billed amount (that can include adjustments to previously billed amounts). An estimate can be admitted only if at least six months have passed since the commencement of the annual experience period. The estimated amount represents the reporting entity's best estimate of the receivable related to the contract period from inception to the reporting date.

When determining its estimate, the reporting entity should use the most accurate methods possible that utilize inception-to-date encounter data relative to outpatient surgery encounters, hospital days, etc. If the reporting entity cannot reasonably estimate its risk-sharing receivables, then such amounts must be nonadmitted.

14. Q: The SSAP requires that the determination of the risk share balance begin within six months from the end of the annual experience period, and further requires that the final amount must be invoiced no later than eight months following the close of such period. Must data accumulation stop with month six? Can the reporting entity utilize experience data from months seven and eight in its calculation?

A: The reporting entity should use as much experience data as possible within the 8-month invoicing requirement of paragraph 19.a. This requirement was included to ensure that reporting entities are being proactive when determining risk share balances but was in no way intended to limit the amount of experience data considered.

15. Q: Describe a situation when a receivable and payable would exist with the same provider under a risk-sharing arrangement?

A: This could happen 1) if the risk-share arrangement requires separate risk sharing for each line of business, for certain large groups, etc. or 2) where two contract/evaluation periods under a risk-sharing arrangement are involved.

16. Q: Please explain the transition period related to the invoicing of risk-sharing receivables.

A: The transition applies to all reporting periods preceding January 1, 2003, and allows transition for the invoicing provision found in paragraph 19. Throughout the transition period, the reporting entity may invoice its risk-sharing receivables within 11 months of the end of the contract period, i.e. 11/30/20X2 for a risk-sharing contract with an annual period ending

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12/31/20X1. Therefore, during the transition period estimated amounts may be admitted for an additional three-month time period, i.e. from 7/1/20X1 through 11/30/20X2.

17. Q: The disclosure for risk-sharing receivables seems confusing. Please explain what should be included in columns three through six that address estimated and billed/invoiced balances.

A: The third column from the left contains the heading "Risk-Sharing Receivable as Estimated and Reported in the Prior Year." This column should reflect the amount of risk-sharing receivables as determined in the prior year and reported as admitted assets on the prior year's financial statement. Therefore, there will never be information reported for the year subsequent to the year in question, as contracts with evaluation periods ending in the following year cannot have risk-sharing receivables recorded in the previous year.

The fourth column, "Risk-Sharing Receivable as Estimated and Reported in the Current Year," should contain the admitted amounts of risk-sharing receivables on the current year's financial statement. These amounts should be segregated between those agreements with contract periods ending in the current year and those ending in the following year.

The fifth column from the left contains the heading "Risk-Sharing Receivable Invoiced" and will contain the amount of risk-sharing receivables invoiced during the designated year, regardless of whether such are outstanding as of the financial statement date.

The sixth column, reflecting the heading "Risk-Sharing Receivable Not Invoiced," should contain the current year-end receivable balance for agreements which qualify for estimation under paragraph 19.b., i.e., the contract has been in effect for at least six months but no amounts have been invoiced. Note that a particular reporting entity might not have any estimated receivables, if that entity's risk-sharing contracts have not been in effect for at least six months.

Be aware that in 2001 and 2002, this disclosure will be included under Note 20, Other Items. In 2003, this disclosure will be a separate note.

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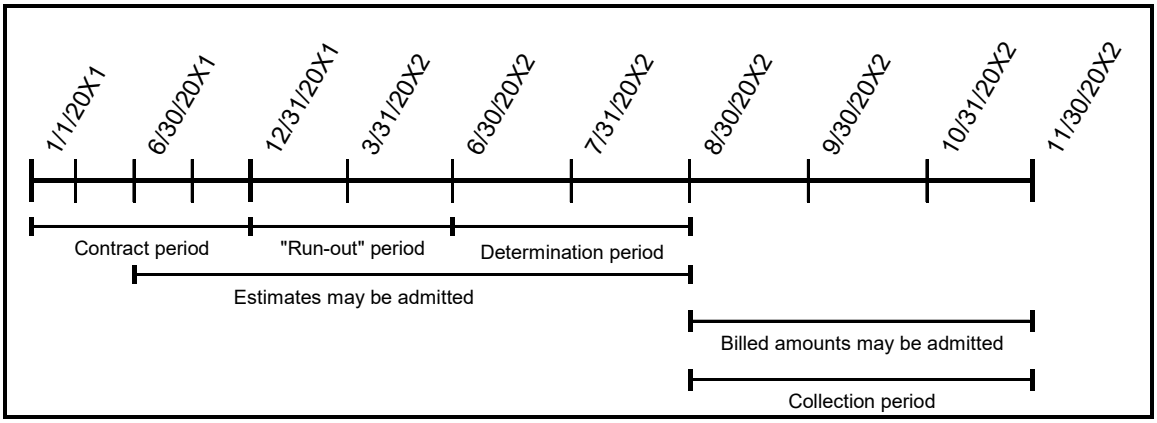
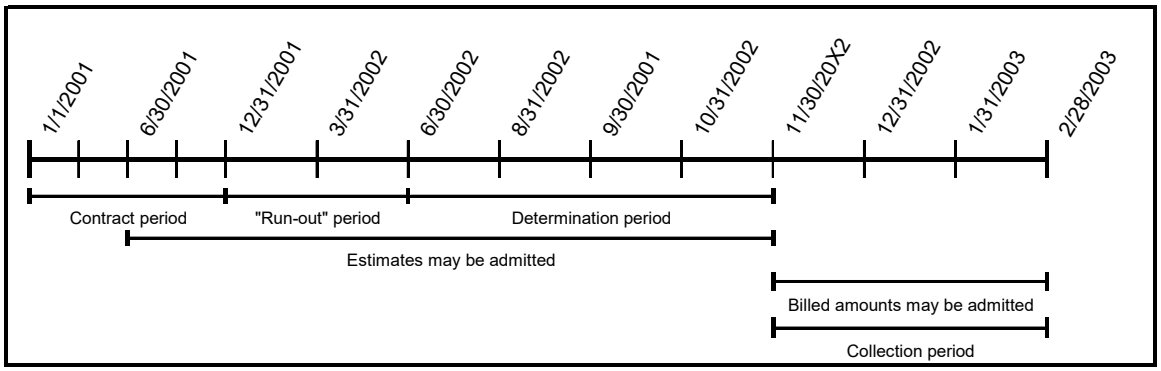
Illustrative timeline of SSAP No. 84 requirements relative to risk-sharing receivables, assuming the reporting entity has one risk-sharing agreement in place with an effective date of 1/1/20X1:



Illustrative timeline of SSAP No. 84 transition guidance as related to risk-sharing receivables, assuming the reporting entity has one risk-sharing agreement in place with an effective date of 1/1/2001:



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Statement of Statutory Accounting Principles No. 86

Derivatives

STATUS

Type of Issue	Common Area
Issued	Finalized May 14, 2002; Substantively revised August 10, 2022, and December 13, 2022
Effective Date	January 1, 2003; Substantive revisions in 2022 effective January 1, 2023
Affects	Supersedes SSAP No. 31
Affected by	No other pronouncements
Interpreted by	INT 20-01; INT 20-09; INT 22-01
Relevant Appendix A Guidance	None

STATUS **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for derivative instruments and hedging, income generation, and replication (synthetic asset) transactions using selected concepts outlined in *FASB Statement No. 133*, *Accounting for Derivative Instruments and Hedging Activities* (FAS 133).

2. This statement supersedes the provisions of *SSAP No. 31— Derivative Instruments*.

SUMMARY CONCLUSION

3. This statement addresses the recognition of derivatives and measurement of derivatives used in:

   a. Hedging transactions;

   b. Income generation transactions; and

   c. Replication (synthetic asset) transactions.

   d. Other Derivatives – (Derivatives that are not used in hedging, income generation or replication transactions.)

Definitions (for purposes of this statement)

4. "Derivative instrument" means an agreement, option, instrument or a series or combination thereof:

   a. To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or

   b. That has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests.

5. Derivative instruments include, but are not limited to; options, warrants used in a hedging transaction and not attached to another financial instrument, caps, floors, collars, swaps, forwards, futures, structured notes with risk of principal/original investment loss based on the terms of the agreement (in addition to default risk), and any other agreements or instruments substantially similar thereto or any series or combination thereof.

   a. "Caps" are option contracts in which the cap writer (seller), in return for a premium, agrees to limit, or cap, the cap holder's (purchaser) risk associated with an increase in a reference rate or index. For example, in an interest rate cap, if rates go above a specified interest rate level (the strike price or the cap rate), the cap holder is entitled to receive cash payments equal to the excess of the market rate over the strike price multiplied by the notional principal amount. Because a cap is an option-based contract, the cap holder has the right but not the obligation to exercise the option. If rates move down, the cap holder has lost only the premium paid. A cap writer has virtually unlimited risk resulting from increases in interest rates above the cap rate.

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b. "Collar" means an agreement to receive payments as the buyer of an option, cap or floor and to make payments as the seller of a different option, cap or floor.

c. "Floors" are option contracts in which the floor writer (seller), in return for a premium, agrees to limit the risk associated with a decline in a reference rate or index. For example, in an interest rate floor, if rates fall below an agreed rate, the floor holder (purchaser) will receive cash payments from the floor writer equal to the difference between the market rate and an agreed rate multiplied by the notional principal amount.

d. "Forwards" are agreements (other than futures) between two parties that commit one party to purchase and the other to sell the instrument or commodity underlying the contract at a specified future date. Forward contracts fix the price, quantity, quality, and date of the purchase and sale. Some forward contracts involve the initial payment of cash and may be settled in cash instead of by physical delivery of the underlying instrument.

e. "Futures" are standardized forward contracts traded on organized exchanges. Each exchange specifies the standard terms of futures contracts it sponsors. Futures contracts are available for a wide variety of underlying instruments, including insurance, agricultural commodities, minerals, debt instruments (such as U.S. Treasury bonds and bills), composite stock indices, and foreign currencies.

f. "Options" are contracts that give the option holder (purchaser of the option rights) the right, but not the obligation, to enter into a transaction with the option writer (seller of the option rights) on terms specified in the contract. A call option allows the holder to buy the underlying instrument, while a put option allows the holder to sell the underlying instrument. Options are traded on exchanges and over the counter.

g. "Structured Notes" in scope of this statement are instruments defined in *SSAP No. 26R—Bonds* (often in the form of debt instruments), in which the amount of principal repayment or return of original investment is contingent on an underlying variable/interest[1]. Structured notes that are "mortgage-referenced securities" are captured in *SSAP No. 43R—Loan-Backed and Structured Securities*.

h. "Swaps" are contracts to exchange, for a period of time, the investment performance of one underlying instrument for the investment performance of another underlying instrument, typically, but not always, without exchanging the instruments themselves. Swaps can be viewed as a series of forward contracts that settle in cash and, in some instances, physical delivery. Swaps generally are negotiated over-the-counter directly between the dealer and the end user. Interest rate swaps are the most common form of swap contract. However, foreign currency, commodity, and credit default swaps also are common.

[1] The "structured notes" captured within scope of this statement is specific to instruments in which the terms of the agreement make it possible that the reporting entity could lose all or a portion of its original investment amount (for other than failure of the issuer to pay the contractual amounts due). These instruments incorporate both the credit risk of the issuer, as well as the risk of an underlying variable/interest (such as the performance of an equity index or the performance of an unrelated security). Securities that are labeled "principal-protected notes" are captured within scope of this statement if the "principal protection" involves only a portion of the principal and/or if the principal protection requires the reporting entity to meet qualifying conditions in order to be safeguarded from the risk of loss from the underlying linked variable. Securities that may have changing positive interest rates in response to a linked underlying variable or the passage of time, or that have the potential for increased principal repayments in response to a linked variable (such as U.S. Treasury Inflation-Indexed Securities) that do not incorporate risk of original investment/principal loss (outside of default risk) are not captured as structured notes in scope of this statement.

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i. "Swaptions" are contracts granting the owner the right, but not the obligation, to enter into an underlying swap. Although options can be traded on a variety of swaps, the term "swaption" typically refers to options on interest rate swaps. A swaption hedges the buyer against downside risk, as well as lets the buyer take advantage of any upside benefits. That is, it gives the buyer the benefit of the agreed-upon rate if it is more favorable than the current market rate, with the flexibility of being able to enter into the current market swap rate if it is preferable. Conversely, the seller of swaptions assumes the downside risk, but benefits from the amount paid for the swaption, regardless if it is exercised by the buyer and the swap is entered into.

j. "Warrants" are instruments that give the holder the right to purchase an underlying financial instrument at a given price and time or at a series of prices and times outlined in the warrant agreement. Warrants may be issued alone or in connection with the sale of other securities, for example, as part of a merger or recapitalization agreement, or to facilitate divestiture of the securities of another business entity. Publicly traded stock warrants are captured in scope of *SSAP No. 30R—Unaffiliated Common Stock* or *SSAP No. 32R—Preferred Stock*. All other warrants, including non-publicly traded stock warrants, shall be captured in scope of SSAP No. 86.

6. "Derivative Premium" is the cost to acquire or write a derivative contract. Derivative premium is not an "underlying" in a derivative contract and is not impacted by changes in an underlying interest of the derivative agreement. A derivative with contract terms that finance the derivative premium, so that the cost is paid or received throughout the derivative term or at derivative maturity, does not result with an "embedded derivative" addressed in paragraph 17.

7. "Firm commitment" is an agreement with an unrelated party, binding on both parties and expected to be legally enforceable, with the following characteristics:

a. The agreement specifies all significant terms, including the quantity to be exchanged, the fixed price, and the timing of the transaction. The fixed price may be expressed as a specified amount of an entity's functional currency or of a foreign currency. It may also be expressed as a specified interest rate or specified effective yield;

b. The agreement includes a disincentive for nonperformance that is sufficiently large to make performance probable; and

c. For investments in subsidiary, controlled, and affiliated entities (as defined by *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*) and investments in limited liability companies (as defined by *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*) it must be probable that acquisition will occur within a reasonable period of time.

8. A hedging transaction is defined as a derivative(s) transaction which is entered into and maintained to reduce:

a. The risk of a change in the fair value or cash flow of assets and liabilities which the reporting entity has acquired or incurred or has a firm commitment to acquire or incur or for which the entity has forecasted acquisition or incurrence; or

b. The currency exchange rate risk or the degree of foreign currency exposure in assets and liabilities which a reporting entity has acquired or incurred or has a firm commitment to acquire or incur or for which the entity has forecasted acquisition or incurrence.

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9. "Income generation transaction" is defined as derivatives written or sold to generate additional income or return to the reporting entity. They include covered options, caps, and floors (e.g., a reporting entity writes an equity call option on stock that it already owns).

10. "Replication (Synthetic Asset) transaction" is a derivative transaction entered into in conjunction with other investments in order to reproduce the investment characteristics of otherwise permissible investments. A derivative transaction entered into by an insurer as a hedging or income generation transaction shall not be considered a replication (synthetic asset) transaction.

11. "Forecasted transaction" is a transaction that is expected to occur for which there is no firm commitment. Because no transaction or event has yet occurred and the transaction or event when it occurs will be at the prevailing market price, a forecasted transaction does not give an entity any present rights to future benefits or a present obligation for future sacrifices.

12. An "underlying" is a specified interest rate, security price, commodity price, foreign exchange rate, index of prices or rates, or other variable (including the occurrence or nonoccurrence of a specified event such as a scheduled payment under contract). An underlying may be a price or rate of an asset or liability but is not the asset or liability itself.

13. "Benchmark Interest Rate" is a widely recognized and quoted rate in an active financial market that is broadly indicative of the overall level of interest rates attributable to high-credit-quality obligors in that market. It is a rate that is widely used in a given financial market as an underlying basis for determining the interest rates of individual financial instruments and commonly referenced in interest-rate-related transactions. In theory, the benchmark interest rate should be a risk-free rate (that is, has no risk of default). In some markets, government borrowing rates may serve as a benchmark. In other markets, the benchmark interest rate may be an interbank offered rate. In the United States, the interest rates on direct Treasury obligations of the U.S. government, the London Interbank Offered Rate (LIBOR) swap rate, the Fed Funds Effective Rate Overnight Index Swap Rate, the Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Rate, and the Secured Overnight Financing Rate (SOFR) Overnight Index Swap Rate are considered to be benchmark interest rates.

14. "Weather derivatives" are defined as a forward-based or option-based contract for which settlement is based on a climatic or geological variable. One example of such a variable is the occurrence or nonoccurrence of a specified amount of snow at a specified location within a specified period of time. (See Exhibit C – Weather Derivative Illustration.)

15. "Notional amount" is defined[2] as the face value of a financial instrument in a derivatives transaction as of a reporting date which is used to calculate future payments in the reporting currency. Notional amount may also be referred to as notional value or notional principal amount. The notional amount reported should remain static over the life of a trade unless the instrument is partially unwound or has a contractually amortizing notional. The notional amount shall apply to derivative transactions as follows:

a. For derivative instruments other than futures contracts (e.g., options, swaps, forwards), the notional amount is either the amount to which interest rates are applied in order to calculate periodic payment obligations or the amount of the contract value used to

[2] The definition in paragraph 15 is intended to be a principle for determining notional for all derivative instruments. To the extent a derivative type is not explicitly addressed in paragraph 15.a. through paragraph 15.c., notional should be reported in a manner consistent with this principle.

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determine the cash obligations. Non-U.S. dollar contracts must be multiplied or divided by the appropriate inception foreign currency rate.

b. For futures contracts, with a U.S. dollar-denominated contract size (e.g., Treasury note and bond contracts, Eurodollar futures) or underlying, the notional amount is the number of contracts at the reporting date multiplied by the contract size (value of one point multiplied by par value).

c. For equity index and similar futures, the number of contracts at the reporting date is multiplied by the value of one point multiplied by the transaction price. Non-U.S. dollar contract prices must be multiplied or divided by the appropriate inception foreign currency rate.

16. "Variation Margin" reflects the daily change in market value of derivative contracts (e.g., daily gain/loss on a derivative contract due to market movements). Amounts received/paid to adjust variation margin on derivative contracts that are both cleared and settled on an exchange shall be recognized as an adjustment to the carrying value of the derivative contract (e.g., futures). Amounts received/paid to adjust variation margin on all other derivative contracts shall be recognized on the balance sheet as an asset or liability separate from the carrying value of the derivative instrument. This treatment shall occur under statutory accounting regardless if the counterparty/exchange considers amounts exchanged for variation margin to be legal settlement or collateral. Changes in variation margin shall not be treated as realized gains or adjustments to the basis of the hedged item until the derivative contract has been sold, matured or expired.

Embedded Derivative Instruments

17. Contracts that do not in their entirety meet the definition of a derivative instrument, such as bonds, insurance policies, and leases, may contain "embedded" derivative instruments—implicit or explicit terms that affect some or all of the cash flows or the value of other exchanges required by the contract in a manner similar to a derivative instrument. The effect of embedding a derivative instrument in another type of contract ("the host contract") is that some or all of the cash flows or other exchanges that otherwise would be required by the contract, whether unconditional or contingent upon the occurrence of a specified event, will be modified based on one or more underlyings. An embedded derivative instrument shall not be separated from the host contract and accounted for separately as a derivative instrument.

Impairment

18. This statement adopts the impairment guidelines established by *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* for the underlying financial assets or liabilities.

Derivative Premium

19. Derivative premium is the amount paid (acquired derivative) or received (written derivative) to enter into a derivative contract. At inception, the premium generally represents the fair value of the derivative. Derivative premium that is not paid or received at inception represents a liability or receivable for the reporting entity. Derivatives with premiums not remitted at acquisition are considered "financed derivatives." Financed derivatives shall be reported in accordance with the following provisions:

a. At acquisition and subsequently, the gross reported fair value of the derivative shall exclude the impact of financing premiums. Only market changes in the actual fair value of the derivative shall be reflected as unrealized gains or losses.

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b. At acquisition and subsequently, premiums payable (acquired derivative) and premiums receivable (written derivatives) shall be separately reported as "payable for securities" and "receivables for securities."

Recognition of Derivatives

20. Derivative instruments represent rights or obligations that meet the definitions of assets (*SSAP No. 4*—Assets *and Nonadmitted Assets*) or liabilities (SSAP No. 5R) and shall be reported in financial statements. In addition, derivative instruments also meet the definition of financial instruments as defined in *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures*. Should the cost basis of the derivative instrument be undefined (i.e., no premium is paid), the instrument shall be disclosed in accordance with paragraphs ~~44-48~~46-50 of *SSAP No. 100R—Fair Value*. Derivative instruments used in hedging, income generation or replication (synthetic asset) transactions shall be recognized and measured in accordance with the specific provisions within this statement and are admitted assets to the extent they conform to the requirements of this statement.

21. Derivative instruments that are not used in hedging, income generation or replication (synthetic asset) transactions shall be considered "Other" derivatives. These derivatives shall be accounted for at fair value and the changes in fair value shall be recorded as unrealized gains or losses. These derivatives do not qualify as admitted assets.

Derivatives Used in Hedging Transactions

22. Derivative instruments used in hedging transactions that meet the criteria of a highly effective hedge shall be considered an effective hedge and are permitted to be valued and reported in a manner that is consistent with the hedged asset or liability (referred to as hedge accounting). For instance, assume an entity has a financial instrument on which it is currently receiving income at a variable rate but wishes to receive income at a fixed rate and thus enters into a swap agreement to exchange the cash flows. If the transaction qualifies as an effective hedge and a financial instrument on a statutory basis is valued and reported at amortized cost, then the swap would also be valued and reported at amortized cost. Derivative instruments used in hedging transactions that do not meet or no longer meet the criteria of an effective hedge, or that meet the required criteria but the entity has chosen not to apply hedge accounting, shall be accounted for at fair value and the changes in the fair value shall be recorded as unrealized gains or unrealized losses (referred to as fair value accounting)[3].

23. Entities shall not bifurcate the effectiveness of derivatives. A derivative instrument is either classified as an effective hedge or an ineffective hedge. Entities must account for the derivative using fair value accounting if it is deemed to be ineffective or becomes ineffective. Derivative instruments classified as effective with excluded components in determining hedge effectiveness pursuant to Exhibit A, paragraph 8, shall account for the derivative and excluded components pursuant to the guidance in paragraph 40. Entities may redesignate a derivative in a hedging relationship even though the derivative was used in a previous hedging relationship that proved to be ineffective. A change in the counterparty to a derivative instrument that has been designated as the hedging instrument in an existing hedging relationship would not, in and of itself, be considered a termination of the derivative instrument. An entity shall prospectively discontinue hedge accounting for an existing hedge if any one of the following occurs:

a. Any criterion in paragraphs 26-38 is no longer met;

[3] Pursuant to paragraph 19, the gross reported value of a derivative and the determination of unrealized gains or losses shall exclude the impact of financing premiums. Premiums payable or receivable from the acquisition or writing of a derivative shall not be reflected in the gross reporting of derivatives or in determining the fair value change in a derivative.

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b. The derivative expires or is sold, terminated, or exercised (the effect is recorded as realized gains or losses or, for effective hedges of firm commitments or forecasted transactions, in a manner that is consistent with the hedged transaction – see paragraph 24);

c. The entity removes the designation of the hedge; or

d. The derivative is deemed to be impaired in accordance with paragraph 18. A permanent decline in a counterparty's credit quality/rating is one example of impairment required by paragraph 18, for derivatives used in hedging transactions.

24. For those derivatives which qualify for hedge accounting, the change in the carrying value or cash flow of the derivative shall be recorded consistently with how the changes in the carrying value or cash flow of the hedged asset, liability, firm commitment or forecasted transaction are recorded. Upon termination of a derivative that qualified for hedge accounting, the gain or loss shall adjust the basis of the hedged item and be recognized in income in a manner that is consistent with the hedged item (alternatively, if the item being hedged is subject to Interest Maintenance Reserve (IMR), the gain or loss on the hedging derivative may be realized and shall be subject to IMR upon termination.) Entities who choose the alternative method shall apply it consistently thereafter.

Hedge Designations

25. An entity may designate a derivative instrument as hedging the exposure to:

a. Changes in the fair value of an asset or a liability or an identified portion thereof that is attributable to a particular risk. This type of hedge can be utilized regardless of whether the hedged asset or liability is recorded in the financial statements at fair value;

b. Variability in expected future cash flows that are attributable to a particular risk. That exposure may be associated with an existing recognized asset or liability (such as all or certain future interest payments on variable-rate debt) or a forecasted transaction; or

c. Foreign currency exposure. Specific examples include a fair value or cash flow hedge of a foreign-currency-denominated firm commitment or financial instrument.

Fair Value Hedges

26. Fair value hedges qualify for hedge accounting if all of the following criteria are met:

a. At inception of the hedge, the formal documentation requirements of paragraph 42 are met;

b. Both at inception of the hedge and on an ongoing basis, the hedging relationship must be highly effective in achieving offsetting changes in fair value attributable to the hedged risk during the period that the hedge is designated. An assessment of effectiveness is required whenever financial statements or earnings are reported, and at least every three months. All assessments of effectiveness shall be consistent with the risk management strategy documented for that particular hedging relationship;

c. The term highly effective describes a cash flow hedging relationship where the change in fair value of the derivative hedging instrument is within 80% to 125% ~~percent~~ of the opposite change in the fair value of the hedged item attributable to the hedged risk. It shall also apply when an R-squared of .80 or higher is achieved when using a regression analysis technique. Further guidance on determining effectiveness can be found within Exhibit A;

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d. The hedged item is specifically identified as either all, a specific portion, or the partial term of a recognized asset, or all of a specific portion of a recognized liability or of an unrecognized firm commitment. The hedged item is a single asset or liability (or a specific portion or partial term thereof) or is a portfolio of similar assets or a portfolio of similar liabilities (or a specific portion thereof) or a closed portfolio of assets (pursuant to paragraph 26.f. and Exhibit A, paragraph 46) where assumed layer or layers is anticipated to be outstanding (or a specific portion thereof)[4]. For a partial term hedge of one or more consecutive selected contractual cash flows where the hedged item begins when the first hedge cash flow begins to accrue and ends at the end of the designation hedge period, the assumed maturity of the hedged item occurs at the end of the designated hedge period;

e. If similar assets or similar liabilities are aggregated and hedged as a portfolio, the individual assets or individual liabilities must share the risk exposure for which they are designated as being hedged. The change in fair value attributable to the hedged risk for each individual item in a hedged portfolio must be expected to respond in a generally proportionate manner to the overall change in fair value of the aggregate portfolio attributable to the hedged risk;

f. For a closed portfolio of financial assets or one or more beneficial interests secured by a portfolio of financial instruments, an entity may designate as the hedged item or items a hedged layer or layers (this designation is referred to throughout as the "portfolio layer method" detailed in Exhibit A); and

g. If the hedged item is a financial asset or liability, a recognized loan servicing right, or a nonfinancial firm commitment with financial components, the designated risk being hedged is:

   i. The risk of changes in the overall fair value of the entire hedged item;

   ii. The risk of changes in its fair value attributable to changes in benchmark interest rate;

   iii. The risk of changes in its fair value attributable to changes in the related foreign currency exchange rates; or

   iv. The risk of changes in its fair value attributable to both changes in the obligor's creditworthiness and changes in the spread over the benchmark interest rate with respect to the related financial asset's or liability's credit sector at inception of the hedge (referred to as credit risk).

   If the risk designated as being hedged is not the risk in paragraph 26.g.i., two or more of the other risks (benchmark interest rate risk, foreign currency exchange risk, and credit risk) may simultaneously be designated as being hedged.

   The benchmark interest rate being hedged in a hedge of interest rate risk must be specifically identified as part of the designation and documentation at the inception of the hedging relationship. In calculating the change in the hedged item's fair value attributable

[4] For clarity, partial-term hedges and portfolio hedges addressed in paragraph 26.f. are limited to the situations in which the hedged item(s) is a recognized asset or a closed portfolio of financial assets. These hedging accounting methods are not permitted to hedge liabilities.

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to changes in the benchmark interest rate, the estimated coupon cash flows used in calculating fair value shall be based on either the full contractual cash flows or the benchmark rate component of the contractual coupon cash flows of the hedged item determined at hedge inception. An entity may designate a fair value hedge of interest rate risk in which the hedged item is a prepayment instrument. The entity may consider only how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity (for example, an entity may consider only how change in the benchmark interest rate affect an obligor's decision to call a debt instrument when it has the right to do so). The entity need not consider other factors that would affect this decision (for example, credit risk) when assessing hedge effectiveness. An entity may not simply designate prepayment risk as the risk being hedged for a financial asset. However, it can designate the option component of a prepayable instrument as the hedged item in a fair value hedge of the entity's exposure to changes in the fair value of that "prepayment" option, perhaps thereby achieving the objective of its desire to hedge prepayment risk. The effect of an embedded derivative of the same risk class must be considered in designating a hedge of an individual risk. For example, the effect of an embedded prepayment option must be considered in designating a hedge of benchmark interest rate risk.

Cash Flow Hedges

27. Cash flow hedges qualify for hedge accounting if all of the following criteria are met:

a. At inception of the hedge, the formal documentation requirements of paragraph 42 are met;

b. Both at inception of the hedge and on an ongoing basis, the hedging relationship shall be highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the hedge. An assessment of effectiveness is required whenever financial statements or earnings are reported, and at least every three months. All assessments of effectiveness shall be consistent with the originally documented risk management strategy for that particular hedging relationship; and

c. The term highly effective describes a cash flow hedging relationship where the change in cash flows or present value of cash flows of the derivative hedging instrument is within 80% to 125% ~~percent~~ of the opposite change in the cash flows or present value of the cash flows of the hedged item attributable to the hedged risk. It shall also apply when an R-squared of .80 or higher is achieved when using a regression analysis technique. Further guidance on determining effectiveness can be found within Exhibit A.

Hedging Forecasted Transactions

28. A forecasted transaction is eligible for designation as a hedged transaction in a cash flow hedge if all of the following additional criteria are met:

a. The forecasted transaction is specifically identified as a single transaction or a group of individual transactions. If the hedged transaction is a group of individual transactions, those individual transactions must share the same risk exposure for which they are designated as being hedged. Thus, a forecasted purchase and a forecasted sale cannot both be included in the same group of individual transactions that constitute the hedged transaction.

b. The occurrence of the forecasted transaction is probable. An assessment of the likelihood that a forecasted transaction will take place should not be based solely on management's

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intent because intent is not verifiable. The transaction's probability should be supported by observable facts and the attendant circumstances. Consideration should be given to the following circumstances in assessing the likelihood that a transaction will occur:

i. The frequency of similar past transactions;

ii. The financial and operational ability of the entity to carry out the transaction;

iii. Substantial commitments of resources to a particular activity (for example, a manufacturing facility that can be used in the short run only to process a particular type of commodity);

iv. The extent of loss or disruption of operations that could result if the transaction does not occur; and

v. The likelihood that transactions with substantially different characteristics might be used to achieve the same business purpose (for example, an entity that intends to raise cash may have several ways of doing so, ranging from a short-term bank loan to a common stock offering).

The term probable requires a significantly greater likelihood of occurrence than the phrase more likely than not. In addition, both the length of time until a forecasted transaction is projected to occur and the quantity of the forecasted transaction are considerations in determining probability. Other factors being equal, the more distant a forecasted transaction is, the less likely it is that the transaction would be considered probable and the stronger the evidence that would be needed to support an assertion that it is probable. For example, a transaction forecasted to occur in five years may be less likely than a transaction forecasted to occur in one year. However, forecasted interest payments for the next 20 years on variable-rate debt typically would be probable if supported by an existing contract. Additionally, other factors being equal, the greater the physical quantity or future value of a forecasted transaction, the less likely it is that the transaction would be considered probable and the stronger the evidence that would be required to support an assertion that it is probable. For example, less evidence generally would be needed to support forecasted investments of $100,000 in a particular month than would be needed to support forecasted investments of $950,000 in that month by an entity, even if its investments have averaged $950,000 per month for the past 3 months.

A forecasted transaction that is expected to occur within 2 months of the original forecasted date (or time frame) may still be considered probable. If the transaction will not occur until greater than 2 months after the original forecasted date, it is no longer probable.

If a forecasted transaction is determined to no longer be probable, hedge accounting shall cease immediately and any deferred gains or losses on the derivative must be recognized in unrealized gains or losses. If an entity demonstrates a pattern of determining that hedged forecasted transactions probably will not occur, such action would call into question both the entity's ability to accurately predict forecasted transactions and the propriety of using hedge accounting in the future for similar forecasted transactions. Accordingly, hedge accounting for transactions forecasted by that entity will no longer be permitted.

c. If the hedged transaction is the forecasted purchase or sale of a nonfinancial asset, the designated risk being hedged is (1) the risk of changes in the functional-currency-equivalent cash flows attributable to changes in the related foreign currency exchange

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rates or (2) the risk of changes in the cash flows relating to all changes in the purchase price or sales price of the asset (reflecting its actual location if a physical asset), not the risk of changes in the cash flows relating to the purchase or sale of a similar asset in a different location or of a major ingredient.

d. If the hedged transaction is the forecasted purchase or sale of a financial asset or liability or the variable cash inflow or outflow of an existing financial asset or liability, the designated risk being hedged is (1) the risk of changes in the cash flows of the entire asset or liability, such as those relating to all changes in the purchase price or sales price (regardless of whether that price and the related cash flows are stated in the entity's functional currency or a foreign currency), (2) the risk of changes in its cash flows attributable to changes in the designated benchmark interest rate, (3) the risk of changes in the functional-currency-equivalent cash flows attributable to changes in the related foreign currency exchange rates, or (4) the risk of changes in its cash flows attributable to default or changes in the obligor's creditworthiness, and changes in the spread over the benchmark interest rate with respect to the hedged item's credit sector at inception of the hedge. Two or more of the above risks may be designated simultaneously as being hedged. The benchmark interest rate being hedged in a hedge of interest rate risk must specifically be identified as part of the designation and documentation at the inception of the hedging relationship. An entity may not designate prepayment risk as the risk being hedged.

Foreign Currency Hedges

29. If the hedged item is denominated in a foreign currency, an entity may designate the following types of hedges of foreign currency exposure, as specified in paragraphs 26-28:

a. A fair value hedge of an unrecognized firm commitment or a recognized asset or liability;

b. A cash flow hedge of a forecasted transaction, an unrecognized firm commitment, the forecasted functional-currency-equivalent cash flows associated with a recognized asset or liability, or a forecasted intercompany transaction; or

c. A hedge of a net investment in a foreign operation.

30. The recognition in earnings of the foreign currency transaction gain or loss on a foreign-currency-denominated asset or liability based on changes in the foreign currency spot rate is not considered to be the remeasurement of that asset or liability with changes in fair value attributable to foreign exchange risk recognized in earnings. Thus, those criteria are not impediments to either a foreign currency fair value or cash flow hedge of such a foreign-currency-denominated asset or liability or a foreign currency cash flow hedge of the forecasted acquisition or incurrence of a foreign-currency-denominated asset or liability whose carrying amount will be remeasured at spot exchange rates. A foreign currency derivative instrument that has been entered into with another member of a holding company can be a hedging instrument in a fair value hedge or in a cash flow hedge of a recognized foreign-currency-denominated asset or liability or in a net investment hedge only if that other member has entered into an offsetting contract with an unrelated third party to hedge the exposure it acquired from issuing the derivative instrument to the affiliate that initiated the hedge.

31. The provisions in paragraph 30 that permit a recognized foreign-currency-denominated asset or liability to be the hedged item in a fair value or cash flow hedge of foreign currency exposure also pertain to a recognized foreign-currency-denominated receivable or payable that results from a hedged forecasted foreign-currency-denominated sale or purchase on credit. An entity may choose to designate a single cash flow hedge that encompasses the variability of functional currency cash flows attributable to foreign exchange risk related to the settlement of a foreign-currency-denominated receivable or payable resulting

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from a forecasted sale or purchase on credit. Alternatively, an entity may choose to designate a cash flow hedge of the variability of functional currency cash flows attributable to foreign exchange risk related to a forecasted foreign-currency-denominated sale or purchase on credit and then separately designate a foreign currency fair value hedge of the resulting recognized foreign-currency-denominated receivable or payable. In that case, the cash flow hedge would terminate (be dedesignated) when the hedged sale or purchase occurs and the foreign-currency-denominated receivable or payable is recognized. Although the use of the same foreign currency derivative instrument for both the cash flow hedge and the fair value hedge is not prohibited, some ineffectiveness may result.

Foreign Currency Fair Value Hedges

32. *Unrecognized firm commitment*. A derivative instrument or a nonderivative financial instrument that may give rise to a foreign currency transaction gain or loss can be designated as hedging changes in the fair value of an unrecognized firm commitment, or a specific portion thereof, attributable to foreign currency exchange rates. The designated hedging relationship qualifies for hedge accounting if all the fair value hedge criteria in paragraph 26 are met.

33. *Recognized asset or liability*. A nonderivative financial instrument shall not be designated as the hedging instrument in a fair value hedge of the foreign currency exposure of a recognized asset or liability. A derivative instrument can be designated as hedging the changes in the fair value of a recognized foreign-currency-denominated asset or liability (or a specific portion thereof) for which a foreign currency transaction gain or loss is recognized in earnings. All recognized foreign-currency-denominated assets or liabilities for which a foreign currency transaction gain or loss is recorded in earnings may qualify for hedge accounting if all the fair value hedge criteria in paragraph 26 are met.

34. *Securities carried at fair value*. A nonderivative financial instrument shall not be designated as the hedging instrument in a fair value hedge of the foreign currency exposure of security carried at fair value. A derivative instrument can be designated as hedging the changes in the fair values of an debt security carried at fair value (or a specific portion thereof) attributable to changes in foreign currency exchange rates. The designated hedging relationship qualifies for hedge accounting if all the fair value hedge criteria in paragraph 26 are met. An equity security carried at fair value can be hedged for changes in the fair value attributable to changes in foreign currency exchange rates and qualify for hedge accounting if all the fair value hedge criteria in paragraph 26 are met and the following two conditions are satisfied.

a. The security is not traded on an exchange (or other established marketplace) on which trades are denominated in the investor's functional currency; and

b. Dividends or other cash flows to holders of the security are all denominated in the same foreign currency as the currency expected to be received upon sale of the security.

35. Gain and losses on a qualifying foreign currency fair value hedge shall be accounted for as specified in paragraphs 22-24 and Exhibit B. The gain or loss on a nonderivative hedging instrument attributable to foreign currency risk is the foreign currency transaction gain or loss as determined under *SSAP No. 23—Foreign Currency Transactions and Translations*.

Foreign Currency Cash Flow Hedges

36. A nonderivative financial instrument shall not be designated as a hedging instrument in a foreign currency cash flow hedge. A derivative instrument designated as hedging the foreign currency exposure to variability in the functional-currency-equivalent cash flows associated with a forecasted transaction (for example, a forecasted sale to an unaffiliated entity with the price to be denominated in a foreign currency), a recognized asset or liability, an unrecognized firm commitment, or a forecasted intercompany

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transaction (for example, a forecasted sale to a foreign subsidiary or a forecasted royalty from a foreign subsidiary) qualifies for hedge accounting if all the following criteria are met:

a. The hedged transaction is denominated in a currency other than the hedging unit's functional currency.

b. All of the criteria in paragraph 27 are met.

c. If the hedged transaction is a group of individual forecasted foreign-currency-denominated transactions, a forecasted inflow of a foreign currency and a forecasted outflow of the foreign currency cannot both be included in the same group.

d. If the hedged item is a recognized foreign-currency-denominated asset or liability, all the variability in the hedged item's functional-currency-equivalent cash flows must be eliminated by the effect of the hedge. (For example, with a variable-rate foreign-currency-denominated asset or liability a cash flow hedge cannot be used to hedge changes in exchange rates alone because the derivative would not eliminate all the variability in the functional currency cash flows.)

e. If the hedged transaction is the forecasted purchase or sale of a financial asset or liability or the interest payments on that financial asset or liability or the variable cash inflow or outflow of an existing financial asset or liability, the designated risk being hedged is (1) the risk of overall change in the hedged cash flows related to the asset or liability, such as those relating to all changes in the purchase price or sales price (regardless of whether that price and the related cash flows are stated in the entity's functional currency or a foreign currency), (2) the risk of changes in its cash flows attributable to changes in the designated benchmark interest rate (referred to as interest rate risk), (3) the risk of changes in the functional-currency-equivalent cash flows attributable to changes in the related foreign currency exchange rates, or (4) the risk of changes in its cash flows attributable to default, changes in the obligor's creditworthiness, and changes in the spread over the benchmark interest rate with respect to the hedged item's credit sector at inception of the hedge (referred to as credit risk). Two or more of the above risks may be designated simultaneously as being hedged. An entity may not designate prepayment risk as the risk being hedged.

The benchmark interest rate being hedged in a hedge of interest rate risk must be specifically identified as part of the designation and documentation at the inception of the hedging relationship. In a cash flow hedge of a variable-rate financial asset or liability, either existing or forecasted, the designated risk being hedged cannot be the risk of changes in its cash flows attributable to changes in the specifically identified benchmark interest rate if the cash flows of the hedged transaction are explicitly based on a different index, for example, based on a specific bank's prime rate, which cannot qualify as the benchmark rate. However, the risk designated as being hedged could potentially be the risk of overall changes in the hedged cash flows related to the asset or liability, provided that the other criteria for a cash flow hedge have been met.

37. A qualifying foreign currency cash flow hedge shall be accounted for in accordance with paragraphs 22-24 and Exhibit B.

Hedges of the Foreign Currency Exposure of a Net Investment in a Foreign Operation

38. A derivative instrument or a nonderivative financial instrument that may give rise to a foreign currency transaction gain or loss under SSAP No. 23 can be designated as hedging the foreign currency exposure of a net investment in a foreign operation. The gain or loss on a hedging derivative instrument

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(or the foreign currency transaction gain or loss on the nonderivative instrument) that is designated as, and is effective as, an economic hedge of the net investment in a foreign operation shall be reported in the same manner as a translation adjustment to the extent it is effective as a hedge. The hedged net investment shall be accounted for consistent with SSAP No. 23; the provisions of this statement for recognizing the gain or loss on assets designated as being hedged in a fair value hedge do not apply to the hedge of a net investment in a foreign operation.

Hedge Effectiveness

39. The measurement of hedge effectiveness for a particular hedging relationship shall be consistent with the entity's risk management strategy and the method of assessing hedge effectiveness that was documented at the inception of the hedging relationship, as discussed in paragraph 42.

40. The gain or loss on a derivative designated as a hedge and assessed to be effective is reported consistently with the hedged item. (Therefore, if the hedged item is reported at amortized cost, and the hedging instrument is consistent with that measurement method, fluctuations in fair value would not be recognized as unrealized gains or losses for either the hedging item nor hedging instrument.) If an entity's defined risk management strategy for a particular hedging relationship excludes a specific component of the gain or loss, or related cash flows, on the hedging derivative from the assessment of hedge effectiveness (as discussed in Exhibit A, paragraph 8), specific accounting treatment shall be followed for the excluded component:

a. If the excluded component pertains to the difference between a foreign currency spot price and the forward or future price (e.g., a forward spot rate), then this premium/discount shall be amortized into income over the life of the contract or hedged program. (This guidance addresses the excluded component in Exhibit A, paragraph 8.d.)

b. If the excluded component pertains to a foreign currency swap cross-currency basis spread, the impact of fair value changes shall be reflected as a component of the foreign currency swap's periodic interest accrual. (This guidance addresses the excluded component in Exhibit A, paragraph 8.e.)

c. For all other excluded components, the excluded component shall be measured and reported at fair value, with changes in fair value recognized as unrealized gains or losses. (This guidance shall be applied to excluded components detailed in Exhibit A, paragraphs 8.a. through 8.c.)

41. Hedging instruments with excluded components shall be identified in the financial statement investment schedule (Schedule DB) and shall be disclosed pursuant to paragraph 43.g.

Documentation Guidance

42. At inception of the hedge, documentation must include:

a. A formal documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge, including identification of the hedging instrument, the hedged item, the nature of the risk being hedged, and how the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or variability in cash flows attributable to the hedged risk will be assessed, including whether an entity will perform subsequent effectiveness assessments on a qualitative basis (per paragraph 46) and how it intends to carry out that qualitative assessment. There must be a reasonable basis for how the entity plans to assess the hedging instrument's effectiveness;

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b. An entity's defined risk management strategy for a particular hedging relationship may exclude certain components of a specific hedging derivative's change in fair value, such as time value, from the assessment of hedge effectiveness, as discussed in paragraph 40 and Exhibit A;

c. Signature of approval, for each instrument, by person(s) authorized, either by the entity's board of directors or a committee authorized by the board, to approve such transactions; and

d. A description of the reporting entity's methodology used to verify that opening transactions do not exceed limitations promulgated by the state of domicile.

43. At inception, if an entity is required to perform an initial prospective assessment of hedge effectiveness on a quantitative basis (using information applicable as of the date of hedge inception[5]), the assessment is considered to be performed concurrently at hedge inception if it is completed by the earliest of the following:

a. The first quarterly hedge effectiveness assessment date;

b. The date that financial statements that include the hedged transaction are available to be issued;

c. The date that the hedging instrument and hedged item no longer qualify for hedge accounting;

d. The date of expiration, sale, termination or exercise of the hedging instrument;

e. The date of redesignation of the hedging relationship; or

f. For a cash flow hedge of a forecasted transaction, the date that the forecasted transaction occurs.

g. For hedging instruments with excluded components for determining hedge effectiveness:

i. In the investment schedule, identify hedging instruments with excluded components and report the current fair value of the excluded component, the fair value of the excluded component that is reflected in the reported BACV for the hedging instrument (this item would not be applicable for foreign-currency forwards and currency swaps where the forward points or cross-currency basis, respectively, are the excluded component), and the change in fair value reported as an unrealized gain/loss.

ii. In the notes to the financial statements, provide information on the aggregate excluded components by category: Time Value, ~~Intrinsic~~Volatility Value, Forward Points, and Cross Currency Basis Spread. The aggregate amounts reported should include the following (as applicable): current fair value, recognized unrealized gain/loss, the fair value reflected in BACV, and for the

[5] Entities are required to perform an initial prospective assessment unless qualifying for an exception in accordance with ASU 2017-12, paragraph 815-20-25-3.

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excluded forward points (e.g., forward spot rates), the aggregate amount owed at maturity, along with current year and remaining amortization.

44. For all derivatives terminated, expired, or exercised during the year:

a. Signature of approval, for each instrument, by person(s) authorized, either by the entity's board of directors or a committee authorized by the board, to approve such transactions;

b. A description, for each instrument, of the nature of the transaction, including:

i. The date of the transaction;

ii. A complete and accurate description of the specific derivative, including description of the underlying securities, currencies, rates, indices, commodities, derivatives, or other financial market instruments;

iii. Number of contracts or notional amount;

iv. Date of maturity, expiry or settlement;

v. Strike price, rate or index (termination price for futures contracts);

vi. Counterparty, or exchange on which the transaction was traded; and

vii. Consideration paid or received, if any, on termination.

c. Description of the reporting entity's methodology to verify that derivatives were effective hedges; and

d. Identification of any derivatives that ceased to be effective as hedges.

45. For derivatives open at quarter-end:

a. A description of the methodology used to verify the continued effectiveness of hedges, and whether the entity is using qualitative assessments pursuant to paragraph 46[6];

b. An identification of any derivatives that have ceased to be effective as hedges;

c. A description of the reporting entity's methodology to determine fair values of derivatives;

d. Copy of Master Agreements, if any, where indicated on Schedule DB Part D.

46. An entity may subsequently qualitatively assess hedge effectiveness, on a hedge-by-hedge basis, if both the conditions in paragraphs 46.a. and 46.b. were initially met. When an entity performs subsequent qualitative assessments of hedge effectiveness, it shall verify and document whenever financial statements or earnings are reported and at least every three months that the facts and circumstances related to the hedging relationship have not changed such that it can assert qualitatively

[6] For purposes of this requirement, this statement adopts the guidance for effectiveness assessment after initial designation reflected in ASU 2017-12, including the concepts and restrictions for use of the short-cut method and the critical terms match method.

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that the hedging relationship was and continues to be highly effective. An entity may perform a quantitative assessment in any reporting period to validate whether qualitative assessments remain appropriate. When facts and circumstances change such that an entity no longer can assert qualitatively that the hedging relationship continues to be highly effective, then the entity shall begin performing quantitative assessments.

a. An entity performs an initial quantitative test of hedge effectiveness on a prospective basis (that is, it is not assuming that the hedging relationship is perfectly effective at hedge inception) and the results of that quantitative test demonstrate highly effective offset.

b. At hedge inception, an entity can reasonably support an expectation of high effectiveness on a qualitative basis in subsequent periods.

Derivatives Used in Income Generation Transactions

General

47. Income generation transactions are defined as derivatives written or sold to generate additional income or return to the reporting entity. They include covered options, caps, and floors (e.g., a reporting entity writes an equity call option on stock that it already owns).

48. Because these transactions require writing derivatives, they expose the reporting entity to potential future liabilities for which the reporting entity receives a premium up front. Because of this risk, dollar limitations and additional constraints are imposed requiring that the transactions be "covered" (i.e., offsetting assets can be used to fulfill potential obligations). To this extent, the combination of the derivative and the covering asset works like a reverse hedge where an asset owned by the reporting entity in essence hedges the derivative risk.

49. As with derivatives in general, these instruments include a wide variety of terms regarding maturities, range of exercise periods and prices, counterparties, underlying instruments, etc.

50. The principal features of income generation transactions are:

a. Premium received is initially recorded as a deferred liability.

b. The accounting of the covering asset or underlying interest controls the accounting of the derivative. The covering asset/underlying interest is accounted at either fair value (e.g., common stocks) or (amortized) cost (e.g., bonds).

c. The gain/loss on termination of the derivative is a capital item. For life insurance companies, it shall be subject to IMR treatment if interest rate related.

d. For options that are exercised, the remaining premium shall adjust the proceeds (cost) associated with the exercise resulting in no explicit gain or loss reported for the derivative itself.

Written Fixed Income Covered Call Options

51. The principal features of written fixed income covered call options are:

a. The general approach is to value at cost (i.e., consideration received) without amortization over the life of the contract if the original duration is less than one year, otherwise carry at amortized cost.

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b. An alternative to the general approach combines the accounting of the written option with the covering asset and then uses standard accounting for callable bonds (yield to worst amortization) on the adjusted asset. This method prevents the possibility of future loss recognition upon exercise while at the same time providing recognition of the income feature of the option over time. This approach would appear most relevant for longer-lived covered European call options, which are in substance like callable bonds.

c. For life insurance companies, the gain or loss flows through the IMR if the covering asset or underlying interest is subject to the IMR using callable bond rules to determine the remaining life.

d. Reporting entities are responsible for timely recognition of any probable losses that may occur as a result of the strategy. If the exercise price is below the covering asset's book value, the asset shall be evaluated for write down or disclosure treatment in accordance with SSAP No. 5R. All relevant factors such as whether the option is currently exercisable, the fair value of the bond relative to its exercise price, to what extent the statement value of the option premium offsets any loss on the asset, or how any IMR transaction on exercise would affect unassigned funds (surplus) and income shall be considered.

52. Written fixed income covered call options shall be accounted for as follows:

STATUS OF OPTION	COVERING ASSET VALUED AT AMORTIZED COST	COVERING ASSET VALUED AT FAIR VALUE
Open	Record premium as deferred liability. Carry at amortized value. (Alternatively carry at consideration received if original duration is less than 1 year to maturity.) Alternatively, attach premium to covering asset and amortize (under yield to worse scenario) using standard callable bond accounting.	Record premium as deferred liability. Changes in fair value recorded as unrealized adjustments to unassigned funds (surplus) – gain/loss.
Closed – Expired	Premium received recognized as realized capital gain. Gain from expiration to flow through IMR, if applicable. (1)	Premium received recognized as realized capital gain.
Closed – Exercised	Adjust disposition proceeds. (Include in capital gain/loss of disposed asset.) Gain or loss from disposition to flow through IMR, if applicable. (1)	Adjust disposition proceeds. (Include in capital gain/loss of disposed asset.)

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STATUS OF OPTION	COVERING ASSET VALUED AT AMORTIZED COST	COVERING ASSET VALUED AT FAIR VALUE
Closed – Terminated	Recognize net amount as realized capital gain/loss. Gain or loss from disposition to flow through IMR, if applicable. (1)	Recognize net amount as realized capital gain/loss.

NOTE (1) If premium is attached to covering asset, the accounting treatment for the covering asset applies.

Written Covered Put Options

53. The principal features of written covered put options are:

a. The accounting for the underlying interest instead of the covering asset governs the accounting of the written put while it is open. For example, if a reporting entity wrote a put requiring it to purchase a certain common stock (underlying interest) at a specific price, the reporting entity might cover that option by holding cash or cash equivalents (covering asset). The accounting for the common stock would govern the accounting of the option in this case.

b. As with covered call writing for life insurance companies, gain/loss on termination may be subject to IMR over the remaining life of the underlying interest.

c. As with covered call writing, entities writing put options for income generation purposes are responsible for timely recognition of any probable losses that may occur as a result of the strategy.

54. Written covered put options shall be accounted for as follows:

STATUS OF OPTION	UNDERLYING INTEREST VALUED AT AMORTIZED COST	UNDERLYING INTEREST VALUED AT FAIR VALUE
Open	Record premium as deferred liability. Carry at amortized value. (Alternatively carry at consideration received if original duration is less than 1 year to maturity.)	Record premium as deferred liability. Changes in fair value recorded as unrealized adjustments to unassigned funds (surplus) – gain/loss.
Closed – Expired	Premium received recognized as realized capital gain. Gain from expiration to flow through IMR, if applicable.	Premium received recognized as realized capital gain.
Closed – Exercised	Adjust acquisition cost by premium received.	Adjust acquisition cost by premium received.

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STATUS OF OPTION	UNDERLYING INTEREST VALUED AT AMORTIZED COST	UNDERLYING INTEREST VALUED AT FAIR VALUE
Closed – Terminated	Recognize net amount as realized capital gain/loss. Gain or loss from disposition to flow through IMR, if applicable.	Recognize net amount as realized capital gain/loss.

Written Fixed Income Caps and Floors

55. The principal features of written fixed income caps and floors are:

a. The value of the premium received shall be amortized into income over the life of the contract. For caps and floors, where the entity is selling off possible excess interest/income, the value of the covering asset is not relevant.

b. Gain/loss may be subject to IMR. The expected maturity would be the derivative contract's maturity.

56. Written fixed income caps and floors shall be accounted for as follows:

STATUS OF OPTION	COVERING ASSET VALUED AT AMORTIZED COST	COVERING ASSET VALUED AT FAIR VALUE
Open	Record premium as deferred liability. Carry at amortized value. (Alternatively carry at consideration received if original duration is less than 1 year to maturity.) Amortize over life of contract to produce constant yield. Record any interest expense as "Other Investment Income" – negative value.	Record premium as deferred liability. Changes in fair value recorded as unrealized adjustments to unassigned funds (surplus) – gain/loss.
Closed – Matured	Would usually mature at zero amortized value. Any remaining unamortized value recognized as ordinary income through a final amortization adjustment.	Premium received recognized as realized capital gain.
Closed – Exercised	Not applicable.	Not applicable.
Closed – Terminated	Recognize net amount as realized capital gain/loss. Gain/loss on termination to flow through IMR, if applicable.	Recognize net amount as realized capital gain/loss.

Derivatives Used in Replication (Synthetic Asset) Transactions

57. Replication (Synthetic Asset) transaction means a derivative transaction entered into in conjunction with other investments in order to reproduce the investment characteristics of otherwise

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permissible investments. A derivative transaction entered into by an insurer as a hedging or income generation transaction shall not be considered a replication (synthetic asset) transaction.

58. Any premium paid or received shall be carried as an asset or liability on the balance sheet (Derivative line on the Assets (or) Liabilities pages). Premiums paid or received on the replication (synthetic asset) derivative should be amortized into investment income or expense until the exercise, termination or maturity date of the derivative.

59. If the replication (synthetic asset) transaction would be carried at amortized cost and the cash instrument used is carried at amortized cost, then the derivative used should be carried at amortized cost. The derivative may be valued at fair value when both the replication (synthetic asset) and the cash instrument are valued at amortized cost. This is consistent with the alternative valuation methods available for hedges. If the replication (synthetic asset) transaction would be carried at fair value and/or the cash instrument used is carried at fair value, then the derivative used should be carried at fair value.

	(a)	(b)	(c)	(d)
	If the Replication (Synthetic Asset) is Valued at:	And Cash Instrument(s) Used is (are) Valued at:	The Derivative is Valued at:	Alternative Derivative Value Basis:
1.	Amortized Cost	Amortized Cost	Amortized Cost	Fair value
2.	Fair value	Fair value	Fair value	N/A
3.	Amortized Cost	Fair value	Fair value	N/A
4.	Fair value	Amortized Cost	Fair value	N/A

60. In the case of No. 3 in the chart above, the fair values for the cash instrument and derivative, when added together, shall not exceed the replication (synthetic asset) statement value. If this does occur, the excess shall reduce the fair value of the derivative and shall be recorded as an unrealized gain separate from the Asset Valuation Reserve (AVR).

61. If the replication (synthetic asset) transaction involves the exchange of interest related cash flows (default free assets), then the cash flows should be accrued as investment income. If the replication (synthetic asset) transaction involves the exchange of total return or change in index cash flows, then the cash flows should be segregated between interest income and fair value (equity) changes. The interest income portion should be accrued as investment income.

62. If the derivative is carried at fair value, the periodic change in the fair value should be recorded as an unrealized gain or loss adjustment to surplus until the transaction is terminated. If the replication (synthetic asset) transaction involves the exchange of total return or change in index cash flows, then the cash flows should be segregated between interest income and fair value (equity) changes. The fair value (equity) change should be recognized as a deferred asset/liability until the termination of the contract. Gains or losses on the derivative at termination or sale should be recognized as realized.

Disclosure Requirements

63. Reporting entities shall disclose the following for all derivative contracts used:

a. General disclosures:

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i. A description of the reporting entity's objectives for using derivatives, i.e., hedging, income generation or replication;

ii. A description of the context needed to understand those objectives and its strategies for achieving those objectives;

iii. The description for hedging objectives shall identify the category, e.g., fair value hedges, cash flow hedges, or foreign currency hedges, and for all objectives, the type of instrument(s) used;

iv. A description of the accounting policies for derivatives including the policies for recognizing (or reasons for not recognizing) and measuring the derivatives used, and when recognized, where those instruments and related gains and losses are reported;

v. Identification of whether the reporting entity has derivative contracts with financing premiums. (For purposes of this term, this includes scenarios in which the premium cost is paid at the end of the derivative contract or throughout the derivative contract.);

vi. The net gain or loss recognized in unrealized gains or losses during the reporting period representing the component of the derivative instruments' gain or loss, if any, excluded from the assessment of hedge effectiveness; and

vii. The net gain or loss recognized in unrealized gains or losses during the reporting period resulting from derivatives that no longer qualify for hedge accounting. For portfolio layer method hedges, disclose circumstances that led to the breach.

b. Disclosures by type of instrument outstanding, e.g., call options, floors, etc.:

i. Notional or contract amounts;

ii. Carrying and fair values; and

iii. A discussion of the market risk, credit risk, and cash requirements of the derivatives.

c. For derivatives held for other-than-hedging purposes in addition to paragraphs 63.a. and 63.b.:

i. Average fair value of the derivatives during the reporting period together with the related end-of-period fair value distinguishing between assets and liabilities; and

ii. Net gains or losses detailed by class, business activity or other category that is consistent with the management of those activities and where the net gains or losses are reported.

d. The financial statements shall disclose details of covered items and/or written transactions to allow evaluation of cash flow implications for all written covered options used for income generation.

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e. A seller[7] of credit derivatives[8] shall disclose information[9] about its credit derivatives and hybrid instruments[10] that have embedded credit derivatives to enable users of financial statements to assess their potential effect on its financial position, income and cash flows. The seller of a credit derivative shall disclose the following information for each credit derivative, or each group of credit derivatives, even if the likelihood of the seller's having to make any payments under the credit derivative is remote. With respect to hybrid instruments that have embedded credit derivatives, the seller of the embedded credit derivative shall disclose the required information for the entire hybrid instrument, not just the embedded credit derivative.

i. The nature of the credit derivative, including the approximate term of the credit derivative, the reason(s) for entering into the credit derivative, the events or circumstances that would require the seller to perform under the credit derivative, and the current status (that is, as of the date of the statement of financial position) of the payment/performance risk of the credit derivative. For example, the current status of the payment/performance risk of a credit derivative could be based on either recently issued external credit ratings or current internal groupings used by the seller to manage its risk. An entity that uses internal groupings shall disclose how those groupings are determined and used for managing risk.

ii. The maximum potential amount of future payments (undiscounted) the seller could be required to make under the credit derivative. That maximum potential amount of future payments shall not be reduced by the effect of any amounts that may possibly be recovered under recourse or collateralization provisions in the credit derivative (which are addressed under paragraph 63.e.iv.). If the terms of the credit derivative provide for no limitation to the maximum potential future payments under the contract, that fact shall be disclosed. If the seller is unable to develop an estimate of the maximum potential amount of future payments under the credit derivative, the seller shall disclose the reasons why it cannot estimate the maximum potential amount.

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[7] The term "seller" refers to the party that assumes credit risk, which could be a guarantor in a guarantee-type contract, and any party that provides the credit protection in an option-type contract, a credit default swap, or any other credit derivative contract. A seller is also sometimes referred to as a writer of the contract.

[8] A credit derivative instrument is (1) in which one or more of its underlyings are related to the credit risk of a specified entity (or a group of entities) or an index based on the credit risk of a group of entities and (2) that exposes the seller to potential loss from credit-risk-related events specified in the contract. Examples of credit derivatives within the scope of this paragraph include, but are not limited to, credit default swaps, credit spread options, and credit index products. This also includes a hybrid instrument that has an embedded credit derivative (e.g., a credit-linked note). The disclosures required by this paragraph do not apply to an embedded derivative feature related to the transfer of credit risk that is only in the form of subordination of one financial instrument to another.

[9] One way to present the information for groups of similar credit derivatives would be first to segregate the disclosures by major types of contracts (single-name credit default swaps, traded indexes, other portfolio products and swaptions) and then, for each major type, provide additional subgroups for major types of referenced/underlying asset classes (e.g., corporate debt, sovereign debt, and structured finance).

[10] A hybrid instrument is considered a contract that includes the host contract and an embedded derivative. Unlike FAS 133, statutory accounting guidance in *SSAP No. 86—Accounting for Derivative Instruments and Hedging Activities* does not permit embedded derivatives to be separated from the host contract and accounted for separately as a derivative instrument. As noted in paragraph 63.e., the seller of the hybrid instrument shall disclose the required information for the entire hybrid instrument, not just the embedded credit derivative.

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iii. The fair value of the credit derivative as of the date of the statement of financial position.

iv. The nature of (1) any recourse provisions that would enable the seller to recover from third parties any of the amounts paid under the credit derivative and (2) any assets held either as collateral or by third parties that, upon the occurrence of any specified triggering event or condition under the credit derivative, the seller can obtain and liquidate to recover all or a portion of the amounts paid under the credit derivative. The seller shall indicate, if estimable, the approximate extent to which the proceeds from liquidation of those assets would be expected to cover the maximum potential amount of future payments under the credit derivative. In its estimate of potential recoveries, the seller of credit protection shall consider the effect of any purchased credit protection with identical underlying(s).

f. A holder of a financial instrument with an embedded credit derivative[11] that exposes the holder to the possibility (however remote) of being required to make future payments (not merely receive reduced cash inflows) because the possibility of those future payments is not caused by subordination (such as the subordination of one beneficial interest to another tranche of a securitization, thereby redistributing credit risk) shall provide the following disclosures for the entire hybrid instrument, not just the embedded credit derivative:

i. The nature of the embedded credit derivative, including the approximate term of the embedded credit derivative, the events or circumstances that would require the holder to perform under the embedded credit derivative, and the current status (that is, as of the date of the statement of financial position) of the payment/performance risk of the embedded credit derivative.

ii. The maximum potential amount of future payments (undiscounted) the holder could be required to make under the embedded credit derivative. That maximum potential amount of future payments shall not be reduced by the effect of any amounts that may possibly be recovered under recourse or collateralization provisions in the embedded credit derivative (which are addressed under paragraph 63.f.iv.). If the terms of the embedded credit derivative provide for no limitation to the maximum potential future payments under the contract, that fact shall be disclosed. If the holder is unable to develop an estimate of the maximum potential amount of future payments under the embedded credit derivative, the holder shall disclose the reasons why it cannot estimate the maximum potential amount.

iii. The fair value of the hybrid instrument containing the embedded credit derivative as of the date of the statement of financial position.

iv. The nature of (1) any recourse provisions that would enable the holder to recover from third parties any of the amounts paid under the embedded credit derivative and (2) any assets held either as collateral or by third parties that, upon the occurrence of any specified triggering event or condition under the embedded

[11] This disclosure is required even though the embedded credit derivative is not separated under statutory accounting and recognized as a derivative. These requirements are also applicable to hybrid instruments that are beneficial interests in securitized financial assets.

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credit derivative, the holder can obtain and liquidate to recover all or a portion of the amounts paid under the credit derivative. The holder shall indicate, if estimable, the approximate extent to which the proceeds from liquidation of those assets would be expected to cover the maximum potential amount of future payments under the embedded credit derivative. In its estimate of potential recoveries, the holder of credit protection shall consider the effect of any purchased credit protection with identical underlying(s).

g. For derivatives accounted for as cash flow hedges of a forecasted transaction, disclose:

i. The maximum length of time over which the entity is hedging its exposure to the variability in future cash flows for forecasted transactions excluding those forecasted transactions related to the payment of variable interest on existing financial instruments; and

ii. The amount of gains and losses classified in unrealized gains/losses related to cash flow hedges that have been discontinued because it was no longer probable that the original forecasted transactions would occur by the end of the originally specified time period or within 2 months of that date.

h. For derivative contracts with financing premiums:

i. Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums excluding the impact of the deferred or financing premiums.

ii. For each derivative contract with financing premiums:

(a) Whether premium cost is paid throughout the contract, or at derivative maturity;

(b) Next premium cost payment date;

(c) Total premium cost;

(d) Premium cost paid in prior years;

(e) Current year premium cost paid;

(f) Future unpaid premium cost;

i. All derivatives are required to be shown gross on Schedule DB. However, derivatives may be reported net in the financial statements (pages 2 and 3 of the statutory financial statements) in accordance with *SSAP No. 64—Offsetting and Netting of Assets and Liabilities* when a valid right to offset exists. Derivatives offset in accordance with SSAP No. 64 and reported net in the financial statement shall follow the disclosure requirements in SSAP No. 64, paragraph 6. (Derivative Assets and Derivative Liabilities reported on the balance sheet shall agree to columns 5 and 6, respectively, after netting, on Schedule DB – Part D – Section 1.)

j. The disclosure requirements of paragraphs 63.a., 63.b., and 63.g. shall be included in the annual statement. Refer to the Preamble for further discussion regarding interim disclosure requirements. The disclosure requirements of paragraphs 63.a. through 63.g. shall be included in the annual audited statutory financial reports. The disclosure

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requirements in paragraph 63.h. shall be included in statutory financial statements (annual and quarterly). Paragraph 63 of the Preamble states that disclosures made within specific schedules or exhibits to the annual statement need not be duplicated in a separate note.

64. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

65. This statement adopts the framework established by FAS 133, *FASB Statement No. 137, Accounting for Derivative Instruments and Hedging Activities—Deferral of the Effective Date of FASB Statement No. 133, An amendment of FASB Statement No. 133* (FAS 137) and *FASB Statement No. 138, Accounting* for *Certain Derivative Instruments and Certain Hedging Activities, An amendment of FASB Statement No. 133* (FAS 138), for fair value and cash flow hedges, including its technical guidance to the extent such guidance is consistent with the statutory accounting approach to derivatives utilized in this statement. This statement adopts the provisions of FAS 133 and 138 related to foreign currency hedges. With the exception of guidance specific to foreign currency hedges and amendments specific to refining the hedging of interest rate risk (under FAS 138, the risk of changes in the benchmark interest rate would be a hedged risk), this statement rejects FAS No. 137 and 138 as well as the various related Emerging Issues Task Force interpretations. This statement adopts paragraphs 4 and 25 of *FASB Statement No. 149: Amendment of Statement 133 on Derivative Instruments and Hedging Activities* (FAS 149) regarding the definition of an underlying and guidance for assessing hedge effectiveness. (The adoption from FAS 149 on the assessment of hedge effectiveness is impacted by the adoption with modification of guidance from ASU 2017-12 as detailed in paragraph 66.b., with the guidance from ASU 2017-12 superseding the prior adoption to the extent applicable.) All other paragraphs in FAS 149 are rejected as not applicable for statutory accounting. This statement adopts FSP FAS 133-1 and FIN 45-5*: Disclosures about Credit Derivatives and Certain Guarantees, An Amendment of FASB Statement No. 133 and FASB Interpretation No.45 and Clarification of the Effective Date of FASB Statement No. 161 (*FSP FAS 133-1 and FIN 45-4) and requires disclosures by sellers of credit derivatives. This statement rejects *FSP FIN 39-1, Amendments of FASB Interpretation No. 39*, and *ASU 2014-03, Derivatives and Hedging – Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps – Simplified Hedge Accounting Approach*.

66. This statement adopts, with modification, certain revisions to ASC 815-20 included in ASU 2017-12. Remaining provisions of ASU 2017-12 will be subsequently assessed for statutory accounting and shall not be considered adopted for statutory accounting until that assessment is complete.

a. Revisions effective January 1, 2019, with early adoption permitted, are limited to specific provisions, and related transition guidance, pertaining to the documentation and assessment of hedge effectiveness and only includes: 1) provisions allowing more time to perform the initial quantitative hedge effectiveness assessment; 2) provisions allowing subsequent assessments of hedge effectiveness to be performed qualitatively if certain conditions are met; and 3) revisions regarding use of the critical terms and short-cut methods for assessing hedge effectiveness.

b. Revisions effective January 1, 2023, with early adoption permitted, are limited to the criteria for initial and subsequent hedge effectiveness detailed in the FASB Accounting Standards Codification (ASC) paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12. This adoption reflects statutory modifications to specify that the accounting and reporting of hedging instruments, including excluded components of the instruments, shall follow statutory-specific guidance detailed in the statement. The intent of this guidance is to clarify that the determination of whether a hedging instrument qualifies as an effective hedge shall converge with U.S. GAAP, but that the measurement method shall continue to follow statutory-specific provisions. The adoption of the referenced ASC paragraphs only

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extends to revisions incorporated through ASU 2017-12; therefore, any subsequent U.S. GAAP edits would require statutory accounting consideration before considered adopted.

c. Revisions effective January 1, 2023, with early adoption permitted, are limited to the criteria for the portfolio layer method detailed in ASU 2022-01, criteria to only consider how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity date in 815-20-25-6B, adding option in calculating the change in the hedged item's fair value attributed to changes in the benchmark interest rate based on the benchmark rate components of the contractual cash flows detailed in FASB ASC 815-25-35-13, and the partial-term hedging method detailed in FASB ASC 815-25-35-13B. The adoption of the partial term hedging method reflects statutory modifications that limits its use only when the hedged item is a recognized asset. This is different than U.S. GAAP, which permits the partial term method for hedged liabilities. The statutory limitation is established to prevent interim basis adjustments to hedged liabilities that could present a reduction of reported liabilities on the financial statements when the actual liability has not been reduced. Reconsideration of this statutory limitation may occur after a broader project to consider how derivative basis adjustments to hedged liabilities shall be reflected in the financial statements.

67. This statement adopts with modification revisions to ASC 815 as reflected within *ASU 2016-05, Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships*. This guidance is modified to require prospective application, as such it is only applicable to future counterparty changes in derivative instruments, and this guidance cannot be used to adjust derivative transactions previously terminated. This statement adopts revisions to ASC 815-20-25-15 as reflected within *ASU 2010-08, Technical Corrections to Various Topics*. This statement adopts revisions to ASC 815-10-50-4K as reflected within *ASU 2010-11, Derivatives and Hedging (Topic 815), Scope Exception Related to Embedded Credit Derivatives.*

a. This statement rejects all other GAAP revisions from ASU 2010-11 and *ASU 2014-16, Derivatives and Hedging, Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity* and *ASU 2016-06, Derivatives and Hedging, Contingent Put and Call Options in Debt Instruments*. These GAAP revisions are rejected as embedded derivatives are not separated from the host contract and recognized as derivatives under SSAP No. 86. Revisions are also incorporated to SSAP No. 86 to require disclosures on embedded credit derivatives that expose the holder of a financial instrument to the possibility of being required to make future payments. This disclosure is a modification to the GAAP disclosures specific to statutory accounting as embedded credit derivatives are not separately recognized under statutory accounting.

b. This statement rejects *ASU 2017-11, Accounting for Certain Financial Instruments with Down Round Features; Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Noncontrolling Interests with a Scope Exception*.

68. It should be noted that the conclusions reached in this statement are not intended to usurp the rules and regulations put forth by states in their respective investment laws. The contents of this statement are intended to provide accounting guidance on the use of derivatives as allowed by an insurer's state of domicile. It is not intended to imply that insurers may use derivatives or cash instruments that the insurer's state of domicile does not allow under the state's insurance regulatory requirements, e.g., in replication transactions.

69. This statement adopts revisions to ASC 815-20 as reflected within *ASU 2013-10, Derivatives and Hedging,* Inclusion *of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a*

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benchmark interest rate for Hedge Accounting Purposes. These revisions define a benchmark interest rate, clarify what can be used in the U.S. for a benchmark interest rate, and eliminate the prior restriction on using different benchmark rates for similar hedges. This statement adopts revisions to the benchmark interest rates as reflected in *ASU 2017-12, Targeted Improvements to Accounting for Hedging Activities* and *ASU 2018-16, Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as Benchmark Interest Rate for Hedge Accounting Purposes* to incorporate the Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Rate, and the Secured Overnight Financing Rate (SOFR) Overnight Index Swap Rate.

70. This statement adopts U.S. GAAP guidance for determining whether short sales are considered a derivative instrument including the regular-way security trade exception. The adopted GAAP guidance includes ASC 815-10-55-57 through 59 and 815-10-15-15 through 17. As a result, short sales shall generally be accounted for in accordance with *SSAP No. 103R—Short Sales*. Contracts that may resemble "short sales" but do not meet the criteria may be in scope of SSAP No. 86 as forward contracts.

71. This statement adopts with modification *ASC Topic 815-45: Weather Derivatives.* Weather derivatives are within the scope of SSAP No. 86 and shall be accounted and reported as other derivatives. The guidance in this statement does not apply to contracts written by insurance entities that entitle the holder to be compensated only if, as a result of an insurable event, the holder incurs a liability or there is an adverse change in the value of a specific asset or liability for which the holder is at risk.

72. This statement rejects revisions to ASC 815-15, as reflected within *ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts*. Pursuant to the ASU, market risk benefits are excluded from the U.S. GAAP embedded derivative bifurcation requirements. However, under SSAP No. 86, embedded derivatives shall not be separated from the host contract.

73. This statement rejects *ASU 2022-05, Transition for Sold Contracts*, *2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40), Accounting for Convertible Instruments and Contracts in an Entity's Own Equity*, *ASU 2020-01, Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815), Clarifying the Interactions between Topic 321, Topic 323 and Topic 815, ASU 2018-03, Recognition and Measurement of Financial Assets and Financial* Liabilities, and *ASU 2016-03, Intangibles—Goodwill and Other, Business Combinations, Consolidation, Derivatives and Hedging*. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

74. This statement is effective for derivative transaction entered into or modified on or after January 1, 2003. A modification is any revision or change in contractual terms of the derivative. SSAP No. 31 applies to derivative transaction prior to January 1, 2003. Alternatively, an insurer may choose to apply this statement to all derivatives to which the insurer is a party as of January 1, 2003. In either case, the insurer is to disclose the transition approach that is being used.

a. Revisions adopted to paragraph 65 to reject FSP FIN 39-1 is effective January 1, 2013, for companies that have previously reported a position in the balance sheet that was net

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of counterparty agreements. (Companies that have previously reported derivative instruments and/or related collateral gross shall not be impacted by these revisions.)

b. Revisions adopted in paragraph 16 clarify the reporting for amounts received/paid to adjust variation margin until the derivative contract has ended and are effective January 1, 2018, on a prospective basis, for reporting entities that have previously considered these amounts to reflect settlement or realized gains/losses. (Companies that have previously reported variation margin changes in line with the revisions shall not be impacted by these revisions.)

c. Revisions to incorporate limited provisions from ASU 2017-12 pertaining to the documentation of hedge effectiveness (detailed in paragraph 66) are effective January 1, 2019, with early adoption permitted for year-end 2018. However, if the reporting entity is a U.S. GAAP filer, the reporting entity may only elect early adoption if the entity has also elected early adoption of ASU 2017-12 for year-end 2018.

d. Revisions adopted April 2019 to explicitly include structured notes in scope of this statement are effective December 31, 2019. Revisions adopted July 2020 to define "derivative premium," require gross reporting of derivatives without the impact of financing premiums and require separate recognition of premiums payable and premiums receivable, are effective January 1, 2021.

e. Revisions adopted August 2022 that adopt with modification the criteria for initial and subsequent hedge effectiveness detailed in the FASB ASC paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12 and that incorporate statutory accounting revisions for the accounting and reporting of excluded components are effective January 1, 2023, with early adoption permitted. These revisions shall be applied prospectively for all new and existing hedges. Entities shall detail the adoption of this guidance as a change in accounting principle pursuant to *SSAP No. 3—Accounting Changes and Corrections of Error*.

f. Revisions adopted December 13, 2022, that adopt U.S. GAAP guidance for the portfolio layer method, U.S. GAAP guidance to only consider how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity, U.S. GAAP guidance adding option in calculating the change in the hedged item's fair value attributed to changes in the benchmark interest rate based on the benchmark rate component of the contractual coupon cash flows, that and adopt with modification U.S. GAAP guidance for partial term hedging are effective January 1, 2023, with early adoption permitted. These revisions shall be applied prospectively to qualifying new hedges.

REFERENCES

Other

- *SSAP No. 31—Derivative Instruments*
- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*

Relevant Issue Papers

- *Issue Paper No. 114—Accounting for Derivative Instruments and Hedging Activities*
- *Issue Paper No. 167—Derivatives and Hedging*

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EXHIBIT A – DISCUSSION OF HEDGE EFFECTIVENESS

The guidance within this exhibit reflects the adoption, with modification, of *FASB Accounting Standards Codification (ASC) 815-20-25-72 through 815-20-35-20*, as revised through the issuance of *ASU 2017-12: Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities* (ASU 2017-12) (issued on August 28, 2017). This adoption captures the U.S. GAAP guidance for the assessment and determination of hedge effectiveness, with modification to require the accounting and reporting of hedging instruments, including excluded components of hedging instruments to follow specific statutory accounting guidance in SSAP No. 86. The intent of this guidance is to clarify that the determination of whether a hedging instrument and derivative transaction qualifies as an effective hedge shall converge with U.S. GAAP, but that the measurement and reporting of effective hedge transactions shall follow statutory specific provisions. The adoption only extends to revisions incorporated to the FASB ASC through ASU 2017-12, therefore any subsequent U.S. GAAP edits to the ASC would require statutory accounting adoption before application. The guidance within this exhibit reflects excerpts from the U.S. GAAP ASC, but do not reflect the full U.S. GAAP guidance referenced in the adopted language. The exclusion of cited guidance is to manage the extent of detail included within SSAP No. 86. Excerpts not duplicated within from the cited U.S. GAAP guidance are considered adopted unless subject to the specific accounting and reporting statutory exclusion. This exhibit intends to supplement the guidance in SSAP No. 86 on hedge effectiveness. In any event in which this exhibit could be interpreted as conflicting with the SSAP No. 86 guidance, the guidance in the body of SSAP No. 86 shall be followed.

Hedge Effectiveness Criteria Applicable to Both Fair Value Hedges and Cash Flow Hedges

1. This guidance addresses hedge effectiveness criteria applicable to both fair value hedges and cash flow hedges.

2. To qualify for hedge accounting, the hedging relationship, both at inception of the hedge and on an ongoing basis, shall be expected to be highly effective in achieving either of the following:

    a. Offsetting changes in fair value attributable to the hedged risk during the period that the hedge is designated (if a fair value hedge)

    b. Offsetting cash flows attributable to the hedged risk during the term of the hedge (if a cash flow hedge), unless the hedging instrument is used to modify the contractually specified interest receipts or payments associated with a recognized financial asset liability from one variable rate to another variable rate.

3. If the hedging instrument (such as an at-the-money option contract) provides only one-sided offset of the hedged risk, either of the following conditions shall be met:

    a. The increases (or decreases) in the fair value of the hedging instrument are expected to be highly effective in offsetting the decreases (or increases) in the fair value of the hedged item (if a fair value hedge).

    b. The cash inflows (outflows) from the hedging instrument are expected to be highly effective in offsetting the corresponding change in the cash outflows or inflows of the hedged transaction (if a cash flow hedge).

4. There would be a mismatch between the change in fair value or cash flows of the hedging instrument and the change in fair value or cash flows of the hedged item or hedged transaction in any of the following circumstances, among others:

    a. A difference between the basis of the hedging instrument and the hedged item or hedged transaction, to the extent that those bases do not move in tandem.

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b. Differences in critical terms of the hedging instrument and hedged item or hedged transaction, such as differences in any of the following:

i. Notional amounts

ii. Maturities

iii. Quantity

iv. Location (not applicable for hedging relationships in which the variability in cash flows attributable to changes in a contractually specified component is designated as the hedged risk)

v. Delivery Dates

5. An entity shall consider hedge effectiveness in two different ways—in prospective considerations and in retrospective evaluations:

a. Prospective considerations. The entity's expectation that the relationship will be highly effective over future periods in achieving offsetting changes in fair value or cash flows, which is forward looking, must be assessed on a quantitative basis at hedge inception unless one of the exceptions detailed in ASU 2017-12, paragraph 815-20-25-3(b)(2)(iv)(01)[12] is met. Prospective assessments shall be subsequently performed whenever financial statements or earnings are reported and at least every three months. The entity shall elect at hedge inception whether to perform subsequent retrospective and prospective hedge effectiveness assessments on a quantitative or qualitative basis. A quantitative assessment can be based on regression or other statistical analysis of past changes in fair values or cash flows as well as on other relevant information. The quantitative prospective assessment of hedge effectiveness shall consider all reasonably possible changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument and the hedged items for the period used to assess whether the requirement for expectation of highly effective offset is satisfied. The quantitative prospective assessment may not be limited only to the likely or expected changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument or the hedged items. Generally, the process of formulating an expectation regarding the effectiveness of a proposed hedging relationship involves a probability-weighted analysis of the possible changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument and the hedged items for the hedge period. Therefore, a probable future change in fair value will be more heavily weighted than a reasonably possible future change.

b. Retrospective evaluations. An assessment of effectiveness may be performed on a quantitative or qualitative basis on the basis of the entity's election at hedge inception. That assessment shall be performed whenever financial statements or earnings are reported, and at least every three months. At inception of the hedge, an entity electing a

[12] Reference to this ASU 2017-12 guidance is consistent with the guidance in SSAP No. 86, paragraph 43, footnote 5.

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dollar-offset approach to perform retrospective evaluations on a quantitative basis may choose either a period-by-period approach or a cumulative approach in designating how effectiveness of a fair value hedge or of a cash flow hedge will be assessed retrospectively under that approach, depending on the nature of the hedge initially documented.

6. All assessments of effectiveness shall be consistent with the originally documented risk management strategy for that particular hedging relationship. An entity shall use the quantitative effectiveness assessment method defined at hedge inception consistently for the periods that the entity either elects or is required to assess hedge effectiveness on a quantitative basis.

7. This guidance does not specify a single method for assessing whether a hedge is expected to be highly effective. The method of assessing effectiveness shall be reasonable. The appropriateness of a given method of assessing hedge effectiveness depends on the nature of the risk being hedged and the type of hedging instrument used. Ordinarily, an entity shall assess effectiveness for similar hedges in a similar manner, including whether a component of the gain or loss on a derivative instrument is excluded in assessing effectiveness for similar hedges. Use of different methods for similar hedges shall be justified. The mechanics of isolating the change in time value of an option discussed beginning in paragraph 13 also shall be applied consistently.

8. In defining how hedge effectiveness will be assessed, an entity shall specify whether it will include in that assessment all of the gain or loss on a hedging instrument. An entity may exclude all or a part of the hedging instrument's time value from the assessment of hedge effectiveness, as follows:

a. If the effectiveness of a hedge with an option is assessed based on changes in the option's intrinsic value, the change in the time value of the option would be excluded from the assessment of hedge effectiveness.

b. If the effectiveness of a hedge with an option is assessed based on changes in the option's minimum value, that is, its intrinsic value plus the effect of discounting, the change in the volatility value of the contract shall be excluded from the assessment of hedge effectiveness.

c. An entity may exclude any of the following components of the change in an option's time value from the assessment of hedge effectiveness:

   i. The portion of the change in time value attributable to the passage of time (theta).

   ii. The portion of the change in time value attributable to changes due to volatility (vega).

   iii. The portion of the change in time value attributable to changes due to interest rates (rho).

d. If the effectiveness of a hedge with a forward contract or futures contract is assessed based on changes in fair value attributable to changes in spot prices, the change in the fair value of the contract related to the changes in the difference between the spot price and the forward or futures price shall be excluded from the assessment of hedge effectiveness.

e. An entity may exclude the portion of the change in fair value of a currency swap attributable to a cross-currency basis spread.

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9. No other components of a gain or loss on the designated hedging instrument shall be excluded from the assessment of hedge effectiveness nor shall an entity exclude any aspect of a change in an option's value from the assessment of hedge effectiveness that is not one of the permissible components of the change in an option's time value. For example, an entity shall not exclude from the assessment of hedge effectiveness the portion of the change in time value attributable to changes in other market variables (that is, other than rho and vega).

10. If the critical terms of the hedging instrument and of the hedged item or hedged forecasted transaction are the same, the entity could conclude that changes in fair value or cash flows attributable to the risk being hedged are expected to completely offset at inception and on an ongoing basis. For example, an entity may assume that a hedge of a forecasted purchase of a commodity with a forward contract will be perfectly effective if all of the following criteria are met:

a. The forward contract is for purchase of the same quantity of the same commodity at the same time and location as the hedged forecasted purchase. Location differences do not need to be considered if an entity designates the variability in cash flows attributable to changes in a contractually specified component as the hedged risk and the requirements in paragraphs 815-20-25-22A through 25-22B of the FASB Codification are met.

b. The fair value of the forward contract at inception is zero.

c. Either of the following criteria is met:

i. The change in the discount or premium on the forward contract is excluded from the assessment of effectiveness pursuant to paragraphs 7-9.

ii. The change in expected cash flows on the forecasted transaction is based on the forward price for the commodity.

11. In a cash flow hedge of a group of forecasted transactions in accordance with paragraph 28.a. of the SSAP guidance, an entity may assume that the timing in which the hedged transactions are expected to occur and the maturity date of the hedging instrument match in accordance with paragraph 10.a. if those forecasted transactions occur and the derivative matures within the same 31-day period or fiscal month.

12. If all of the criteria in paragraphs 10-11 are met, an entity shall still perform and document an assessment of hedge effectiveness at the inception of the hedging relationship and, on an ongoing basis throughout the hedge period. No quantitative effectiveness assessment is required at hedge inception if the criteria in paragraphs 10-11 are met.

Computing Changes in an Option's Time Value

13. In computing the changes in an option's time value that would be excluded from the assessment of hedge effectiveness, an entity shall use a technique that appropriately isolates those aspects of the change in time value. Generally, to allocate the total change in an option's time value to its different aspects—the passage of time and the market variables—the change in time value attributable to the first aspect to be isolated is determined by holding all other aspects constant as of the beginning of the period. Each remaining aspect of the change in time value is then determined in turn in a specified order based on the ending values of the previously isolated aspects.

14. Based on that general methodology, if only one aspect of the change in time value is excluded from the assessment of hedge effectiveness (for example, theta), that aspect shall be the first aspect for which the change in time value is computed and would be determined by holding all other parameters

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constant for the period used for assessing hedge effectiveness. However, if more than one aspect of the change in time value is excluded from the assessment of hedge effectiveness (for example, theta and vega), an entity shall determine the amount of that change in time value by isolating each of those two aspects in turn in a prespecified order (one first, the other second). The second aspect to be isolated would be based on the ending value of the first isolated aspect and the beginning values of the remaining aspects. The portion of the change in time value that is included in the assessment of effectiveness shall be determined by deducting from the total change in time value the portion of the change in time value attributable to excluded components.

Assuming Perfect Hedge Effectiveness in a Hedge with an Interest Rate Swap

15. The conditions for the shortcut method do not determine which hedging relationships qualify for hedge accounting; rather, those conditions determine which hedging relationships qualify for a shortcut version of hedge accounting that assumes perfect hedge effectiveness. If all of the applicable conditions in the list in paragraph 17 are met, an entity may assume perfect effectiveness in a hedging relationship of interest rate risk involving a recognized interest-bearing asset or liability (or a firm commitment arising on the trade [pricing] date to purchase or issue an interest-bearing asset or liability) and an interest rate swap (or a compound hedging instrument composed of an interest rate swap and a mirror-image call or put option as discussed in paragraph 17.e.) provided that, in the case of a firm commitment, the trade date of the asset or liability differs from its settlement date due to generally established conventions in the marketplace in which the transaction is executed. The shortcut method's application shall be limited to hedging relationships that meet each and every applicable condition. That is, all the conditions applicable to fair value hedges shall be met to apply the shortcut method to a fair value hedge, and all the conditions applicable to cash flow hedges shall be met to apply the shortcut method to a cash flow hedge. A hedging relationship cannot qualify for application of the shortcut method based on an assumption of perfect effectiveness justified by applying other criteria. The verb *match* is used in the specified conditions in the list to mean *exactly the same* or *correspond exactly*.

16. Implicit in the conditions for the shortcut method is the requirement that a basis exist for concluding on an ongoing basis that the hedging relationship is expected to be highly effective in achieving offsetting changes in fair values or cash flows. In applying the shortcut method, an entity shall consider the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative that require the counterparty to make payments to the entity.

17. All of the following conditions apply to both fair value hedges and cash flow hedges:

a. The notional amount of the interest rate swap matches the principal amount of the interest-bearing asset or liability being hedged.

b. If the hedging instrument is solely an interest rate swap, the fair value of that interest rate swap at the inception of the hedging relationship must be zero, with one exception. The fair value of the swap may be other than zero at the inception of the hedging relationship only if the swap was entered into at the relationship's inception, the transaction price of the swap was zero in the entity's principal market (or most advantageous market), and the difference between transaction price and fair value is attributable solely to differing prices within the bid-ask spread between the entry transaction and a hypothetical exit transaction. The guidance in the preceding sentence is applicable only to transactions considered *at market* (that is, transaction price is zero exclusive of commissions and other transaction costs). If the hedging instrument is solely an interest rate swap that at the inception of the hedging relationship has a positive or negative fair value, but does not meet the one exception specified in this paragraph, the shortcut method shall not be used even if all the other conditions are met.

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c. If the hedging instrument is a compound derivative composed of an interest rate swap and mirror-image call or put option as discussed in paragraph 17.e., the premium for the mirror-image call or put option shall be paid or received in the same manner as the premium on the call or put option embedded in the hedged item based on the following:

i. If the implicit premium for the call or put option embedded in the hedged item is being paid principally over the life of the hedged item (through an adjustment of the interest rate), the fair value of the hedging instrument at the inception of the hedging relationship shall be zero (except as discussed previously in paragraph 17.b. regarding differing prices due to the existence of a bid-ask spread).

ii. If the implicit premium for the call or put option embedded in the hedged item was principally paid at inception-acquisition (through an original issue discount or premium), the fair value of the hedging instrument at the inception of the hedging relationship shall be equal to the fair value of the mirror-image call or put option.

d. The formula for computing net settlements under the interest rate swap is the same for each net settlement. That is, both of the following conditions are met:

i. The fixed rate is the same throughout the term.

ii. The variable rate is based on the same index and includes the same constant adjustment or no adjustment. The existence of a stub period and stub rate is not a violation of the criterion in paragraph 17.d. that would preclude application of the shortcut method if the stub rate is the variable rate that corresponds to the length of the stub period.

e. The interest-bearing asset or liability is not prepayable, that is, able to be settled by either party before its scheduled maturity, or the assumed maturity date if the hedged item is measured as a partial-term hedge of interest rate risk in which the assumed maturity of the hedged items ends at the end of the designated hedge period, in accordance with paragraph 815-25-35-13B, with the following qualifications:

i. This criterion does not apply to an interest-bearing asset or liability that is prepayable solely due to an embedded call option (put option) if the hedging instrument is a compound derivative composed of an interest rate swap and a mirror-image call option (put option).

ii. The call option embedded in the interest rate swap is considered a mirror image of the call option embedded in the hedged item if all of the following conditions are met:

(a) The terms of the two call options match exactly, including all of the following:

(1) Maturities

(2) Strike price (that is, the actual amount for which the debt instrument could be called) and there is no termination payment equal to the deferred debt issuance costs that remain unamortized on the date the debt is called

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(3) Related notional amounts

(4) Timing and frequency of payments

(5) Dates on which the instruments may be called.

(b) The entity is the writer of one call option and the holder (purchaser) of the other call option.

f. Any other terms in the interest-bearing financial instruments or interest rate swaps meet both of the following conditions:

i. The terms are typical of those instruments.

ii. The terms do not invalidate the assumption of perfect effectiveness.

18. All of the following incremental conditions apply to fair value hedges only:

a. The expiration date of the interest rate swap matches the maturity date of the interest-bearing asset or liability or the assumed maturity date if the hedged item is measured as a partial-term hedge of interest rate risk in which the assumed maturity of the hedged items ends at the end of the designated hedge period.

b. There is no floor or cap on the variable interest rate of the interest rate swap.

c. The interval between repricings of the variable interest rate in the interest rate swap is frequent enough to justify an assumption that the variable payment or receipt is at a market rate (generally three to six months or less).

d. For fair value hedges of a proportion of the principal amount of the interest-bearing asset or liability, the notional amount of the interest rate swap designated as the hedging instrument matches the portion of the asset or liability being hedged.

e. For fair value hedges of portfolios (or proportions thereof) of similar interest-bearing assets or liabilities, both of the following criteria are met:

i. The notional amount of the interest rate swap designated as the hedging instrument matches the aggregate notional amount of the hedged item (whether it is all or a proportion of the total portfolio).

ii. The remaining criteria for the shortcut method are met with respect to the interest rate swap and the individual assets or liabilities in the portfolio.

f. The index on which the variable leg of the interest rate swap is based matches the benchmark interest rate designated as the interest rate risk being hedged for that hedging relationship.

19. All of the following incremental conditions apply to cash flow hedges only:

a. All interest receipts or payments on the variable-rate asset or liability during the term of the interest rate swap are designated as hedged.

b. No interest payments beyond the term of the interest rate swap are designated as hedged.

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c. Either of the following conditions is met:

i. There is no floor or cap on the variable interest rate of the interest rate swap.

ii. The variable-rate asset or liability has a floor or cap and the interest rate swap has a floor or cap on the variable interest rate that is comparable to the floor or cap on the variable-rate asset or liability. For purposes of this paragraph, comparable does not necessarily mean equal. For example, if an interest rate swap's variable rate is based on LIBOR and an asset's variable rate is LIBOR plus 2% ~~percent~~, a 10% ~~percent~~ cap on the interest rate swap would be comparable to a 12% ~~percent~~ cap on the asset.

d. The repricing dates of the variable-rate asset or liability and the hedging instrument must occur on the same dates and be calculated the same way (that is, both shall be either prospective or retrospective). If the repricing dates of the hedged item occur on the same dates as the repricing dates of the hedging instrument but the repricing calculation for the hedged item is prospective whereas the repricing calculation for the hedging instrument is retrospective, those repricing dates do not match.

e. For cash flow hedges of the interest payments on only a portion of the principal amount of the interest-bearing asset or liability, the notional amount of the interest rate swap designated as the hedging instrument matches the principal amount of the portion of the asset or liability on which the hedged interest payments are based.

f. For a cash flow hedge in which the hedged forecasted transaction is a group of individual transactions (as permitted by paragraph 28.a. of the SSAP guidance), if both of the following criteria are met:

i. The notional amount of the interest rate swap designated as the hedging instrument matches the notional amount of the aggregate group of hedged transactions.

ii. The remaining criteria for the shortcut method are met with respect to the interest rate swap and the individual transactions that make up the group. For example, the interest rate repricing dates for the variable-rate assets or liabilities whose interest payments are included in the group of forecasted transactions shall match (that is, be exactly the same as) the reset dates for the interest rate swap.

g. The index on which the variable leg of the interest rate swap is based matches the contractually specified interest rate designated as the interest rate being hedged for that hedging relationship.

20. The shortcut method may be applied to a hedging relationship that involves the use of an interest rate swap-in-arrears provided all of the applicable conditions are met.

21. Any discount or premium in the hedged debt's carrying amount (including any related deferred issuance costs) is irrelevant to and has no direct impact on the determination of whether an interest rate swap contains a mirror-image call option under paragraph 17.e.i. Typically, the call price is greater than the par or face amount of the debt instrument. The carrying amount of the debt is economically unrelated to the amount the issuer would be required to pay to exercise the call embedded in the debt.

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22. The fixed interest rate on a hedged item need not exactly match the fixed interest rate on an interest rate swap designated as a fair value hedge. Nor does the variable interest rate on an interest-bearing asset or liability need to be the same as the variable interest rate on an interest rate swap designated as a cash flow hedge. An interest rate swap's fair value comes from its net settlements. The fixed and variable interest rates on an interest rate swap can be changed without affecting the net settlement if both are changed by the same amount. That is, an interest rate swap with a payment based on LIBOR and a receipt based on a fixed rate of 5% ~~percent~~ has the same net settlements and fair value as an interest rate swap with a payment based on LIBOR plus 1% ~~percent~~ and a receipt based on a fixed rate of 6% ~~percent~~.

23. Comparable credit risk at inception is not a condition for assuming perfect effectiveness even though actually achieving perfect offset would require that the same discount rate be used to determine the fair value of the swap and of the hedged item or hedged transaction. To justify using the same discount rate, the credit risk related to both parties to the swap as well as to the debtor on the hedged interest-bearing asset (in a fair value hedge) or the variable-rate asset on which the interest payments are hedged (in a cash flow hedge) would have to be the same. However, because that complication is caused by the interaction of interest rate risk and credit risk, which are not easily separable, comparable creditworthiness is not considered a necessary condition for assuming perfect effectiveness in a hedge of interest rate risk.

24. If a fair value hedge or cash flow hedge initially qualifies for hedge accounting, the entity would continue to assess whether the hedge meets the effectiveness test on either a quantitative basis (using either a dollar-offset test or a statistical method such as regression analysis) or a qualitative basis. If the hedge fails the effectiveness test at any time (that is, if the entity does not expect the hedge to be highly effective at achieving offsetting changes in fair values or cash flows), the hedge ceases to qualify for hedge accounting. At least quarterly, the hedging entity shall determine whether the hedging relationship has been highly effective in having achieved offsetting changes in fair value or cash flows through the date of the periodic assessment.

Effectiveness Assessment on a Qualitative Basis

25. An entity may qualitatively assess hedge effectiveness if both of the following criteria are met:

a. An entity performs an initial quantitative test of hedge effectiveness on a prospective basis (that is, it is not assuming that the hedging relationship is perfectly effective at hedge inception), and the results of that quantitative test demonstrate highly effective offset.

b. At hedge inception, an entity can reasonably support an expectation of high effectiveness on a qualitative basis in subsequent periods.

26. An entity may elect to qualitatively assess hedge effectiveness in accordance with paragraph 25 on a hedge-by-hedge basis. If an entity makes this qualitative assessment election, only the quantitative method specified in an entity's initial hedge documentation must comply with paragraph 7.

27. When an entity performs qualitative assessments of hedge effectiveness, it shall verify and document whenever financial statements or earnings are reported and at least every three months that the facts and circumstances related to the hedging relationship have not changed such that it can assert qualitatively that the hedging relationship was and continues to be highly effective. While not all-inclusive, the following is a list of indicators that may, individually or in the aggregate, allow an entity to continue to assert qualitatively that the hedging relationship is highly effective:

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a. An assessment of the factors that enabled the entity to reasonably support an expectation of high effectiveness on a qualitative basis has not changed such that the entity can continue to assert qualitatively that the hedging relationship was and continues to be highly effective.

b. There have been no adverse developments regarding the risk of counterparty default.

28. If an entity elects to assess hedge effectiveness on a qualitative basis and then facts and circumstances change such that the entity no longer can assert qualitatively that the hedging relationship was and continues to be highly effective in achieving offsetting changes in fair values or cash flows, the entity shall assess effectiveness of that hedging relationship on a quantitative basis in subsequent periods. In addition, an entity may perform a quantitative assessment of hedge effectiveness in any reporting period to validate whether qualitative assessments of hedge effectiveness remain appropriate. In both cases, the entity shall apply the quantitative method that it identified in its initial hedge documentation.

29. When an entity determines that facts and circumstances have changed and it no longer can assert qualitatively that the hedging relationship was and continues to be highly effective, the entity shall begin performing subsequent quantitative assessments of hedge effectiveness as of the period that the facts and circumstances changed. If there is no identifiable event that led to the change in the facts and circumstances of the hedging relationship, the entity may begin performing quantitative assessments of effectiveness in the current period.

30. After performing a quantitative assessment of hedge effectiveness for one or more reporting periods as discussed in paragraphs 28-29, an entity may revert to qualitative assessments of hedge effectiveness if it can reasonably support an expectation of high effectiveness on a qualitative basis for subsequent periods.

Quantitative Hedge Effectiveness Assessments After Hedge Designation

31. Quantitative assessments can be based on regression or other statistical analysis of past changes in fair values or cash flows as well as on other relevant information.

32. If an entity elects at the inception of a hedging relationship to use the same regression analysis approach for both prospective considerations and retrospective evaluations of assessing effectiveness, then during the term of that hedging relationship both of the following conditions shall be met:

a. Those regression analysis calculations shall generally incorporate the same number of data points.

b. That entity must periodically update its regression analysis (or other statistical analysis).

33. Electing to use a regression or other statistical analysis approach instead of a dollar-offset approach to perform retrospective evaluations of assessing hedge effectiveness may affect whether an entity can apply hedge accounting for the current assessment period.

34. In periodically (that is, at least quarterly) assessing retrospectively the effectiveness of a fair value hedge (or a cash flow hedge) in having achieved offsetting changes in fair values (or cash flows) under a dollar-offset approach, an entity shall use either a period-by-period approach or a cumulative approach on individual fair value hedges (or cash flow hedges):

a. Period-by-period approach. The period-by-period approach involves comparing the changes in the hedging instrument's fair values (or cash flows) that have occurred during the period being assessed to the changes in the hedged item's fair value (or hedged

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transaction's cash flows) attributable to the risk hedged that have occurred during the same period. If an entity elects to base its comparison of changes in fair value (or cash flows) on a period-by-period approach, the period cannot exceed three months. Fair value (or cash flow) patterns of the hedging instrument or the hedged item (or hedged transaction) in periods before the period being assessed are not relevant.

b. Cumulative approach. The cumulative approach involves comparing the cumulative changes (to date from inception of the hedge) in the hedging instrument's fair values (or cash flows) to the cumulative changes in the hedged item's fair value (or hedged transaction's cash flows) attributable to the risk hedged.

35. If an entity elects at inception of a hedging relationship to base its comparison of changes in fair value (or cash flows) on a cumulative approach, then that entity must abide by the results of that methodology as long as that hedging relationship remains designated. Electing to utilize a period-by-period approach instead of a cumulative approach (or vice versa) to perform retrospective evaluations of assessing hedge effectiveness under the dollar-offset method may affect whether an entity can apply hedge accounting for the current assessment period.

Assessing Effectiveness Based on Whether the Critical Terms of the Hedging Instrument and the Hedged Items Match

36. If, at inception, the critical terms of the hedging instrument and the hedged forecasted transaction are the same (see paragraphs 10-11), the entity can conclude that changes in cash flows attributable to the risk being hedged are expected to be completely offset by the hedging derivative. Therefore, subsequent assessments can be performed by verifying and documenting whether the critical terms of the hedging instrument and the forecasted transaction have changed during the period in review.

37. Because the assessment of hedge effectiveness in a cash flow hedge involves assessing the likelihood of the counterparty's compliance with the contractual terms of the derivative instrument designated as the hedging instrument, the entity must also assess whether there have been adverse developments regarding the risk of counterparty default, particularly if the entity planned to obtain its cash flows by liquidating the derivative instrument at its fair value.

38. If there are no such changes in the critical terms or adverse developments regarding counterparty default, the entity may conclude that the hedging relationship is perfectly effective. In that case, the change in fair value of the derivative instrument can be viewed as a proxy for the present value of the change in cash flows attributable to the risk being hedged.

39. However, the entity must assess whether the hedging relationship is expected to continue to be highly effective using a quantitative assessment method (either a dollar-offset test or a statistical method such as regression analysis) if any of the following conditions exist:

a. The critical terms of the hedging instrument or the hedged forecasted transaction have changed.

b. There have been adverse developments regarding the risk of counterparty default.

Possibility of Default by the Counterparty to Hedging Derivative

40. For an entity to conclude on an ongoing basis that the hedging relationship is expected to be highly effective in achieving offsetting changes in cash flows, the entity shall not ignore whether it will collect the payments it would be owed under the contractual provisions of the derivative instrument. In complying with the requirements of paragraph 2.b., the entity shall assess the possibility of whether the

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counterparty to the derivative instrument will default by failing to make any contractually required payments to the entity as scheduled in the derivative instrument. In making that assessment, the entity shall also consider the effect of any related collateralization or financial guarantees. The entity shall be aware of the counterparty's creditworthiness (and changes therein) in determining the fair value of the derivative instrument. Although a change in the counterparty's creditworthiness would not necessarily indicate that the counterparty would default on its obligations, such a change shall warrant further evaluation.

41. If the likelihood that the counterparty will not default ceases to be probable, an entity would be unable to conclude that the hedging relationship in a cash flow hedge is expected to be highly effective in achieving offsetting cash flows.

42. In contrast, a change in the creditworthiness of the derivative instrument's counterparty in a fair value hedge would have an immediate effect because that change in creditworthiness would affect the change in the derivative instrument's fair value, which would immediately affect both of the following:

a. The assessment of whether the relationship qualifies for hedge accounting

b. The amount of mismatch between the change in the fair value of the hedging instrument and the hedged item attributable to the hedged risk recognized in earnings under fair value hedge accounting.

43. Paragraph 16 states that, in applying the shortcut method, an entity shall consider the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative that require the counterparty to make payments to the entity. That paragraph explains that implicit in the criteria for the shortcut method is the requirement that a basis exist for concluding on an ongoing basis that the hedging relationship is expected to be highly effective in achieving offsetting changes in fair values or cash flows.

Change in Hedge Effectiveness Method When Hedge Effectiveness if Assessed on a Quantitative Basis

44. If the entity identifies an improved method of assessing hedge effectiveness in accordance with the guidance in paragraph 6 and wants to apply that method prospectively, it shall do both of the following:

a. Discontinue the existing hedging relationship.

b. Designate the relationship anew using the improved method.

45. The new method of assessing hedge effectiveness shall be applied prospectively and shall also be applied to similar hedges unless the use of a different method for similar hedges is justified. A change in the method of assessing hedge effectiveness by an entity shall not be considered a change in accounting principle as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors*.

Portfolio Layer Method

46. For a closed portfolio of financial assets or one or more beneficial interests secured by a portfolio of financial instruments, an entity may designate as the hedged item or items a hedged layer or layers. (This designation is referred to throughout as the "portfolio layer method.")

a. As part of the initial hedge documentation, an analysis is completed and documented to support the entity's expectation that the hedged item or items (that is, the hedged layer or layers in aggregate) is anticipated to be outstanding for the designated hedge period. That analysis shall incorporate the entity's current expectations of prepayments, defaults, and

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other factors affecting the timing and amount of cash flows associated with the closed portfolio.

b. For purposes of its analysis in paragraph 46.a., the entity assumes that as prepayments, defaults, and other factors affecting the timing and amount of cash flows occur, they first will be applied to the portion of the closed portfolio that is not hedged; and

c. The entity applies the partial-term hedging guidance to the assets or beneficial interest used to support the entity's expectation in paragraph 46.a. An asset that matures on a hedged layer's assumed maturity date meets this requirement.

47. After a closed portfolio is established in accordance with paragraph 46, and entity may designate new hedging relationships associated with the closed portfolio without dedesignating any existing hedging relationships associated with the closed portfolio if the criteria of paragraph 46 are met for those newly designated hedging relationships.

48. For the portfolio layer method, if both of the following conditions exist, the quantitative test described for similar assets (shared risk exposure) may be performed qualitatively on a hedge-by-hedge basis and only at hedge inception:

a. The hedged item is a hedged layer in a portfolio layer hedge and designated in accordance with paragraph 26.f. of SSAP No. 86.

b. An entity measures the change in fair value of the hedged item based on the benchmark rate component of the contractual coupon cash flows.

Using the benchmark rate component of the contractual coupon cash flows when all assets have the same assumed maturity date and prepayment risk does not affect the measurement of the hedged item results in all hedged items having the same benchmark rate component coupon cash flows.

49. For one or more hedging relationships designated under the portfolio layer method, an entity shall discontinue (or partially discontinue) hedge accounting in the following circumstances:

a. If the entity cannot support on a subsequent testing date that the hedged layer or layers are anticipated to be outstanding for the designated hedge (that is, a breach is anticipated), it shall discontinue (or partially discontinue) hedge accounting for one or more hedging relationships for the portion of the hedged item that is no longer anticipated to be outstanding for the designated hedge period.

b. If on a subsequent testing date the outstanding amount of the closed portfolio of financial assets or one or more beneficial interests is less than the hedged layer or layers (that is, a breach has occurred), the entity shall discontinue (or partially discontinue) hedge accounting for one or more hedging relationships for the portion of the hedged item that is no longer outstanding.

50. In the event of either an anticipated breach (as described in paragraph 49.a.) or a breach that has occurred (as described in paragraph 49.b.) for portfolio layer method, if multiple hedged layers are associated with a closed portfolio, an entity shall determine which hedge or hedges to discontinue (or partially discontinue) in accordance with an accounting policy election. That accounting policy election shall specify a systematic and rational approach to determining which hedge or hedges to discontinue (or partially discontinue). An entity shall establish its accounting policy no later than when it first anticipates a breach or when a breach has occurred (whichever comes first). After an entity establishes its accounting policy, it shall consistently apply its accounting policy to all portfolio layer method breaches (anticipated and occurred).

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EXHIBIT B – SPECIFIC HEDGE ACCOUNTING PROCEDURES FOR DERIVATIVES

Synopsis: Derivatives may be designated as hedges of changes in the fair value or variability in expected cash flows of assets, liabilities, forecasted transactions or firm commitments due to one or more of the following risks: interest rate, security price, commodity price, foreign exchange rate, index of prices or rates or other variables (excluding risks of identifiable insurable events such as death, disability, accident, illness, damage to property or damage or injury to an insured or third party). Derivatives used in hedging transactions that meet the criteria of a highly effective hedge shall be considered an effective hedge and valued and reported in a manner that is consistent with the hedged asset or liability (referred to as hedge accounting). Under hedge accounting the valuation method used for the derivative shall be consistent with the valuation method used for the hedged item: e.g., amortized cost or fair value. Changes in the carrying value (i.e., amortization or fair value changes) or cash flow of the derivative shall be recognized in the same period and in the same category of income or surplus as the amortization or fair value changes of the hedged item: e.g. net gain from operations, realized capital gains and losses on investments, unrealized capital gains and losses on investments, or unrealized foreign exchange capital gain or loss.

The effects of hedge accounting are reflected in a manner that does not change the reporting of the item being hedged, consistent with the financial statement category that would normally be required under statutory accounting principles. Generally, if the change in the item being hedged is reported as a component of net gain from operations, the change in the derivative shall be reported in its appropriate component of net gain from operations. For example, a change in the aggregate reserve liabilities is reflected in its appropriate annual statement line change in aggregate reserves. A change in the related derivatives that are hedging that item is reflected through other income.

In the case where a portion of the item being hedged is reported as a component of net gain from operations, with the remainder reported as an other change to surplus, then the change in the hedging derivative is bifurcated; a portion is reported as a component of net gain from operations, in the appropriate category and included in the net gain from operations with the remainder reported as an other change to surplus.

For example, in the hedge of a foreign currency denominated asset the change in the value of the asset due to fluctuations in foreign exchange rates is recorded as unrealized capital gains or losses until the asset is sold. A derivative instrument that is in an effective hedging relationship of that item, shall have its change in value associated with fluctuations in foreign currency exchange rates bifurcated and recorded in unrealized capital gains and losses with the remaining change in value recorded consistent with the item being hedged (amortized cost or fair value).

A common purpose of entering into derivatives such as interest rate swaps and forwards as hedges is to change the interest rate characteristics of hedged items. Consistent with this purpose and the hedge accounting concept of matched accounting between the hedging and hedged item, hedged items may be viewed as bearing the changed interest rate characteristics and the cost of the derivatives may therefore be combined with the hedged items. All derivatives shall be reported on Schedule DB. When one or more derivatives hedge more than one asset, liability, forecasted transaction or firm commitment (or a portfolio of hedged items), a company may allocate the total derivative(s) to hedged items individually or in the aggregate. If derivatives are allocated to hedged items, indicate on Schedule DB the nature of the items hedged and the schedule or exhibit where they are presented.

An open derivative hedging a forecasted transaction or firm commitment shall be recorded at cost until the hedged transaction occurs. When the hedged forecasted transaction or firm commitment occurs, an open derivative shall be accounted for in a manner consistent with the hedged item (i.e., amortized cost or fair value).

Upon termination of a derivative that qualified for hedge accounting of an existing asset or liability or a forecasted transaction or firm commitment, the resulting gain or loss shall be recognized in income in a

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manner that is consistent with the hedged item. If the hedged item is recorded at amortized cost, the gain or loss shall adjust, individually or in the aggregate, the basis of the hedged item subject to amortization. Alternatively, if the item being hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination. For terminated derivatives, indicate on Schedule DB, Section 2, Parts A and B the nature of the assets or liabilities so adjusted and the schedule or exhibit where they are presented.

Derivative instruments used in hedging transactions that (i) do not meet or no longer meet the criteria of an effective hedge or (ii) meet the required hedge criteria but the entity has chosen not to apply hedge accounting shall be accounted for at fair value and the changes in the fair value shall be recorded in surplus as unrealized gains or unrealized losses (referred to as fair value accounting). Hedge accounting may not be applied upon inception, redesignation or termination of a derivative designated in a hedging relationship if documentation is not maintained in accordance with SSAP No. 86, paragraphs 42-46.

Specific hedge accounting procedures for derivative instruments are outlined below.

1. Call and Put Options, Warrants, Caps, and Floors:

   a. Accounting at Date of Acquisition (purchase) or Issuance (written): The premium paid or received for purchasing or writing a call option, put option, warrant, cap or floor shall either be (i) recorded as an asset (purchase) or liability (written) on the Derivative line on the Assets (or) Liabilities pages or (ii) combined with the hedged item(s) individually or in the aggregate;

   b. Statement Value:

      i. Open derivatives hedging items recorded at amortized cost:

         (a) Options, warrants, caps, and floors purchased or written shall be valued at amortized cost in a manner consistent with the hedged item. (Components of a hedging instrument excluded from the determination of hedge effectiveness shall be recognized at fair value, with changes in fair value recognized as unrealized gains/losses throughout the duration of the hedging instrument. These components are not captured within the guidance for effective hedges detailed within this section.)

         (b) The amortization period and methods used shall result in a constant effective yield over the life of the hedged item or program. (For floating rate hedged items, the estimated effective yield shall be based on the current rate so the changes in yields attributable to changes in interest rates will be recognized in the period of change.) Specific treatment includes:

            (1) Holdings in derivatives purchased or written within a year of maturity or expiry need not be amortized;

            (2) For hedges of forecasted transactions or firm commitments, the derivative may be recorded at cost until the hedged transaction occurs or it is determined that the hedge was not effective (see (d) in this section 1.b.i.);

            (3) For other derivatives, the amortization period is usually from date of acquisition (issuance) of the derivative to maturity of the hedged item or program.

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(c) For hedges where the cost of the derivative is combined with the hedged item, the statement value is zero. The fair value of the derivative and hedged item shall be determined and reported separately, either individually or in the aggregate;

(d) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost until (1) the hedged transaction occurs or (2) it is determined that the hedge was not effective (when the derivative is valued in accordance with (e) in this section);

(e) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, valuation at amortized cost ceases and the derivative or the designated portion of the derivative shall be valued at its current fair value with gains and losses recognized in unrealized gains or unrealized losses to the extent it ceased to be an effective hedge.

ii. Open derivatives hedging items recorded at fair value (where gains and losses on the hedged item are recognized as adjustments to unassigned funds (surplus)):

(a) Options, warrants, caps, or floors purchased or written shall be valued at current fair value with changes in fair value recognized currently consistent with the hedged item; this will result in unrealized gain/loss treatment with adjustment to unassigned funds (surplus).

(b) For hedges where the cost of the derivative is combined with the hedged item, the fair value of the derivative and hedged item will be determined and reported separately, either individually or in the aggregate. The cost (book value) basis used to figure unrealized gain/loss on the derivative on Schedule DB is zero.

(c) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost until the hedged transaction occurs or it is determined that the hedge was not effective (when fair value accounting is applied as described in the Introduction above).

iii. Open derivatives hedging items recorded at fair value, where gains and losses on the hedged item are recognized currently in earnings: options, warrants, caps, or floors purchased or written shall be valued at current fair value with changes in fair value recognized currently in earnings together with the gains and losses on the hedged item.

(a) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost until (1) the hedged transaction occurs or (2) it is determined that the hedge was not effective (when fair value accounting is applied as described in (b) of this section).

(b) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, recognition of changes in fair value through earnings ceases. The derivative or the designated portion of the derivative shall continue to be valued at its current fair value, but thereafter gains or losses shall be recognized in unrealized gains or unrealized losses to the extent it ceased to be an effective hedge.

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c. Cash Flows and Income

i. Where the cost of the derivative is not combined with the hedged item:

(a) Amortization of premium or discount on derivatives is an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of the hedged item;

(b) Periodic cash flows and accruals of income/expense shall be reported in a manner consistent with the hedged item, such as net investment income or interest and adjustments on policy or deposit-type contract funds (operating income) or net realized capital gains.

ii. Where the cost of the derivative is combined with the hedged item, the cash flows and income of the derivative on Schedule DB will be zero. All related amortization and cash flow accounting shall be reported with the hedged item instead of with the derivative.

d. Gain/Loss on Termination of an option, warrant, cap or floor accounted for under hedge accounting (includes closing, exercise, maturity, and expiry):

i. Exercise of an Option: The remaining book value of the derivative shall become an adjustment to the cost or proceeds of the hedged item(s) received or disposed of individually or in aggregate;

ii. Sale, maturity, expiry, or other closing transaction of a derivative which is an effective hedge—Any gain or loss on the transaction, except for excluded components, will adjust the basis (or proceeds) of the hedged item(s) individually or in aggregate. Alternatively, if the item being hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination. For hedging instruments with excluded components in determining hedge effectiveness, the unrealized gain/loss from the change in fair value of the excluded component shall be realized upon the closing transaction. This gain/loss shall not be used to adjust the basis or proceeds of the hedged item.

iii. Gain/loss on termination of derivatives will be recognized currently in net income (realized gain/loss) to the extent they ceased to be effective hedges.

iv. Upon the redesignation of a derivative from a currently effective hedging relationship:

(a) with an item(s) carried at amortized cost to another effective hedging relationship with an item(s) carried at amortized cost, the derivative shall continue to be recorded at amortized cost and no gain or loss on the derivative shall be recognized.

(b) with an item(s) carried at amortized cost or fair value to an effective relationship with an item(s) carried at fair value, the accounting for the derivative shall be consistent with (ii) above.

(c) with an item(s) carried at fair value to an effective relationship with an item(s) carried at amortized cost, the accounting for the derivative shall be consistent with (ii) above.

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2. Swaps, Collars, and Forwards (see also discussion in Introduction above):

a. Accounting at Date of Opening Position:

i. Any premium paid or received at date of opening shall either be (a) recorded on the Derivative line on the Assets (or) Liabilities pages or (b) combined with the hedged item(s), individually or in the aggregate;

b. Statement Value:

i. Open derivatives hedging items recorded at amortized cost:

(a) Swaps, collars, and forwards shall be valued at amortized cost in a manner consistent with hedged item. (Components of a hedging instrument excluded from the determination of hedge effectiveness not addressed in paragraph 2.b.iii. shall be recognized at fair value, with changes in fair value of the excluded component recognized as unrealized gains/losses throughout the duration of the hedging instrument. These components are not captured within the guidance for effective hedges detailed within this section.)

(b) The amortization period and methods used shall result in a constant effective yield over the life of the hedged item or program. (For floating rate hedged items the estimated effective yield shall be based on the current rate so the changes in yields attributable to changes in interest rates will be recognized in the period of change.) Specific treatment includes:

(1) Holdings in derivatives purchased or written within a year of maturity or expiry need not be amortized;

(2) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost until (a) the hedged transaction occurs or (b) it is determined that the hedge was not effective (see (5) in this section 2.b.i.);

(3) For other derivatives the amortization period is usually from date of acquisition (issuance) of the derivative to maturity of the hedged item or program;

(4) For hedges where the cost of the derivative is combined with the hedged item, the statement value is zero. The fair value of the derivative and hedged item shall be determined and reported separately, either individually or in the aggregate;

(5) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, valuation at amortized cost ceases and the derivative or a designated portion of the derivative shall be valued at its current fair value with gains and losses recorded in unrealized gains or unrealized losses to the extent that it ceased to be an effective hedge. Upon redesignation into an effective hedging relationship, the derivative's mark to fair value through unrealized gain or loss shall be reversed.

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ii. Open derivatives hedging items recorded at fair value (where gains and losses on the hedged item are recognized as adjustments to unassigned funds (surplus)):

(a) Swaps, collars, or forwards shall be valued at current fair value with changes in fair value recognized currently consistent with the hedged item; this will result in unrealized gain/loss treatment with adjustment to unassigned funds (surplus);

(b) For hedges where the derivative is combined with the hedged item, the fair value of the derivative and hedge item shall be determined and reported separately, either individually or in the aggregate. The cost (book value) basis used to figure gain/loss on the derivative is zero.

iii. Open foreign currency swap and forward contracts hedging foreign currency exposure on items denominated in a foreign currency and translated into U.S. dollars where fair value accounting is not being used:

(a) The foreign exchange premium (discount) is defined as the foreign currency (notional) amount to be received (paid) times the net of the forward rate minus the spot rate at the time the contract was opened. For forward contracts, an excluded component representing a foreign exchange premium (discount) (forward points) on the currency contract shall be amortized into income over the life of the contract or hedge program. Amortization is not required if the contract was entered into within a year of maturity. For foreign currency swaps, an excluded component representing a cross-currency basis spread, is recognized into income through the foreign currency swap's periodic interest accruals;

(b) A foreign currency translation adjustment shall be reflected as an unrealized gain/loss (unassigned funds (surplus) adjustment) using the same procedures as done to translate the hedged item;

(c) The unrealized gain/loss for the period equals the foreign currency (notional) amount to be received (paid) times the net of the current spot rate minus the prior period end spot rate.

(d) The statement value of the derivative equals the amortized cost plus:

(1) For forward contracts, the amortized (premium) discount plus the cumulative unrealized gain/(loss) on the contract;

(2) For foreign currency swaps, the cumulative unrealized gain/(loss) on the contract. The cross-currency basis spread is recorded through the Investment Income Due and Accrued or Other Liabilities, as a component of the foreign currency swap's periodic interest accrual.

The cumulative unrealized gain/loss equals the foreign currency (notional) amount to be received (paid) times the net of the current spot rate minus the spot rate at the time the contract was opened.

(e) Recognition of unrealized gains/losses and amortization of foreign exchange premium/discount on derivatives hedging forecasted transactions or firm commitments shall be deferred until the hedged

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transaction occurs. These deferred gains/losses will adjust the basis or proceeds of the hedged transaction when it occurs;

(f) For hedges where the cost of the foreign currency contract is combined with the hedged item, the statement value on Schedule DB is zero. The fair value of the derivative and hedged item shall be determined and reported separately, either individually or in the aggregate.

(g) The derivative shall be recorded at fair value and a cumulative unrealized gain/loss (surplus adjustment) shall be recognized equal to the difference between the carrying value of the derivative on the balance sheet and the fair value of the derivative if either of the following occur:

(1) During the life of the currency contract, it or a designated portion of the currency contract is not effective as a hedge;

(2) The entity decides to terminate the derivative in advance of scheduled maturity.

iv. Open derivatives hedging items recorded at fair value, where gains and losses on the hedged item are recognized currently in earnings: swaps, collars and forwards shall be valued at current fair value with changes in fair value recognized currently in earnings together with the gains and losses on the hedged item:

(a) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, recognition of changes in fair value through earnings ceases. The derivative shall continue to be valued at its current fair value, but thereafter gains or losses shall be recognized in unrealized gains or unrealized losses to the extent it ceased to be an effective hedge.

c. Cash Flows and Income:

i. Where the cost of the derivative is not combined with the hedged item:

(a) Amortization of premium paid or received on derivatives is an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of the hedged item;

(b) Periodic cash flows and accruals of income/expense are to be reported in a manner consistent with the hedged item, usually as net investment income or another appropriate caption within operating income.

ii. Where the cost of the derivative is combined with the hedged item, the cash flows and income of the derivative on Schedule DB is zero. All related amortization and cash flow accounting shall be reported with the hedged item instead of with the derivative.

d. Gain/Loss on Termination of a swap, collar or forward accounted for under hedge accounting (includes closing, exercise, maturity, and expiry):

i. Exercise – The remaining book value of the derivative shall become an adjustment to the cost or proceeds of the hedged item(s) received or disposed of individually or in aggregate;

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ii. Sale, maturity, expiry, or other closing transaction of a derivative which is an effective hedge – Any gain or loss on the transaction, except for excluded components, will adjust the basis (or proceeds) of the hedged item(s) individually or in aggregate. If a portfolio layer method hedging relationship is discontinued (or partially discontinued) in a voluntary dedesignation or in anticipation of a breach, the basis adjustment associated with the dedesignated amount as of the discontinuation date shall be allocated to the remaining individual assets in the closed portfolio that supported the dedesignated hedged layer using a systematic and rational method. Alternatively, if the item being hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination;

iii. Gain/loss on termination of derivatives will be recognized currently in net income (realized gain/loss) to the extent they ceased to be effective hedges;

iv. Upon the redesignation of a derivative from a currently effective hedging relationship:

(a) With an item(s) carried at amortized cost to another effective hedging relationship with an item(s) carried at amortized cost, the derivative shall continue to be recorded at amortized cost and no gain or loss on the derivative shall be recognized;

(b) With an item(s) carried at amortized cost or fair value to an effective relationship with an item(s) carried at fair value, the accounting for the derivative shall be consistent with (ii) above;

(c) With an item(s) carried at fair value to an effective relationship with an item(s) carried at amortized cost, the accounting for the derivative shall be consistent with (ii) above.

3. Futures (see also discussion in Introduction above):

a. Accounting at Date of Acquisition:

i. Positions in futures contracts shall be initially valued at the amount of cash deposits (i.e., basis or book value of the contract), if any, placed with a broker and either be (a) recorded as an asset (paid) or liability (received) on the Derivative line on the Assets (or) Liabilities pages or (b) combined with the hedged item. Subsequent additions (reductions) in cash deposits plus changes in contract value from date of contract opening (i.e., variation margin) paid (received) will increase (decrease) the book value of the futures contract (hedge accounting).

b. Statement Value:

i. Hedges of Items Recorded at Amortized Cost:

(a) Futures shall be valued at book value;

(b) Book value of open futures contracts need not be amortized;

(c) For hedges where the variation margin portion of the cost of the futures contract is combined with the hedged item, the statement value of the futures contract would be equal to cash deposits outstanding, if any. The

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fair value of the futures contract and the hedged item will be determined and reported separately, either individually or in the aggregate. Fair value on futures contracts is limited to the value of the cash deposits outstanding;

(d) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost (with the variation margin deferred) until (1) the hedged transaction occurs or (2) it is determined that the hedge was not effective (see (e) in this section);

(e) If during the life of the futures contract it or a designated portion of the futures contract is no longer effective as a hedge, hedge accounting for the variation margin ceases. A gain/(loss) equal to the variation margin received (paid) shall be recognized in unrealized gains or unrealized losses (surplus adjustment) to the extent it or a designated portion of the variation margin ceased to be an effective hedge. Statement value will be limited to the cash deposits outstanding, if any, and subsequent changes in the variation margin will be recognized in unrealized gains or unrealized losses (surplus adjustment).

ii. Hedges of Items Recorded at Fair Value (where gains and losses on the hedged item are recognized as adjustments to unassigned funds (surplus)):

(a) Changes in futures contract value from date of contract opening (i.e., variation margin) shall be recognized currently consistent with the hedged item. Statement value will be limited to the cash deposits outstanding, if any;

(b) This will result in unrealized gain/loss treatment with adjustment to unassigned funds (surplus);

(c) For hedges where the variation margin of the futures contract is combined with the hedged item, the fair value of the futures contract and the hedged item will be determined and reported separately, either individually or in the aggregate.

iii. Open foreign currency futures contracts hedging foreign currency exposure on item(s) denominated in a foreign currency and translated into U.S. dollars (where fair value accounting is not being used):

(a) The foreign exchange premium (discount) on the currency contract will be amortized into net investment income over the life of the contract or hedge program. The foreign exchange premium (discount) is defined as the foreign currency (notional) amount to be received (paid) times the net of the forward rate minus the spot rate at the time the contract was opened.

Amortization is not required if the contract was entered into within a year of maturity;

(b) A foreign currency translation adjustment shall be reflected as an unrealized gain/loss (unassigned funds (surplus) adjustment) using the same procedures as is done to translate the hedged item. The cumulative unrealized gain/(loss) which equals the foreign currency (notional) amount to be received (paid) times the net of the current spot rate minus

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the spot rate at the time the contract was opened shall be reported as recognized variation margin;

(c) The statement value of the currency futures contract is book value, including any cash deposits outstanding and increase (decrease) for amortization of foreign exchange (premium) discount plus the foreign exchange translation gain/(loss), which is reported as deferred variation margin;

(d) Recognition of unrealized gains/losses and amortization of foreign exchange premium/discount on derivatives hedging forecasted transactions or firm commitments shall be deferred until the hedged transaction occurs. These deferred gains/losses will adjust the basis or proceeds of the hedged transaction when it occurs;

(e) For hedges where the variation margin of the foreign currency contract is combined with the hedged item, the statement value of the foreign currency contract would equal the cash deposits outstanding, if any. The fair value of the derivative and the hedged item will be determined and reported separately, either individually or in the aggregate. Fair value on futures contracts is limited to the value of the cash deposits outstanding;

(f) If during the life of the currency contract it or a designated portion of the currency contract is not effective as a hedge, valuation at amortized cost ceases. To the extent it ceases to be an effective hedge, an unrealized gain/loss will be recognized equal to the notional amount or a designated portion of the notional amount times the difference between the forward rate available for the remaining maturity of the contract (i.e., the forward rate as of the balance sheet date) and the forward rate at the time it ceased to be an effective hedge.

iv. Open futures hedging items recorded at fair value, where gains and losses on the hedging item are recognized currently in earnings shall be valued at current fair value with changes in fair value recognized currently in earnings:

(a) If during the life of the futures contract it or a designated portion of the futures contract is no longer effective as a hedge, current recognition in earnings of changes in fair value ceases. Prospective changes in the variation margin shall be recognized in unrealized gains or unrealized losses (surplus adjustment) to the extent it or a designated portion of the variation margin ceased to be an effective hedge. Statement value of the derivative will thereafter be limited to the cash deposits outstanding, if any.

c. Gain/Loss on Termination of a futures contract accounted for under hedge accounting:

i. Settlement at maturity of a futures contract—The remaining variation margin of the futures contract shall become an adjustment to the cost or proceeds of the hedged item(s) received, disposed of or held, individually or in aggregate;

ii. Sale, or other closing transaction of a futures contract which is an effective hedge—Any gain or loss on the transaction will adjust the basis (or proceeds) of the hedged item(s) individually or in aggregate. Alternatively, if the item being

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hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination;

iii Gain/loss on termination of futures contracts will be recognized currently in net income (realized gain/loss) to the extent they ceased to be effective hedges;

iv. Upon the redesignation of a derivative from a currently effective hedging relationship:

(a) with an item(s) carried at amortized cost to another effective hedging relationship with an item(s) carried at amortized cost, the derivative shall continue to be recorded at amortized cost and no gain or loss on the derivative shall be recognized;

(b) with an item(s) carried at amortized cost or fair value to an effective relationship with an item(s) carried at fair value, the accounting for the derivative shall be consistent with (ii) above;

(c) with an item(s) carried at fair value to an effective relationship with an item(s) carried at amortized cost, the accounting for the derivative shall be consistent with (ii) above.

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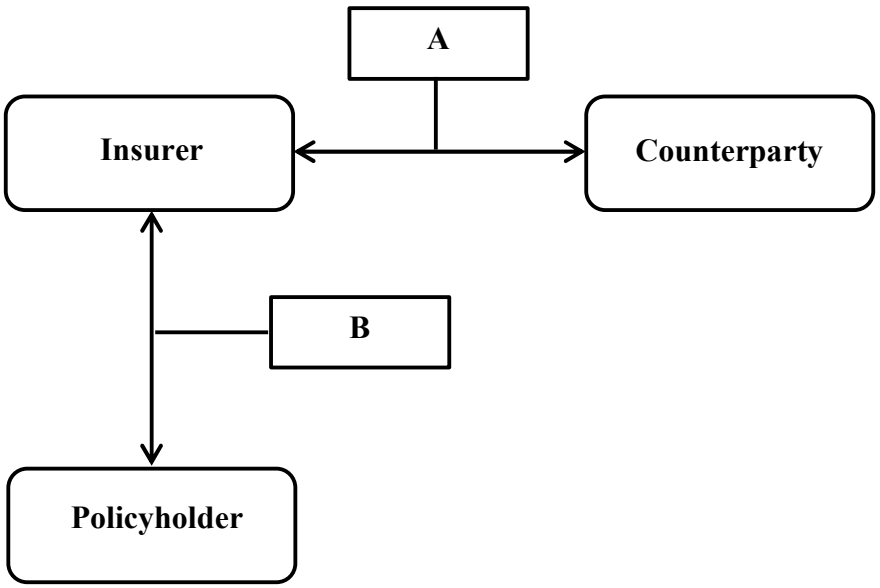
EXHIBIT C – WEATHER DERIVATIVE ILLUSTRATION



A: Security issued directly (or through a broker), in which settlement is based on a climatic or geological variable (i.e., earthquake). This security would meet the definition of a weather derivative (incorporated into SSAP No. 86) and shall be accounted for and reported consistent with other derivatives in SSAP No. 86.

B: A policy issued directly from the insurer to the policyholder in which coverage (and payment of claims) is based on a climatic or geological variable (i.e., earthquake coverage). This would be classified as insurance contract and be subject to the scope exclusion in ASC 815-45-15-2 that is also included in SSAP No. 86.

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Statement of Statutory Accounting Principles No. 90

Impairment or Disposal of Real Estate Investments

STATUS

Type of Issue	Common Area
Issued	June 13, 2005
Effective Date	January 1, 2006
Affects	Supersedes paragraphs 11, 12 and 25 of SSAP No. 40R
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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Long-Lived Assets to Be Disposed of Other Than By Sale 4
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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the impairment or disposal of real estate investments and the treatment of long-lived assets associated with discontinued operations including nonadmitted intangible assets other than goodwill, such as trade names (referred to collectively as long-lived assets). This statement is not intended to conflict with guidance concerning operating results associated with discontinued operations, which is contained in *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items*.

2. This statement supersedes *SSAP No. 40R—Real Estate Investments*, paragraphs 11, 12 and 25.

3. This statement does not apply to (a) goodwill, (b) servicing assets, (c) financial instruments, including investments in equity securities accounted for under the cost or equity method, (d) deferred policy acquisition costs, and (e) deferred tax assets. This statement also does not apply to long-lived assets for which the accounting is prescribed by *FASB Codification 985-20 – Costs of Software to be*

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Sold, Leased or Marketed (ASC 985-20) as adopted with modification to preclude the capitalization of software development costs in *SSAP No. 16R—Electronic Data Processing Equipment and Software*. For a discussion on software development costs, see the guidance also in SSAP No. 16R. Statutory guidance on goodwill is in *SSAP No. 68—Business Combinations and Goodwill*.

SUMMARY CONCLUSION

Recognition and Measurement of an Impairment Loss

4. An impairment loss shall be recognized only if the carrying amount of a long-lived asset is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. That assessment shall be based on the carrying amount of the asset at the date it is tested for recoverability, whether in use or under development. An impairment loss shall be measured as the amount by which the carrying amount of a long-lived asset exceeds its fair value as discussed in paragraph 16.

When to Test a Long-Lived Asset for Recoverability

5. A long-lived asset shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The following are examples of such events or changes in circumstances:

a. A significant decrease in the fair value of a long-lived asset

b. A significant adverse change in the extent or manner in which a long-lived asset is being used or in its physical condition

c. A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset, including an adverse action or assessment by a regulator

d. An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset

e. A current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset

f. A current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

6. Real estate investment properties occupied by the company (per SSAP No. 40R) shall not be subject to recoverability testing under paragraphs 4 and 5 of this statement. However, if any of the following conditions are present, the reporting entity's property occupied by the company on a property by property basis shall be subject to immediate recoverability testing, by determining the fair value of the property using the criteria in SSAP No. 40R, paragraph 13:

a. The financial condition of the reporting entity is in question as described in paragraph 7 of this statement.

b. The property occupied by the company is held for sale as defined in paragraph 21 of this statement.

c. A significant adverse change in the physical condition of the property occupied by the company has occurred.

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d. The management of the reporting entity has voluntarily determined a need for recoverability testing.

7. The following, while not meant to be an all-inclusive listing, are factors, which would indicate that the financial condition of the reporting entity is in question:

a. Entity is subject to regulatory action such as administrative supervision, corrective order based on hazard to policyholders, or substantially similar proceeding, whether voluntary or involuntary;

b. Entity is at any action or control level under Risk Based Capital;

c. Grounds exist for conservation, receivership, rehabilitation or liquidation;

d. Independent certified public accounting report issues a going concern opinion, adverse opinion or disclaimer of opinion.

8. When a long-lived asset is tested for recoverability, it also may be necessary to review depreciation estimates and methods as required by *SSAP No. 3—Accounting Changes and Corrections of Errors*. Any revision to the remaining useful life of a long-lived asset resulting from that review also shall be considered in developing estimates of future cash flows used to test the asset for recoverability. However, any change in the accounting method for the asset resulting from that review shall be made only after applying this statement.

New Cost Basis

9. If an impairment loss is recognized, the adjusted carrying amount of a long-lived asset shall be its new cost basis. For a depreciable long-lived asset, the new cost basis shall be depreciated (amortized) over the remaining useful life of that asset. Restoration of a previously recognized impairment loss is prohibited.

Estimates of Future Cash Flows Used to Test a Long-Lived Asset for Recoverability

10. Estimates of future cash flows used to test the recoverability of a long-lived asset shall include only the future cash flows (cash inflows less associated cash outflows) that are directly associated with, and that are expected to arise as a direct result of, the use and eventual disposition of the asset, however properties occupied by company are exempt from this requirement and should follow the guidance in paragraphs 6 and 7 of this statement. Those estimates shall exclude interest charges that will be recognized as an expense when incurred.

11. Estimates of future cash flows used to test the recoverability of a long-lived asset shall incorporate the entity's own assumptions about its use of the asset and shall consider all available evidence. The assumptions used in developing those estimates shall be reasonable in relation to the assumptions used in developing other information used by the entity for comparable periods, such as internal budgets and projections, accruals related to incentive compensation plans, or information communicated to others. However, if alternative courses of action to recover the carrying amount of a long-lived asset are under consideration or if a range is estimated for the amount of possible future cash flows associated with the likely course of action, reporting entities shall use their best estimate in testing the recoverability of a long-lived asset.

12. Estimates of future cash flows used to test the recoverability of a long-lived asset shall be made for the remaining useful life of the asset to the entity.

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13. Estimates of future cash flows used to test the recoverability of a long-lived asset that is in use, including a long-lived asset for which development is substantially complete, shall be based on the existing service potential of the asset at the date it is tested. The service potential of a long-lived asset encompasses its remaining useful life, cash-flow-generating capacity, and for tangible assets, physical output capacity. Those estimates shall include cash flows associated with future expenditures necessary to maintain the existing service potential of a long-lived asset, including those that replace the service potential of component parts of a long-lived asset (for example, the roof of a building). Those estimates shall exclude cash flows associated with future capital expenditures that would increase the service potential of a long-lived asset.

14. Estimates of future cash flows used to test the recoverability of a long-lived asset that is under development shall be based on the expected service potential of the asset when development is substantially complete. Those estimates shall include cash flows associated with all future expenditures necessary to develop a long-lived asset, including interest payments that will be capitalized as part of the cost of the asset.

15. If a long-lived asset that is under development is in use, estimates of future cash flows used to test the recoverability of that asset shall include the cash flows associated with future expenditures necessary to maintain the existing service potential of the asset as well as the cash flows associated with all future expenditures necessary to substantially complete the asset that is under development.

Fair Value

16. A discussion of fair value is contained in *SSAP No. 100R—Fair Value*. This statement requires real estate investment properties occupied by the company (per SSAP No. 40R), that are determined to be subject to recoverability testing as discussed in paragraphs 6 and 7, to follow the guidance in SSAP No. 40R, paragraph 13.

Long-Lived Assets Categories for Real Estate Investments

17. SSAP No. 40R states that real estate investments shall be reported in the balance sheet categories of properties occupied by the company, properties held for the production of income, and properties held for sale. Accounting guidance in *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets* (FAS 144) distinguishes between long-lived assets to be held and used and long-lived assets to be disposed of. For statutory accounting purposes, long-lived assets to be held and used encompass real estate investments classified under SSAP No. 40R as properties occupied by the company and properties held for the production of income. Further, FAS 144 bifurcates the category of long-lived assets to be disposed of into long-lived assets to be disposed of other than by sale and long-lived assets to be disposed of by sale. Long-lived real estate investments to be disposed of other than by sale shall be classified either as properties occupied by the company or as properties held for the production of income. Long-lived real estate investments to be disposed of by sale shall be classified as properties held for sale.

Long-Lived Assets to Be Disposed of Other Than By Sale

18. A long-lived asset to be disposed of other than by sale (for example, by abandonment, in an exchange measured based on the recorded amount of the nonmonetary asset relinquished, or in a distribution to owners in a spinoff) shall continue to be classified as held and used until disposal. Paragraphs 4-17, and 31-34 shall apply while the asset is classified as held and used. If a long-lived asset is to be abandoned or distributed to owners in a spinoff together with other assets (and liabilities) as a group and that disposal group is a segment, paragraphs 31-34 shall apply to the disposal group at the date of disposal.

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Long-Lived Assets to Be Abandoned

19. For purposes of this statement, a long-lived asset to be abandoned is disposed of when it ceases to be used. If an entity commits to a plan to abandon a long-lived asset before the end of its previously estimated useful life, depreciation estimates shall be revised in accordance with SSAP No. 3 to reflect the use of the asset over its shortened useful life. A long-lived asset that has been temporarily idled shall not be accounted for as if abandoned.

Long-Lived Assets to Be Exchanged or to Be Distributed to Owners in a Spinoff

20. For purposes of this statement, a long-lived asset to be disposed of in an exchange measured based on the recorded amount of the nonmonetary asset relinquished or to be distributed to owners in a spinoff is disposed of when it is exchanged or distributed. If the asset is tested for recoverability while it is classified as held and used, the estimates of future cash flows used in that test shall be based on the use of the asset for its remaining useful life, assuming that the disposal transaction will not occur. In addition to any impairment losses required to be recognized while the asset is classified as held and used, an impairment loss, if any, shall be recognized when the asset is disposed of if the carrying amount of the asset exceeds its fair value[1].

Long-Lived Assets to Be Disposed Of By Sale

Recognition

21. Real estate investment properties classified as held for sale or a long-lived asset to be sold shall be classified as held for sale in the period in which all of the following criteria are met:

a. Management, having the authority to approve the action, commits to a plan to sell the asset.

b. The asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets.

c. An active program to locate a buyer and other actions required to complete the plan to sell the asset have been initiated.

d. The sale of the asset is probable, and transfer of the asset is expected to qualify for recognition as a completed sale, within one year, except as permitted by paragraph 22.

e. The asset is being actively marketed for sale at a price that is reasonable in relation to its current fair value.

f. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

If at any time the criteria in this paragraph are no longer met (except as permitted by paragraph 22), a long-lived asset classified as held for sale shall be reclassified as held and used in accordance with paragraphs 29 and 30.

22. Events or circumstances beyond an entity's control may extend the period required to complete the sale of a long-lived asset beyond one year. An exception to the one-year requirement in paragraph 21.d. shall apply in the following situations in which such events or circumstances arise:

[1] The provisions of this paragraph apply to nonmonetary exchanges that are not recorded at fair value under the provisions of *SSAP No. 95—Nonmonetary Transactions*.

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a. If at the date an entity commits to a plan to sell a long-lived asset the entity reasonably expects that others (not a buyer) will impose conditions on the transfer of the asset that will extend the period required to complete the sale and (1) actions necessary to respond to those conditions cannot be initiated until after a firm purchase commitment is obtained and (2) a firm purchase commitment is probable within one year.

b. If an entity obtains a firm purchase commitment and, as a result, a buyer or others unexpectedly impose conditions on the transfer of a long-lived asset previously classified as held for sale that will extend the period required to complete the sale and (1) actions necessary to respond to the conditions have been or will be initiated in a timely manner and (2) a favorable resolution of the delaying factors is expected.

c. If during the initial one-year period, circumstances arise that previously were considered unlikely and, as a result, a long-lived asset previously classified as held for sale is not sold by the end of that period and (1) during the initial one-year period the entity initiated actions necessary to respond to the change in circumstances, (2) the asset is being actively marketed at a price that is reasonable given the change in circumstances, and (3) the criteria in paragraph 21 are met.

23. A long-lived asset that is newly acquired and that will be sold rather than held and used shall be classified as held for sale at the acquisition date only if the one-year requirement in paragraph 21.d. is met (except as permitted by paragraph 22) and any other criteria in paragraph 21 that are not met at that date are probable of being met within a short period following the acquisition (usually within three months).

24. If the criteria in paragraph 21 are met after the balance sheet date but before issuance of the financial statements, a long-lived asset shall continue to be classified as held and used in those financial statements when issued. The information required by paragraph 36 shall be disclosed in the notes to the financial statements. If the asset is tested for recoverability (on a held-and-used basis) as of the balance sheet date, the estimates of future cash flows used in that test shall consider the likelihood of possible outcomes that existed at the balance sheet date, including the assessment of the likelihood of the future sale of the asset. That assessment made as of the balance sheet date shall not be revised for a decision to sell the asset after the balance sheet date. An impairment loss, if any, to be recognized shall be measured as the amount by which the carrying amount of the asset exceeds its fair value at the balance sheet date.

Measurement

25. Real estate investment properties classified as held for sale or a long-lived asset to be sold shall be measured at the lower of its carrying amount or fair value less encumbrances and estimated costs to sell the property. If the asset is newly acquired, the carrying amount of the asset shall be established based on its fair value less encumbrances and estimated costs to sell the property at the acquisition date. A long-lived asset shall not be depreciated (amortized) while it is classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal classified as held for sale shall continue to be accrued.

26. Costs to sell are the incremental direct costs to transact a sale, that is, the costs that result directly from and are essential to a sale transaction and that would not have been incurred by the entity had the decision to sell not been made. Those costs include broker commissions, legal and title transfer fees, and closing costs that must be incurred before legal title can be transferred.

27. The carrying amounts of any assets that are not covered by this statement that are included in a disposal classified as held for sale shall be adjusted in accordance with other applicable statements of statutory accounting principles prior to measurement.

28. A realized loss shall be recognized in the summary of operations for any initial or subsequent write-down to fair value less cost to sell. A gain shall not be recognized for any subsequent increase in

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fair value less cost to sell until the asset is sold. The loss shall adjust only the carrying amount of a long-lived asset, whether classified as held for sale individually or as part of a disposal group. A gain or loss not previously recognized that results from the sale of a long-lived asset shall be recognized at the date of sale.

Changes to a Plan of Sale

29. If circumstances arise that previously were considered unlikely and, as a result, an entity decides not to sell a long-lived asset previously classified as held for sale, the asset shall be reclassified as held and used. A long-lived asset that is reclassified shall be measured individually at the lower of its (a) carrying amount before the asset was classified as held for sale, adjusted for any depreciation (amortization) expense that would have been recognized had the asset been continuously classified as held and used, or (b) fair value at the date of the subsequent decision not to sell.

30. Any required adjustment to the carrying amount of a long-lived asset that is reclassified as held and used shall be included in income from continuing operations in the period of the subsequent decision not to sell. That adjustment shall be reported in the same income statement caption used to report a loss, if any, recognized in accordance with paragraph 31.

Reporting Long-Lived Assets and Disposal Groups to Be Disposed Of

Reporting Disposal Gains or Losses in Operations

31. Any disposal gain or loss recognized for long-lived assets shall be included as a net realized gain or loss in the summary of operations.

Reporting a Long-Lived Asset or Disposal Group Classified as Held for Sale

32. The results of operations of a segment that either has been disposed of or is classified as held for sale shall be reported consistently with the entity's reporting of continuing operations.

33. A long-lived asset classified as held for sale shall be presented separately in the balance sheet. The assets and liabilities of a disposal classified as held for sale shall be presented separately in the asset and liability sections, respectively, of the balance sheet. Those assets and liabilities shall not be offset and presented as a single amount. The major classes of assets and liabilities classified as held for sale, in the case of real estate shall be separately disclosed either on the face of the balance sheet or in the notes to financial statements (paragraph 36).

Reporting Impairment Losses

34. Any impairment loss recognized on long-lived assets shall be recorded in the summary of operations as a realized loss.

Disclosures

35. The following information shall be disclosed in the notes to the financial statements that include the period in which an impairment loss is recognized:

a. A description of the impaired assets and the facts and circumstances leading to the impairment;

b. The amount of the impairment loss and how fair value was determined; and

c. The caption in the summary of operations which includes the impairment loss.

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36. The following information shall be disclosed in the notes to the financial statements that cover the period in which a long-lived asset either has been sold or is classified as held for sale:

a. A description of the facts and circumstances leading to the expected disposal, the expected manner and timing of that disposal.

b. If applicable, the gain or loss recognized and if not separately presented on the face of the summary of operations, the caption in the summary of operations that includes that gain or loss.

37. If paragraph 29 applies, a description of the facts and circumstances leading to the decision to change the plan to sell the asset; and its effect on the results of operations for the period and any prior periods presented shall be disclosed in the notes to financial statements that include the period of that decision.

Relevant Literature

38. FAS 144 supersedes *FASB Statement No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of* (FAS 121) and in part *Accounting Principles Board Opinion No. 30, Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*. FAS 144 retains the requirements of FAS 121 to (a) recognize an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows and (b) measure an impairment loss as the difference between the carrying amount and fair value of the asset. FAS 144 requires that a long-lived asset to be abandoned, exchanged for a similar productive asset, or distributed to owners in a spinoff be considered held and used until it is disposed of. FAS 144 also sets forth that the accounting model for long-lived assets to be disposed of by sale is used for all long-lived assets, whether previously held and used or newly acquired. FAS 144 also resolves implementation issues that came about in the application of existing guidance. This statement adopts with modification *FAS 153, Exchanges of Nonmonetary Assets, An Amendment of APB Opinion No. 29* (FAS 153) for the accounting guidance of long-lived assets to be disposed of other than by sale addressed in paragraphs 18-20.

39. This statement adopts FAS 144 with modification to paragraphs 9, 17, 18, 19, 21, 25, 28, 35, 36, 37, 41, 42, 44, 45 and 47. Further, this statement rejects paragraphs 10-14, paragraphs 22-24, 26.d., and 43 of FAS 144. Refer to paragraph 40 of this statement for additional information with regard to these paragraphs.

40. The modifications to FAS 144 were made in order to maintain consistency with current statutory accounting principles and the Statement of Concepts:

a. Paragraph 9 is amended to require that changes in depreciation estimates and methods and amortization periods found as a result of a test for recoverability should be accounted for in accordance with SSAP No. 3;

b. Paragraphs 10-14, which address the grouping of assets, are rejected, as reporting entities should apply the guidance in this statement to each of its assets on an individual basis;

c. Paragraphs 17, 18, 19 and 21 discuss estimates of future cash flows used to test the recoverability of a long-lived asset, and states that a probability-weighted approach may be useful in considering the likelihood of those possible outcomes. For statutory accounting purposes, reporting entities shall use their best estimate in testing the recoverability of a long-lived asset;

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d. Paragraphs 22-24, which discuss fair value, are rejected. The definition of fair value is in *SSAP No. 100R—Fair Value*.

e. Paragraph 25 is amended to require that an impairment loss on properties occupied by the company and properties held for the production of income shall be recorded in the summary of operations as a realized loss;

f. Paragraph 28 is amended to require that changes in depreciation estimates shall be accounted for in accordance with SSAP No. 3;

g. If the sale is expected to occur beyond one year, paragraph 35 allows the cost to sell to be discounted. For statutory accounting purposes, the cost to sell shall not be discounted;

h. Paragraph 35 allows for expected future losses associated with the operations of a long-lived asset (disposal group) while it is held for sale to be excluded from the costs to sell. For statutory accounting purposes, the cost to sell shall be calculated in accordance with SSAP No. 24, paragraphs 5 and 6.

i. Paragraph 36 is amended to remove the reference to goodwill, as FAS 144 does not include goodwill within its scope unless such goodwill is included in an asset group that is or includes a reporting unit; paragraph 40.n. of this statement does not recognize a reporting unit. Paragraph 36 is further amended to require reporting entities to adjust all assets in accordance with other applicable statements of statutory accounting principles prior to measurement;

j. Paragraph 37 is amended to clarify that losses recognized as a result of adjustments to fair value less cost to sell shall be recorded in the summary of operations as a realized gain/loss. Paragraph 37 is also modified to disallow the recognition of any gain for subsequent increases in fair value less cost to sell until the asset is sold. This is consistent with the concept of conservatism found in the Statement of Concepts;

k. Paragraph 42 is amended to state that the results of operations of a discontinued operation shall be reported consistently with the entity's reporting of continuing operations. This is consistent with the guidance found in paragraph 7 of SSAP No. 24;

l. Paragraph 44 is amended to state that adjustments to amounts previously reported related to continuing operations shall be reported consistently with the entity's reporting of continuing operations. This is consistent with the guidance found in paragraph 7 of SSAP No. 24. In addition, paragraphs 44.a. through 44.c. are adopted into paragraph 7 of SSAP No. 24;

m. Paragraph 45 is amended to state that a gain or loss on an asset classified as held for sale that has been disposed of shall be included in the summary of operations as a realized gain or loss;

n. The disclosures in paragraphs 47.a. and 47.b. are adopted with respect to properties held for sale, except for the disclosures related to major classes of assets, as grouping has been rejected in this statement. Paragraphs 47.c. and 47.d. are rejected as such paragraphs relate to discontinued operations and segment reporting. The disclosures included in paragraphs 11-15 of SSAP No. 24 are more appropriate given the differences between statutory and generally accepted accounting principles reporting of discontinued operations;

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o. Paragraph 26.d. requires the disclosure of the segment in which an impaired asset is reported. This paragraph is rejected, as statutory accounting requires accounting and reporting at the legal entity level. Further, any additional references to segments, reporting units, or disposal groups found in FAS 144 are also rejected, except with regard to a segment within the context of discontinued operations; and

p. Paragraph 43 is rejected and the guidance related to the recognition of losses/income expected between the measurement date and the expected disposal date included in paragraphs 5 and 6 of SSAP No. 24 is retained, as such guidance is consistent with the concept of conservatism in the Statement of Concepts.

41. *FASB Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets* (FAS 144) supersedes FAS 121, but specifically scopes out the concept of goodwill. Paragraphs 12-14 of FAS 121 address the impairment of goodwill and paragraphs 12, 14.a. and 14.b. of FAS 121 were adopted in SSAP No. 68. However, paragraph 12 of FAS 121 was superseded by *FASB Statement No. 142, Goodwill and Other Intangible Assets* (FAS 142), which was rejected in SSAP No. 68. Given the applicability of the guidance found in paragraph 12 of FAS 121 to statutory accounting principles, the impairment guidance found in FAS 121, paragraph 12 is retained. Paragraph 12 of FAS 121 has been excerpted in *Issue Paper No. 68—Business Combinations and Goodwill*, paragraph 31. This statement rejects *ASU 2017-04, Simplifying the Test for Goodwill Impairment*, *ASU 2014-02, Accounting for Goodwill (a consensus of the private Company Council)*, *ASU 2012-02, Testing Indefinite-Lived Intangible Assets for Impairment*, *ASU 2011-08, Testing Goodwill for Impairment* and *ASU 2010-28, When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts.*

Effective Date and Transition

42. The provisions of this statement shall be applied to all assets on the books of the reporting entity within the scope of this statement for reporting periods beginning on and after January 1, 2006. The guidance within paragraphs 18-20 was originally amended with the adoption of SSAP No. 95, included in that statement, and effective for fiscal periods beginning after January 1, 2007. The original guidance included in this SSAP with tracked changes showing the amendments from SSAP No. 95 are retained for historical purposes within Issue Paper No. 127.

REFERENCES

Other

- *Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy*
- *SSAP No. 3—Accounting Changes and Corrections of Errors*
- *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items*
- *SSAP No. 40R—Real Estate Investments*

Relevant Issue Papers

- *Issue Paper No. 121—Accounting for the Impairment or Disposal of Real Estate Investments*
- *Issue Paper No. 127—Exchanges of Nonmonetary Assets, A Replacement of SSAP No. 28—Nonmonetary Transactions*

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Statement of Statutory Accounting Principles No. 92

Postretirement Benefits Other Than Pensions

STATUS

Type of Issue	Common Area
Issued	Finalized March 3, 2012
Effective Date	January 1, 2013
Affects	Supersedes SSAP No. 14; Nullifies INT 99-26, INT 01-16 and INT 13-03
Affected by	No other pronouncements
Interpreted by	INT 04-17
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **2**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles and related reporting for employers' postretirement plans other than pensions.

2. This statement applies to all postretirement benefits expected to be provided by an employer to current and former employees (including retirees, disabled employees, and other former employees who are expected to receive postretirement benefits), their beneficiaries, and covered dependents, pursuant to the terms of an employer's undertaking to provide those benefits. Other postretirement benefits include, but are not limited to, postretirement health care; life insurance provided outside a pension plan to retirees; and other welfare benefits such as tuition assistance, day care, legal services, and housing subsidies provided after retirement. Often those benefits are in the form of a reimbursement to plan participants or direct payment to providers for the cost of specified services as the need for those services arises, but they may also include benefits payable as a lump sum, such as death benefits. Much of the guidance in this statement focuses on postretirement health care plans. Nevertheless, this statement applies equally to all postretirement benefits other than pensions. A postretirement benefit plan may be part of a larger plan or arrangement that provides benefits currently to active employees as well as to retirees. In those circumstances, the promise to provide benefits to present and future retirees under the plan shall be segregated from the promise to provide benefits currently to active employees and shall be accounted for in accordance with the provisions of this statement. Absent evidence to the contrary, it shall be presumed that an employer that has provided postretirement benefits in the past or is currently promising those benefits to employees will continue to provide those future benefits. This statement supersedes the guidance in *SSAP No. 14—Postretirement Plans Other Than Pensions*, nullifies and incorporates the guidance in *INT 99-26: Offsetting Pension Assets and Liabilities* and nullifies *INT 01-16: Measurement Date for SSAP No. 8 Actuarial Valuations*.

SUMMARY CONCLUSION

Single-Employer Defined Benefit Postretirement Plans

3. A defined benefit postretirement plan is one that defines the postretirement benefits in terms of (a) monetary amounts or (b) benefit coverage to be provided. In some cases, an employer may limit its obligation through an individual or an aggregate "cap" on the employer's cost or benefit obligation. Plans of that nature are considered to be defined benefit postretirement plans. (Hybrid postretirement plans or "cash-balance" plans are considered defined benefit plans for purposes of applying this statement.) For defined benefit plans, reporting entities shall adopt *FAS 158: Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132 (R)* (FAS 158) and *FASB Staff Position FAS 136(R)-1, Employers' Disclosures about Postretirement Benefit Plan Assets* (FSP FAS 136(R)-1) with modifications as discussed in paragraph 102.

4. A postretirement benefit is part of the compensation paid to an employee for services rendered. In a defined benefit plan, the employer promises to provide, in addition to current wages and benefits, future benefits during retirement. Generally, the amount of those benefits depends on the benefit formula (which may include factors such as the number of years of service rendered or the employee's compensation before retirement or termination), the longevity of the retiree and any beneficiaries and covered dependents, and the incidence of events requiring benefit payments (for example, illnesses affecting the amount of health care required). In most cases, services are rendered over a number of years before an employee retires and begins to receive benefits or is entitled to receive benefits as a need arises. Even though the services rendered by the employee are complete and the employee has retired, the total amount of benefits the employer has promised and the cost to the employer of the services rendered are not precisely determinable but can be estimated using the plan's benefit formula and estimates of the effects of relevant future events.

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Elements of Accounting for Postretirement Benefits

5. Any method of accounting that recognizes the cost of postretirement benefits over employee service periods (before the payment of benefits to retirees) must deal with two factors that stem from the nature of the arrangement. First, estimates or assumptions must be made about the future events that will determine the amount and timing of the benefit payments. Second, an attribution approach that assigns benefits and the cost of those benefits to individual years of service must be selected.

6. The expected postretirement benefit obligation for an employee is the actuarial present value as of a particular date of the postretirement benefits expected to be paid by the employer's plan to or for the employee, the employee's beneficiaries, and any covered dependents pursuant to the terms of the plan. Measurement of the expected postretirement benefit obligation is based on the expected amount and timing of future benefits, taking into consideration the expected future cost of providing the benefits and the extent to which those costs are shared by the employer, the employee (including consideration of contributions required during the employee's active service period and following retirement, deductibles, coinsurance provisions, and so forth), or others (such as through governmental programs).

7. The accumulated postretirement benefit obligation as of a particular date is the actuarial present value of all future benefits attributed to an employee's service rendered to that date pursuant to paragraphs 30-31 and 42-45, assuming the plan continues in effect and that all assumptions about future events are fulfilled. Prior to the date on which an employee attains full eligibility for the benefits that employee is expected to earn under the terms of the postretirement benefit plan (the full eligibility date), the accumulated postretirement benefit obligation for an employee is a portion of the expected postretirement benefit obligation. On and after the full eligibility date, the accumulated postretirement benefit obligation and the expected postretirement benefit obligation for an employee are the same. Determination of the full eligibility date is affected by plan terms that provide incremental benefits expected to be received by or on behalf of an employee for additional years of service, unless those incremental benefits are trivial. Determination of the full eligibility date is not affected by plan terms that define when benefit payments commence or by an employee's current dependency status.

8. Net periodic postretirement benefit cost comprises several components that reflect different aspects of the employer's financial arrangements. The service cost component of net periodic postretirement benefit cost is the actuarial present value of benefits attributed to services rendered by employees during the period (the portion of the expected postretirement benefit obligation attributed to service in the period). The service cost component is the same for an unfunded plan, a plan with minimal funding, and a well-funded plan. The other components of net periodic postretirement benefit cost are interest cost (interest on the accumulated postretirement benefit obligation, which is a discounted amount), actual return on plan assets[1], amortization of any prior service cost or credit included in unassigned funds (surplus), amortization of the transition obligation or transition asset, and the gain or loss component which includes, to the extent recognized, amortization of the net gain or loss included in unassigned funds (surplus) (refer to paragraph 49).

[1] To address a question on how the expected return on plan assets affects the determination of net periodic benefit cost if the actual return on plan assets for a period is a component of net periodic benefit cost, it is noted that the expected return on plan assets generally will be different from the actual return on plan assets for the year. This statement provides for recognition of that difference (a net gain or loss) in unassigned funds in the period it arises. The amount recognized in unassigned funds is also a component of net periodic benefit cost for the current period. Thus, the amount recognized in unassigned funds and the actual return on plan assets, when aggregated, equal the expected return on plan assets. The amount recognized in unassigned funds affects future net periodic benefit cost through subsequent amortization, if any, of the net gain or loss. (This footnote reflects guidance included in E12 of FSP FAS 158-1.)

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Measurement of Cost and Obligations[2]

Accounting for the Substantive Plan

9. An objective of this statement is that the accounting reflects the terms of the exchange transaction that takes place between an employer that provides postretirement benefits and the employees who render services in exchange for those benefits, as those terms are understood by both parties to the transaction. Generally, the extant written plan provides the best evidence of the terms of that exchange transaction. However, in some situations, an employer's cost-sharing policy, as evidenced by past practice or by communication of intended changes to a plan's cost-sharing provisions, or a past practice of regular increases in certain monetary benefits may indicate that the substantive plan—the plan as understood by the parties to the exchange transaction—differs from the extant written plan. The substantive plan shall be the basis for the accounting.

10. Except as provided in paragraph 11, an employer's cost-sharing policy, as evidenced by the following past practice or communication, shall constitute the cost-sharing provisions of the substantive plan if either of the following conditions exist. Otherwise, the extant written plan shall be considered to be the substantive plan.

a. The employer has a past practice of (1) maintaining a consistent level of cost sharing between the employer and its retirees through changes in deductibles, coinsurance provisions, retiree contributions, or some combination of those changes or (2) consistently increasing or reducing the employer's share of the cost of the covered benefits through changes in retired or active plan participants' contributions toward their retiree health care benefits, deductibles, coinsurance provisions, out-of-pocket limitations, and so forth, in accordance with the employer's established cost-sharing policy.

b. The employer has the ability, and has communicated to affected plan participants its intent, to institute different cost-sharing provisions at a specified time or when certain conditions exist (for example, when health care cost increases exceed a certain level).

11. An employer's past practice of maintaining a consistent level of cost sharing with its retirees or consistently increasing or reducing its share of the cost of providing the covered benefits shall not constitute provisions of the substantive plan if accompanied by identifiable offsetting changes in other benefits or compensation or if the employer incurred significant costs, such as work stoppages, to effect that cost-sharing policy. Similarly, an employer's communication of its intent to institute cost-sharing provisions that differ from the extant written plan or the past cost-sharing practice shall not constitute provisions of the substantive plan (a) if the plan participants would be unwilling to accept the change without adverse consequences to the employer's operations or (b) if other modifications of the plan, such as the level of benefit coverage, or providing offsetting changes in other benefits, such as pension benefits, would be required to gain plan participants' acceptance of the change to the cost-sharing arrangement.

12. A past practice of regular increases in postretirement benefits defined in terms of monetary amounts may indicate that the employer has a present commitment to make future improvements to the

[2] In addition to a properly weighted average rate, an entity may elect to measure the service cost and interest cost components of net periodic benefit cost by using individual spot rates derived from an acceptable high-quality corporate bond yield curve and matched with separate cash flows for each future year (also known as the spot rate approach). If the election is made to switch from a weighted-average approach to the spot rate approach, this approach shall be consistently applied to all defined benefit plans and to the measurement of both service and interest cost. This change shall be reflected as a change in estimate as prescribed in *SSAP No. 3—Accounting Changes and Corrections of Errors* and once changed; the company should not revert back to the weighted-average discount rate in future periods. This change in estimate shall be appropriately disclosed in accordance with this statement, SSAP No. 3 and the Preamble.

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plan and that the plan will provide monetary benefits attributable to prior service that are greater than the monetary benefits defined by the extant written plan. In those situations, the substantive commitment to increase those benefits shall be the basis for the accounting. Changes in the benefits, other than benefits defined in terms of monetary amounts, covered by a postretirement health care plan or by other postretirement benefit plans shall not be anticipated.

13. Contributions expected to be received from active employees toward the cost of their postretirement benefits and from retired plan participants are treated similarly for purposes of measuring an employer's expected postretirement benefit obligation. That obligation is measured as the actuarial present value of the benefits expected to be provided under the plan, reduced by the actuarial present value of contributions expected to be received from the plan participants during their remaining active service and postretirement periods. In determining the amount of the contributions expected to be received from those participants toward the cost of their postretirement benefits, consideration is given to any related substantive plan provisions, such as an employer's past practice of consistently increasing or reducing the contribution rates as described in paragraphs 10-11. An obligation to return contributions received from employees who do not attain eligibility for postretirement benefits and, if applicable, any interest accrued on those contributions shall be recognized as a component of an employer's postretirement benefit obligation.

14. Automatic benefit changes specified by the plan that are expected to occur shall be included in measurements of the expected and accumulated postretirement benefit obligations and the service cost component of net periodic postretirement benefit cost. Also, plan amendments shall be included in the computation of the expected and accumulated postretirement benefit obligations once they have been contractually agreed to, even if some provisions take effect only in future periods. For example, if a plan amendment grants a different benefit level for employees retiring after a future date, that increased or reduced benefit level shall be included in current-period measurements for employees expected to retire after that date.

15. Measuring the net periodic postretirement benefit cost and accumulated postretirement benefit obligation based on best estimates is superior to implying, by a failure to accrue, that no cost or obligation exists prior to the payment of benefits. This statement requires the use of explicit assumptions, each of which individually represents the best estimate of a particular future event, to measure the expected postretirement benefit obligation. A portion of that expected postretirement benefit obligation is attributed to each period of an employee's service associated with earning the postretirement benefits, and that amount is accrued as service cost for that period.

16. The service cost component of postretirement benefit cost, any prior service cost, and the accumulated postretirement benefit obligation are measured using actuarial assumptions and present value techniques to calculate the actuarial present value of the expected future benefits attributed to periods of employee service. Each assumption used shall reflect the best estimate solely with respect to that individual assumption. All assumptions shall presume that the plan will continue in effect in the absence of evidence that it will not continue. Principal actuarial assumptions include the time value of money (discount rates); participation rates (for contributory plans); retirement age; factors affecting the amount and timing of future benefit payments, which for postretirement health care benefits consider past and present per capita claims cost by age, health care cost trend rates, Medicare reimbursement rates, and so forth; salary progression (for pay-related plans); and the probability of payment (turnover, dependency status, mortality, and so forth).

17. Assumed discount rates shall reflect the time value of money as of the measurement date in determining the present value of future cash outflows currently expected to be required to satisfy the postretirement benefit obligation. In making that assumption, employers shall look to rates of return on high-quality fixed-income investments currently available whose cash flows match the timing and amount of expected benefit payments. If settlement of the obligation with third-party insurers is possible (for example, the purchase of nonparticipating life insurance contracts to provide death benefits), the interest

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rates inherent in the amount at which the postretirement benefit obligation could be settled are relevant in determining the assumed discount rates. Assumed discount rates are used in measurements of the expected and accumulated postretirement benefit obligations and the service cost and interest cost components of net periodic postretirement benefit cost.

18. Pursuant to paragraph 17, an employer shall look to rates of return on high-quality fixed-income investments in determining assumed discount rates. The objective of selecting assumed discount rates using that method is to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments, would provide the necessary future cash flows to pay the postretirement benefits when due. Notionally, that single amount, the accumulated postretirement benefit obligation, would equal the current fair value of a portfolio of high-quality zero coupon bonds whose maturity dates and amounts would be the same as the timing and amount of the expected future benefit payments. Because cash inflows would equal cash outflows in timing and amount, there would be no reinvestment risk in the yields to maturity of the portfolio. However, in other than a zero coupon portfolio, such as a portfolio of long-term debt instruments that pay semiannual interest payments or whose maturities do not extend far enough into the future to meet expected benefit payments, the assumed discount rates (the yield to maturity) need to incorporate expected reinvestment rates available in the future. Those rates shall be extrapolated from the existing yield curve at the measurement date. The determination of the assumed discount rate is separate from the determination of the expected rate of return on plan assets whenever the actual portfolio differs from the hypothetical portfolio described above. Assumed discount rates shall be reevaluated at each measurement date. If the general level of interest rates rises or declines, the assumed discount rates shall change in a similar manner.

19. The expected long-term rate of return on plan assets shall reflect the average rate of earnings expected on the existing assets that qualify as plan assets and contributions to the plan expected to be made during the period. In estimating that rate, appropriate consideration should be given to the returns being earned on the plan assets currently invested and the rates of return expected to be available for reinvestment. If the return on plan assets is taxable to the trust or other fund under the plan, the expected long-term rate of return shall be reduced to reflect the related income taxes expected to be paid under existing law. There is no assumption of an expected long-term rate of return on plan assets for plans that are unfunded or that have no assets that qualify as plan assets pursuant to this statement.

20. The service cost component of net periodic postretirement benefit cost and the expected and accumulated postretirement benefit obligations shall reflect future compensation levels to the extent the postretirement benefit formula defines the benefits wholly or partially as a function of future compensation levels. For pay-related plans, assumed compensation levels shall reflect the best estimate of the actual future compensation levels of the individual employees involved, including future changes attributed to general price levels, productivity, seniority, promotion, and other factors. All assumptions shall be consistent to the extent that each reflects expectations about the same future economic conditions, such as future rates of inflation. Measuring service cost and the expected and accumulated postretirement benefit obligations based on estimated future compensation levels entails considering any indirect effects, such as benefit limitations, that would affect benefits provided by the plan.

Assumptions Unique to the Postretirement Health Care Benefits

21. Measurement of an employer's postretirement health care obligation requires the use of several assumptions unique to health care benefits. Most significantly, it includes several assumptions about factors that will affect the amount and timing of future benefit payments for postretirement health care. Those factors include consideration of historical per capita claims cost by age, health care cost trend rates (for plans that provide a benefit in kind), and medical coverage to be paid by governmental authorities and other providers of health care benefits.

22. In principle, an employer's share of the expected future postretirement health care cost for a plan participant is developed by reducing the assumed per capita claims cost at each age at which the plan

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participant is expected to receive benefits under the plan by (a) the effects of coverage by Medicare(INT 04-17) and other providers of health care benefits, and (b) the effects of the cost-sharing provisions of the plan (deductibles, copayment provisions, out-of-pocket limitations, caps on the limits of the employer-provided payments, and retiree contributions). The resulting amount represents the assumed net incurred claims cost at each age at which the plan participant is expected to receive benefits under the plan. If contributions are required to be paid by active plan participants toward their postretirement health care benefits, the actuarial present value of the plan participants' future contributions reduces the actuarial present value of the aggregate assumed net incurred claims costs.

23. The assumed per capita claims cost by age is the annual per capita cost, for periods after the measurement date, of providing the postretirement health care benefits covered by the plan from the earliest age at which an individual could begin to receive benefits under the plan through the remainder of the individual's life or the covered period, if shorter. The assumed per capita claims cost shall be the best estimate of the expected future cost of the benefits covered by the plan. It may be appropriate to consider other factors in addition to age, such as sex and geographical location, in developing the assumed per capita claims cost.

24. Past and present claims data for the plan, such as a historical pattern of gross claims by age (claims curve), should be used in developing the current per capita claims cost to the extent that those data are considered to be indicative of the current cost of providing the benefits covered by the plan. Those current claims data shall be adjusted by the assumed health care cost trend rate. The resulting assumed per capita claims cost by age, together with the plan demographics, determines the amount and timing of expected future gross eligible charges.

25. In the absence of sufficiently reliable plan data about the current cost of the benefits covered by the plan, the current per capita claims cost should be based, entirely or in part, on the claims information of other employers to the extent those costs are indicative of the current cost of providing the benefits covered by the plan. For example, the current per capita claims cost may be based on the claims experience of other employers derived from information in data files developed by insurance companies, actuarial firms, or employee benefits consulting firms. The current per capita claims cost developed on those bases shall be adjusted to best reflect the terms of the employer's plan and the plan demographics. For example, the information should be adjusted, as necessary, for differing demographics, such as the age and sex of plan participants, health care utilization patterns by men and women at various ages, and the expected geographical location of retirees and their dependents, and for significant differences between the nature and types of benefits covered by the employer's plan and those encompassed by the underlying data.

26. The assumption about health care cost trend rates represents the expected annual rates of change in the cost of health care benefits currently provided by the postretirement benefit plan, due to factors other than changes in the demographics of the plan participants, for each year from the measurement date until the end of the period in which benefits are expected to be paid. Past and current health care cost trends shall be used in developing an employer's assumed health care cost trend rates, which implicitly consider estimates of health care inflation, changes in health care utilization or delivery patterns, technological advances, and changes in the health status of plan participants. Differing services, such as hospital care and dental care, may require the use of different health care cost trend rates. It is appropriate for that assumption to reflect changes in health care cost trend rates over time. For example, the health care cost trend rates may be assumed to continue at the present level for the near term, or increase for a period of time, and then grade down over time to an estimated health care cost trend rate ultimately expected to prevail.

27. Certain medical claims may be covered by governmental programs under existing law or by other providers of health care benefits. Benefit coverage by those governmental programs shall be assumed to continue as provided by the present law and by other providers pursuant to their present plans. Presently enacted changes in the law or amendments of the plans of other health care providers that take effect in

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future periods and that will affect the future level of their benefit coverage shall be considered in current-period measurements for benefits expected to be provided in those future periods. Future changes in laws concerning medical costs covered by governmental programs and future changes in the plans of other providers shall not be anticipated.

28. In some cases, determining the assumed per capita claims cost by age as described in paragraphs 23-25 may not be practical because credible historical information about the gross per capita cost of covered benefits may not be available or determinable to satisfy the stated measurement approach. However, credible historical information about incurred claims costs may be available. In those cases, an alternative method of developing the assumed per capita claims cost may be used provided the method results in a measure that is the best estimate of the expected future cost of the benefits covered by the plan. For example, the assumed health care cost trend rates may be determined by adjusting the expected change in the employer's share of per capita incurred claims cost by age by a factor that reflects the effects of the plan's cost-sharing provisions. However, an approach that projects net incurred claims costs using unadjusted assumed health care cost trend rates would implicitly assume changes in the plan's cost-sharing provisions at those assumed rates and, therefore, is not acceptable unless the plan's cost-sharing provisions are indexed in that manner or the substantive plan operates in that manner.

29. Assumed discount rates include an inflationary element that reflects the expected general rate of inflation. Assumed compensation levels include consideration of future changes attributable to general price levels. Similarly, assumed health care cost trend rates include an element that reflects expected general rates of inflation for the economy overall and an element that reflects price changes of health care costs in particular. To the extent that those assumptions consider similar inflationary effects, the assumptions about those effects shall be consistent.

Attribution

30. An equal amount of the expected postretirement benefit obligation for an employee generally shall be attributed to each year of service in the attribution period (a benefit/years-of-service approach). However, some plans may have benefit formulas that attribute a disproportionate share of the expected postretirement benefit obligation to employees' early years of service. For that type of plan, the expected postretirement benefit obligation shall be attributed in accordance with the plan's benefit formula.

31. The beginning of the attribution period generally shall be the date of hire. However, if the plan's benefit formula grants credit only for service from a later date and that credited service period is not nominal in relation to employees' total years of service prior to their full eligibility dates, the expected postretirement benefit obligation shall be attributed from the beginning of that credited service period. In all cases, the end of the attribution period shall be the full eligibility date.

Recognition of Liabilities and Assets

32. An employer that sponsors one or more single-employer defined benefit postretirement plans other than pensions shall recognize in its statement of financial position the funded statuses of those plans. The status for each plan shall be measured as the difference between the fair value of plan assets and the accumulated postretirement benefit obligation (considering both vested and nonvested employees) as it is defined in this statement.

33. The employer shall aggregate the statuses of all overfunded plans and recognize that amount as a nonadmitted asset in its statement of financial position. It also shall aggregate the statuses of all underfunded plans and recognize that amount as a liability in its statement of financial position. It is not acceptable statutory accounting practice to offset pension or postretirement benefits other than pensions liability generated by one plan against the prepaid assets of another plan.

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Recognition of Net Periodic Postretirement Benefit Cost

34. As with other forms of deferred compensation, the cost of providing postretirement benefits shall be attributed to the periods of employee service rendered in exchange for those future benefits pursuant to the terms of the plan. That cost notionally represents the change in the unfunded accumulated postretirement benefit obligation for the period, ignoring employer contributions to the plan, plan settlements, and payments made by the employer directly to retirees. However, changes in that unfunded obligation that arise from experience gains and losses and the effects of changes in assumptions may be recognized as a component of net periodic postretirement benefit cost on a delayed basis. In addition, the effects of a plan initiation or amendment generally are recognized on a delayed basis.

35. The following components shall be included in the net postretirement benefit cost recognized for a period by an employer sponsoring a defined benefit postretirement plan: a) Service cost; b) Interest cost; c) Actual return on plan assets, if any; d) Amortization of any prior service cost or credit included in unassigned funds (surplus) to the extent required by paragraphs 40-45; e) Gain or loss (including the effects of changes in assumptions) to the extent recognized; and f) Amortization of any obligation or asset existing at the date of initial application of this statement, hereinafter referred to as the transition obligation or transition asset remaining in unassigned funds (surplus).

Service Cost

36. The service cost component recognized in a period shall be determined as the portion of the expected postretirement benefit obligation attributed to employee service during that period. The measurement of the service cost component requires identification of the substantive plan and the use of assumptions and an attribution method, which are discussed in paragraphs 9-31.

37. The prior service cost for nonvested employees not previously recognized[3] is not required to be included in net postretirement benefit cost entirely in the year this standard is adopted. Unrecognized prior service cost for nonvested employees shall be amortized as a component of the net postretirement benefit cost by assigning an equal amount to each expected future period of service before vesting occurs for nonvested employees active at the date of the amendment. Unassigned funds (surplus) is adjusted each period as prior service cost is amortized (refer to paragraphs 105-108 for transition guidance related to the recognition of the prior service cost for nonvested employees through unassigned surplus).

Interest Cost

38. The interest cost component recognized in a period shall be determined as the increase in the accumulated postretirement benefit obligation to recognize the effects of the passage of time. Measuring the accumulated postretirement benefit obligation as a present value requires accrual of an interest cost at rates equal to the assumed discount rates.

Actual Return on Plan Assets

39. For a funded plan, the actual return on plan assets shall be determined based on the fair value of plan assets at the beginning and end of the period, adjusted for contributions and benefit payments. If the fund holding the plan assets is a taxable entity, the actual return on plan assets shall reflect the tax expense or benefit for the period determined in accordance with generally accepted accounting principles. Otherwise, no provision for taxes shall be included in the actual return on plan assets.

[3] The previous statutory accounting guidance in *SSAP No. 14—Postretirement Benefits Other Than Pensions* excluded nonvested employees from the service cost calculation. This exclusion has been eliminated with the issuance of this SSAP.

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Prior Service Cost

40. Plan amendments (including initiation of a plan) may include provisions that attribute the increase or reduction in benefits to employee service rendered in prior periods or only to employee service to be rendered in future periods. For purposes of measuring the accumulated postretirement benefit obligation, the effect of a plan amendment on a plan participant's expected postretirement benefit obligation shall be attributed to each year of service in that plan participant's attribution period, including years of service already rendered by that plan participant, in accordance with the attribution of the expected postretirement benefit obligation to years of service as discussed in paragraphs 30-31. If a plan is initiated that grants benefits solely in exchange for employee service after the date of the plan initiation or a future date, no portion of the expected postretirement benefit obligation is attributed to prior service periods because, in that case, the credited service period for the current employees who are expected to receive benefits under the plan begins at the date of the plan initiation or the future date.

41. Plan amendments that improve benefits are granted with the expectation that the employer will realize economic benefits in future periods. Consequently, except as discussed in paragraph 44, this statement does not permit the cost of benefit improvements (that is, prior service cost) to be included in net periodic postretirement benefit cost entirely in the year of the amendment. Rather, paragraph 42 provides for recognition of prior service cost arising from benefit improvements during the remaining years of service to the full eligibility dates of those plan participants active at the date of the plan amendment.

42. A plan amendment that retroactively increases benefits (including benefits that are granted to fully eligible plan participants) increases the accumulated postretirement benefit obligation. The cost of the benefit improvement shall be recognized as a charge to unassigned funds (surplus) at the date of the amendment. Except as specified in the next sentence and in paragraphs 43-44, that prior service cost shall be amortized as a component of net periodic postretirement benefit cost by assigning an equal amount to each remaining year of service to the full eligibility date of each plan participant active at the date of the amendment who was not yet fully eligible for benefits at that date. If all or almost all of a plan's participants are fully eligible for benefits, the prior service cost shall be amortized based on the remaining life expectancy of those plan participants rather than on the remaining years of service to the full eligibility dates of the active plan participants. Unassigned funds (surplus) is adjusted as a result of amortizing prior service cost.

43. To reduce the complexity and detail of the computations required, consistent use of an alternative approach that more rapidly amortizes the prior service cost recognized in unassigned funds (surplus) is permitted. For example, a straight-line amortization of the cost over the average remaining years of service to full eligibility for benefits of the active plan participants is acceptable.

44. In some situations, a history of regular plan amendments and other evidence may indicate that the period during which the employer expects to realize economic benefits from an amendment that grants increased benefits is shorter than the remaining years of service to full eligibility for benefits of the active plan participants. Identification of those situations requires an assessment of the individual circumstances of the particular plan. In those circumstances, the amortization of prior service cost shall be accelerated to reflect the more rapid expiration of the employer's economic benefits and to recognize the cost in the periods benefited.

45. A plan amendment that retroactively reduces, rather than increases, benefits decreases the accumulated postretirement benefit obligation. The reduction in benefits shall be recognized as a corresponding credit (prior service credit) to unassigned funds (surplus) that shall be used first to reduce any remaining prior service cost included in unassigned funds (surplus), then to reduce any transition obligation remaining in unassigned funds (surplus). The excess, if any, shall be amortized as a component of net periodic postretirement benefit cost on the same basis as specified in paragraph 42 for prior service cost. Immediate recognition of the excess is not permitted.

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Gains and Losses

46. Gains and losses are changes in the amount of either the accumulated postretirement benefit obligation or plan assets resulting from experience different from that assumed or from changes in assumptions. This statement generally does not distinguish between those sources of gains and losses. Gains and losses include amounts that have been realized as well as amounts that are unrealized. Because gains and losses may reflect refinements in estimates as well as real changes in economic values and because some gains in one period may be offset by losses in another or vice versa, this statement does not require recognition of gains and losses as components of net postretirement benefit cost in the period in which they arise, except as described in paragraph 51. Gains and losses that are not recognized immediately as a component of net periodic postretirement benefit cost shall be recognized as increases or decreases in unassigned funds (surplus) as they arise.

47. The expected return on plan assets shall be determined based on the expected long-term rate of return on plan assets and the fair value of plan assets.

48. Plan asset gains and losses are differences between the actual return on plan assets during a period and the expected return on plan assets for that period. Plan asset gains and losses include changes reflected in the fair value of plan assets.

49. As a minimum, amortization of a net gain or loss included in unassigned funds (surplus) shall be included as a component of net periodic postretirement benefit cost for a year if, as of the beginning of the year, that net gain or loss exceeds 10% ~~percent~~ of the greater of the accumulated postretirement benefit obligation or the fair value of plan assets. If amortization is required, the minimum amortization shall be that excess divided by the average remaining service period of active plan participants. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants shall be used instead of the average remaining service period.

50. Any systematic method of amortizing gains and losses included in unassigned funds (surplus) may be used in place of the minimum amortization specified in paragraph 49 provided that (a) the minimum amortization is recognized in any period in which it is greater (reduces the net gain or loss balance by more) than the amount that would be recognized under the method used, (b) the method is applied consistently, (c) the method is applied similarly to both gains and losses, and (d) the method used is disclosed. If an enterprise uses a method of consistently recognizing gains and losses immediately, any gain that does not offset a loss previously recognized in income pursuant to this paragraph shall first offset any transition obligation remaining in unassigned funds (surplus); any loss that does not offset a gain previously recognized in income pursuant to this paragraph shall first offset any transition asset remaining in unassigned funds (surplus).

51. In some situations, an employer may forgive a retrospective adjustment of the current or past years' cost-sharing provisions of the plan as they relate to benefit costs already incurred by retirees or may otherwise deviate from the provisions of the substantive plan to increase or decrease the employer's share of the benefit costs incurred in the current or past periods. The effect of a decision to temporarily deviate from the substantive plan shall be immediately recognized as a loss or gain.

52. The gain or loss component of net periodic postretirement benefit cost shall consist of (a) the difference between the actual return on plan assets and the expected return on plan assets, (b) any gain or loss immediately recognized or the amortization of the net gain or loss included in unassigned funds (surplus), and (c) any amount immediately recognized as a gain or loss pursuant to paragraph 51.

Measurement of Plan Assets

53. Plan assets are assets—usually stocks, bonds, and other investments (except certain insurance ~~contracts~~annuities as noted in paragraph 57)—that have been segregated and restricted (usually in a trust)

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to be used for postretirement benefits. The amount of plan assets includes amounts contributed by the employer, and by plan participants for a contributory plan, and amounts earned from investing the contributions, less benefits, income taxes, and other expenses incurred. Plan assets ordinarily cannot be withdrawn by the employer except under certain circumstances when a plan has assets in excess of obligations and the employer has taken certain steps to satisfy existing obligations. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

54. Assets not segregated in a trust, or otherwise effectively restricted, so that they cannot be used by the employer for other purposes are not plan assets for purposes of this statement, even though the employer may intend that those assets be used to provide postretirement benefits. Those assets shall be accounted for in the same manner as other employer assets of a similar nature and with similar restrictions. Amounts accrued by the employer but not yet paid to the plan are not plan assets for purposes of this statement.

55. Plan investments, whether equity or debt securities, real estate, or other, shall be measured at their fair value as of the measurement date.

56. Plan assets used in plan operations (for example, buildings, equipment, furniture and fixtures, and leasehold improvements) shall be measured at cost less accumulated depreciation or amortization for all purposes.

~~Insurance~~Annuity Contracts

57. For purposes of this statement, an ~~insurance~~annuity contract is defined as a contract in which an insurance company unconditionally undertakes a legal obligation to provide specified benefits to specific individuals in return for a fixed consideration or premium; an ~~insurance~~annuity contract is irrevocable and involves the transfer of significant risk from the employer (or the plan) to the insurance company. Benefits covered by ~~insurance~~annuity contracts shall be excluded from the accumulated postretirement benefit obligation. ~~Insurance~~Annuity contracts shall be excluded from plan assets.

58. Some ~~insurance~~annuity contracts include participation rights (participating ~~insurance~~annuity contracts), which provide that the purchaser (either the plan or the employer) may participate in the experience of the insurance company. Under those contracts, the insurance company ordinarily pays dividends to the purchaser, the effect of which is to reduce the cost of the plan. If the participating ~~insurance~~annuity contract causes the employer to remain subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance company, that contract is not an ~~insurance~~annuity contract for purposes of this statement, and the purchase of that contract does not constitute a settlement pursuant to paragraphs 83-88. Endorsement split-dollar life ~~insurance~~annuity contracts[4] do not settle a liability for a postretirement benefit obligation. For these contracts and other ~~insurance~~annuity contracts that do not constitute settlement, reporting entities shall accrue a liability for the postretirement benefit arrangement in accordance with this statement.

59. The purchase price of a participating ~~insurance~~annuity contract ordinarily is higher than the price of an equivalent contract without a participation right. The difference is the cost of the participation right.

[4] An endorsement split-dollar life insurance arrangement is a split-dollar life insurance arrangement in which the entity owns and controls the insurance policy. The employer enters into a separate agreement that splits the policy benefits between the employer and the employee. The employer owns the policy, controls all rights of ownership, and may terminate the insurance policy (and, in turn, the policy benefits promised to the employee). To effect the split-dollar arrangement, the employer endorses a portion of the death benefits to the employee (the employee designates a beneficiary for this portion of the death benefits). Upon the death of the employee, the employee's beneficiary typically receives the designated portion of the death benefits directly from the insurance entity and the employer receives the remainder of the death benefits. SSAP No. 21R, paragraph 8, provides guidance for amounts reporting entities can realize when they are owner and beneficiary, or otherwise have obtained rights to control insurance policies.

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The cost of the participation right shall be recognized at the date of purchase as a nonadmitted asset. In subsequent periods, the participation right shall be nonadmitted and measured at its fair value if the contract is such that fair value is reasonably estimable. Otherwise, the participation right shall be measured at its amortized cost (not in excess of its net realizable value), and the cost shall be amortized systematically over the expected dividend period under the contract.

60. To the extent that ~~insurance~~annuity contracts are purchased during the period to cover postretirement benefits attributed to service in the current period (such as life insurance benefits), the cost of those benefits shall be the cost of purchasing the coverage under the contracts, except as provided in paragraph 59 for the cost of a participation right. If all the postretirement benefits attributed to service in the current period are covered by nonparticipating ~~insurance~~annuity contracts purchased during that period, the cost of the contracts determines the service cost component of net postretirement benefit cost for that period. Benefits attributed to current service in excess of benefits provided by nonparticipating ~~insurance~~annuity contracts purchased during the current period shall be accounted for according to the provisions of this statement applicable to plans not involving ~~insurance~~annuity contracts.

61. Other contracts with insurance companies may not meet the definition of an ~~insurance~~annuity contract because the insurance company does not unconditionally undertake a legal obligation to provide specified benefits to specified individuals. Those contracts shall be accounted for as investments and measured at fair value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value. For some contracts, the best available estimate of fair value may be contract value.

Measurement Date

62. The measurements of plan assets and benefit obligations required by this statement shall be as of the date of the employer's fiscal year-end statement of financial position. Even though the postretirement benefit measurements are required as of a particular date, all procedures are not required to be performed after that date. As with other financial statement items requiring estimates, much of the information can be prepared as of an earlier date and projected forward to account for ~~subsequent~~ events occurring between the most recent valuation date and the plan's year end (for example, employee service and benefit payments).

63. Measurements of net periodic postretirement benefit cost for both interim and annual financial statements generally shall be based on the assumptions at the beginning of the year (assumptions used for the previous year-end measurements of plan assets and obligations) unless more recent measurements of both plan assets and the accumulated postretirement benefit obligation are available. For example, if a significant event occurs, such as a plan amendment, settlement, or curtailment, that ordinarily would call for remeasurement, the assumptions used for those later measurements shall be used to remeasure net periodic postretirement benefit cost from the date of the event to the year-end measurement date. Unless an employer remeasures both its plan assets and benefit obligations during the fiscal year, the funded status it reports in its interim-period statement of financial position shall be the same asset or liability recognized in the previous year-end statement of financial position adjusted for (a) subsequent accruals of net periodic postretirement benefit cost that exclude the amortization of amounts previously recognized in unassigned funds (surplus) (for example, subsequent accruals of service cost, interest cost, and return on plan assets) and (b) contributions to a funded plan, or benefit payments. Upon remeasurement, a business entity shall adjust its statement of financial position in a subsequent interim period to reflect the overfunded or underfunded status of the plan consistent with that measurement date.

64. If a significant event caused by the employer (such as a plan amendment, settlement, or curtailment) that requires an employer to re-measure both plan assets and benefit obligations does not coincide with a month-end, the employer may elect to re-measure plan assets and benefit obligations using the month-end that is closest to the date of the significant event. This re-measurement would not

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eliminate the requirement for a year-end measurement of plan assets and benefit obligations required in paragraph 62.

65. If an employer re-measures plan assets and benefit obligations during the fiscal year in accordance with paragraph 64, the employer shall adjust the fair value of plan assets and the actuarial present value of benefit obligations for any effects of the significant event that may or may not be captured in the month-end measurement (for example, if the closest month-end is before the date of a partial settlement, then the measurement of plan assets may include assets that are no longer part of the plan). An employer shall not adjust the fair value of plan assets and the actuarial present value of benefit obligations for other events occurring between the month-end date used to re-measure plan assets and benefit obligations and the employer's fiscal year-end that may be significant to the measurement of defined benefit plan assets and obligations, but are not caused by the employer (for example, changes in market prices or interest rates).

Disclosures - Single-Employer Defined Postretirement Plans

66. An employer that sponsors one or more other defined benefit postretirement plans shall provide the following information for postretirement benefit plans other than pensions. Amounts related to the employer's results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer's statement of financial position, shall be disclosed as of the date of each statement of financial position presented.

a. A reconciliation of beginning and ending balances of the benefit obligation showing separately, if applicable, the effects during the period attributable to each of the following: service cost, interest cost, contributions by plan participants, actuarial gains and losses, foreign currency exchange rate changes, benefits paid, plan amendments, business combinations, divestitures, curtailments, settlements, and special termination benefits.

b. A reconciliation of beginning and ending balances of the fair value of plan assets showing separately, if applicable, the effects during the period attributable to each of the following: actual return on plan assets, foreign currency exchange rate changes, contributions by the employer, contributions by plan participants, benefits paid, business combinations, divestitures, and settlements.

c. The funded status of the plans and the amounts recognized in the statement of financial position, showing separately the assets (nonadmitted) and liabilities recognized.

d. The objectives of the disclosures about postretirement benefit plan assets are to provide users of financial statements with an understanding of:

    i. How investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies;

    ii. The classes of plan assets;

    iii. The inputs and valuation techniques used to measure the fair value of plan assets;

    iv. The effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period;

    v. Significant concentrations of risk within plan assets.

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An employer shall consider those overall objectives in providing the following information about plan assets:

(a) A narrative description of investment policies and strategies, including target allocation percentages or range of percentages considering the classes of plan assets disclosed pursuant to (b) below, as of the latest statement of financial position presented (on a weighted-average basis for employers with more than one plan), and other factors that are pertinent to an understanding of those policies and strategies such as investment goals, risk management practices, permitted and prohibited investments including the use of derivatives, diversification, and the relationship between plan assets and benefit obligations. For investment funds disclosed as classes as described in (b) below, a description of the significant investment strategies of those funds shall be provided.

(b) The fair value of each class of plan assets as of each date for which a statement of financial position is presented. Asset classes shall be based on the nature and risks of assets in an employer's plan(s). Examples of classes of assets include, but are not limited to, the following: cash and cash equivalents; equity securities, (segregated by industry type, company size, or investment objective); debt securities, issued by national, state, and local governments; corporate debt securities; asset-backed securities; structured debt; derivatives on a gross basis (segregated by type of underlying risk in the contract, for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, and other contracts); investment funds (segregated by type of fund); and real estate. Those examples are not meant to be all inclusive. An employer should consider the overall objectives in paragraph 66.d. in determining whether additional classes of plan assets or further disaggregation of classes should be disclosed.

(c) A narrative description of the basis used to determine the overall expected long-term rate-of-return-on-assets assumption, such as the general approach used, the extent to which the overall rate-of-return-on-assets assumption was based on historical returns, the extent to which adjustments were made to those historical returns in order to reflect expectations of future returns, and how those adjustments were determined. The description should consider the classes of assets described in (b) above, as appropriate.

(d) Information that enables users of financial statements to assess the inputs and valuation techniques used to develop fair value measurements of plan assets at the reporting date. For fair value measurements using significant unobservable inputs, an employer shall disclose the effect of the measurements on changes in plan assets for the period. To meet those objectives, the employer shall disclose the following information for each class of plan assets disclosed pursuant to (b) above for each annual period:

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(1) The level within the fair value hierarchy in which the fair value measurements in their entirety fall,[5] segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3)

(2) Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.

e. The benefits (as of the date of the latest statement of financial position presented) expected to be paid in each of the next five fiscal years, and in the aggregate for the five fiscal years thereafter. The expected benefits should be estimated based on the same assumptions used to measure the company's benefit obligation at the end of the year and should include benefits attributable to estimated future employee service.

f. The employer's best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the next fiscal year beginning after the date of the latest statement of financial position presented. Estimated contributions may be presented in the aggregate combining (1) contributions required by funding regulations or laws, (2) discretionary contributions, and (3) noncash contributions.

g. The amount of net periodic benefit cost recognized, showing separately the service cost component, the interest cost component, the expected return on plan assets for the period, the gain or loss component, the prior service cost or credit component, the transition asset or obligation component, and the gain or loss recognized due to settlements or curtailments.

h. Separately the net gain or loss and net prior service cost or credit recognized in unassigned funds (surplus) for the period pursuant to paragraphs 42 and 46, and reclassification adjustments of unassigned funds (surplus) for the period, as those amounts, including amortization of the net transition asset or obligation, are recognized as components of net periodic benefit cost.

i. The amounts in unassigned funds (surplus) that have not yet been recognized as components of net periodic benefit cost, showing separately the net gain or loss, net prior service cost or credit, and net transition asset or obligation.

j. On a weighted-average basis, the following assumptions used in the accounting for the plans: discount rates, rates of compensation increase (for pay-related plans), expected long-term rates of return on plan assets specifying, in a tabular format, the assumptions used to determine the benefit obligation and the assumptions used to determine net benefit cost, and interest crediting rates (for cash balance plans and other plans with promised interest crediting rates).

k. The assumed health care cost trend rate(s) for the next year used to measure the expected cost of benefits covered by the plan (gross eligible charges), and a general description of

[5] In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. The level in the fair value hierarchy within which the fair value measurement in its entirety falls shall be determined based on the lowest level input that is significant to the fair value measurement in its entirety. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability.

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the direction and pattern of change in the assumed trend rates thereafter, together with the ultimate trend rate(s) and when that rate is expected to be achieved.

l. If applicable, the amounts and types of securities of the employer and related parties included in plan assets.

m. If applicable, any alternative method used to amortize prior service amounts or net gains and losses pursuant to paragraphs 43 and 50.

n. If applicable, any substantive commitment, such as past practice or a history of regular benefit increases, used as the basis for accounting for the benefit obligation.

o. If applicable, the cost of providing special or contractual termination benefits recognized during the period and a description of the nature of the event.

p. An explanation of the following information:

i. The reasons for significant gains and losses related to changes in the defined benefit obligation for the period.

ii. Any other significant change in the benefit obligation or plan assets not otherwise apparent in the other required disclosures in this statement.

Employers with Two or More Plans

67. Postretirement benefits offered by an employer may vary in nature and may be provided to different groups of employees. As discussed in paragraph 68, in some cases an employer may aggregate data from unfunded plans for measurement purposes in lieu of performing separate measurements for each unfunded plan (including plans whose designated assets are not appropriately segregated and restricted and thus have no plan assets as that term is used in this statement). Net periodic postretirement benefit cost, the accumulated postretirement benefit obligation, and plan assets shall be determined for each separately measured plan or aggregation of plans by applying the provisions of this statement to each such plan or aggregation of plans.

68. The data from all unfunded postretirement health care plans may be aggregated for measurement purposes if (a) those plans provide different benefits to the same group of employees or (b) those plans provide the same benefits to different groups of employees. Data from other unfunded postretirement welfare benefit plans may be aggregated for measurement purposes in similar circumstances, such as when an employer has a variety of welfare benefit plans that provide benefits to the same group of employees. However, a plan that has plan assets (as defined herein) shall not be aggregated with other plans but shall be measured separately.

Disclosures – Employers with Two or More Defined Benefit Plans

69. The disclosures required by this statement shall be aggregated for all of an employer's other defined benefit postretirement plans unless disaggregating in groups is considered to provide useful information or is otherwise required by this paragraph and paragraph 70 of this statement. Disclosures shall be as of the date of each statement of financial position presented. If aggregate disclosures are presented, an employer shall disclose, as of the date of each statement of financial position presented:

a. The accumulated benefit obligation and fair value of plan assets for plans with accumulated benefit obligations in excess of plan assets.

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70. A U.S. reporting entity may combine disclosures about pension plans or other postretirement benefit plans outside the United States with those for U.S. plans unless the benefit obligations of the plans outside the United States are significant relative to the total benefit obligation and those plans use significantly different assumptions.

Interim Financial Disclosures – Defined Benefit Plans

71. The following shall be disclosed within interim financial statements that include a statement of income:

a. The amount of net periodic benefit cost recognized, for each period for which a statement of income is presented, showing separately the service cost component, the interest cost component, the expected return on plan assets for the period, the gain or loss component, the amount prior service cost or credit component, the transition asset or obligation component, and the gain or loss recognized due to a settlement or curtailment.

b. The total amount of the employer's contributions paid, and expected to be paid, during the current fiscal year, if significantly different from amounts previously disclosed pursuant to paragraph 66.f. of this statement. Estimated contributions may be presented in the aggregate combining, (1) contributions required by funding regulations or laws, (2) discretionary contributions, and (3) noncash contributions.

Multiemployer Plans

72. For purposes of this statement, a multiemployer plan is a postretirement benefit plan to which two or more unrelated employers contribute, usually pursuant to one or more collective-bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer.

73. An employer participating in a multiemployer plan shall recognize as net postretirement benefit cost the required contribution for the period, which shall include both cash and the fair value of noncash contributions, and shall recognize as a liability any unpaid contributions required for the period.

74. In some situations, withdrawal from a multiemployer plan may result in an employer having an obligation to the plan for a portion of the plan's unfunded accumulated postretirement benefit obligation. If it is either probable or reasonably possible that (a) an employer would withdraw from the plan under circumstances that would give rise to an obligation or (b) an employer's contribution to the fund would be increased during the remainder of the contract period to make up a shortfall in the funds necessary to maintain the negotiated level of benefit coverage (a "maintenance of benefits" clause), the employer shall apply the provisions *SSAP No. 5R—Liabilities, Contingencies, and Impairments of Assets*.

Disclosures - Multiemployer Plans

75. An employer shall disclose the amount of contributions to multiemployer plans for each annual period for which a statement of income is presented. An employer may disclose total contributions to multiemployer plans without disaggregating the amounts attributable to pension plans and other postretirement benefit plans. The disclosures shall include a description of the nature and effect of any changes affecting comparability, such as a change in the rate of employer contributions, a business combination, or a divestiture. This disclosure shall identify whether the contributions represent more than 5% ~~percent~~ of total contributions to the plan as indicated in the plan's most recently available annual report.

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76. In addition to the requirements of paragraph 75, the following information shall be disclosed:

a. Whether a funding improvement plan or rehabilitation plan had been implemented or is pending.

b. Whether the reporting entity paid a surcharge to the plan.

c. A description of minimum contributions required for future periods, if applicable.

d. A qualitative description of the extent to which the employer could be responsible for the obligations of the plan, including benefits earned by employees during employment with another employer.

77. Pursuant to paragraph 74, if withdrawal under circumstances that would give rise to an obligation is either probable or reasonably possible, the provisions and disclosures of SSAP No. 5R, shall apply.

Multiple-Employer Plans

78. Some postretirement benefit plans to which two or more unrelated employers contribute are not multiemployer plans. Rather, those multiple-employer plans are in substance aggregations of single-employer plans, combined to allow participating employers to pool plan assets for investment purposes or to reduce the costs of plan administration. Those plans ordinarily do not involve collective-bargaining agreements. They may also have features that allow participating employers to have different benefit formulas, with the employer's contributions to the plan based on the benefit formula selected by the employer. Those plans shall be considered single-employer plans rather than multiemployer plans for purposes of this statement, and each employer's accounting shall be based on its respective interest in the plan.

Postretirement Benefit Plans Outside the United States

79. This statement includes no special provisions applicable to postretirement benefit arrangements outside the United States. Those arrangements are subject to the provisions of this statement. The applicability of this statement to those arrangements is determined by the nature of the obligation and by the terms or conditions that define the amount of benefits to be paid, not by whether or how a plan is funded, whether benefits are payable at intervals or as a single amount, or whether the benefits are required by law or custom or are provided under a plan the employer has elected to sponsor.

Business Combinations

80. When an employer is acquired in a business combination and that employer sponsors a single-employer defined benefit postretirement plan, the assignment of the purchase price to individual assets acquired and liabilities assumed shall include a liability for the accumulated postretirement benefit obligation in excess of the fair value of the plan assets or an asset for the fair value of the plan assets in excess of the accumulated postretirement benefit obligation. The accumulated postretirement benefit obligation assumed shall be measured based on the benefits attributed by the acquired entity to employee service prior to the date the business combination is consummated, adjusted to reflect (a) any changes in assumptions based on the purchaser's assessment of relevant future events (as discussed in paragraphs 9-29) and (b) the terms of the substantive plan (as discussed in paragraphs 9-14) to be provided by the purchaser to the extent they differ from the terms of the acquired entity's substantive plan.

81. If the postretirement benefit plan of the acquired entity is amended as a condition of the business combination (for example, if the change is required by the seller as part of the consummation of the acquisition), the effects of any improvements attributed to services rendered by the participants of the acquired entity's plan prior to the date of the business combination shall be accounted for as part of the accumulated postretirement benefit obligation of the acquired entity. Otherwise, if improvements to the

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postretirement benefit plan of the acquired entity are not a condition of the business combination, credit granted for prior service shall be recognized as a plan amendment as discussed in paragraphs 40-45. If it is expected that the plan will be terminated or curtailed, the effects of those actions shall be considered in measuring the accumulated postretirement benefit obligation. Otherwise, no future changes to the plan shall be anticipated.

82. As a result of applying the provisions of paragraphs 80-81, any previously existing net gain or loss, prior service cost or credit, or transition obligation or transition asset remaining in unassigned funds (surplus) is eliminated for the acquired employer's plan.

Accounting for Settlement of a Postretirement Benefit Obligation

83. For purposes of this statement, a settlement is defined as a transaction that (a) is an irrevocable action, (b) relieves the employer (or the plan) of primary responsibility for a postretirement benefit obligation, and (c) eliminates significant risks related to the obligation and the assets used to effect the settlement. Examples of transactions that constitute a settlement include making lump-sum cash payments to plan participants in exchange for their rights to receive specified postretirement benefits and purchasing long-term nonparticipating ~~insurance~~annuity contracts for the accumulated postretirement benefit obligation for some or all of the plan participants.

84. A transaction that does not meet the three criteria of paragraph 83 does not constitute a settlement for purposes of this statement. For example, investing in a portfolio of high-quality fixed-income securities with principal and interest payment dates similar to the estimated payment dates of benefits may avoid or minimize certain risks. However, that investment decision does not constitute a settlement because that decision can be reversed, and investing in that portfolio does not relieve the employer (or the plan) of primary responsibility for a postretirement benefit obligation nor does it eliminate significant risks related to that obligation.

85. For purposes of this statement, the maximum gain or loss subject to recognition in income when a postretirement benefit obligation is settled is the net gain or loss included in unassigned funds (surplus) defined in paragraphs 46-50 plus any transition asset remaining in unassigned funds (surplus). That maximum gain or loss includes any gain or loss resulting from remeasurements of plan assets and the accumulated postretirement benefit obligation at the time of settlement.

86. If the entire accumulated postretirement benefit obligation is settled and the maximum amount subject to recognition is a gain, the settlement gain shall first reduce any transition obligation remaining in unassigned funds (surplus); any excess gain shall be recognized in income. If the entire accumulated postretirement benefit obligation is settled and the maximum amount subject to recognition is a loss, the maximum settlement loss shall be recognized in income. If only part of the accumulated postretirement benefit obligation is settled, the employer shall recognize in income the excess of the pro rata portion (equal to the percentage reduction in the accumulated postretirement benefit obligation) of the maximum settlement gain over any remaining transition obligation or a pro rata portion of the maximum settlement loss.

87. If the purchase of a participating ~~insurance~~annuity contract constitutes a settlement, the maximum gain (but not the maximum loss) shall be reduced by the cost of the participation right before determining the amount to be recognized in income. As detailed in paragraph 58, the purchase of an endorsement split-dollar life ~~insurance~~annuity contract does not settle a liability for a postretirement benefit obligation.

88. If the cost of all settlements in a year is less than or equal to the sum of the service cost and interest cost components of net postretirement benefit cost for the plan for the year, gain or loss recognition is permitted but not required for those settlements. However, the accounting policy adopted shall be applied consistently from year to year.

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Accounting for a Plan Curtailment

89. For purposes of this statement, a curtailment is an event that significantly reduces the expected years of future service of active plan participants or eliminates the accrual of defined benefits for some or all of the future services of a significant number of active plan participants. Curtailments include:

a. Termination of employees' services earlier than expected, which may or may not involve closing a facility or discontinuing a component of an entity.

b. Termination or suspension of a plan so that employees do not earn additional benefits for future service. In the latter situation, future service may be counted toward eligibility for benefits accumulated based on past service.

90. The prior service cost included in unassigned funds (surplus) associated with the portion of the future years of service that had been expected to be rendered, but as a result of a curtailment are no longer expected to be rendered, is a loss. For purposes of measuring the effect of a curtailment, prior service cost includes the cost of plan amendments and any remaining transition obligation. For example, a curtailment may result from the termination of a significant number of employees who were plan participants at the date of a prior plan amendment. The loss associated with that curtailment is measured as the portion of the remaining prior service cost included in unassigned funds (surplus) related to that (and any prior) plan amendment attributable to the previously expected remaining future years of service of the employees who were terminated and the portion of the remaining transition obligation attributable to the previously expected remaining future years of service of the terminated employees who were plan participants at the date of transition.

91. The accumulated postretirement benefit obligation may be decreased (a gain) or increased (a loss) by a curtailment. That (gain) loss shall reduce any net loss (gain) included in unassigned funds (surplus).

a. To the extent that such a gain exceeds any net loss included in unassigned funds (surplus) (or the entire gain, if a net gain exists), it is a curtailment gain.

b. To the extent that such a loss exceeds any net gain included in unassigned funds (surplus) (or the entire loss, if a net loss exists), it is a curtailment loss.

For purposes of applying the provisions of this paragraph, any transition asset remaining in unassigned funds (surplus) shall be treated as a net gain and shall be combined with the unrecognized net gain or loss arising subsequent to transition to this statement.

92. If the sum of the effects identified in paragraphs 90-91 is a net loss, it shall be recognized in income when it is probable that a curtailment will occur and the net effect is reasonably estimable. If the sum of those effects is a net gain, it shall be recognized in income when the related employees terminate or the plan suspension or amendment is adopted.

93. A settlement and a curtailment may occur separately or together. If benefits expected to be paid in future periods are eliminated for some plan participants (for example, because a significant portion of the work force is dismissed or a plant is closed) but the plan remains in existence and continues to pay benefits, to invest assets, and to receive contributions, a curtailment has occurred but not a settlement. If an employer purchases nonparticipating ~~insurance~~annuity contracts for the accumulated postretirement benefit obligation and continues to provide defined benefits for future service, either in the same plan or in a successor plan, a settlement has occurred but not a curtailment. If a plan termination occurs (that is, the obligation is settled and the plan ceases to exist) and the plan is not replaced by a successor defined benefit plan, both a settlement and a curtailment have occurred (whether or not the employees continue to work for the employer).

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Measurement of the Effects of Termination Benefits

94. An employer that offers special or contractual termination benefits to employees shall recognize a liability and a loss when the employees accept the offer and the amount can be reasonably estimated. An employer that provides contractual termination benefits shall recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated. A situation involving special or contractual termination benefits may also result in a curtailment to be accounted for under paragraphs 89-92.

95. The liability and loss recognized for employees who accept an offer of special termination benefits to be provided by a postretirement benefit plan shall be the difference between (a) the accumulated postretirement benefit obligation for those employees, assuming that those employees (active plan participants) not yet fully eligible for benefits would terminate at their full eligibility date and that fully eligible plan participants would retire immediately, without considering any special termination benefits and (b) the accumulated postretirement benefit obligation as measured in (a) adjusted to reflect the special termination benefits.

Defined Contribution Plans

96. For purposes of this statement, a defined contribution postretirement plan is a plan that provides postretirement benefits in return for services rendered, provides an individual account for each participant, and has terms that specify how contributions to the individual's account are to be determined rather than the amount of postretirement benefits the individual is to receive. Under a defined contribution plan, the postretirement benefits a plan participant will receive are limited to the amount contributed to the plan participant's account, the returns earned on investments of those contributions, and forfeitures of other plan participants' benefits that may be allocated to the plan participant's account.

97. To the extent a plan's defined contributions to an individual's account are to be made for periods in which that individual renders services, the net postretirement benefit cost for a period shall be the contribution called for in that period. If a plan calls for contributions for periods after an individual retires or terminates, the estimated cost shall be accrued during the employee's service period.

98. A postretirement benefit plan having characteristics of both a defined benefit plan and a defined contribution plan requires careful analysis. If the substance of the plan is to provide a defined benefit, as may be the case with some "target benefit" plans, the accounting requirements shall be determined in accordance with the provisions of this statement applicable to a defined benefit plan and the disclosure requirements within paragraph 66 shall be followed.

Disclosures - Defined Contribution Plans

99. An employer shall disclose the amount of cost recognized for defined contribution postretirement benefit plans for all periods presented separately from the amount of cost recognized for defined benefit plans. The disclosures shall include a description of the nature and effect of any significant changes during the period affecting comparability, such as a change in the rate of employer contributions, a business combination, or a divestiture.

Consolidated/Holding Company Plans

100. The employees of many reporting entities are eligible for certain postretirement benefits other than pensions provided by a parent company or holding company. A reporting entity with employees who are eligible for those benefits and is not directly liable for those related obligations shall recognize an expense equal to its allocation of the benefits earned during the period. A liability shall be established for any such amounts due but not yet paid.

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101. The reporting entity shall disclose in the financial statements that its employees participate in a plan sponsored by the holding company for which the reporting entity has no legal obligation. The amount of the postretirement benefit expense incurred and the allocation methodology utilized by the provider of such benefits shall also be disclosed. If the reporting entity is directly liable for postretirement benefits other than pensions, then the requirements outlined in paragraphs 1-99 and paragraphs 102-116 of this statement shall be applied.

Relevant Literature

102. This statement adopts with modification paragraphs 1-7 and 16-18 as well as Appendix D – Amendments to Statement 106 and Appendix E – Amendments to Statement 132(R) of *FASB Statement No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)* (FAS 158). Paragraphs 8-10 and D2.u providing specific guidance for not-for-profit organizations are rejected. Paragraphs 11-15 regarding the effective dates for FAS 158 are rejected and paragraph 19 providing an alternative method for remeasuring plan assets and benefits obligations as of the fiscal year the measurement date provisions are applied is also rejected. The disclosure included within FAS 132 (R), as amended by FAS 158, pertaining specifically to pensions (paragraph 5.e.) has been rejected for inclusion within this standard. This statement adopts the revisions to paragraph 5.d. of FAS 132(R) as amended by *FASB Staff Position FAS 132(R)-1, Employers' Disclosures about Postretirement Benefit Plan Assets* (FSP FAS 132(R)-1) and *ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASU 2010-06). Other revisions to disclosure requirements as amended by FSP FAS 132(R)-1 relate to nonpublic entities and are rejected. This statement adopts *EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. This statement adopts by reference revisions to ASC 715-80 as detailed in *ASU 2011-09, Compensation – Retirement Benefits – Multiemployer Plans* with limited additional disclosures required within statutory financial statements. This statement adopts by reference *FSP FASB 158-1, Conforming Amendments to the Illustrations in FASB Statements No. 87, No. 88, and No. 106 and to the Related Staff Implementation Guides* (FSP FAS 158-1) to the extent that the examples and related implementation guides comply with the adopted GAAP guidance previously identified within this statement, as modified for statutory accounting. The statement adopts with modification the disclosure revisions reflected in *ASU 2018-14, Changes to the Disclosure Requirements for Defined Benefit Plans*, consistent with the modifications from the adoption of FAS 158 and FAS 106. The following modifications from the adopted paragraphs of FAS 158 and FAS 106 have been incorporated within this standard:

a. All references to "other comprehensive income" or "accumulated other comprehensive income" within FAS 158 have been revised to reflect "unassigned funds (surplus)."

b. Any prepaid asset resulting from the excess of the fair value of plan assets over the accumulated postretirement benefit obligation shall be nonadmitted. Furthermore, any asset recognized from the cost of a "participation right" of an annuity contract per paragraph 59 shall also be nonadmitted.

c. Provisions within paragraph 57 and 58 of FAS 106, as amended by FAS 158, permitting a calculated market-related value of plan assets has been eliminated with only the fair value measurement method for plan assets retained.

d. The reduced disclosure requirements for nonpublic entities described in paragraph 8 of FAS 132(R), as amended by FAS 158, are rejected. All reporting entities shall follow the disclosure requirements within this statement which have been adopted from paragraph 5 of FAS 132(R), as amended by FAS 158.

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e. Clarification has been included within this standard to ensure both vested and nonvested employees are included within the recognition of net postretirement benefit cost and in the accumulated postretirement benefit obligation. Although this is consistent with GAAP, this is a change from previous statutory accounting. As nonvested employees were excluded from statutory accounting under SSAP No. 14, guidance has been included to indicate that the unrecognized prior service cost attributed to nonvested individuals is not required to be included in net postretirement benefit cost entirely in the year this standard is adopted. The unrecognized prior service cost for nonvested employees shall be amortized as a component of net postretirement benefit cost by assigning an equal amount to each expected future period of service before vesting occurs for nonvested employees active at the date of the amendment. Unassigned funds (surplus) is then adjusted each period as prior service cost is amortized. (Guidance is included within the transition related to the recognition of the prior service cost for nonvested employees through unassigned surplus.)

f. Conclusion of *Interpretation 99-26: Offsetting Pension Assets and Liabilities* prohibiting the offset of defined benefit liabilities of one plan with prepaid assets of another plan has been incorporated within paragraph 33 of this statement.

g. Provisions within paragraph 44B of FAS 106, as amended by FAS 158, regarding the classification of underfunded liabilities as current or noncurrent liabilities and the classification of assets from overfunded plans as noncurrent assets has been rejected as inconsistent with statutory accounting.

h. Provisions within paragraph 65 of FAS 106, as amended by FAS 158, defining the fair value of investments have been rejected. Fair value definitions and measurement for investments shall be determined in accordance with statutory accounting guidance.

i. Provisions within paragraph 72 of FAS 106, as amended by FAS 158, regarding the plan assets measurement date for consolidating subsidiaries or entities utilizing the equity method under APB Opinion No. 18 has been rejected. For statutory accounting, all entities shall follow the measurement date guidance within paragraph 62 of this statement.

j. The disclosure requirement included within paragraph 5.e. of FAS 132(R) has been rejected for this statement as it specifically pertains to pensions.

k. Transition under FAS 158 is different from the requirements of this statement. FAS 158 requires publicly traded equity securities to initially apply the requirement to recognize the funded status of a postretirement benefit plan; the gains/losses, prior service costs/credits and transition obligations/assets that have not yet been included in net periodic benefit cost; and the disclosure requirements as of the end of the fiscal year ending after December 15, 2006. Transition guidelines for statutory accounting are defined in paragraphs 105-116 of this statement.

l. FAS 158 provided two approaches for an employer to transition to a fiscal year-end measurement date. For purposes of statutory accounting, the second approach permitting reporting entities to use earlier measurements determined for year-end reporting as of the fiscal year immediately preceding the year that the measurement date provisions is rejected. For consistency purposes, all reporting entities shall follow the first approach and remeasure plan assets and benefit obligations as of the beginning of the fiscal year that the measurement date provisions are applied.

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103. This statement adopts the revisions to ASC 715-60 as it relates to interim re-measurement due to a *significant* event as detailed in *ASU 2015-04, Practical Expedient for the Measurement Date of An Employer's Defined Benefit Obligation and Plan Assets*. Other revisions are rejected as statutory accounting requires the annual measurement of benefit obligations and plan assets to be measured as of a year-end measurement date.

104. This statement rejects *ASU 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. Existing statutory disclosures on the components of benefit costs shall be completed.

Effective Date and Transition

105. Reporting entities are required to disclose the accumulated postretirement benefit obligation and the fair value of plan assets for defined postretirement benefit plans in the first reporting period after the effective date of this standard and in each subsequent reporting period. This disclosure shall specifically note the funded/underfunded status of the postretirement benefit plan. Reporting entities shall also specifically note the surplus impact necessary, at each reporting date, to reflect the full benefit obligation within the financial statements.

106. This statement is effective for quarterly and annual reporting periods beginning on or after January 1, 2013 (transition date) with early adoption permitted. Any unfunded defined benefit amounts, as determined when the accumulated benefit obligation exceeds the fair value of plan assets, is a liability under SSAP No. 5R and shall be reported in the first quarter statutory financial statements after the transition date with a corresponding entry to unassigned funds (surplus). If the fair value of plan assets exceeds the accumulated benefit obligation, the asset shall be considered a nonadmitted asset. Net periodic benefit cost shall include a component for unrecognized prior service cost for nonvested employees beginning in 2013.

~~107. Gains or losses, prior service costs or credits (including prior service costs for non-vested participants pursuant to paragraph 37), and remaining transition assets or obligations (collectively referred to as "unrecognized items") from prior application of SSAP No. 14 that have not yet been included in net periodic benefit cost as of December 31, 2012[6] shall be recognized as components of the ending balance of unassigned funds (surplus), net of tax, as of January 1, 2013 (provided that alternative transition is not elected per paragraph 108.b.). The offset to unassigned funds is reported separately as an "Aggregate Write-In for Other Than Invested Assets" or as an "Aggregate Write-In for Other Liabilities." After recognition, the full unfunded or overfunded status or the plan shall be reflected within the financial statements. Any prepaid asset resulting from an overfunded plan shall be nonadmitted.~~

~~108. Due to the potential impact to surplus as a result of immediately applying the accounting guidance in paragraph 107, reporting entities may elect one of the following two methods, on an individual plan basis, to recognize the transition surplus impact:~~

~~a. Reporting entities may elect to recognize the entire transition surplus impact calculated from applying paragraph 107, on an individual plan basis, as of January 1, 2013.~~

~~b. Alternatively, reporting entities may elect to recognize the entire surplus impact from applying paragraph 07, on an individual plan basis, over a period not to exceed ten (10) years. The surplus impact initially recognized as of January 1, 2013, under this transition option, and subsequently over the transition period, shall be the greater of:~~

~~[6] The intent of the guidance is to recognize the unrecognized amounts as of December 31, 2012, annual statements, even if new actuarial projections (expected postretirement benefit obligations) are calculated as of January 1, 2013. (These projections would be considered in the recognition of the 2013 pension cost.)~~

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i. Ten percent of the calculated surplus impact as of the transition date; and

ii. Amortization[7] of the "unrecognized items" (defined in paragraph 107) into net periodic benefit cost, including any accelerated amortization of these items from curtailments or settlements that occur after the transition date. (If the amortization cannot be determined at transition, at a minimum, the amount amortized for "unrecognized items" during the prior year shall be utilized for this component of the calculation. If the amount recognized for transition (greater of both components in paragraph 108.b.) is subsequently determined to be less than what is amortized for the year (paragraph 108.b.ii.), the difference between what was recognized for transition, and what is amortized must immediately be recognized as an adjustment to the transition impact to unassigned funds – surplus.)

109. If the surplus deferral (paragraph 108.b.) is elected at the transition date, subsequently, starting with the 2014 year-end financial statement, the reporting entity shall annually recognize the remaining surplus impact (collectively referred to as the "transition liability"[8]) on a systematic basis over a period not to exceed nine years. The minimum amount recognized each subsequent year shall be an amount that reflects the conditions within paragraph 108.b. Reporting entities that elect the transition option in paragraph 108.b. are permitted to recognize the remaining transition liability, or an amount in excess of the minimum requirement, at any time after the transition date.

110. Reporting entities that elect the transition option in paragraph 108.b. must recognize any remaining transition liability to the extent that the plan reflects a prepaid benefit cost. (For example, if changes in circumstances have resulted with the plan reflecting an overfunded status, the remaining transition liability must be recognized to the extent that the plan is overfunded.) The transition guidance in paragraph 108.b. is not intended (on a net basis for each plan) to result in more favorable subsequent surplus OPEB positions when there are remaining unrecognized liabilities as a result of the reporting entity's initial election for surplus deferral. Therefore, if there is a plan curtailment, settlement, or other plan amendment resulting in a reduction of benefit obligations, or net benefit obligation gains due to revisions in assumptions (e.g., discount rates) or plan experience differing from assumptions, or plan asset gains due to the actual return on plan assets exceeding the expected return on plan assets, a corresponding amount of unrecognized liability from the surplus deferral shall be recognized. For this purpose, net gains, if any, are the net aggregation of all gains and losses (excluding plan amendments that increase benefit obligations) from factors such as those listed above, determined as of a measurement or remeasurement date. This shall occur regardless if the impact from the change results with the plan being in an overfunded state, or whether the gain is recognized in earnings. The transition guidance was to provide surplus relief from the immediate surplus impact from adopting this statement, but in no instance should changes (on a net basis for each plan) attributed to OPEB plans result in more favorable, subsequent surplus positions when there are unrecognized liabilities remaining as a result of the reporting entity's initial election for surplus deferral. (The guidance in this paragraph was originally contained within *INT 13-03: Clarification of Surplus Deferral in SSAP No. 92 & SSAP No. 102* and was effective December 15, 2013.)

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[7] Unless otherwise impacted from the provisions within this statement or in accordance with changes to the benefit plan, the amortization of the unrecognized items into net periodic benefit cost shall continue to follow the existing amortization schedules in effect on the transition date.

[8] If the surplus deferral from paragraph 108.b. is elected, the deferred liability, although comprised of the previous "unrecognized items" shall be collectively referred to as the "transition liability." Although reporting entities will need to continue to track the unrecognized items for amortization into net periodic cost (offset through unassigned funds), reporting entities shall not allocate the recognized surplus impact from transition to these categories. As noted in paragraph 108.b.ii., the minimum amount of liability recognized under the deferral option must cover the annual amortization of the "unrecognized items" into net periodic benefit cost to prevent a surplus benefit.

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~~111. The transition guidance in paragraphs 107-110 is specific to the transition surplus impact from initially applying this statement on January 1, 2013. Thus, this transition guidance does not apply to additional liability calculated from subsequent comparison of the fair value of plan assets to the accumulated benefit obligation, or the impact of subsequent plan amendments.~~

~~112. Reporting entities electing to apply the transition guidance in paragraph 108.b. must disclose the full transition surplus impact calculated from applying paragraph 107 in the first quarter statutory financial statements after the transition date and each reporting period thereafter. This disclosure shall include the initial "transition liability" calculated under paragraph 107 and the annual amortization amount of the "unrecognized items" into net periodic benefit cost. This disclosure shall include a schedule of the entity's anticipated recognition of the remaining surplus impact over the transition period.~~

~~113. The requirement to measure plan assets and benefit obligations as of the date of the reporting entity's financial statement year-end is effective for financial statement years beginning January 1, 2014. (The measurement date change will be initially reflected in the December 31, 2014, financial statements.)~~

~~114. In order to transition to a fiscal year-end measurement date, the reporting entity shall remeasure plan assets and benefit obligations as of the beginning of the fiscal year that the measurement date provisions are applied. The reporting entity shall use those new measurements to determine the effects of the measurement date change as of the beginning of the fiscal year that the measurement date provisions are applied.~~

~~115. The reporting entity shall measure plan assets and benefit obligations as of the beginning of the fiscal year that the measurement date provisions are applied. This would result with the following:~~

~~a. Net periodic benefit cost for the period between the measurement date that is used for the immediately preceding fiscal year-end and the beginning of the fiscal year that the measurement date provisions are applied, exclusive of any curtailment or settlement gain or loss, shall be recognized, net of tax, as a separate adjustment of the opening balance of unassigned funds (surplus). That is, the pretax amount recognized as an adjustment to unassigned funds (surplus) is the net periodic benefit cost that without a change in measurement date otherwise would have been recognized on a delayed basis during the first interim period for the fiscal year that the measurement date provisions are applied.~~

~~b. Any gain or loss arising from a curtailment or settlement between the measurement date that is used for the immediately preceding fiscal year-end and the beginning of the fiscal year that the measurement date provisions are applied shall be recognized in earnings in that period and not as an adjustment to unassigned funds (surplus). This provision prohibits a reporting entity from early application of the measurement date provisions when the reporting entity has issued financial statements for the prior year without recognition of such a settlement or curtailment.~~

~~c. Other changes in the fair value of plan assets and the benefit obligations (for example, gains or losses) for the period between the measurement date that is used for the immediately preceding fiscal year-end and the beginning of the fiscal year that the measurement date provisions are applied shall be recognized, net of tax, as a separate adjustment of the opening balance of unassigned funds (surplus) for the fiscal year that the measurement date provisions are applied.~~

~~116. Earlier application of the recognition or measurement date provisions is encouraged, however, early applications must be for all of the reporting entity's benefit plans. If early application is elected, the transition date shall reflect the January 1st of the year in which this standard is initially applied. Retrospective application is not permitted.~~

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REFERENCES

Other

- *Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy*
- *SSAP No. 14—Employers' Accounting for Postretirement Benefits Other Than Pensions*

Relevant Issue Papers

- *Issue Paper No. 133—Accounting for Postretirement Benefits Other Than Pensions, A Replacement of SSAP No. 14*

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Statements of Statutory Accounting Principles No. 93

Low-Income Housing Tax Credit Property Investments

STATUS

Type of Issue..... Common Area
Issued ..... June 13, 2005
Effective Date ..... January 1, 2006
Affects..... No other pronouncements
Affected by..... No other pronouncements
Interpreted by..... INT 06-07
Relevant Appendix A Guidance ..... None

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investments in federal and certain state sponsored Low-Income Housing Tax Credit (LIHTC) properties owned through limited liability entities that are flow-through entities for tax purposes. State sponsored LIHTC programs that have the following characteristics are within the scope of and shall be accounted for in accordance with this statement:

a. The program is based upon Internal Revenue Code (IRC) section 42.

b. The investment requires an ongoing interest in a limited liability entity, which is a flow-through entity, and cannot be transferred apart from this interest.

c. Resale value of the investment is not based upon the fair value of the underlying real estate.

d. Fair value of the investment is directly tied to the remaining stream of tax credits and deductible losses available to investors.

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e. The critical element of value is known with a high degree of certainty before being marketed to investors.

f. The proportional amortization method (as modified by this statement) is more indicative of liquidation value than the equity method.

State sponsored LIHTC programs requiring ownership in a partnership or limited liability entity that do not have the foregoing characteristics shall continue to be accounted for in accordance with the requirements of *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*.

2. Some states have enacted laws that create programs by which transferable and non-transferable state tax credits are granted to entities under certain specified conditions (e.g., an entity makes an investment in a particular industry). Investments in transferable and non-transferable state tax credits are not within the scope of this statement. See *SSAP No. 94R—Transferable and Non-Transferable State Tax Credits*.

SUMMARY CONCLUSION

3. LIHTC investments held by reporting entities meet the definition of an asset as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement.

4. Resale valuation of these investments is based on the present value of the future stream of tax credits and deductible losses, and not the fair value of the underlying real estate.

5. Investors in entities that manage or invest in low-income housing projects receive tax benefits in the form of tax deductions from operating losses and tax credits. The tax credits are allowable on the tax return each year over a 10-year period as a result of renting a sufficient number of units to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. These credits are subject to recapture over a 15-year period starting with the first year tax credits are earned. Corporate investors generally purchase an interest in a limited liability entity that manages or invests in the low-income housing projects.

Accounting

6. LIHTC investments shall be initially recorded at cost and carried at proportional amortized cost as specified in this statement unless considered impaired as discussed in paragraphs 16-19. An illustration has been provided in Exhibit A of this statement.

7. A reporting entity investor using the proportional amortized cost method shall amortize any excess of the carrying amount of the investment over its estimated residual value during the periods in which tax benefits are allocated to the investor. The estimated residual value used in determining the amount to be amortized is the estimated residual value at the end of the last period in which tax benefits are allocated to the investor and should not reflect anticipated inflation. Annual amortization shall be based on the proportion of tax benefits received in the current year to total estimated tax benefits to be allocated to the investor. The amortization amount shall be calculated as follows:

a. The initial investment balance less any expected residual value of the investment, multiplied by,

b. The percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be received by the reporting entity over the life of the investment.

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8. Under the proportional amortized cost method, the amortization of the investment in the limited liability entity is recognized in the income statement as a component of net investment income/expense. The current tax credit (or benefit) shall be accounted for as a component of income tax expense.

9. Federal tax credits shall be recognized in the income statement as an offset to federal taxes in the tax reporting year in which the tax credit is utilized in accordance with *SSAP No. 101—Income Taxes*. State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized. Tax benefits received, other than tax credits, shall be accounted for pursuant to SSAP No. 101.

10. At the time of initial investment, immediate recognition of the entire benefit of the tax credits to be received during the term of an investment in a low-income housing project is not appropriate. (That is, low-income housing tax credits shall not be recognized in the financial statements before their inclusion in the investor's tax return.)

11. Many LIHTC investments require future equity contributions by the investor (equity contributions), that may be contingent on a variety of conditions, such as receiving representations, contract performance, meeting occupancy requirements, etc. If the commitment by the investor to provide equity contributions meets the definition of a liability as defined in *SSAP No. 5R—Liabilities Contingencies and Impairments of Assets,* a liability shall be recorded.

12. If the commitment to provide equity contributions does not meet the definition of a liability, the contingent commitment shall be disclosed in the notes to the financial statements with other contingent commitments. A liability shall also be recognized for equity contributions that are contingent on a future event when that contingent event becomes probable.

13. Additional funding that does not result in additional tax credits for the reporting entity (investor) shall be expensed as a component of net investment income. In the event a reporting entity obtains additional tax credits for a LIHTC investment, the following shall be applied:

a. If additional tax credits are allocated without additional funding, the additional tax credits shall not be afforded any value; rather, the tax benefit is only recognized when realized.

b. If additional funding directly related to the additional tax credits is required, the provisions of this statement shall be followed as if the additional funding were a new investment in LIHTC property.

14. An investment amortized to residual value in accordance with paragraph 7 of this statement shall not be revalued under any other method during or subsequent to the amortization period, other than as discussed in this statement.

15. Changes in estimated losses shall be accounted for in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* as a change in estimate and included as a component of net investment income.

Impairment

16. Reporting entities with investments in LIHTC properties shall complete and document an impairment analysis at each reporting period. If it is determined that an impairment exists, the book value of the LIHTC investment shall be compared to the present value of future tax benefits discounted at a risk free rate of return, i.e., the rate on U.S. Treasury obligations of a similar duration, and the investment shall be written-down if the book value is higher. This will result in a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries in fair value.

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17. Among other things, an other-than-temporary impairment(INT 06-07) shall be considered to have occurred if it is probable that future tax benefits will not be received as expected. For example, for LIHTC properties based on state tax credits, if the reporting entity intends to decrease premium volume in that state, it may affect whether or not the tax credits in that state are realizable. The best available information about market share or premiums by state and premiums by line of business generally should be used to estimate the amount of future tax credits that are realizable. For purposes of determining impairment, future tax benefits consist of both estimated tax losses and anticipated tax credits. Loan default or a reasonable probability of credit recapture would signify that tax benefits would not be received as expected.

18. In a multi-tiered partnership, whereby one limited partnership exists only to hold interests in other limited partnerships that are each invested in different developments, the impairment should be determined at the lowest tier. The partnership that holds the assets in which the impairment is determined to exist will be adjusted to a new cost basis representing the lower of book value or the present value of future tax benefits discounted at a risk-free rate of interest. This new cost basis and related realized loss shall be recognized by the holder of a LIHTC investment.

19. It should be noted that a foreclosure of a single property within an LIHTC investment fund only affects the loss of tax credits on a proportional basis. For example, a foreclosure of one property in a six-property fund generating equal levels of credits would only eliminate 1/6 of the credits, thereby, only affecting 1/6 of the LIHTC investment fund value to the individual investors.

Audited Financial Statements

20. The reporting entity's return and book value of an LIHTC investment is reliant upon maintaining tax credit eligibility and not its share of the equity as reported on a financial statement. As such, a reporting entity shall monitor the tax credit eligibility of an LIHTC investment through requiring either audited GAAP or audited tax basis financial statements. In the event an audited GAAP or audited tax basis financial statement is not obtained, the asset shall be nonadmitted.

Disclosures

21. Disclose the number of remaining years of unexpired tax credits and the required holding period for the LIHTC investments.

22. Disclose the amount of low-income housing tax credits and other tax benefits recognized during the years presented.

23. Disclose the balance of the investment recognized in the statement of financial position for the reporting period(s) presented.

24. Disclose if the LIHTC property is currently subject to any regulatory reviews and the status of such review. (Example investigations by the housing authority.)

25. Any commitment or contingent commitment (e.g., guarantees or commitments to provide additional capital contributions) including the amount of equity contributions that are contingent commitments related to LIHTC properties investments and the year(s) that contingent commitments are expected to be paid shall be disclosed.

26. The significance of an investment to the reporting entity's financial position and results of operations shall be considered in evaluating the extent of disclosures of the financial position and results of operations of an investment in a LIHTC. If in the aggregate the LIHTC investments exceed 10% of the total admitted assets of the reporting entity the following disclosures shall be made:

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a. (i) The name of each partnership or limited liability entity and percentage of ownership, (ii) the accounting policies of the reporting entity with respect to investments in partnerships and limited liability entities (iii) the difference, if any, between the amount at which the investment is carried and the amount of underlying equity in net assets (i.e., nonadmitted goodwill or other nonadmitted assets) and (iv) the accounting treatment of the difference;

b. For partnerships, and limited liability entities for which a quoted fair value is available, the aggregate value of each partnership, or limited liability entity investment based on the quoted fair value; and

c. Summarized information as to assets, liabilities and results of operations for partnerships, and limited liability entities, either individually or in groups.

27. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment and how fair value was determined.

28. Disclose the amount and nature of the write-downs or reclassifications made during the year resulting from the forfeiture or ineligibility of tax credits, etc. These write-downs may be based on actual property level foreclosure, loss of qualification due to occupancy levels, compliance issues with tax code provisions within an LIHTC investment, or other issues.

29. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

30. This statement adopts with modification *ASU 2014-01, Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects*. The modifications include:

a. ASU 2014-01 allows the election of using the proportional amortization method if an affordable housing project investment meets several criteria, including the lack of significant influence. This statement requires the proportional amortization method, with modifications as discussed in this statement, for all investments within its scope. Although the terminology is updated, the balance sheet amount and timing of amortization should be the same under this statement and the proportional amortization method in ASU 2014-01.

b. The proportional amortization method in ASU 2014-01 utilizes a net presentation in the income statement by including the amortized initial cost of the investment and the tax credits and benefits received within income tax expense. This statement requires a gross presentation on the income statement, with proportional amortization of the initial cost of the investment in investment income and the tax credits and benefits included in income tax expense.

c. Paragraphs 323-740-50-2c and 323-740-50-2d related to disclosures of the optionality of the method used and net reporting, are rejected as not applicable to statutory accounting.

d. Disclosures should be followed as indicated in the disclosures section in this statement.

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31. This statement adopts with modification *EITF 94-1: Accounting for Tax Benefits from Investments in Affordable Housing Projects* as applicable to statutory accounting to the extent it is not modified by ASU 2014-01. In 2006, this statement modified *Issue Paper No. 99—Nonapplicable GAAP Pronouncements* to remove the reference to EITF 94-1.

32. ASU 2014-01 and EITF 94-1 are modified for the following statutory concepts:

a. The elective effective yield method and the net income statement reporting in EITF 94-1 are rejected. The elective proportional amortization method in ASU 2014-01, which replaced the effective yield method, is required for only the balance sheet calculation reflecting the timing and amount of amortization. The proportional amortization method net income statement reporting in ASU 2014-01 is rejected for statutory accounting.

b. Investments that meet the criteria of this statement are required to use a proportional amortization method as prescribed in this statement. This method requires the tax credits and benefits to be recognized in proportion to the percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be received by the reporting entity over the life of the investment. This statement requires a gross presentation on the financial statements, with amortization in investment income.

c. Federal tax credits shall be recognized in the income statement as an offset to federal income taxes in the tax reporting year in which the tax credit is utilized in accordance with *SSAP No. 101—Income Taxes*. State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax reporting year in which the credit is utilized.

d. Tax benefits received, other than tax credits, shall be accounted for pursuant to SSAP No. 101. Amortization shall be reported as a component of net investment income.

e. Reporting entities shall follow the guidance in paragraphs 11 and 12 regarding the application of the definition of a liability and contingent commitments from *SSAP No. 5R—Liabilities Contingencies and Impairments of Assets* to equity contributions.

f. *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* shall be utilized to account for investments that qualify as subsidiary, controlled or affiliated entities.

g. The impairment guidance contained in this statement shall be followed.

h. For statutory accounting purposes, deferred taxes are not reported as a component of income from continuing operations in the income statement; rather deferred taxes are recognized as a separate component of gains and losses in unassigned funds (surplus).

33. *AICPA Statement of Position 78-9, Accounting for Investments in Real Estate Ventures* (SOP 78-9) is rejected for purposes of statutory accounting in SSAP No. 48. This statement does not intend to establish SOP 78-9 as applicable to statutory accounting.

34. *FASB Interpretation No. 46, Consolidation of Variable Interest Entities* (FIN 46) is rejected for purposes of statutory accounting in SSAP No. 3. This statement does not intend to establish FIN 46 as applicable to statutory accounting.

35. *EITF 85-16: Leveraged Leases* (EITF 85-16) is adopted for purposes of statutory accounting in *SSAP No. 22R–Leases*. This statement does not intend to readdress the conclusions reached in SSAP No. 22R.

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Effective Date and Transition

36. This statement is effective for reporting periods beginning on or after January 1, 2006. Early adoption is permitted. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. The guidance previously in paragraph 3 of this statement superseded paragraph 1 of SSAP No. 48. In 2011, this guidance was moved to *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* and deleted from this statement. The original guidance included in this standard is retained for historical purposes in Issue Paper No. 125. The guidance from ASU 2014-01 is effective for reporting periods beginning on or after January 1, 2015, with early adoption permitted.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 125—Accounting for Low-Income Housing Tax Credit Property Investments*

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EXHIBIT A – LOW-INCOME HOUSING TAX CREDIT PROPERTY INVESTMENTS

A Limited Partnership Investment in an Affordable Housing Project Accounted for Using the Amortized Cost Method (modified to include tax benefits and record amortization as a component of net investment income):

This exhibit is based on ASU 2014-01, paragraph 323-740-55-7 of the Accounting Standards Codification. The amount and timing of amortization in the proportional amortization method is consistent with the statutory modifications; therefore, the table incorporated in this exhibit is based on the proportional amortization table. The statutory income statement requires a gross presentation on the income statement, with proportional amortization of the initial cost of the investment in investment income and the tax credits and benefits included in income tax expense.

Terms:
Date of Investment: January 1, 20X1
Purchase Price of Investment: $100,000

Assumptions:

1. All cash flows (except initial investment) occur at the end of each year.

2. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).

3. The investor made a $100,000 investment for a 5% ~~percent~~ limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.

4. The partnership finances the project cost of $4,000,000 with 50% ~~percent~~ equity and 50% ~~percent~~ debt.

5. The annual tax credit allocation (equal to 4% ~~percent~~ of the project's original cost) will be received for a period of 10 years.

6. The investor's tax rate is 40% ~~percent~~.

7. For simplicity, the project will operate with break-even pretax cash flows including debt service during the first 15 years of operations.

8. The project's taxable loss will be equal to depreciation expense. The cumulative book loss (and thus the cumulative depreciation expense) recognized by the investor is limited to the $100,000 investment.

9. It is assumed that all requirements are met to retain allocable tax credits so there will be no recapture of tax credits.

10. The investor expects that the estimated residual value of the investment will be zero.

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Proportional Amortization Method with Statutory Modifications

Year	Net Investment (1)	Amortization of Investment (2)	Tax Credits (3)	Net Losses/Tax Depreciation (4)	Other Tax Benefits from Tax Depreciation (5)	Tax Credits and Other Tax Benefits (6)
	100,000					
1	90,909	9,091	8,000	7,273	2,909	10,909
2	81,818	9,091	8,000	7,273	2,909	10,909
3	72,727	9,091	8,000	7,273	2,909	10,909
4	63,636	9,091	8,000	7,273	2,909	10,909
5	54,545	9,091	8,000	7,273	2,909	10,909
6	45,454	9,091	8,000	7,273	2,909	10,909
7	36,363	9,091	8,000	7,273	2,909	10,909
8	27,272	9,091	8,000	7,273	2,909	10,909
9	18,181	9,091	8,000	7,273	2,909	10,909
10	9,090	9,091	8,000	7,273	2,909	10,909
11	6,666	2,424		7,273	2,909	2,909
12	4,242	2,424		7,273	2,909	2,909
13	1,818	2,424		7,273	2,909	2,909
14	0	1,818		5,451	2,183	2,183
15	0					0
Total		100,000	80,000	100,000	40,000	120,000

(1) End-of-year investment for a 5% ~~percent~~ limited liability interest in the project net of amortization in Column (2).

(2) Initial investment of $100,000 x (total tax benefits received during the year in Column (6)/total anticipated tax benefits over the life of the investment of $120,000).

(3) ~~Four percent~~A 4% tax credit on $200,000 tax basis of the underlying assets.

(4) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.5 years up to the amount of the initial investment of $100,000.

(5) Column (4) x 40% tax rate.

(6) Column (3) + Column (5).

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Statements of Statutory Accounting Principles No. 94 – Revised

Transferable and Non-Transferable State Tax Credits

STATUS

Type of Issue	Common Area
Issued	June 12, 2006; Substantively revised December 7, 2011
Effective Date	December 31, 2006; Substantive revisions detailed in Issue Paper No. 145 effective December 31, 2011
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **2**

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EXHIBIT A – ACCOUNTING FOR TRANSFERABLE STATE TAX CREDITS **5**

EXHIBIT B – ACCOUNTING FOR NON-TRANSFERABLE STATE TAX CREDITS **6**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for transferable and non-transferable state tax credits that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).

2. Investments in Low-Income Housing Tax Credits as discussed in *SSAP No. 93—Low-Income Housing Tax Credit Property Investments*, which involve an investment by a reporting entity in a limited liability company or similar entity that earns tax credits as a consequence of its operating activities involving low-income housing developments and passes those tax credits to its investors, are not within the scope of this statement.

3. Investments in a CAPCO (Certified Capital Company), organized as a partnership or an LLC, which is a company, authorized by state statute that borrows from investors (insurance companies), in

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order to make venture capital investments in "qualified" businesses, are not within the scope of this statement. Although associated with tax credits, the insurance company is paid principal and interest on its investment with the CAPCO. Depending upon the terms of the CAPCO offering, principal and interest payments to the insurance company will come from the CAPCO and/or the state. The CAPCO will make cash payments directly to the insurance company while the state will make payments in the form of premium or income tax credits.

SUMMARY CONCLUSION

4. The criteria in paragraphs 5 and 6 are for transferable state tax credits (i.e., credits which may be sold or assigned). The criteria in paragraphs 7 and 8 are for non-transferable state tax credits (i.e., those which cannot be sold or assigned to other parties).

Transferable State Tax Credits

5. Some states have enacted laws that create programs by which transferable state tax credits are granted to entities under certain specified conditions (e.g., an entity makes an investment in a particular industry). The terms of these state tax credits vary from state to state and, within a state, from program to program. However, many of these transferable state tax credit programs share the following four characteristics:

a. The tax credit is nonrefundable;

b. The holder of the transferable state tax credit may sell or otherwise transfer the transferable state tax credit to another entity, which can likewise resell or transfer the credit;

c. The transferable state tax credit will expire if not used by a predetermined date; and

d. The transferable state tax credit can be applied against either state income tax or state premium tax.

6. For purposes of this statement, such programs will be referred to as "transferable state tax credits." The criteria in paragraphs 5.b., 5.c. and 5.d. must be present in order for the transferable state tax credit to receive the accounting treatment described in this statement. When a reporting entity purchases a transferable state tax credit from another entity, the transaction does not result in a continuing investment in a business entity (i.e. limited partnership).

Non-Transferable State Tax Credits

7. If the original or subsequent holder of the transferable tax credit is not able to transfer the tax credit, then the admissibility criteria in paragraph 8 for non-transferable tax credits apply. These non-transferable state tax credits share the following characteristics:

a. The tax credit is nonrefundable;

b. The successive holder of a state tax credit must redeem the credit by April 15 of the subsequent year to the entity's acquisition of the state tax credit and is not permitted to carry-over, carry-back, obtain a refund, sell or assign the credit;

c. The non-transferable state tax credit will expire if not used by the predetermined date; and

d. The non-transferable state tax credit can be applied against either state income tax or state premium tax.

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8. The criteria in paragraphs 7.b., 7.c. and 7.d. must be present in order for the non-transferable state tax credit to receive the accounting treatment described in this statement.

9. Transferable and non-transferable state tax credits as defined within this SSAP held by reporting entities meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement. If the criteria in paragraphs 6 or 8 are not met, the tax credits are nonadmitted.

Acquisition

10. Transferable and non-transferable state tax credits are recorded at cost at the date of acquisition.

Balance Sheet Treatment

11. Transferable and non-transferable state tax credits expected to be realized are initially recorded at cost.

12. Transferable and non-transferable state tax credits shall be established gross of any related state tax liabilities and reported in the category of other-than-invested assets (not reported net).

13. As transferable and non-transferable state tax credits are redeemed, the carrying value of the tax credits is reduced dollar for dollar by the amount of state tax credits applied toward the reporting entity's applicable state tax liability.

Income Statement Treatment

14. Gains on transferable and non-transferable state tax credits are deferred until the value of the state tax credits utilized exceeds the cost of the state tax credits or until the state tax credits are sold to other entities and the payment received is greater than the book value.

15. Losses on transferable and non-transferable state tax credits are recognized when known.

16. Gains and losses on transferable and non-transferable state tax credits are reflected in other income.

Impairment

17. An impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to recover the carrying amount of the transferable or non-transferable state tax credits. State tax credits should be evaluated for impairment at each reporting date.

18. When there is a decline in the realizability of a transferable or non-transferable state tax credit owned by the reporting entity that is other than temporary, the asset shall be written down to the expected realizable amount and the amount of the write down shall be accounted for as a realized loss. The expected realizable value is the new cost basis.

19. The new cost basis shall not be changed for subsequent recoveries in realizability.

Disclosures

20. The following disclosures shall be made in the financial statements. For purposes of this disclosure, total unused transferable and non-transferable state tax credits represent the entire transferable and non-transferable state tax credits available:

a. Carrying value of transferable and non-transferable state tax credits gross of any related state tax liabilities by state and in total,

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b. Total unused transferable and non-transferable state tax credits by state;

c. Method of estimating utilization of remaining transferable and non-transferable state tax credits or other projected recovery of the current carrying value.

d. Impairment amount recognized in the reporting period, if any.

e. Identify state tax credits by transferable and non-transferable classifications, and identify the admitted and Nonadmitted portions of each classification.

Effective Date and Transition

21. This statement is effective for reporting periods ending on or after December 31, 2006. Early adoption is permitted. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. Substantive revisions to 1) revising the title; 2) incorporating the criteria for non-transferable state tax credits as described in paragraphs 7 and 8; 3) adding a disclosure; and 4) updating terminology throughout the document as appropriate, are effective for reporting periods ending on or after December 31, 2011.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 126—Accounting for Transferable State Tax Credits*
- *Issue Paper No. 145—Accounting for Transferable and Non-Transferable State Tax Credits*

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EXHIBIT A – ACCOUNTING FOR TRANSFERABLE STATE TAX CREDITS

On 1/1/X1 SAM Insurance Company purchased transferable state tax credits for a cost of $100,000. The transferable state tax credits are redeemable for $160,000 and expire at the end of 12/31/X4. SAM initially expects to utilize the tax credits before expiration in their state of domicile in the amount of $40,000 per year. In year X4, SAM sells the remaining $30,000 in transferable state tax credits for $20,000

1/1/x1	Transferable state tax credits	100,000	
	Cash		100,000
	To record the purchase of the tax credits		
6/30/x1	Premium tax expense	40,000	
	Premium taxes payable to domiciliary state		40,000
	To record premium tax expense and accrue the liability in Year 1.		
10/1/x1	Premium tax payable	40,000	
	Transferable state tax credits		40,000
	To record the use of tax credits in Year 1. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x2	Premium tax expense	60,000	
	Premium taxes payable to domiciliary state		60,000
	To record premium tax expense and accrue the liability in Year 2.		
9/30/x2	Premium tax payable	60,000	
	Transferable state tax credits		60,000
	To record the use of taxes credits in Year 2. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x3	Premium tax expense	30,000	
	Premium taxes payable to domiciliary state		30,000
	To record premium tax expense and accrue the liability in Year 3.		
9/30/x3	Premium tax payable	30,000	
	Other income		30,000
	To record the use of premium tax credits in excess of cost and recognize a gain on premium tax credits in other income. The Company intends to sell the remaining tax credits in year 4.		
6/30/x4	Cash	20,000	
	Other income		20,000
	To record the sale of the remaining tax credits.		

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EXHIBIT B – ACCOUNTING FOR NON-TRANSFERABLE STATE TAX CREDITS

On 7/1/X1 LJW Insurance Company purchased non-transferable state tax credits for a cost of $100,000. The state tax credits are redeemable for $110,000, are not transferable and expire on, April 15, 20x2. LJW expects to utilize the tax credits before expiration in their state of domicile in the amount of $110,000.

7/1/x1	State tax credits	100,000	
	Cash		100,000
	To record the purchase of the tax credits		
9/30/x1	Premium tax expense	200,000	
	Premium taxes payable to domiciliary state		200,000
	To record premium tax expense and accrue the liability.		
3/15/x2	Premium tax payable	110,000	
	Other Income		10,000
	State tax credits		100,000
	To record the use of premium tax credits in excess of cost and recognize a gain on premium tax credits in other income. (The additional $90,000 of premium taxes payable would still be due.)		

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Statements of Statutory Accounting Principles No. 95

Nonmonetary Transactions

STATUS

Type of Issue	Common Area
Issued	September 11, 2006
Effective Date	January 1, 2007
Affects	Supersedes SSAP No. 28; Nullifies and incorporates INT 00-29, INT 02-19 and INT 03-16; Nullifies INT 99-21
Affected by	No other pronouncements
Interpreted by	INT 00-26; INT 06-13; INT 08-05
Relevant Appendix A Guidance	None

STATUS **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. The statement establishes statutory accounting principles for nonmonetary transactions. Specific statutory requirements for certain types of nonmonetary transactions are addressed in other statements.

2. This statement supersedes the conclusions reached in *SSAP No. 28—Nonmonetary Transactions* by updating conclusions reached in SSAP No. 28 related to APB 29 with those included in FAS 153. Consequently, this statement adopts with modification FAS 153 to change GAAP references to those applicable to statutory accounting. In addition, references made to APB 29 within SSAP No. 28 will be replaced with the actual amended guidance resulting from FAS 153.

SUMMARY CONCLUSION

Definitions

3. The definitions of certain terms used in this statement are:

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a. **Monetary assets and liabilities** are assets and liabilities whose amounts are fixed in terms of units of currency by contract or otherwise. Examples are cash; amounts due from agents, brokers, and intermediaries; policy loans; accounts payable; and other amounts receivable or payable in cash;

b. **Nonmonetary assets and liabilities** are assets and liabilities other than monetary ones. Examples are common stocks; furniture, fixtures, and equipment; real estate and liabilities for rent collected in advance;

c. **Exchange (or exchange transaction)** is a reciprocal transfer between a reporting entity and another entity that results in the reporting entity acquiring assets or services or satisfying liabilities by surrendering other assets or services or incurring other obligations. A reciprocal transfer of a nonmonetary asset shall be deemed an exchange only if the transferor has no substantial continuing involvement in the transferred asset such that the usual risks and rewards of ownership of the asset are transferred;

d. **Nonreciprocal transfer** is a transfer of assets or services in one direction, either from a reporting entity to its owners (whether or not in exchange for their ownership interests) or another entity, or from owners or another entity, to the reporting entity. An insurance company's reacquisition of its outstanding stock is an example of a nonreciprocal transfer.

4. Nonmonetary transactions shall be accounted for in accordance with this statement, except as addressed by other statements or interpretations including but not limited to *SSAP No. 12—Employee Stock Ownership Plans*, *SSAP No. 25—Affiliates and Other Related Parties*, *SSAP No. 68—Business Combinations and Goodwill*, *SSAP No. 72—Surplus and Quasi-Reorganizations*, *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, *SSAP No. 104R—Share-Based Payments*, and *INT 00-26: EITF 98-3: Determining Whether a Nonmonetary Transactions Involves Receipt of Productive Assets or of a Business*.

Basic Principle

5. Accounting for nonmonetary transactions shall generally be based on the fair values of the assets (or services) involved, as defined in paragraph 13, which is the same basis as that used in monetary transactions. Thus, the cost of a nonmonetary asset acquired in exchange for another nonmonetary asset (reciprocal transactions) is the fair value of the asset surrendered to obtain it, and a gain or loss should be recognized on the exchange. The fair value of the asset received should be used to measure the cost if it is more clearly evident than the fair value of the asset surrendered. Similarly, a nonmonetary asset received in a nonreciprocal transfer should be recorded at the fair value of the asset received as defined in paragraph 6. A transfer of a nonmonetary asset to a stockholder or to another entity in a nonreciprocal transfer should be recorded at the fair value of the asset transferred, and a gain or loss should be recognized on the disposition of the asset. The fair value of a reporting entity's own stock reacquired may be a more clearly evident measure of the fair value of the asset distributed in a nonreciprocal transfer if the transaction involves distribution of a nonmonetary asset to eliminate a disproportionate part of owners' interests (that is, to acquire stock for the treasury or for retirement).

6. Fair value of assets received or transferred in a nonreciprocal transfer shall be measured based on statutory accounting principles for the type of asset transferred. Accordingly, the value shall be determined in accordance with *SSAP No. 26R—Bonds*, *SSAP No. 30R—Unaffiliated Common Stock*, *SSAP No. 32R—Preferred Stock*, SSAP No. 37*—Mortgage Loans*, *SSAP No. 39—Reverse Mortgages*, *SSAP No. 40R—Real Estate Investments*, *SSAP No. 43R—Loan-Backed and Structured Securities*, *SSAP No. 90—Impairment or Disposal of Real Estate Investments* or other applicable statements. The guidance provided in SSAP No. 25 shall be followed in accounting for nonreciprocal transactions with affiliates and other related parties as defined in that statement.

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Modifications of the Basic Principle

7. A nonmonetary exchange shall be measured based on the recorded amount (after reduction, if appropriate, for an indicated impairment of value) of the nonmonetary asset(s) relinquished, and not on the fair values of the exchanged assets, if any of the following conditions apply:

a. *Fair Value Not Determinable*. The fair value of neither the asset(s) received nor the asset(s) relinquished is determinable within reasonable limits (paragraph 14).

b. *Exchange Transaction to Facilitate Sales to Customers*. The transaction is an exchange of a product or property held for sale in the ordinary course of business for a product or property to be sold in the same line of business to facilitate sales to customers other than the parties to the exchange.

c. *Exchange Transaction That Lacks Commercial Substance*. The transaction lacks commercial substance (paragraph 8).

Commercial Substance

8. A nonmonetary exchange has commercial substance if the entity's future cash flows are expected to significantly change as a result of the exchange. The entity's future cash flows are expected to significantly change if either of the following criteria is met:

a. The configuration (risk, timing, and amount)[1] of the future cash flows of the asset(s) received differs significantly from the configuration of the future cash flows of the asset(s) transferred.

b. The entity-specific value[2] of the asset(s) received differs from the entity-specific value of the asset(s) transferred, and the difference is significant in relation to the fair values of the assets exchanged.

A qualitative assessment will, in some cases, be conclusive in determining that the estimated cash flows of the entity are expected to significantly change as a result of the exchange.

9. In the United States and some other tax jurisdictions, a transaction is not given effect for tax purposes unless it serves a legitimate business purpose other than tax avoidance. In assessing the commercial substance of an exchange, tax cash flows that arise solely because the tax business purpose is based on achieving a specified financial reporting result shall not be considered.

Additional Guidance

10. Stock received in the form of a stock dividend or stock split shall not result in the recognition of income. The cost basis of stock held shall be reallocated ratably to the total shares held after receipt of the stock dividend or stock split.

[1] The configuration of future cash flows is composed of the risk, timing, and amount of the cash flows. A change in any one of those elements would be a change in configuration.

[2] An entity-specific value (referred to as an entity-specific measurement in Concepts Statement 7) is different from a fair value measurement. As described in paragraph 24.b. of Concepts Statement 7, an entity-specific value attempts to capture the value of an asset or liability in the context of a particular entity. For example, an entity computing an entity-specific value of an asset would use its expectations about its use of that asset rather than the use assumed by marketplace participants. If it is determined that the transaction has commercial substance, the exchange would be measured at fair value, rather than at the entity-specific value.

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11. The exchanges of nonmonetary assets that would otherwise be based on recorded amounts (paragraphs 7 and 8) may include an amount of monetary consideration. The recipient of the monetary consideration has realized gain on the exchange to the extent that the amount of the monetary receipt exceeds a proportionate share of the recorded amount of the asset surrendered. The portion of the cost applicable to the realized amount should be based on the ratio of the monetary consideration to the total consideration received (monetary consideration plus the estimated fair value of the nonmonetary asset received) or, if more clearly evident, the fair value of the nonmonetary asset transferred. However, the entity paying the monetary consideration should not recognize any gain on a transaction covered in paragraphs 7 and 8, but should record the asset received at the amount of the monetary consideration paid plus the recorded amount of the nonmonetary asset surrendered. If a loss is indicated by the terms of a transaction described in this paragraph or in paragraphs 7 and 8, the entire indicated loss on the exchange should be recognized.

12. *Nonreciprocal Transfers to Owners*. Accounting for the distribution of nonmonetary assets to owners of an enterprise in a spin-off (INT 06-13 and INT 08-05) or other form of reorganization or liquidation or in a plan that is in substance the rescission of a prior business combination should be based on the recorded amount (after reduction, if appropriate, for an indicated impairment of value) (An indicated impairment of value of a long-lived asset covered by SSAP No. 90 shall be determined in accordance with paragraph 4 of SSAP No. 90) of the nonmonetary assets distributed. A pro rata distribution to owners of an enterprise of shares of a subsidiary or other investee company that has been or is being controlled or that has been or is being accounted for under the equity method is to be considered to be equivalent to a spin-off. Other nonreciprocal transfers of nonmonetary assets to owners should be accounted for at fair value if the fair value of the nonmonetary asset distributed is objectively measurable and would be clearly realizable to the distributing entity in an outright sale at or near the time of the distribution

Applying the Basic Principle

13. Fair value of a nonmonetary asset transferred to or from a reporting entity in a nonmonetary transaction should be determined in accordance with *SSAP No. 100R—Fair Value*. If one of the parties in a nonmonetary transaction could have elected to receive cash instead of the nonmonetary asset, the amount of cash that could have been received may be evidence of the fair value of the nonmonetary assets exchanged.

14. Fair value should be regarded as not determinable within reasonable limits if major uncertainties exist about the realizability of the value that would be assigned to an asset received in a nonmonetary transaction accounted for at fair value. An exchange involving parties with essentially opposing interests is not considered a prerequisite to determining a fair value of a nonmonetary asset transferred; nor does an exchange insure that a fair value for accounting purposes can be ascertained within reasonable limits. If neither the fair value of a nonmonetary asset transferred nor the fair value of a nonmonetary asset received in exchange is determinable within reasonable limits, the book adjusted carrying value of the nonmonetary asset transferred from the enterprise may be the only available measure of the transaction.

15. A difference between the amount of gain or loss recognized for tax purposes and that recognized for accounting purposes may constitute a temporary difference to be accounted for according to *SSAP No. 101—Income Taxes*.

16. Involuntary conversions of nonmonetary assets to monetary assets (for example, as a result of total or partial destruction, theft, seizure, or condemnation) are monetary transactions for which gain or loss shall be recognized even though a reporting entity reinvests or is obligated to reinvest the monetary assets in replacement nonmonetary assets. In some cases, a nonmonetary asset may be destroyed or damaged in one accounting period, and the amount of monetary assets to be received is not determinable until a subsequent accounting period. In those cases, gain or loss shall be recognized in accordance with the conclusions in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Gain or loss resulting from an involuntary conversion of a nonmonetary asset to monetary assets shall be reported

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consistently with the reporting entity's reporting of continuing operations and disclosed in the notes to financial statements in accordance with *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items*.

Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services, or Services and Cash (in Combination or Individually), or ~~a Combination of Goods or Services and Cash~~as Consideration Payable to a Customer

17. The guidance in paragraph 18 addresses a convertible instrument that is issued or granted to a nonemployee in exchange for goods or services, or a combination of goods or services and cash, or consideration payable to a customer. The convertible instrument contains a nondetachable conversion option that permits the holder to convert the instrument into the issuer's stock.

18. Once an instrument is considered "issued" for accounting purposes, pursuant to SSAP No. 104R, distributions paid or payable should be characterized as financing costs (that is, as interest or dividends). Before that time, distributions paid or payable under the instrument should be characterized as a cost of the underlying goods or services. If the convertible instrument is issued for cash proceeds that indicate that the instrument includes a beneficial conversion feature and the purchaser of the instrument also provides (receives) goods or services to (from) the issuer that are the subject of a separate contract, the convertible instrument shall be recognized with a corresponding increase or decrease in the purchase or sales price of the goods or services.

19. To determine the fair value of a convertible instrument granted as part of a share-based payment transaction to a nonemployee in exchange for goods or services or as consideration payable to a customer that is equity in form or, if debt in form, that can be converted into equity instruments of the issuer, the entity shall first apply SSAP No. 104R.

20. The requirements of this statement shall then be applied such that the fair value determined pursuant to SSAP No. 104R is considered the proceeds from issuing the instrument for purposes of determining whether a beneficial conversion option exists. The measurement of the intrinsic value, if any, of the conversion option (for separate recognition as additional paid-in capital) shall then be computed by comparing the proceeds received for the instrument (the instrument's fair value under SSAP No. 104R) to the fair value of the common stock that the grantee would receive upon exercising the conversion option. For purposes of determining whether a convertible instrument contains a beneficial conversion feature for separate recognition as additional paid-in capital, an entity shall use the effective conversion price based on the proceeds allocated to the convertible instrument to compute the intrinsic value, if any, of the embedded conversion option.

21. SSAP No. 104R shall be used to measure the fair value of the convertible instrument and to measure the intrinsic value, if any, of the conversion option as of the date the convertible instrument granted as part of the share-based payment award becomes fully vested. That is, in measuring the intrinsic value of the conversion option for separate recognition as additional paid-in capital, the fair value of the issuer's equity securities into which the instrument can be converted shall be determined as of the date the convertible instrument granted as part of a share-based payment award becomes fully vested, and not on the commitment date. Both of the following guidelines for determining the fair value of convertible instruments shall be used:

a. Recent issuances of similar convertible instruments for cash to parties that only have an investor relationship with the issuer may provide the best evidence of fair value of the convertible instrument.

b. If reliable information about paragraph 21.a. is not available, the fair value of the convertible instrument should be deemed to be no less than the fair value of the equity shares into which it can be converted.

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22. In cases where a reporting entity issues a convertible instrument for cash proceeds that indicate that the instrument includes a beneficial conversion option, and the purchaser of the instrument provides (receives) goods or services to (from) the issuer that are the subject of a separate contract, the terms of both the agreement for goods or services and the convertible instrument shall be evaluated to determine whether their separately stated pricing is equal to the fair value of the goods or services and convertible instrument. If that is not the situation, the terms of the respective transactions should be adjusted by measuring the convertible instrument initially at its fair value with a corresponding increase or decrease in the purchase or sales price of the goods or services. It may be difficult to evaluate whether the separately stated pricing of a convertible instrument is equal to its fair value. If an instrument issued to a goods or services provider (or purchaser) is part of a larger issuance, a substantive investment in the issuance by unrelated investors (who are not also providers or purchasers of goods or services) may provide evidence that the price charged to the goods or services provider represents the fair value of the convertible instrument.

Disclosures

23. A reporting entity that engages in a nonmonetary transaction during a period shall disclose the following in the financial statements:

a. The nature of the transaction;

b. The basis of accounting for the assets transferred; and

c. Gains or losses recognized on transfers.

24. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosure in paragraph 23 shall be included in the annual audited statutory financial reports only.

25. Entities shall disclose the amount of revenue and expense recognized from advertising barter transactions for each income statement period presented. In addition, if an entity engages in advertising barter transactions for which the fair value is not determinable within the limits of this Issue, information regarding the volume and type of advertising surrendered and received (such as the number of equivalent pages, the number of minutes, or the overall percentage of advertising volume) shall be disclosed for each income statement period presented.

Relevant Literature

26. Although not meant to be all inclusive, accounting for specific nonmonetary transactions and unique circumstances is addressed in the following statements of statutory accounting principles:

- *SSAP No. 12—Employee Stock Ownership Plans*
- *SSAP No. 25—Affiliates and Other Related Parties*
- *SSAP No. 68—Business Combinations and Goodwill*
- *SSAP No. 72—Surplus and Quasi-Reorganizations*
- *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*
- *SSAP No. 104R—Share-Based Payments*
- *INT 00-26: EITF 98-3: Determining Whether a Nonmonetary Transactions Involves Receipt of Productive Assets or of a Business*

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27. This statement updates general statutory guidance for accounting for nonmonetary transactions not specifically addressed in the statements of statutory accounting principles noted above and carries forward current statutory guidance for stock dividends and stock splits received, other types of nonmonetary transactions and involuntary conversions of nonmonetary assets to monetary assets. The guidance in this statement remains consistent with the guidance provided in SSAP No. 30R, which addresses cash dividends and requires that dividends on common stock be recorded as investment income when declared with a corresponding receivable to be extinguished upon receipt of cash. This statement carries forward the disclosure requirements related to nonmonetary transactions from SSAP No. 28.

28. This statement adopts *Accounting Principles Board Opinion No. 29, Accounting for Nonmonetary Transactions* (APB 29) as modified by *FASB No. 153: Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29* (FAS 153).

29. This statement adopts FAS 153 with modifications for references to statements of statutory accounting principles.

30. This statement continues the adoption of *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins* (ARB 43), Chapter 7, Section B, *Stock Dividends and Stock Split-ups* paragraphs 1-9 as such relates to the receipt of stock in the form of a stock in the form of a stock dividend or stock split. This conclusion is consistent with the recognition concept included in the Statement of Concepts, which states, "Revenue should be recognized only as the earnings process of the underlying underwriting or investment business is completed".

31. This statement continues the adoption of *FASB Interpretation No. 30, Accounting for Involuntary Conversions of Nonmonetary Assets to Monetary Assets* (FIN 30) with modification to provide that gain or loss contingencies be recognized in accordance with the conclusion in SSAP No. 5R and that gain or loss resulting from an involuntary conversion of nonmonetary assets to monetary assets be accounted for in continuing operations and disclosed in accordance with SSAP No. 24.

32. This statement continues the adoption of *FASB Emerging Issues Task Force Issue No. 86-29: Nonmonetary Transactions: Magnitude of Boot and the Exceptions to the Use of Fair Value* (EITF 86-29) and *FASB Emerging Issues Task Force Issue No. 93-11: Accounting for Barter Transactions Involving Barter Credits* (EITF 93-11) consistent with the general rule discussed in paragraph 27 of this statement. This statement also adopts with modification *FASB Emerging Issues Task Force Issue No. 99-17, Accounting for Advertising Barter Transactions*.

33. This statement nullifies *INT 99-21: EITF No. 98-7, Accounting for Exchanges of Similar Equity Method Investments*.

34. This statement continues the rejection of paragraph 16 of *Accounting Principles Board Opinion No. 6, Status of Accounting Research Bulletins* and *Emerging Issues Task Force No. 96-4, Accounting for Reorganizations Involving a Non-Pro Rata Split-off of Certain Nonmonetary Assets to Owners*.

35. This statement adopts with modification *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*.

Effective Date and Transition

~~35.~~36. The provisions of this statement shall be effective for nonmonetary asset exchanges occurring in fiscal periods beginning after January 1, 2007. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this statement is issued. The provisions of this statement shall be applied prospectively. The guidance in paragraph 21 related to long-lived assets to be disposed of other than by sale was previously included within *SSAP No. 90—Impairment or Disposal of Real Estate Investments*. In 2012, the guidance from SSAP No. 95 was incorporated within SSAP No.

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90, with those paragraphs in SSAP No. 95 being nullified. The original guidance included in this statement, as well as the original guidance adopted in SSAP No. 90 for long-lived assets to be disposed of other than by sale, are retained for historical purposes in Issue Paper No. 127.

~~36.~~37. This statement adopts the consensus positions of *EITF 01-1: Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash* with certain modifications to incorporate guidance in EITF 96-18 regarding the measurement date. EITF 96-18 was previously rejected by the working group in *INT 99-13: EITF 96-18: Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services* in the context of *SSAP No. 13—Stock Options and Stock Purchase Plans*; however, the measurement guidance included in Issue 1 of EITF 96-18 is adopted in this statement. The reference in paragraph 4 to *INT 03-16: Contribution of Stock*, was deleted as guidance was incorporated into SSAP No. 25 and SSAP No. 68. The guidance in paragraph 25 of this statement was originally contained within *INT 00-29: EITF 99-17: Accounting for Advertising Barter Transactions* and was effective June 12, 2000. The guidance in paragraphs 21-22 was originally contained within *INT 02-19: EITF 01-1: Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash* and was effective December 8, 2002.

REFERENCES

Relevant Issue Papers

- Issue Paper No. 127—Exchanges of Nonmonetary Assets, A Replacement of SSAP No. 28—Nonmonetary Transactions

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Statement of Statutory Accounting Principles No. 97

Investments in Subsidiary, Controlled and Affiliated Entities

STATUS

Type of Issue	Common Area
Issued	December 2, 2007
Effective Date	December 31, 2007
Affects	Supersedes SSAP No. 88; Nullifies and incorporates INT 01-07, INT 03-03, INT 04-10 and INT 08-03
Affected by	No other pronouncements
Interpreted by	INT 00-24, INT 06-07
Relevant Appendix A Guidance	A-820

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investments in subsidiaries, controlled and affiliated entities, hereinafter referred to as SCA entities.

2. This statement supersedes the conclusions reached in *SSAP No. 88—Investments in Subsidiary, Controlled, and Affiliated Entities*.

SUMMARY CONCLUSION

Definitions

3. Parent and subsidiary are defined as follows:

   a. Parent—An entity that directly or indirectly owns and controls the reporting entity;

   b. Subsidiary—An entity that is, directly or indirectly, owned and controlled by the reporting entity.

4. An affiliate is defined as an entity that is within the holding company system or a party that, directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with the reporting entity. An affiliate includes a parent or subsidiary and may also include partnerships, joint ventures, and limited liability companies as defined in *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*. Those entities are accounted for under the guidance provided in SSAP No. 48, which requires an equity method for all such investments.

5. Control is defined as the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of the investee, whether through the (a) ownership of voting securities, (b) by contract other than a commercial contract for goods or nonmanagement services, (c) by common management, or (d) otherwise. Control shall be presumed to exist if a reporting entity and its affiliates directly or indirectly, own, control, hold with the power to vote, or hold proxies representing 10% or more of the voting interests of the entity[1].

[1] Investments in an exchange traded fund (ETF), a mutual fund (as defined by the SEC) or a foreign open-end investment fund governed and authorized in accordance with regulation established by the applicable foreign jurisdiction does not reflect ownership in an underlying entity, regardless of the ownership percentage the reporting entity (or the holding company group) has of the ETF, mutual fund or foreign open-end investment fund unless ownership of the fund actually results in "control" with the power to direct or cause the direction of management of an underlying company. ETFs, mutual funds and foreign open-end investment funds are comprised of portfolios of securities subject to the regulatory requirements of the federal securities laws or the applicable foreign jurisdictions laws. ETFs, mutual funds and foreign open-end investment funds held by a reporting entity shall be reported as common stock, unless the fund qualifies for bond or preferred stock treatment per the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. Reporting entities are not required to verify that SCAs (subject to SSAP No. 97) are represented in the portfolio of securities held in ETFs, mutual funds or foreign open-end investment funds or to adjust the value of SCAs as a result of investments in ETFs, mutual funds or foreign open-end investment funds.

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6. Control as defined in paragraph 5 shall be measured at the holding company level. For example, if one member of an affiliated group has a 5% interest in an entity and a second member of the group has an 8% interest in the same entity, the total interest is 13% and therefore each member of the affiliated group shall be presumed to have control. This presumption will stand until rebutted by an evaluation of all the facts and circumstances relating to the investment based on the criteria in *FASB Interpretation No. 35, Criteria for Applying the Equity Method of Accounting for Investments in Common Stock, an Interpretation of APB Opinion No. 18.* The corollary is required to demonstrate control when a reporting entity owns less than 10% of the voting securities of an investee. The insurer shall maintain documents substantiating its determination for review by the domiciliary commissioner. An investment in an SCA entity may fall below the level of ownership described in paragraph 5, in which case, the reporting entity would discontinue the use of the equity method, as prescribed in paragraph 13.g. Additionally, through an increase in the level of ownership, a reporting entity may become qualified to use the equity method of accounting (paragraph 8.b.), in which case, the reporting entity shall add the cost of acquiring additional interest to the current basis of the previously held interest and shall apply the equity method prospectively, as of the date the investment becomes qualified for equity method accounting. Examples of situations where the presumption of control may be in doubt include the following:

a. Any limited partner investment in a limited partnership, unless the limited partner is affiliated with the general partner.

b. An entity where the insurer owns less than 50% of an entity and there is an unaffiliated individual or group of investors who own a controlling interest.

c. An entity where the insurer has given up participating rights[2] as a shareholder to the investee.

7. Investments in SCA entities meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

Applying the Market Valuation, Audited Statutory Equity and Audited GAAP Equity Methods

8. The admitted investments in SCA entities shall be valued using either the market valuation approach (as described in paragraph 8.a.), or one of the equity methods (as described in paragraph 8.b.) adjusted as appropriate in accordance with the guidance in *SSAP No. 25—Affiliates and Other Related Parties*, paragraph 18.d.

a. In order to use the market valuation approach for SCA entities, the following requirements apply:

i. The subsidiary must be traded on one of the following major exchanges: (1) the New York Stock Exchange, (2) the NASDAQ, or (3) the Japan Exchange Group;

ii. The reporting entity must submit subsidiary information to the NAIC SCA analysts for calculation of the subsidiary's market value. Such calculation could result in further discounts in market value above the established base discounts based on ownership percentages detailed below;

[2] The term "participating rights" refers to the type of rights that allows an investor to effectively participate in significant decisions related to an investee's ordinary course of business and is distinguished from the more limited type of rights referred to as "protective rights". Refer to the sections entitled: "Protective Rights" and "Substantive Participating Rights" in *EITF 96-16, Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights*. The term "participating rights" shall be used consistent with the discussion of substantive participating rights in this EITF.

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iii. Ownership percentages for determining the discount rate shall be measured at the holding company level;

iv. If an investment in a SCA results in an ownership percentage between 10% and 50%, a base discount percentage between 0% and 20% on a sliding scale basis is required;

v. If an investment in a SCA results in an ownership percentage greater than 50% up to and including 80%, a base discount percentage between 20% and 30% on a sliding scale basis is required;

vi. If an investment in a SCA results in an ownership percentage greater than 80% up to and including 85%, a minimum base discount percentage of 30% is required.

vii. Further, the SCA must have at least two million shares outstanding, with a total market value of at least $50 million in the public's control; and

viii. Any ownership percentages exceeding 85% will result in the SCA being recorded on an equity method.

b. If a SCA investment does not meet the requirements for the market valuation approach in paragraph 8.a. or, if the requirements are met, but a reporting entity elects not to use that approach, the reporting entity's proportionate share of its investments in SCAs shall be recorded as follows:

i. Investments in U.S. insurance SCA entities shall be recorded based on either 1) the underlying audited statutory equity of the respective entity's financial statements, adjusted for any unamortized goodwill as provided for in *SSAP No. 68—Business Combinations and Goodwill*[3] or 2) the underlying audited statutory equity of the respective entity's financial statements, adjusted for any unamortized goodwill, modified to remove the impact of any permitted or prescribed accounting practices that depart from the NAIC *Accounting Practices and Procedures Manual*. Reporting entities shall record investments in U.S. insurance SCA entities on at least a quarterly basis, and shall base the investment value on the most recent quarterly information available from the SCA. Entities may recognize their investment in U.S. insurance SCA entities based on the unaudited statutory equity in the SCAs year-end annual statement if the annual SCA audited financial statements are not complete as of the filing deadline. The recorded statutory equity shall be adjusted for audit adjustments, if any, as soon as the annual audited financial statements have been completed. Annual consolidated or combined audits are allowed if completed in accordance with the Model Regulation Requiring Annual Audited Financial Reports as adopted by the SCA's domiciliary state;

ii. Investments in both U.S. and foreign noninsurance SCA entities that are engaged in the following transactions or activities:

[3] If the insurance SCA employs accounting practices that depart from the NAIC accounting practices and procedures, and the reporting insurance entity has not adjusted the valuation of the insurance SCA to be consistent with the NAIC accounting practices and procedures, (i.e., retains the effect of the permitted or prescribed practice in its valuation), disclosure about those accounting practices that affect the insurance SCA's net income and surplus shall be made pursuant to paragraph 37. If the reporting entity has adjusted the investment in the insurance SCA with the resulting valuation being consistent with the accounting principles of the AP&P Manual, the disclosures in paragraph 37 are not required.

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(a) Collection of balances as described in *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*

(b) Sale/lease or rental of EDP Equipment and Software as described in *SSAP No. 16R—Electronic Data Processing Equipment and Software*

(c) Sale/lease or rental of furniture, fixtures, equipment or leasehold improvements as described in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

(d) Loans to employees, agents, brokers, representatives of the reporting entity or SCA as described in *SSAP No. 20—Nonadmitted Assets*

(e) Sale/lease or rental of automobiles, airplanes and other vehicles as described in *SSAP No. 20—Nonadmitted Assets*

(f) Providing insurance services on behalf of the reporting entity including but not limited to accounting, actuarial, auditing, data processing, underwriting, collection of premiums, payment of claims and benefits, policyowner services

(g) Acting as an insurance or administrative agent or an agent for a government instrumentality performing an insurance function (e.g. processing of state workers compensations plans, managing assigned risk plans, Medicaid processing etc).

(h) Purchase or securitization of acquisition costs

and if 20% or more of the SCA's revenue is generated from the reporting entity and its affiliates, then the underlying equity of the respective entity's audited U.S. Generally Accepted Accounting Principles (GAAP) financial statements shall be adjusted to a limited statutory basis of accounting in accordance with paragraph 9. For purposes of this section, revenue means GAAP revenue reported in the audited U.S. GAAP financial statements excluding realized and unrealized capital gains/losses. Foreign SCA entities are defined as those entities incorporated or otherwise legally formed under the laws of a foreign country. Paragraphs 22-27 provide guidance for investments in holding companies;

iii. Investments in both U.S. and foreign noninsurance SCA entities that do not qualify under paragraph 8.b.ii., shall be recorded based on the audited U.S. GAAP equity of the investee. Foreign SCA entities are defined as those entities incorporated or otherwise legally formed under the laws of a foreign country. Additional guidance on investments in downstream holding companies is included in paragraphs 22-27. Additional guidance on the use of audited foreign GAAP basis financial statements for the U.S. GAAP equity valuation amount is included in paragraph 23.b.

iv. Investments in foreign insurance SCA entities shall be recorded based on the underlying U.S. GAAP equity from the audited U.S. GAAP basis financial statements, adjusted to a limited statutory basis of accounting in accordance with paragraph 9, if available. If the audited U.S. GAAP basis financial statements are not available, the investment can be recorded on the audited foreign statutory basis financial statements of the respective entity adjusted to a limited statutory basis of accounting in accordance with paragraph 9 and adjusted for reserves of the foreign

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insurance SCA with respect to the business it assumes directly and indirectly from a U.S. insurer using the statutory accounting principles promulgated by the NAIC in the *Accounting Practices and Procedures Manual*. The audited foreign statutory basis financial statements must include an audited footnote that reconciles net income and equity on the foreign statutory basis of accounting to the U.S. GAAP basis. Foreign insurance SCA entities are defined as alien insurers formed according to the legal requirements of a foreign country.

c. The following provides guidance regarding the audits for entities covered under paragraph 8.b.:

i. The investment in the SCA shall be nonadmitted if the audited financial statements include substantial doubt about the entity's ability to continue as a going concern. Additionally, the investment shall be nonadmitted on the basis/contents of the audit opinion as detailed in paragraph 21.

ii. The recorded GAAP equity shall be adjusted for any audit adjustments resulting from either the annual audited GAAP financial statements of the respective entity or, if the entity is a member of a consolidated or combined group of insurers, the annual audited GAAP financial statements of the consolidated or combined group of companies, as soon as determined. GAAP is defined as those pronouncements included in the FASB codification.

iii. Annual consolidated or combined audits are allowed for the valuation of U.S. insurance entities if completed in accordance with the Model Regulation Requiring Annual Audited Reports as adopted by the SCA's domiciliary state.

iv. Consolidated or combined financial statements are allowed for the valuation of downstream SCA entities, including downstream SCA entities, that directly or indirectly own U.S. insurance entities, provided that the statutory financial statements of such U.S. insurance entities are audited. The audited financial statements of the downstream SCA entities shall include, as other financial information, consolidating or combining balance sheet schedule(s) showing the equity of all relevant SCA entities, non-SCA SSAP No. 48 entities, and any required intercompany eliminations. The consolidating or combining balance sheet of the downstream SCA entities shall then be adjusted for GAAP to SAP differences of the insurance entities and paragraph 8.b.ii. and 8.b.iv. entities owned directly and indirectly by the downstream SCA entities.

v. Investments in foreign SCA entities shall follow the guidance in paragraphs 8.b.ii., 8.b.iii. and 8.b.iv. based upon the nature of the SCA as described in the respective paragraphs. To fulfill the requirement for audited U.S. GAAP basis financial statements, the value of foreign SCA investments may be based on the GAAP equity from audited financial statements prepared on a foreign GAAP basis. The audited foreign GAAP basis financial statements must include an audited footnote that reconciles net income and equity on the foreign GAAP basis of accounting to the U.S. GAAP basis. The statutory carrying value of foreign insurance SCA entities (i.e., paragraph 8.b.iv. entities) and foreign noninsurance paragraph 8.b.ii. SCA entities shall include the additional adjustments as described in paragraph 9.

9. The limited statutory basis of accounting for investments in noninsurance SCA entities, subject to paragraph 8.b.ii. and foreign insurance SCA entities, subject to paragraph 8.b.iv., shall be adjusted for the following:

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a. Nonadmit assets pursuant to the following statutory accounting principles as promulgated by the NAIC in the *Accounting Practices and Procedures Manual*;

i. *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*

ii. *SSAP No. 16R—Electronic Data Processing Equipment and Software*

iii. *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

iv. *SSAP No. 20—Nonadmitted Assets*

v. *SSAP No. 21R—Other Admitted Assets* (e.g., collateral loans secured by assets that do not qualify as investments are nonadmitted under SAP)

vi. *SSAP No. 29—Prepaid Expenses*

vii. *SSAP No. 105R—Working Capital Finance Investments*

b. Expense costs that are capitalized in accordance with GAAP but are expensed pursuant to statutory accounting as promulgated by the NAIC in the *Accounting Practices and Procedures Manual* (e.g., deferred policy acquisition costs, preoperating, development and research costs, etc.);

c. Adjust depreciation for certain assets in accordance with the following statutory accounting principles:

i. *SSAP No. 16R—Electronic Data Processing Equipment and Software*

ii. *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

iii. *SSAP No. 68—Business Combinations and Goodwill*

d. Nonadmit the amount of goodwill of the SCA in excess of 10% of the audited U.S. GAAP equity of the SCA's last audited financial statements.

e. Nonadmit amount of the net deferred tax assets (DTAs) of the SCA in excess of 10% of the audited U.S. GAAP equity of the SCA's last audited financial statements.

f. Nonadmit any surplus notes held by the SCA issued by the reporting entity.

g. Adjust the U.S. GAAP annuity account value reserves of a foreign insurance SCA, with respect to the business it wrote directly, using the commissioners' annuity reserve valuation method (CARVM) as defined in paragraphs 14 and 15 of Appendix A-820 (including the reserving provisions in the various Actuarial Guidelines which support CARVM). The valuation interest rate and mortality tables to be used in applying CARVM should be that prescribed by the foreign insurance SCA's country of domicile. If the Foreign SCA's country of domicile does not prescribe the necessary tables and/or rates, no reserve adjustment shall be made.

Note that the outcome of these adjustments can result in a negative equity valuation of the investment for all paragraph 8.b.ii. entities. For a paragraph 8.b.iv. entity, the application of these adjustments will stop at zero, and will not result in negative equity valuation unless the paragraph 8.b.iv. entity provides services to the reporting entity or its affiliates or holds assets on behalf of the reporting entity. If such services, including reinsurance transactions, are occurring, the adjustments required in this paragraph can result in a

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negative equity valuation. (See additional equity method application guidance in paragraph 13.e. regarding guarantees and financial support.)

10. For investments in entities recorded on an equity method (paragraph 8.b.i. through 8.b.iv.), the amount to be recorded at acquisition shall be defined as the initial investment in an investee at cost as defined in SSAP No. 68, paragraph 3, adjusted to exclude any investments in an investee's preferred stock and/or surplus notes[4]. This guidance shall be followed for initial investments as well as subsequent investments in the investee.

11. For investments in entities recorded on an equity method (paragraph 8.b.i. through 8.b.iv.) after the date of acquisition, the investment amount shall be 1) adjusted for the amortization of statutory goodwill as defined in SSAP No. 68, and 2) adjusted, with a corresponding unrealized gain or loss, for the reporting entity's share of undistributed earnings and losses of the investee (net of dividends declared[5]). (This results in a reduction of the investment amount when dividends declared are in excess of the undistributed accumulated earnings attributable to the investee.) The following additional adjustment, based on the equity method applied for the investment, shall also be made:

a. For investments in scope of paragraph 8.b.i. (based on audited statutory equity) the investment amount shall be adjusted for the reporting entity's share of the change in special surplus funds, other than special surplus funds and unassigned funds (surplus), as defined in *SSAP No. 72—Surplus and Quasi-Reorganizations*. Additionally, the investment amount shall be adjusted, with a corresponding unrealized gain or loss, for the reporting entity's share of other changes in the investee's surplus (e.g., the change in the investee's nonadmitted assets);

b. For investments in scope of paragraphs 8.b.ii., 8.b.iii. and 8.b.iv. (underlying audited GAAP equity), the investment amount shall be adjusted for the reporting entity's share of adjustments recorded directly to the investee's stockholder's equity under GAAP, with a corresponding entry to unrealized gain or loss. For investments in scope of paragraphs 8.b.ii. and 8.b.iv. (underlying audited GAAP with limited statutory adjustments), the investment amount shall also be adjusted in accordance with paragraph 9.

12. If the reporting entity uses the market valuation approach outlined in paragraph 8.a., changes in that valuation after initial acquisition shall be included in unrealized gains and losses

13. On at least a quarterly basis, the procedures set forth below shall be followed by a reporting entity in applying an equity method of accounting (as described in paragraphs 8.b.i. through 8.b.iv.), as applicable, to investments in SCA entities:

a. A difference between the cost of an investment and the underlying equity in the statutory or GAAP book value, as applicable, of the acquired company at the date of acquisition shall be accounted for in accordance with SSAP No. 68 however, positive goodwill for noninsurance SCA entities subject to paragraph 8.b.ii. and foreign insurance SCA entities subject to paragraph 8.b.iv. shall be subject to the admissibility criteria in paragraph 9.d. rather than the admissibility criteria of paragraph 7 of SSAP No. 68.

b. A transaction of an investee of a capital nature that affects the reporting entity's share of stockholders' equity of the investee shall be reflected as an unrealized gain or loss (e.g., where the investee issues additional stock or a new class of stock that impacts the reporting

[4] The guidance in paragraphs 28-32 shall be applied for the separate reporting of preferred stock and surplus notes.

[5] Dividends are recognized in investment income when declared.

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entity's equity ownership in the investee, the reporting entity's recorded investment shall be adjusted to reflect the transaction);

c. Realized gains or losses on the sale of an investment in a SCA entity shall be recorded in an amount equal to the difference at the time of sale between the selling price and carrying amount of the investment plus any previously recorded unrealized gain or loss;

d. If financial statements of an investee are not sufficiently timely for the reporting entity to apply an equity method to the investee's current results of operations, the reporting entity shall record its share of the earnings or losses of an investee from the most recent available financial statements. A lag in reporting shall be consistent from period to period. This paragraph does not apply to a SCA valued under paragraph 8.b.i.;

e. For entities subject to paragraphs 8.b.i., 8.b.ii., 8.b.iii. and 8.b.iv., a reporting entity's share of losses of an investee may equal or exceed the carrying amount of an investment accounted for by an equity method plus advances made by the investor. The reporting entity shall discontinue applying an equity method when the investment (including advances) is reduced to zero[6] and shall not provide for additional losses, while still continuing to track the amount of unreported equity method losses, until any future equity method income can be reported. If the reporting entity has guaranteed obligations of the investee or is otherwise committed to provide further financial support for the investee, the provisions of *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* shall be followed. As the entire equity method loss (subject to the financial guarantee/commitment) shall be recognized under SSAP No. 5R, it does not also need to be recognized under SSAP No. 97. If the investee subsequently reports net income, the reporting entity shall resume applying an equity method only after its share of that net income equals the share of net losses not recognized during the period that an equity method was suspended;

f. When an investee has outstanding cumulative preferred stock, the reporting entity shall compute its share of earnings (losses) after deducting the investee's preferred dividends, whether or not such dividends are declared;

g. An investment in a SCA entity may fall below the level of ownership described in paragraph 5 from the sale of a portion of an investment by the reporting entity, the sale of additional interests by an investee, or other transactions. The reporting entity shall discontinue accruing its share of the earnings or losses of the investee for an investment that no longer qualifies for an equity method. The earnings or losses that relate to the investment interests retained by the reporting entity and that were previously accrued shall remain as a part of the carrying amount of the investment. The investment account shall not be adjusted retroactively under the conditions described in this subparagraph. However, dividends received by the investor in subsequent periods which exceed the reporting entity's share of earnings for such periods shall be applied as a reduction of the carrying amount of the investment.

14. Once the reporting entity elects to use a valuation approach for a particular subsidiary, the reporting entity may not change the valuation method to another method without the approval of the domiciliary commissioner. For instance, if an entity selects the market valuation method, it may not change to an equity

[6] Although the SCA is reported at zero in the investment schedule, a guarantee liability (either contingent or noncontingent) may be required to be reported under SSAP No. 5R. Additionally, refer to the guidance related to discontinuance of an equity method in paragraphs 15-17 and *INT 00-24: EITF 98-13: Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of the Investee* and *EITF 99-10: Percentage Used to Determine the Amount of Equity Method Losses*. As detailed in INT 00-24, a reporting entity's share of losses in an SCA shall be applied to other investments held in the SCA once the SCA (common stock) investment has been reduced to zero.

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method or vice versa without approval from the domiciliary commissioner. Further, in order for an entity to transfer from a paragraph 8.a. or 8.b.ii. valuation to a paragraph 8.b.iii. valuation, the SCA shall not exceed the 20% threshold (as defined in paragraph 8.b.ii.) for three consecutive years prior to making the change. When an investment qualifies for use of another method of accounting, the reporting entity shall adopt the new method of accounting and the investment shall be adjusted to reflect the reporting entity's equity interest in the SCA entity under the new method. A corresponding amount shall be recorded as an unrealized gain or loss.

15. If an additional investment, in whole or in part, represents, in substance, the funding of prior losses, the entity should recognize previously suspended losses only up to the amount of the additional investment determined to represent the funding of prior losses. Whether the investment represents the funding of prior losses depends on the facts and circumstances.

16. Judgment is required in determining whether prior losses are being funded and that all available information should be considered in performing the related analysis. The following are certain factors to consider in that regard. However, no one factor should be considered presumptive or determinative.

a. Whether the additional investment is acquired from a third party or directly from the investee. When the additional investment is purchased from a third party and the investee does not obtain additional funds either from the investor or the third party, it is unlikely that, in the absence of other factors, prior losses are being funded.

b. The fair value of the consideration received in relation to the value of the consideration paid for the additional investment. For example, if the fair value of the consideration received is less than the fair value of the consideration paid, it may indicate that prior losses are being funded to the extent that there is disparity in the value of the exchange.

c. Whether the additional investment results in an increase in ownership percentage of the investee. In instances in which the investment is made directly with the investee, the investor should consider the form of the investment and whether other investors are making simultaneous investments proportionate to their interests. Investments made without a corresponding increase in ownership or other interests, or a pro rata equity investment made by all existing investors, may indicate that prior losses are being funded.

d. The seniority of the additional investment relative to existing equity of the investee. An investment in an instrument that is subordinate to other equity of the investee may indicate that prior losses are being funded.

17. Upon making the additional investment, the investor should evaluate whether it has become otherwise committed to provide financial support to the investee.

18. A reporting entity that owns an interest in itself via direct ownership of shares of an upstream intermediate or ultimate parent shall reduce the value of such shares for the reciprocal ownership. If the shares of the parent are owned indirectly by a reporting entity, via a downstream SCA entity, the directly held entity, which owns the parent's shares, shall have its value reduced for the reciprocal ownership.

19. Any parent reporting entity that owns an interest in itself via either direct or indirect ownership of a down-stream affiliate, which in turn owns shares of the parent reporting entity, shall eliminate its interest in these shares from the valuation of such affiliate.

Investment in Parent-Issued Surplus Notes

20. Any parent reporting entity that has issued a surplus note, which has been acquired by an SCA (held directly or indirectly) shall adjust the investment in the SCA to eliminate the issued surplus note to prevent double counting of the surplus note at the parent reporting entity. Without adjustment, the issued

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surplus note would be reported both as an increase in surplus by the parent reporting entity, as well as an admitted asset of the parent through the "investment in an SCA." The surplus note shall also be eliminated for instances in which the SCA acquires any portion of outstanding surplus notes issued by the parent through any means (e.g., directly acquired from the parent, acquired through a third-party broker, or via the market).

Qualified Versus Unqualified Opinions

21. Various opinions can be issued in which an entity can record certain investments under the GAAP Equity method of accounting. The reporting entity shall record investments that require audited GAAP equity in the manner described below when the audit opinion on the GAAP financial statements contains the following language:

a. The investment shall be nonadmitted if the audit opinion contains a disclaimer of opinion for the most recent statement of financial position presented in the financial statements.

b. The investment shall be nonadmitted if the audit opinion contains a qualified opinion due to a scope limitation that impacts the most recent statement of financial position presented in the financial statements and the impact of the scope limitation cannot be quantified. However, if the impact of the scope limitation is quantified in the audited financial statements or the audit opinion, the investment shall be admitted and the reporting entity's valuation of the investment shall be determined based on the GAAP equity of the investee, adjusted to exclude the impact of the quantified scope limitation.

c. The investment shall be nonadmitted if the audit opinion contains a qualified opinion due to a departure from GAAP that impacts the most recent statement of financial position presented in the financial statements and the impact of such departure is not quantified in either the auditor's report or the footnotes to the financial statements (see quantification exception related to the valuation of a U.S. insurance entity on the basis of U.S. statutory accounting principles discussed below). However, if the impact of the departure from GAAP is quantified in the audited financial statements or the audit opinion, the investment shall be admitted and the reporting entity's valuation of the investment shall be determined based on the GAAP equity of the investee, adjusted to exclude the impact of the quantified departure from GAAP. EXCEPTION: There is no need to quantify the impact of a departure from GAAP in either the auditor's report or the footnotes to the financial statements if a qualified audit opinion is issued due to a departure from GAAP and the departure is related to the valuation of an U.S. insurance entity on the basis of U.S. statutory accounting principles. In such cases, the investment shall be admitted without quantifying the departure.

d. The investment shall be nonadmitted if the audit opinion contains an adverse opinion due to a departure from GAAP that impacts the most recent statement of financial position presented in the financial statements and the impact of such departure is not quantified in either the auditor's report or the footnotes to the financial statements (see quantification exception related to the valuation of a U.S. insurance entity on the basis of U.S. statutory accounting principles discussed below). However, if the impact of the departure from GAAP is quantified in the audited financial statements or the audit opinion, the investment shall be admitted and the reporting entity's valuation of the investment shall be determined based on the GAAP equity of the investee, adjusted to exclude the impact of the quantified departure from GAAP. EXCEPTION: There is no need to quantify the impact of a departure from GAAP in either the auditor's report or the footnotes to the financial statements if an adverse audit opinion is issued due to a departure from GAAP and the departure is related to the valuation of an U.S. insurance entity on the basis of U.S. statutory

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accounting principles. In such cases, the investment shall be admitted without quantifying the departure.

e. The investment shall be nonadmitted if the audit report or accompanying financial statements/notes contains explanatory language indicating there is an unalleviated substantial doubt about the investee's ability to continue as a going concern.

Valuation of Investments in Downstream Holding Companies

22. SSAP No. 48 requires the financial statements of joint ventures, partnerships, and/or limited liability companies in which the downstream noninsurance holding company has a minor ownership interest or otherwise lacks control, i.e., ownership interest is less than 10% (hereinafter referred to as "non-SCA SSAP No. 48 entities"), to be valued using U.S. GAAP basis financial statements. Valuation of a downstream holding company, including its investments in SCA entities, depends upon the nature of the SCA entities and non-SCA SSAP No. 48 entities it holds in accordance with paragraph 8 of this statement. All liabilities, commitments, contingencies, guarantees or obligations of the downstream noninsurance holding company, which are required to be recorded under applicable statutory accounting guidance, shall be reflected in the parent insurance reporting entity's determination of the carrying value of the investment in the downstream noninsurance holding company, if not already recorded in the financial statements of the downstream noninsurance holding company. If an SCA investment of the downstream holding company does not meet the provisions of paragraph 8.a. or if it elects not to use the guidance in paragraph 8.a., and instead uses the guidance in paragraph 8.b., the downstream holding company would be valued as the sum of the following (if applicable):

a. Investments by a downstream holding company in U.S. insurance SCA entities are recorded based upon the guidance in paragraph 8.b.i.;

b. Investments by a downstream holding company in noninsurance SCA entities that are engaged in transactions or activities described in paragraph 8.b.ii., are recorded based upon the guidance in paragraph 8.b.ii.;

c. Investments by a downstream holding company in noninsurance SCA entities that do not qualify under paragraph 22.b. shall be recorded based upon the guidance in paragraph 8.b.iii.;

d. Investments by a downstream holding company in foreign insurance SCA entities shall be recorded based upon the guidance in paragraph 8.b.iv.; and

e. Any other assets and/or liabilities of the downstream holding company (not addressed in paragraphs 22.a. through 22.d.) shall be valued in accordance with the applicable SSAP.

For purposes of applying paragraphs 22-27 of this statement, a downstream holding company shall be considered to be the parent reporting entity's investment in a SCA entity. See paragraphs 26 and 27 for a limited exception to the audited financial statements requirement for downstream noninsurance holding companies which meet specified conditions.

Admissibility Requirements of Investments in Downstream Holding Companies

23. To meet the admissibility requirements of this statement, unless the limited exception to the audited financial statements requirement discussed in paragraphs 26 and 27 applies, an annual audit of the financial statements of SCA entities, including the downstream holding company valued under paragraphs 8.b.i through 8.b.iv. must be obtained. The requirement for audited financial statements may be met by utilizing any one of the following methods:

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a. Audited US GAAP financial statements of the downstream SCA holding company. (Consolidated or combined financial statements are allowed encompassing one or more downstream holding companies, including such holding companies that directly own U.S. insurance entities, provided that the statutory financial statements of such U.S. insurance entities are audited. Annual consolidated or combined audits are allowed for insurance entities if completed in accordance with the Model Regulation Requiring Annual Audited Reports as adopted by the SCA's domiciliary state.) The audited financial statements of the downstream holding company shall include as other financial information, consolidating or combining balance sheet schedule(s) showing the equity of all relevant SCA entities and non-SCA SSAP No. 48 entities, and any required intercompany eliminations. The consolidating or combining balance sheet schedule shall separately present those entities owned directly by the downstream holding company. The consolidating or combining balance sheet shall then be adjusted for GAAP to SAP differences for paragraph 8.b.i., 8.b.ii. and 8.b.iv. entities owned directly or indirectly by the downstream holding company. The adjusted amount would then be the reported value of the investment in the downstream holding company at the higher-level reporting entity; or

b. Audited foreign GAAP-basis financial statements of the downstream SCA holding company. (Consolidated or combined financial statements are allowed encompassing one or more downstream holding companies, including such holding companies that directly own U.S. insurance entities, provided that the statutory financial statements of such U.S. insurance entities are audited. Annual consolidated or combined audits are allowed for insurance entities if completed in accordance with the Model Regulation Requiring Annual Audited Reports as adopted by the SCA's domiciliary state.) The audited foreign GAAP basis financial statements shall include an audited footnote disclosure within the financial statements that reconciles each consolidated entity's net income and equity on a foreign basis of accounting to a U.S. GAAP basis. The audited financial statements of the downstream holding company shall include as other financial information, consolidating or combining balance sheet schedule(s) showing the equity of all relevant SCA entities non-SCA SSAP No. 48 entities, and any required intercompany eliminations. The consolidating or combining balance sheet schedule shall separately present those entities owned directly by the downstream holding company. The consolidating or combining balance sheet shall then be adjusted for GAAP to SAP differences of the insurance entities and paragraph 8.b.ii. and paragraph 8.b.iv. entities owned directly or indirectly by the downstream holding company. The adjusted amount would then be the reported value of the investment in the downstream holding company at the higher-level reporting entity; or

c. Individual audits of the downstream holding company and the downstream holding company's investments in individual SCA entities.

24. If the downstream noninsurance holding company does not meet the requirements of paragraph 26, audited GAAP financial statements, as described in paragraph 23, are required for the downstream noninsurance holding company and its SCA and non-SCA investments in order for the investment in the downstream noninsurance holding company to be classified as an admitted asset.

25. A purchased downstream holding company is valued in accordance with the provisions of paragraphs 22-25 and the provisions of SSAP No. 68.

Limited Exceptions to the Audit Requirements for Downstream Noninsurance Holding Companies

26. This statement requires that investments in SCA entities be recorded using one of the valuation methods described in paragraph 8 in order to be admitted assets. Each of the paragraph 8.b. valuation methods require the financial statements of SCA entities, including downstream noninsurance holding

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companies, to be audited in order for the investments in SCA entities to be admitted assets. Likewise, SSAP No. 48 requires the financial statements of joint ventures, partnerships, and/or limited liability companies in which the downstream noninsurance holding company has a minor ownership interest or otherwise lacks control, i.e., ownership interest is less than 10% to be audited (U.S. GAAP) in order to be admitted assets. There is a limited exception to the requirement to have audited financial statements of a downstream noninsurance holding company, provided that the entities owned by the downstream noninsurance holding company (paragraph 8.b.iii. entity) have audited financial statements as described in paragraphs 26 and 27.

27. The process of admitting audited investments in entities owned by an unaudited downstream noninsurance holding company SCA entity will be known as a "look through." In order to admit the investments in audited SCAs or the audited non-SCA SSAP No. 48 entities owned by an unaudited downstream noninsurance holding company, a reporting entity may apply the look through approach, provided all of the following conditions are met:

a. The downstream noninsurance holding company is an 8.b.iii entity, and

b. The downstream noninsurance holding company does not own any other assets which are material to the downstream holding company other than the audited SCA entities and/or audited non-SCA SSAP No. 48 entities, and

c. The downstream noninsurance holding company is not subject to liabilities, commitments, contingencies, guarantees or obligations which are material to the downstream noninsurance holding company.

If an investment in a downstream noninsurance holding company meets the requirements set forth above, the reporting entity can admit the individual audited SCA entities and/or audited non-SCA SSAP No. 48 entities; however, unaudited immaterial assets of the downstream noninsurance holding company are to be carried at the lesser of the paragraph 8 valuation or nonadmitted (e.g. some equity method investments are required to be carried at a negative value due to either statutory adjustments or to parental obligations to keep funding the subsidiary). If a holding company structure has more than one downstream non-insurance holding company, each downstream non-insurance holding company may be looked through, provided each downstream non-insurance holding company meets all of the conditions in paragraph 27.

Investment in Preferred Stock or Surplus Notes of a Subsidiary, Controlled and Affiliated Entity

28. Investments in common stock, preferred stock and surplus notes are reported separately. Care should be taken to avoid double counting of the separate investments. When the SCA investee has issued multiple equity components such as common stock, preferred stock and/or surplus note(s) the total reported equity of the SCA investee must be separated into the respective components in order to determine the equity attributable to each class.

29. In order to establish the equity value of the common stock investment in an SCA, the reporting entity reduces the total equity of the SCA by the SCA's (issuer's) value of the preferred stock and/or surplus notes on the issuer's balance sheet (not the reporting entity's book/adjusted carrying value for the SCA's preferred stock and/or surplus notes held).

30. Investments in the preferred stock of an SCA shall be accounted for and reported in accordance with the provisions of *SSAP No. 32R—Preferred Stock*.

31. Investments in the surplus notes of an SCA shall be accounted for and reported in accordance with the provisions of *SSAP No. 41R—Surplus Notes*.

32. The following example is provided to illustrate the accounting and reporting. The reporting entity holds 100% of the preferred stock. The SCA issued the preferred stock for $50,000. The investment in the SCA, measured in accordance with this statement is $250,000 including the preferred stock of the SCA.

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The investment in the SCA is $200,000 ($250,000-50,000) and the preferred stock is measured and reported in accordance with SSAP No. 32R.

Impairment

33. For any decline in the fair value of an investment in a SCA entity that is other than temporary(INT 06-07), the investment shall be written down to fair value as the new cost basis and the amount of the write down shall be accounted for as a realized loss. The write down shall first be considered as an adjustment to any portion of the investment that is nonadmitted (e.g., goodwill). The new cost basis shall not be changed for subsequent recoveries in fair value. Future declines in fair value, which are determined to be other than temporary shall be recorded as realized losses. An impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to recover the carrying amount of the investment or there is evidence indicating inability of the investee to sustain earnings, which would justify the carrying amount of the investment. A fair value of an investment that is below the carrying amount based on the statutory equity method or the existence of investee operating losses may indicate a loss in value, however, they are not necessarily indicative of a loss in value that is other than temporary.

Consolidation

34. Majority-owned subsidiaries shall not be consolidated for individual entity statutory reporting. This does not exempt certain reporting entities that are members of an affiliated group from the requirement to issue consolidated or combined annual statements as supplemental information in accordance with NAIC guidelines.

Disclosures

35. All SCA investments within the scope of this statement (except paragraph 8.b.i. entities) shall include disclosure of the SCA balance sheet value (admitted and nonadmitted) as well as information received from the NAIC in response to the SCA filing (e.g., date and type of filing, NAIC valuation amount, whether resubmission of filing is required). This disclosure shall include an aggregate total of all SCAs (except paragraph 8.b.i. entities) with detail of the aggregate gross value under this statement with the admitted and nonadmitted amounts reflected on the balance sheet. (As noted in paragraph 4, joint ventures, partnerships and limited liability companies are accounted for under the guidance in SSAP No. 48. As such, those entities are not subject to the disclosures in this statement, unless specifically directed by SSAP No. 48.)

a. For all periods presented, a reporting entity whose shares of losses in an SCA exceeds its investment in the SCA shall disclose its share of losses. (This is required regardless of a guarantee or commitment of future financial support to the SCA.) This disclosure shall include the following:

   i. The reporting entity's accumulated share of the SCA losses not recognized during the period that the equity method was suspended;

   ii. The reporting entity's share of the SCA's equity, including negative equity;

   iii. Whether a guaranteed obligation or commitment for financial support exists; and

   iv. The amount of the recognized guarantee under SSAP No. 5R.

This disclosure shall apply beginning in the period the SCA's equity initially falls below zero and shall continue to be disclosed as long as the SCA investment is in a deficit position. Additionally, the reporting entity shall detail in a narrative disclosure whether losses in the SCA have impacted other investments as required by *INT 00-24: EITF 98-13: Accounting by an Equity Method Investor*

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for Investee Losses When the Investor Has Loans to and Investments in Other Securities of the Investee and *EITF 99-10: Percentage Used to Determine the Amount of Equity Method Losses.*

36. The significance of an investment to the reporting entity's financial position and results of operations shall be considered in evaluating the extent of disclosures of the financial position and results of operations of an investee. The following disclosures shall be made for all investments in SCA entities that exceed 10% of the total admitted assets of the reporting entity:

a. Financial statements of a reporting entity shall disclose (i) the name of each SCA entity and percentage of ownership of common stock, (ii) the accounting policies of the reporting entity with respect to investments in SCA entities, and (iii) the difference, if any, between the amount at which the investment is carried and the amount of underlying equity in net assets (i.e., goodwill, other nonadmitted assets, fair value or discounted fair value adjustments, adjustments pursuant to SSAP No. 25, paragraph 19.d.) and the accounting treatment of the difference;

b. For those SCA entities for which a quoted market price is available, the aggregate value of each SCA investment based on the quoted price and the difference, if any, between the amount at which the investment is carried and the quoted price shall be disclosed;

c. Summarized information as to assets, liabilities and results of operations shall be presented for SCA entities, either individually or in groups;

d. Conversion of outstanding convertible securities, exercise of outstanding options and warrants and other contingent issuances of an investee may have a significant effect on an investor's share of reported earnings or losses. Accordingly, material effects of possible conversions, exercises or contingent issuances shall be disclosed in notes to the financial statements of the reporting entity; and

e. For those SCA entities in which the reporting entity elected, or was required, to change its valuation method as described in paragraph 14, a description of the reason for the change and the amount of adjustment recorded as unrealized gains or losses shall be disclosed. The entity shall also disclose whether commissioner approval was obtained in accordance with paragraph 14.

37. A reporting entity that reports an investment in an insurance SCA (per paragraph 8.b.i.) for which the audited statutory equity reflects a departure from the NAIC statutory accounting practices and procedures (e.g., permitted or prescribed practices) shall disclose the following:

a. A description of the accounting practice, with a statement that the practice differs from the NAIC statutory accounting practices and procedures.

b. The monetary effect on net income and surplus reflected by the insurance SCA as a result of using an accounting practice that differed from NAIC statutory accounting practices and procedures.

c. Whether the RBC of the insurance SCA would have triggered a regulatory event had it not used a prescribed or permitted practice.

d. The reported entity's investment in the insurance SCA per the audited statutory equity, and the investment in the insurance SCA the reporting entity would have reported if the insurance SCA had completed statutory financial statements in accordance with the NAIC statutory accounting practices and procedures.

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38. A reporting entity that calculates its investment in a foreign insurance subsidiary by adjusting annuity GAAP account value reserves using CARVM and the related Actuarial Guidelines shall disclose the interest rates and mortality assumptions used in the calculation as prescribed by the insurance department of the foreign country.

39. Any commitment or contingent commitment to a SCA entity shall be disclosed (e.g., guarantees or commitments to provide additional capital contributions).

40. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment and how fair value was determined.

41. If a reporting entity holds an investment in a downstream noninsurance holding company, the reporting entity may look-through the downstream noninsurance holding company to the value of (i) SCA entities having audited financial statements and/or (ii) joint ventures, partnerships, and/or limited liability companies having audited financial statements in which the downstream noninsurance holding company has a minor ownership interest or otherwise lacks control, i.e., ownership interest is less than 10% in lieu of obtaining an audit of the financial statements of the downstream noninsurance holding company (provided the limited exception to the audited financial statements requirement contained in paragraphs 26-27 applies).

42. If a reporting entity utilizes the look-through approach for the valuation of the downstream noninsurance holding company instead of obtaining audited financial statements of the downstream noninsurance holding company, the financial statements of the reporting entity shall include the following disclosures:

a. The name of the downstream noninsurance holding company;

b. The carrying value of the investment in the downstream non insurance holding company;

c. The fact that the financial statements of the downstream noninsurance company are not audited;

d. The fact that the reporting entity has limited the value of its investment in the downstream noninsurance holding company to the value contained in the audited financial statements, including adjustments required by this statement, of SCA entities and/or non-SCA SSAP No. 48 entities owned by the downstream noninsurance holding company and valued in accordance with paragraphs 22-25;

e. The fact that all liabilities, commitments, contingencies, guarantees or obligations of the downstream noninsurance holding company, which are required to be recorded as liabilities, commitments, contingencies, guarantees or obligations under applicable accounting guidance, are reflected in the reporting entity's determination of the carrying value of the investment in the downstream noninsurance holding company, if not already recorded in the financial statements of the downstream noninsurance holding company.

43. Investments reported using an equity method from paragraph 8.b.ii. through 8.b.iv. may have fiscal year ends, not calendar year ends. To recognize a change to the reporting year-end of an equity method investee, including changes in, or the elimination of, previously existing differences (lag period) due to the reporting entity's ability to obtain financial results from a reporting period that is more consistent with, or the same as, that of the reporting entity, the guidance included in *FASB Emerging Issues Task Force 06-9:*

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Reporting a Change in (or the elimination of) a Previously Existing Difference between the fiscal Year-End of a Parent Company and That of a Consolidated Entity or between the Reporting Period of an Investor and That of an Equity Method Investee that defines such reporting period changes as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* shall be followed. For instances in which this change in accounting principle occurs, disclosure requirements of SSAP No. 3 shall be followed.

44. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures in paragraph 36.d. shall be included in the annual audited statutory financial reports only.

Relevant Literature

45. This statement adopts the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*.

46. This statement adopts *ASU 2016-07, Investments—Equity and Joint Ventures*, modified to reflect statutory terms, including the definition of control and statutory reporting concepts. This statement adopts *FASB Interpretation No. 35, Criteria for Applying the Equity Method of Accounting for Investments in Common Stock, an Interpretation of APB Opinion No. 18* as guidance to be considered in determining the existence of control.

47. This statement adopts with modification EITF 06-9 to include:

a. Adopt the guidance that defines such reporting period changes as a change in accounting principle in accordance with SSAP No. 3, modified to apply only to equity method investments. For instances in which this change in accounting principle occurs, disclosure requirements of SSAP No. 3 shall be followed.

b. The consolidation guidance in EITF 06-9 is rejected.

c. Changes affecting companies reporting investments in SCA entities using the equity method: Investments in paragraph 8.b.i. entities are required to be calendar year-end. Investments in paragraphs 8.b.ii. through 8.b.iv. entities may have other fiscal year ends, thus this issue could apply to equity method investments under paragraphs 8.b.ii. through 8.b.iv. or under equity method valued investments that fall within the scope of SSAP No. 48.

48. This statement rejects *ASU 2020-01, Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815), Clarifying the Interactions between Topic 321, Topic 323 and Topic 815, ASU 2019-06, Intangibles—Goodwill and Other Business Combinations, and Non-for-Profit Entities, ASU 2011-10, Derecognition of in Substance Real Estate, APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock, AICPA Accounting Interpretations APB 18, The Equity Method of Accounting for Investments in Common Stock:* Accounting Interpretations of *APB Opinion No. 18, FASB Technical Bulletin No. 79-19, Investor's Accounting for Unrealized Losses on Marketable Securities Owned by an Equity Method Investee, FASB Emerging Issues Task Force No. 87-21, Change of Accounting Basis in Master Limited Partnership Transactions, FASB Emerging Issues Task Force No. 96-16, Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights*, *FASB Emerging Issues Task Force No. 98-2: Accounting by a Subsidiary or Joint Venture for an Investment in the stock of Its Parent Company or Joint Venture Partner* and *FASB Staff Position No. APB 18-1*, *Accounting by an Investor for Its Proportionate Share of Accumulated Other Comprehensive Income of an Investee Accounted for under the Equity Method in Accordance with APB Opinion No. 18 upon a Loss of Significant Influence.*

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Effective Date and Transition

49. This statement is effective for reporting periods ending on and after December 31, 2007. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Detail of 2011 amendments that relocated guidance from this statement to SSAP No. 32R and SSAP No. 68 is provided in those statements respectively. Guidance reflected in paragraph 21, incorporated from *INT 03-03: Admissibility of Investments Recorded Based on the Audited GAAP Equity of the Investee when a Qualified Opinion is Provided* was originally effective December 7, 2003. Guidance reflected in paragraphs 15-17 incorporated from *INT 04-10: Accounting for Subsequent Investments in an Investee after Suspension of Equity Method Loss Recognition* was originally effective December 5, 2004. Guidance in paragraph 43 was previously included within *INT 08-03: EITF 06-9: Reporting a Change in (or the elimination of) a Previously Existing Difference between the fiscal Year-End of a Parent Company and That of a Consolidated Entity or between the Reporting Period of an Investor and That of an Equity Method Investee* and was effective for periods beginning May 31, 2008.

REFERENCES

Other

Purposes and Procedures Manual of the NAIC Investment Analysis Office

Relevant Issue Papers

Issue Paper No. 118—Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46

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EXHIBIT A – SCA REPORTING PROCESS

50. SCA entities, except for domestic SCA insurance company investments accounted for under paragraph 8.b.i of this statement, in which the reporting entity has an equity interest (common or preferred stock), are required to be filed with the NAIC. Nonadmitted assets are not required to be filed in a Sub 2 as long as they were nonadmitted, or had a zero value, for the full reporting period (all interim and annual reporting). Immaterial asset SCAs do not have an automatic exclusion from filing, as immateriality of an SCA will be ascertained by the state of domicile of the insurance reporting entity, but companies are allowed to request an exemption from the domiciliary state to not file an SCA on the basis that it is immaterial. The filing process does not include investments within the scope of SSAP No. 48.

51. Except for domestic SCA insurance company investments accounted for under paragraph 8.b.i., all SCA investments within the scope of this statement, purchased during any one calendar year, shall be reported to the NAIC on a Sub 1 form within 90 days of the acquisition or formation of the investment; this includes nonadmitted, zero-valued and immaterial SCAs. The NAIC will process that filing in the same year but will not at that time approve or disapprove a value for the SCA investment. By August 31 of each year, the insurance company shall submit a Sub 2 filing for the previously purchased SCA investment reported on a Sub 1 form and later that year, the NAIC will approve a value for the transaction. For SCAs that routinely receive their audit reports after the August 31 deadline, a filing deadline of one month after the audit date shall be applied. Filers must provide previous years' audit reports to verify an audit report dated after August 31 in order to not be charged a late fee for a Sub 2 filing that is filed after the August 31 deadline. The value approved by the NAIC at the conclusion of the Sub 2 form filing is reported by the insurance company on its financial statement blank. If the insurance company has reported a value for the SCA investment on its financial statement blank that differs from the value approved by the NAIC, the insurer is required to adjust the reported value in its next quarterly financial statement blank unless otherwise directed by the insurer's state of domicile.

52. Insurance companies shall use one of the valuation methods described in paragraph 8 to calculate the value of their investments in insurance and non-insurance SCA companies. An insurance company shall calculate the value of its investments in foreign insurance and all non-insurance company SCA entities and report the value to the NAIC no later than August 31, or one month after the audit report date for SCAs that routinely receive their audits after August 31 for existing SCA investments, and within 90 days of the acquisition or formation of a new SCA investment.

Initial Reporting of SCA Investments

53. Reporting the acquisition or formation of a new investment is accomplished by submitting a completed Sub 1 form for each investment disclosing, (i) the valuation reported or to be reported by the insurance company on its latest or next quarterly financial statement blank, (ii) which method of those described in paragraph 8 was used to arrive at the valuation, (iii) the factual context of the transaction, and (iv) economic and business motivations for the transaction. The submission will be processed by the NAIC only if the NAIC determines it has been provided with all material information with respect to all SCA companies of the reporting insurance company that require valuation.

54. The purpose of a Sub 1 filing is to gather basic information about the SCA. If the NAIC determines that the reported transaction meets the tests specified, it will complete the filing in the VISION database. If the NAIC determines that the transaction does not meet the tests specified, it will not complete the filing in the VISION database and instead shall notify the reporting insurance company and the state of domicile in writing of its determination.

Subsequent Reporting of SCA Investments

55. By August 31 or one month after the audit report date of each year and subsequent to the reporting of an SCA investment on the Sub 1 form, the insurance company shall submit a Sub 2 form filing, with all supporting documentation for foreign SCAs provided in English, for the same SCA investment.

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Additionally, by August 31 or one month after the audit report date of each year, any insurance company that has made a Sub 2 form filing in a previous year must update the information by filing an updated Sub 2 form filing.

56. Each year the NAIC shall compile a list of all SCA investments (excluding insurance company SCAs (paragraph 8.b.i.) nonadmitted and zero-value SCAs) reported as Sub 1 form filings for which a Sub 2 form filing has not yet been received. For these transactions, the NAIC will notify the responsible reporting insurance company and its state of domicile that it has not received a Sub 2 filing for the SCA investment.

57. The purpose of the Sub 2 filing is to determine whether the value calculated by the reporting insurance company for the SCA investment is appropriate and to approve that or some other value for reporting on the insurer's financial statement blank.

58. An insurance company that concludes an SCA transaction at year-end may be unable to file a Sub 1 form prior to the time it would be required to file a Sub 2 form. Where this is the case, the NAIC is authorized to accept and review a Sub 1 filing from such an insurance company and to accept and review the Sub 2 filing after the Sub 1 filing review has been completed.

59. No filing of an investment in a domestic SCA insurance company valued under paragraph 8.b.i. shall be required to be made with the NAIC.

Consistency in Application of Chosen Valuation Method

60. The valuation method used for a specific SCA company shall be determined by the guidance in paragraph 8. If a reporting insurance company previously selected the Market Valuation Method and wished to change to an Equity Method (or vice versa), they may only do so with the approval of the domiciliary commissioner. Once the approval of the domiciliary commissioner has been obtained, the reporting insurance company shall provide the NAIC with evidence of that approval as part of the Sub 1 or Sub 2 filing.

61. For reporting insurance companies that use the Market Valuation Method, the reporting insurance company shall obtain the discount rate to be applied from the NAIC. The discounts identified in Exhibit E are minimum discounts. The NAIC calculation may result in discounts in market value higher than those shown in Exhibit E.

Assessment and Review of Sub 1 Form

62. Upon receipt of the reporting insurance company's Sub 1 filing, the NAIC shall conduct an assessment in the following manner:

a. If the NAIC is aware of any broad regulatory concerns or issues affecting the reporting insurance company or the reported SCA investment, it shall determine whether such concerns or issues are relevant to valuation of the SCA investment. If so, the NAIC shall take such action as seems appropriate under the circumstances.

b. The NAIC shall ensure that the value reported by the insurance company on a Sub 1 form has been arrived at by application of one of the permitted valuation methods described in paragraph 8. If a reporting insurance company submits a Sub 1 form filing that reports a value calculated under an inappropriate method, the NAIC shall contact the insurer to resolve the discrepancy or it shall recalculate the value of the SCA investment under the most appropriate valuation method and notify the reporting insurance company of such action.

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c. The NAIC shall review the factual, business and economic context of the transaction to determine whether, (i) the SCA investment appears to be an arms-length business arrangement with a reasonable economic value to the reporting insurance company, (ii) the valuation method chosen is reasonable in view of the factual, business and economic context of the transaction, (iii) the transaction is reasonable in the context of all the known facts surrounding the insurance company and its operations, and (iv) the value reported appropriately reflects economic value to the insurance company. The NAIC may consider other factors that appear relevant from the context of the transaction including:

i. The specific tax, accounting or other regulatory treatment sought.

ii. Whether the transaction effects a legally effective, binding and permanent transfer of the risks and rewards of ownership.

iii. The effect of the SCA valuation on the solvency of the insurer.

iv. The degree of affiliation between the insurer and the party from whom such company was acquired, the form of the consideration (cash, property or the exchange of stock), evidence of ability to recover cost and whether the acquisition price represented the result of arms-length dealing between economic equals.

v. The right to dividends or other payments from the SCA and any limitations thereto.

vi. The nature, extent and demonstrable financial value of the business operations of the SCA.

vii. The value of the assets owned by the SCA.

If the NAIC determines that the transaction does not seem to present economic value to the insurance company, or that the transaction tends to obscure issues that might be relevant to an NAIC member or that the information provided is insufficient or unreliable as a basis upon which to make a determination, then the NAIC shall notify the reporting insurance company and the NAIC member of the reporting insurance company's state of domicile and request guidance.

d. The NAIC shall review whether the reporting insurance company has correctly applied the correct valuation guidance under paragraph 8 and made adjustments, if applicable, under paragraph 9.

63. If the SCA investment reported on the Sub 1 form filing is deemed to meet the assessment and reviews described in paragraph 62, the NAIC shall complete the filing in the VISION database. A completed filing will be a Sub 1 filing where the reported SCA investment meets the tests described above. The completed filing will be revised to a value if and when the filer submits a Sub 2 form on the same transaction and the NAIC approves a final value based on the information provided. (Assignment of completion to an SCA investment does not mean, and shall not be interpreted to mean, that the NAIC is expressing an opinion as to the value claimed by the reporting insurance company for the reported SCA investment. The completion implies only that, based on the information provided, the NAIC has determined that the SCA investment meets the tests described in paragraph 62.)

Assessment and Review of Sub 2 Form

64. By August 31 or one month after the audit report date of each year, the NAIC shall initiate a review of all SCA investments for which new Sub 2 form filings have been received as well as an annual update review of Sub 2 SCA investments already logged in the VISION database. The NAIC review shall encompass a review of the most recent annual statutory reporting by the parent insurance company's

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Schedule Y (to ascertain the identity of the members of the holding company system and to ensure that information for all SCA companies has been submitted), a review of the parent's financial statement blank to review the last reported value for the SCA investments and a review of the VISION database to determine whether SCA debt and SCA preferred securities have been assigned NAIC designations. As part of its analysis, the NAIC shall review the portion of the bond investments carried by the parent or a subsidiary insurer with a **Z** notation. If the NAIC determines that the portion of the **Z** bonds shown on the documentation is significant, the NAIC shall not process the Sub 2 filing until the insurance company reports the bonds to permit removal of the **Z** notation. Beginning with year-end 2019, two new suffixes will apply: **YE** and **IF**. YE means that the security is a properly filed annual update that the SVO has determined will not be assigned an NAIC designation by the close of the year-end reporting cycle. The symbol YE is assigned by the SVO pursuant to the carryover administrative procedure described in ~~Part Two of~~ the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. When the SVO assigns the symbol YE it also assigns the NAIC designation in effect for the previous reporting year. IF means that the security is an initial filing that has been properly filed with the SVO but which the SVO has determined will not be assigned an NAIC designation by the close of the year-end reporting cycle. The symbol IF is assigned by the SVO and communicates that the insurer should self-designate the security for year-end and identify it with the symbol IF. IF, therefore, also communicates to the regulator that the NAIC designation reported by the insurance company was not derived by or obtained from the SVO, but has been determined analytically by a reporting insurance company.

65. Upon completion of the procedures described above, the NAIC will determine whether the value reported by the insurance company on the current SCA filing was calculated in accordance with the instructions for the valuation method chosen and verify that the filed value reflects the adjustments required by paragraph 9.

66. Upon approval of a value (including making necessary adjustments), the NAIC will complete the Sub 2 filing with the approved value in the status field of the VISION database.

67. The NAIC shall report its determination to the insurance company. If a significant discrepancy exists between the value claimed by the reporting insurance company and the value approved by the NAIC, the NAIC shall communicate the discrepancy with the company. If the NAIC cannot come to a conclusion based on the support provided, the filing can be rejected in VISION, and written notification will be provided to the reporting insurance company and the company's state of domicile of this action. This correspondence will be sent to the domiciliary state. Filers are able to download their review information from the NAIC filing system.

Additional Reporting Instructions

68. A reporting entity that has direct ownership of shares of an upstream intermediate or ultimate parent owns an interest in itself and is required to reduce the value of those shares from the value of the reporting entity. This is referred to as elimination of reciprocal ownership.

69. If the shares of the parent are owned indirectly by a reporting entity, for example, because the reporting entity owns a downstream SCA entity that directly owns shares in the parent, the entity that owns the parent’s shares must reduce its value by the value of the shares in the parent. This is referred to as elimination of the reciprocal ownership.

70. Any parent reporting entity that owns an interest in itself via either direct or indirect ownership of a down-stream affiliate, which in turn owns shares of the parent reporting entity, shall eliminate its proportionate interest in these shares from the valuation of such affiliate.

71. Pursuant to paragraph 22, in lieu of separate GAAP audits of SCA entities of the downstream holding company, the insurer can choose to have a GAAP audit performed at the holding company level with a consolidating balance sheet showing GAAP equity of all the SCA entities. The consolidating balance

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sheet shall then be adjusted for GAAP to SAP differences of the insurance entities as described in this statement. This adjusted amount would then be the reported value of the investment in downstream holding company at the higher-level insurance company.

72. Investments in the surplus notes of an SCA shall be accounted for in accordance with the provisions of SSAP No. 41R. If the reporting entity also holds an investment in preferred stock or surplus notes, refer to paragraphs 28-32 of this statement.

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EXHIBIT B – ILLUSTRATIONS

Accounting for SCAs

This illustration is intended to provide an example of the application of paragraphs 8.b.ii. and 8.b.iii. of this statement. Where an SCA meets the criteria of paragraph 8.b.ii., the illustration further demonstrates the necessary adjustments described in paragraph 9. While not all inclusive, the illustration is representative of the process and adjustments necessary to comply with this statement. That is, the reporting entity must, first, determine which sub-section of paragraph 8 applies with respect to each SCA. Secondly, where the reporting entity has determined that an SCA meets the criteria of paragraph 8.b.ii. or 8.b.iv., then the carrying amount is adjusted in accordance with the sub-section, which includes adjustments contained in the provisions of paragraph 9.

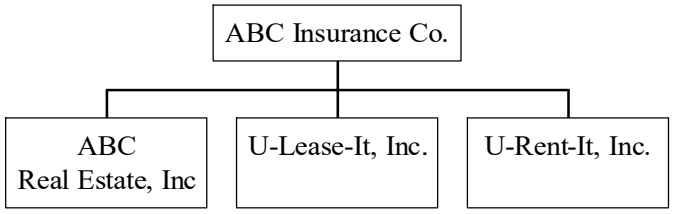
The ABC Insurance Company owns 100% of three subsidiaries:

1. ABC Real Estate, Inc. – owns and manages real estate properties and has no inter-company transactions

2. U-Lease-It, Inc. – leases furniture and equipment to local businesses including the insurance company. Lease fees received from ABC were $10 million each in 20x2 and 20x1.

3. U-Rent-It, Inc. – leases EDP equipment to local businesses including the insurance company. Lease fees received from ABC were $2 million each in 20x2 and 20x1.

ABC Insurance Company



Determination and application of adjustments to audited GAAP equity methods (paragraph 8.b. of this statement)

ABC Real Estate, Inc. – the company is not engaged in any activities described in paragraph 8.b.ii. No adjustments are made, and ABC Insurance Company records its investment based upon audited GAAP equity in accordance with 8b.iii.

U-Lease-It, Inc. – the company is engaged in activities described in paragraph 8.b.ii., leasing furniture and equipment. The fees paid by ABC and reflected in income of U-Lease-It, Inc. exceed 20% of GAAP revenue calculated as follows:

U-Lease-It, Inc.	(Millions)	
	20x1	**20x2**
GAAP revenue	46.5	46.4
Less:		
Realized capital gains/(losses)	6	(.2)
Adjusted GAAP revenue	45.9	46.6
Lease fees from ABC	10.0	10.0
Fees/adjusted GAAP revenue	21.8%	21.5%

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U-Rent-It, Inc. – the company is engaged in activities described in paragraph 8.b.ii., leasing EDP equipment. The fees paid by ABC and reflected in income of U-Rent-It, Inc. do not exceed 20% of GAAP revenue. No adjustments are made, and ABC Insurance Company records its investment based upon audited GAAP equity in accordance with 8b.iii. The calculation test is as follows:

U-Rent-It, Inc.	(Millions)	
	20x2	**20x1**
GAAP revenue	32.6	30.5
Lease fees from ABC	2.0	2.0
Fees/GAAP revenue	6.1%	6.6%

Adjustments to audited GAAP equity for U-Lease-It, Inc.

	(Millions)	
	20x2	**20x1**
Audited GAAP equity	129	130
Nonadmit furniture & equipment	(250)	(260)
Nonadmit excess goodwill *	(2)	(2)
Adjusted GAAP equity	(123)	(132)

*Goodwill adjustment - 20x2=$15- (10% x $130[20x1GAAP equity] and 20x1=$15-(10% x $129.9 [20x0 GAAP equity])

Note: No DTA adjustment since the amount is less than 10% of GAAP equity

Schedule D Affiliated Common Stocks for ABC Insurance Company

	(Millions)	
	20x2	**20x1**
ABC Real Estate Inc.	223	219
U-Lease-It, Inc.	(123)	(132)
U-Rent-It, Inc.	30	27
Total	130	114

Note: The change in carrying value between years of $16 million is reported as an unrealized gain in 20x2.

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Illustrated Balance Sheets

ABC Insurance Company

	20x2	20x1		20x2	20x1
Net Admitted Assets			Liabilities		
Bonds	11,210	11,150	Policy reserves	12,516	12,394
Common stock (unaffiliated)	325	315	Contract claims	30	29
Common Stock (affiliated)	130	114			
Real estate	120	125	Expenses due and accrued	14	13
Mortgage loans	1,685	1,640	Misc. liabilities	250	245
Cash	10	7	Total liabilities	12,810	12,681
Sub-total	13,480	13,351	Common stock	100	100
Other assets	20	14	Unassigned funds	590	584
Total	13,500	13,365	Total equity	690	684
			Total	13,500	13,365

ABC Real Estate, Inc.

	20x2	20x1		20x2	20x1
Assets			Liabilities		
Cash	10	7	Notes payable	260	220
Bonds (available for sale)	110	103	Misc. liabilities	17	11
Real estate investments	330	280	Total liabilities	277	231
Other assets	50	60			
Total	500	450	Common stock	15	15
			Retained earnings	208	204
			Total equity	223	219
			Total	500	450

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U-Lease-It, Inc.

	20x2	20x1		20x2	20x1
Assets			Liabilities		
Cash	5	7	Accounts payable	15	12
Bonds (available for sale)	20	18	Notes payable	183	190
Furniture & equipment	250	260	Total liabilities	198	202
Investments in subs (15.0 mil. Goodwill)	45	42	Common stock	15	15
Federal tax recoverable (DTA)	7	5	Retained earnings	114	115
Total	327	332	Total equity	129	130
			Total	327	332

Summary of Operations

	20x2	20x1
Revenues:		
Interest income	8.1	9.0
Realized capital gains/(losses)	0.6	(0.2)
Investment in sub	3.0	2.6
Lease fees	34.8	35.0
Total	46.5	46.4
Expenses:		
General Administration	6.4	6.2
Depreciation	42.4	41.0
Total	48.8	47.2
Net income before taxes	(2.3)	(0.8)
Federal income tax benefit	0.8	0.3
Net income	(1.5)	(0.5)
Unrealized capital gains/losses	0.4	0.6

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U-Rent-It, Inc.

	20x2	20x1		20x2	20x1
Assets			Liabilities		
Cash	6	6	Accounts payable	3	4
Bonds (available for sale)	5	4	Notes payable	202	199
EDP equipment	220	216	Total liabilities	205	203
Other assets	4	4			
Total	235	230	Common stock	10	10
			Retained earnings	20	17
			Total equity	30	27
			Total	235	230

Summary of Operations

	20x2	20x1
Revenues:		
Interest income	0.5	0.4
Lease fees	32.1	30.1
Total	32.6	30.5
Expenses:		
General Administration	3.0	3.0
Depreciation	25.7	24.5
Total	28.7	27.5
Net income before taxes	3.9	3.0
Federal income tax	(1.3)	(1.0)
Net income	2.6	2.0
Unrealized capital gains/losses	0.4	0.6

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EXHIBIT C – IMPLEMENTATION QUESTIONS AND ANSWERS

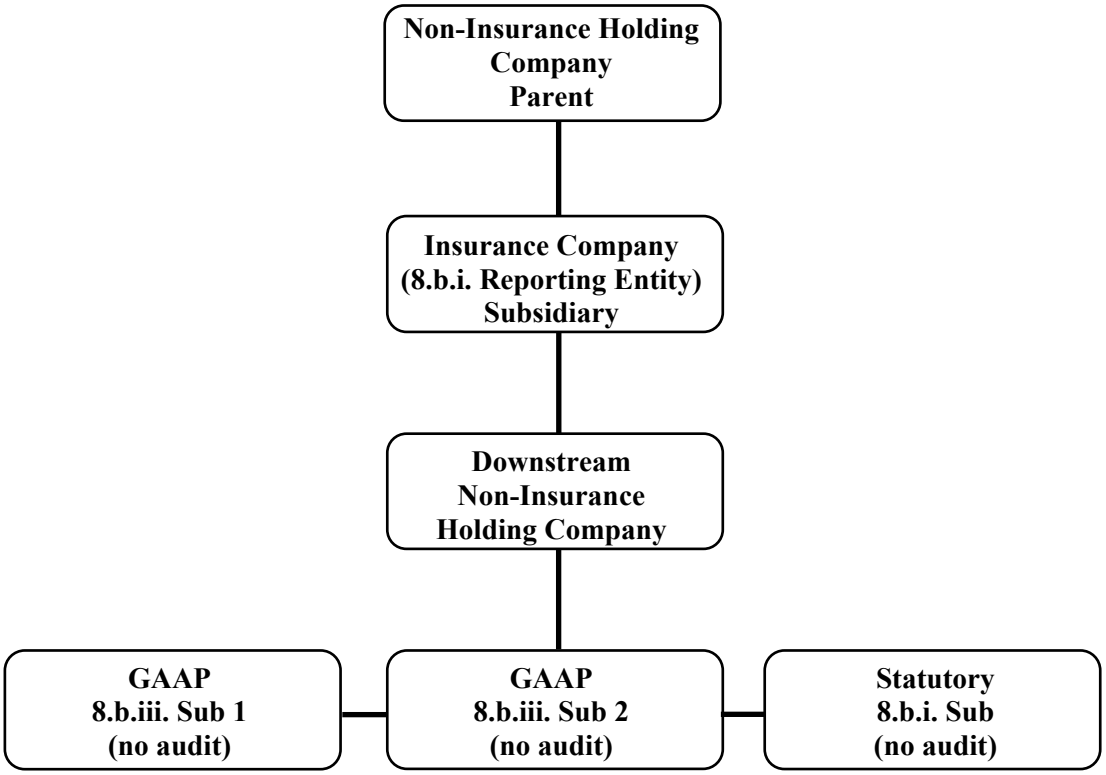
1. **Q – Is the list of activities listed in paragraph 8.b.ii.(f) of SSAP No. 97 meant to be all-inclusive? The guidance is as follows:**

> 8.b.ii.(f) Providing insurance services on behalf of the reporting entity including but not limited to accounting, actuarial, auditing, data processing, underwriting, collection of premiums, payment of claims and benefits, policyowner services

1.1 **A –** No, the Working Group did not intend for this list to be all-inclusive, but rather to be used as examples of the types of functions that can be performed by non-insurance companies. The purpose of the list is to set forth examples of activities that are often performed by an insurer directly that can result in less conservative values if performed by an entity that is not required to utilize statutory accounting as defined within the NAIC *Accounting Practices and Procedures Manual*. Therefore, the reporting entity, the auditor, and the regulator should consider whether the purpose of having the subsidiary is to avoid statutory accounting principles as discussed in *SSAP No. 25—Affiliates and Other Related Parties*, paragraph 18.d., and adjust the value of the SCA as appropriate. SSAP No. 25, paragraph 19.d. reads as follows:

> Transactions which are designed to avoid statutory accounting practices shall be reported as if the reporting entity continued to own the assets or to be obligated for a liability directly instead of through a subsidiary.

2. **Q – As illustrated below, would an audit of the upstream holding company with consolidating balance sheets of the insurance company meet the requirements for auditing the subsidiaries under SSAP No. 97?**



2.1 **A –** No, SSAP No. 97 is specific in that it only allows audited GAAP financial statements of the downstream holding company level (See paragraph 23).

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2.2 So, in the example provided above, the reporting entity cannot use an audit of the upstream holding company as the basis for complying with the audit requirements of SSAP No. 97. The primary purpose of the audit is to provide assurance that the valuation of the entity being considered is not materially misstated. Although assurance of this type would be provided for within an unqualified opinion of an upstream holding company, it would only be provided for in the context of the entity being audited. Since the materiality level for an upstream holding company is likely to be set at a higher level, the potential for material misstatement for the reporting entity's subsidiary(ies) could still exist within that unqualified opinion. It should also be noted, however, that individual state insurance holding company laws would still require an audit of the ultimate controlling entity.

3. **Q – Are consolidated, consolidating or combined audited financial statements allowed to meet the requirements for SSAP No. 97? Definitions of these types of audited financial statements are presented below:**

- Consolidated Audited Financial Statements (*ARB 51: Consolidated Financial Statements*, paragraph 1)

1. The purpose of consolidated statements is to present, primarily for the benefit of the shareholders and creditors of the parent company, the results of operations and the financial position of a parent company and its subsidiaries essentially as if the group were a single company with one or more branches or divisions. There is a presumption that consolidated statements are more meaningful than separate statements and that they are usually necessary for a fair presentation when one of the companies in the group directly or indirectly has a controlling financial interest in the other companies.

- Consolidating Audited Financial Statements (*ARB 51: Consolidated Financial Statements*, paragraph 24)

24. In some cases, parent-company statements may be needed, in addition to consolidated statements, to indicate adequately the position of bondholders and other creditors or preferred stockholders of the parent. Consolidating statements, in which one column is used for the parent company and other columns for particular subsidiaries or groups of subsidiaries, often are an effective means of presenting the pertinent information.

- Combined Audited Financial Statements (*ARB 51: Consolidated Financial Statements*, paragraphs 22 and 23)

23. To justify the preparation of consolidated statements, the controlling financial interest should rest directly or indirectly in one of the companies included in the consolidation. There are circumstances, however, where combined financial statements (as distinguished from consolidated statements) of commonly controlled companies are likely to be more meaningful than their separate statements. For example, combined financial statements would be useful where one individual owns a controlling interest in several corporations which are related in their operations. Combined statements would also be used to present the financial position and the results of operations of a group of unconsolidated subsidiaries. They might also be used to combine the financial statements of companies under common management.

24. Where combined statements are prepared for a group of related companies, such as a group of unconsolidated subsidiaries or a group of commonly controlled companies, intercompany transactions and profits or losses should be eliminated, and if there are problems in connection with such matters as minority interests, foreign operations, different fiscal periods, or income taxes, they should be treated in the same manner as in consolidated statements.

3.1 **A –** In this example, only consolidating and combined financial statements are allowed under SSAP No. 97. Combined audited financial statements are used to present the financial position and results of operations of a group of unconsolidated commonly controlled enterprises. Although U.S. Generally Accepted Auditing Standards requirements for combined statements are similar to those

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required for consolidated financial statements, combined statements are allowed for purposes of meeting the requirements of this statement. (Consolidated or combined financial statements are allowed encompassing one or more downstream SCA entities, including downstream SCA entities that directly or indirectly own U.S. insurance entities provided that the statutory financial statements of such U.S. insurance entities are audited. Annual consolidated or combined audits are allowed for insurance entities if completed in accordance with the Model Regulation Requiring Annual Audited Reports as adopted by the SCA's domiciliary state.)

4. **Q – Does a balance sheet audit meet the admissibility test within SSAP No. 97, or would a full audit be required?**

4.1 **A –** The Working Group intended for a full financial statement audit to be performed, rather than a limited reporting engagement, in accordance with AU Section 508, paragraph 33 which states:

> ***Limited reporting engagements.*** The auditor may be asked to report on one basic financial statement and not on the others. For example, he or she may be asked to report on the balance sheet and not on the statements of income, retained earnings or cash flows. These engagements do not involve scope limitations if the auditor's access to information underlying the basic financial statements is not limited and if the auditor applies all the procedures he considers necessary in the circumstances; rather, such engagements involve limited reporting objectives. [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 79, December 1995.]

4.2 In addition, within SSAP No. 97, paragraph 8.c.ii. (line 1), there is a reference to the "annual GAAP audit," which indicates a full audit. A limited engagement audit was not the intent when SSAP No. 97 or its predecessors, were developed.

4.3 Therefore, SSAP No. 97 requires the presentation of the balance sheet, income statement, statement of surplus and cash flows of each admitted entity to be presented, along with the corresponding notes to the financial statements (which can be accomplished as a whole).

5. **Q – Does the audit opinion provided on the subsidiaries financial statements have to be clean or unqualified in order for the SCA investment to be admitted?**

5.1 **A –** Paragraph 21 addresses various opinions that can be issued in which an entity can record certain investments under the GAAP Equity method of accounting. In certain cases, such as when the audit opinion is a disclaimer of opinion or there is indication that there is substantial doubt about the entity's ability to continue as a going concern, the guidance states the investment shall be nonadmitted. In instances where there is an unalleviated substantial doubt about the entity's ability to continue as a going concern listed in any part of the audit report or accompanying financial statements/notes, the investment shall be nonadmitted. In addition, if there is a qualified opinion due to a departure from GAAP (or an adverse opinion) or due to a scope limitation, the investment shall be nonadmitted unless the impact of the departure is quantified within the audit opinion (see quantification exception related to the valuation of a U.S. insurance entity on the basis of U.S. statutory accounting principles discussed below). In cases where the departure is quantified, the reporting entity would admit the amount after adjusting for the quantified departure from GAAP. An audit report that contains a qualified or adverse opinion for any other reason than for what is stated within paragraph 21 would result in the nonadmissibility of the investment within that subsidiary. There is no need to quantify the impact of a departure from GAAP in either the auditor's report or the footnotes to the financial statements if a qualified audit opinion is issued due to a departure from GAAP and the departure is related to the valuation of an U.S. insurance entity on the basis of U.S. statutory accounting principles. In such cases, the investment shall be admitted without quantifying the departure.

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6. **Q – Do GAAP audits for non-insurance entities need to be completed before the annual statement or audited financial statements are filed? They are required to be completed annually, but should there be clarification on when the audits are due?**

6.1 **A –** Paragraph 13.d. of SSAP No. 97 allows for a lag time if the audits of the investees are not completed as of the reporting date, as long as the lag is on a consistent annual basis and the SCA is not valued under paragraph 8.b.i. The following is an excerpt from paragraph 13.d. (bolded for emphasis). The SCA entity is still required to be audited annually.

> 13.d. If financial statements of an investee are not sufficiently timely for the reporting entity to apply an equity method to the investee's current results of operations, the reporting entity shall record its share of the earnings or losses of an investee from the **most recent available financial statements. A lag in reporting shall be consistent from period to period**. This paragraph does not apply to a SCA valued under paragraph 8.b.i.

7. **Q – Is it possible for an SCA investment valued using an equity method to be reported as a negative value?**

7.1 **A –** Yes, the equity method noninsurance SCA could have a negative equity. For example, SSAP No. 97, paragraph 8.b.ii., relating to noninsurance SCA entities may require some assets to be reported as a negative value (nonadmitted) in paragraph 9. In this example, a paragraph 8.b.ii. SCA subsidiary that is only holding furniture, which is nonadmitted, would be reflected with negative equity to the extent the value of the nonadmitted asset(s) exceed(s) reported equity. It should be noted that although SSAP No. 97, paragraph 13.e., discusses some situations in which the equity method should be discontinued, this does not apply to SCA entities, which meet the requirements of paragraph 8.b.ii. In addition, SSAP No. 97, paragraph 13.e., lists some situations where the equity method for paragraph 8.b.ii. and paragraph 8.b.iv. entities would result in a valuation that is less than zero.

8. **Q – Paragraph 13.e. of SSAP No. 97 lists some situations where the equity method should be discontinued. If the equity method is discontinued, does the reporting entity cease tracking equity losses?**

8.1 **A –** No, the reporting entity does not cease tracking losses related to the investment in the SCA if an equity method is discontinued. If the equity method is discontinued, follow the guidance in paragraphs 15-17 and *INT 00-24: EITF 98-13: Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of the Investee and EITF 99-10: Percentage Used to Determine the Amount of Equity Method Losses*.

8.2 INT 00-24 lists situations that might require the reporting entity to write down other investments in the SCA subsidiary, such as loans, because of continuing losses in the SCA investment. Paragraphs 15-17 provides guidance to assist in determining whether prior losses are being funded if the reporting entity purchases additional stock, etc. after suspending the equity method. Paragraphs 15-17 in INT 00-24 note that even if the equity method is not being applied, the investment should be tracked to determine if additional losses have to be applied to other items and to determine if the investment in the SCA has a future recovery.

9. **Q – SSAP No. 97, paragraphs 28-32, provides guidance on segregating the equity from common stock from the equity in the form of preferred stock and surplus notes. This guidance is required for reporting reasons and to prevent double counting of these items in the SCA equity. This section indicates that preferred stock is deducted from the total equity. The guidance notes that reporting entities report their investments in preferred stock in accordance with *SSAP No. 32R—Preferred Stock*, which requires reporting at book value, fair value, or the lower of book value or fair value. When deducting the preferred stock from the equity of the SCA, which measure of preferred stock is to be utilized; the investor's reporting valuation or the Issuer's value in the equity section of their balance sheet?**

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9.1 **A –** In order to establish the equity value of the common stock investment in an SCA, the reporting entity reduces the total equity of the SCA by the SCA's (Issuer's) value of the preferred stock on the issuer's balance sheet (not the reporting entity's Book/Adjusted Carrying Value for the SCA's preferred stock held). Continuing from the example in paragraph 32, if the reporting entity's Book/Adjusted Carrying Value for the SCA preferred stock is currently $40,000, the SCA's issuing value of the preferred stock ($50,000) would still be used to calculate the total equity of the SCA ($250,000 - $50,000 = $200,000). It should be noted this calculation does not affect the preferred stock valuation of $40,000 on the books of the investor.

10. **Q – If a parent reporting entity owns another insurance company that has obtained a permitted practice, or exemption or waiver from its state of domicile from the annual statutory audit requirement, would the parent be automatically allowed to admit the investment in the unaudited subsidiary?**

10.1 **A –** No, the parent would need to obtain a permitted practice allowing the parent reporting entity to admit the non-audited insurance company due to the admissibility requirements of SSAP No. 97.

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EXHIBIT D – DETERMINING THE VALUATION METHOD UNDER SSAP NO. 97

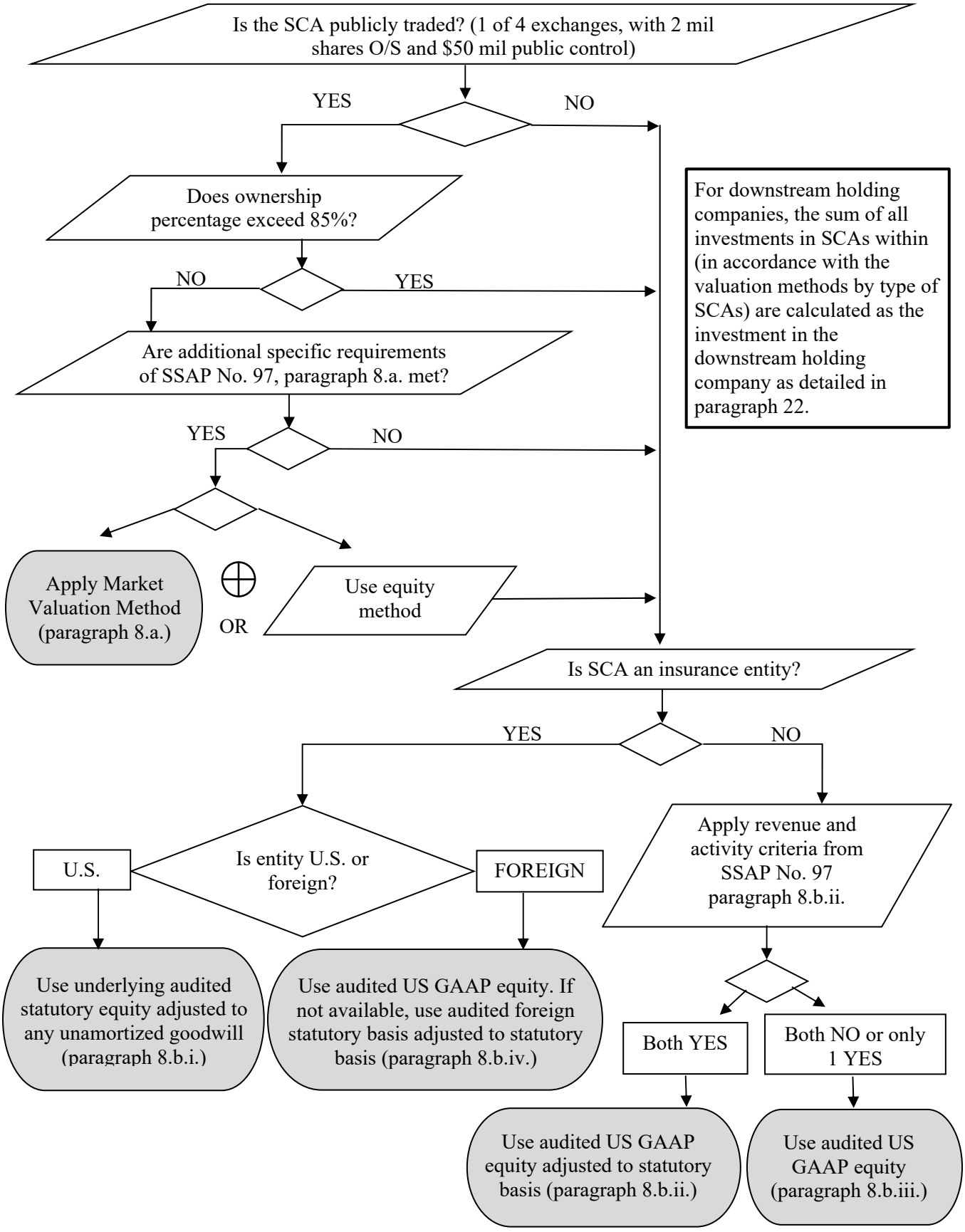

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EXHIBIT E – SLIDING SCALE DISCOUNTING OF SCA ENTITIES USING THE MARKET VALUATION APPROACH

This chart illustrates the sliding scale discounting by ownership percentage that is described in paragraphs 8.a.iv., 8.a.v. and 8.a.vi. of this statement for investments in subsidiary controlled or affiliated entities which are carried using the market valuation approach.

Ownership Percentage	Discount Percentage	Ownership Percentage	Discount Percentage
10%	0.00%	48%	19.00%
11%	0.50%	49%	19.50%
12%	1.00%	50%	20.00%
13%	1.50%	51%	20.33%
14%	2.00%	52%	20.67%
15%	2.50%	53%	21.00%
16%	3.00%	54%	21.33%
17%	3.50%	55%	21.67%
18%	4.00%	56%	22.00%
19%	4.50%	57%	22.33%
20%	5.00%	58%	22.67%
21%	5.50%	59%	23.00%
22%	6.00%	60%	23.33%
23%	6.50%	61%	23.67%
24%	7.00%	62%	24.00%
25%	7.50%	63%	24.33%
26%	8.00%	64%	24.67%
27%	8.50%	65%	25.00%
28%	9.00%	66%	25.33%
29%	9.50%	67%	25.67%
30%	10.00%	68%	26.00%
31%	10.50%	69%	26.33%
32%	11.00%	70%	26.67%
33%	11.50%	71%	27.00%
34%	12.00%	72%	27.33%
35%	12.50%	73%	27.67%
36%	13.00%	74%	28.00%
37%	13.50%	75%	28.33%
38%	14.00%	76%	28.67%
39%	14.50%	77%	29.00%
40%	15.00%	78%	29.33%
41%	15.50%	79%	29.67%
42%	16.00%	80%	30.00%
43%	16.50%	81%	30.00%
44%	17.00%	82%	30.00%
45%	17.50%	83%	30.00%
46%	18.00%	84%	30.00%
47%	18.50%	85%	30.00%

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EXHIBIT F – ILLUSTRATION OF THE APPLICATION OF INT 00-24

XYZ Investment in ABC Company

1. ABC Company is a life insurance company, formed January 2, 20X1, to sell health insurance in the state of New York. On January 2, 20X1, XYZ Insurance Company invested $500,000 in ABC, and purchased 100,000 shares of common stock at par, and 40,000 shares of preferred stock at par. ABC Preferred stock is non-voting, 5% cumulative.

2. XYZ determined it has obtained a controlling interest in ABC as XYZ owns 50% of the voting interests of ABC. XYZ accounted for its investment in ABC Insurance Company under the statutory equity method of accounting. The following table is selected information from the financial statements of ABC Insurance Company.

			20X1 – 20X4		
	1/2/20X1	12/31/20X1	12/31/20X2	12/31/20X3	12/31/20X4
Capital and Surplus:					
Common stock, $1 par, 200,000 shares issued and outstanding	$200,000	$200,000	$200,000	$200,000	$200,000
Preferred stock, $10 par, 100,000 shares issued and outstanding	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Surplus Notes			$500,000	$500,000	$500,000
Unassigned Funds (Surplus)		$130,000	($180,000)	($630,000)	($1,430,000)
Total Capital and Surplus	$1,200,000	$1,330,000	$1,520,000	$1,070,000	$270,000

			20X5 – 20X9		
	12/31/20X5	12/31/20X6	12/31/20X7	12/31/20X8	12/31/20X9
Capital and Surplus:					
Common stock, $1 par, 200,000 shares issued and outstanding	$200,000	$200,000	$200,000	$200,000	$200,000
Preferred stock, $10 par, 100,000 shares issued and outstanding	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Surplus Notes	$500,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Unassigned Funds (Surplus)	($1,980,000)	($1,830,000)	($1,280,000)	($430,000)	$820,000
Total Capital and Surplus	($280,000)	$370,000	$920,000	$1,770,000	$3,020,000

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3. At 1/2/20X1, XYZ recorded the following entry to record its investment in ABC:

Investment in ABC Common stock	$100,000	
Investment in ABC Preferred stock	$400,000	
Cash		$500,000

To record initial investment in ABC Insurance Company

4. During the year ended 12/31/20X1, ABC had statutory net income before dividends of $200,000. At 12/31/20X1, ABC declared and paid a 5% preferred dividend, and a common stock dividend of $.10 per share. XYZ recorded the following entries:

Cash	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X1.

Investment in ABC Common stock	$75,000	
Unrealized Gain/Loss		$75,000

To record 20X1 unrealized gain on investment in ABC Common. (($200,000 - $50,000) * 50%)

Cash	$10,000	
Unrealized Gain/Loss	$10,000	
Dividend Income		$10,000
Investment in ABC Common stock		$10,000

To record 20X1 dividend on ABC Common. (100,000 shares * $.10)

5. During the year ended 12/31/20X2, ABC issued an 8% surplus note of $500,000. XYZ purchased 100% of the surplus note. During that same year, ABC incurred a statutory net loss before dividends of $250,000. At 12/31/20X2, ABC declared and paid a 5% preferred dividend, and a common stock dividend of $.05 per share. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Investment in ABC Surplus Notes	$500,000	
Cash		$500,000

To record investment in ABC Insurance Company surplus notes.

Cash	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X2.

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Unrealized Gain/Loss	$150,000	
Investment in ABC Common stock		$150,000

To record 20X2 unrealized loss on investment in ABC Common. (($-250,000 - $50,000) * 50%)

Cash	$5,000	
Unrealized Gain/Loss	$5,000	
Dividend Income		$5,000
Investment in ABC Common stock		$5,000

To record 20X2 dividend on ABC Common. (100,000 shares * $.05)

6. During the year ended 12/31/20X3, ABC Insurance Company incurred a statutory net loss before dividends of $400,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X3.

Unrealized Gain/Loss	$182,000	
Investment in ABC Preferred stock		$172,000
Investment in ABC Common stock		$10,000

To record 20X3 unrealized loss on investment in ABC Common and Preferred.

Total net loss and preferred stock dividend ($450,000).

Common stock component reduces the Investment in ABC Common stock component to $0. (20,000 * 50%)

Total net loss and preferred dividend (-$400,000 - $50,000)	$450,000
Less amount used to reduce common stock investment to $0	20,000
Amount remaining to be allocated to investment in preferred	430,000
XYZ ownership % of preferred	40%
XYZ reduction in investment in preferred	$172,000

7. During the year ended 12/31/20X4, ABC Insurance Company incurred a statutory net loss before dividends of $750,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X4.

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Unrealized Gain/Loss	$458,000	
Investment in ABC Preferred stock		$228,000
Investment in ABC Surplus note		$230,000

To record 20X4 unrealized loss on investment in ABC Preferred and Surplus Notes.

Total net loss and preferred stock dividend ($800,000).

Common stock component reduces the Investment in ABC Preferred stock component to $0. (570,000 * 40%)

Preferred stock component calculated as:

Total net loss and preferred dividend (-$750,000 - $50,000)	$800,000
Less amount used to reduce preferred stock investment to $0	570,000
Amount remaining to be allocated to investment in surplus note	230,000
XYZ ownership % of surplus note	100%
XYZ reduction in investment in ABC Surplus Notes	$230,000

8. During the year ended 12/31/20X5, ABC Insurance Company incurred a statutory net loss before dividends of $500,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X5.

Unrealized Gain/Loss	$270,000	
Investment in ABC Surplus note		$270,000

To record 20X5 unrealized loss on investment in ABC Surplus Notes.

Total ABC net loss and preferred stock dividend (-$500,000 - $50,000).

Surplus Note component calculated as:

Total net loss and preferred dividend (-$500,000 - $50,000)	$550,000
XYZ ownership % of ABC Surplus Note	100%
	$550,000
Amount of unrealized loss recognized in 20X5	$270,000
Amount of unrealized loss suspended	$280,000

9. Since XYZ had not guaranteed any liabilities of ABC, the reduction they would recognize is limited to their remaining investment in ABC Surplus Notes. Therefore, they would only recognize a 20X5 unrealized loss on their investment in ABC of $270,000.

10. During the year ended 12/31/20X6, ABC Insurance Company realigned their marketing efforts and modified the products they were selling. ABC also issued an additional 8% surplus note of $500,000. This surplus note was purchased by an unaffiliated third party. During the year ended 12/31/X6, ABC Insurance

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Company had statutory net income before dividends of $200,000. ABC Insurance Company did not declare any dividends on common stock but declared and paid current and dividends in arrears on preferred. XYZ recorded the following entries:

Cash	$80,000	
Dividends Receivable		$60,000
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X6, and receipt of preferred dividends receivable for 20X3, 20X4 and 20X5.

11. XYZ did not record any change in their investment in ABC Surplus Notes, ABC Preferred or ABC Common, since ABCs' net income after preferred dividends did not exceed the losses accumulated during the period that XYZ suspended recording unrealized losses.

12. The following amounts were tracked:

Total ABC net income and preferred stock dividend ($200,000 - $50,000).

Surplus Note component calculated as:

Total net income and preferred dividend ($200,000 - $50,000)	$150,000
XYZ ownership % of ABC Surplus Note	50%
	$75,000
Amount of unrealized loss suspended in 20X5	$280,000
Remaining amount of unrealized loss suspended	$205,000

13. During the year ended 12/31/20X7, ABC Insurance Company had statutory net income before dividends of $600,000. At 12/31/20X7, ABC declared and paid a 5% preferred dividend. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Cash	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X7.

Investment in ABC Surplus Notes	$70,000	
Unrealized Gain/Loss		$70,000

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To record 20X7 unrealized gain on investment in ABC Surplus Notes.

Total ABC net income and preferred stock dividend ($600,000 - $50,000).

Surplus Note component calculated as:

Total net income and preferred dividend ($600,000 - $50,000)	$550,000
XYZ ownership % of ABC Surplus Note	50%
	$275,000
Remaining amount of unrealized loss suspended in 20X5	$205,000
20X7 amount of unrealized gain on investment in ABC Surplus Note	$ 70,000

14. During the year ended 12/31/20X8, ABC Insurance Company had statutory net income before dividends of $900,000. At 12/31/20X8, ABC declared and paid a 5% preferred dividend. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Cash	$20,000	
Dividend Income		$20,000

To record preferred dividend income from ABC Insurance Company for 20X8.

Total ABC net income and preferred stock dividend ($900,000 - $50,000).

Surplus Note component calculated as:

Total net income and preferred dividend ($900,000 - $50,000)	$850,000
XYZ ownership % of ABC Surplus Note	50%
20X8 amount of unrealized gain on investment in ABC Surplus Note	$425,000

Investment in ABC Surplus Notes	$425,000	
Unrealized Gain/Loss		$ 425,000

To record 20X8 unrealized gain on investment in ABC Surplus Notes.

15. During the year ended 12/31/20X9, ABC Insurance Company had statutory net income, before interest on surplus notes and dividends, of $1,400,000. The commissioner approved one year's interest payment on the surplus notes. At 12/31/20X9, ABC declared and paid a 5% preferred dividend, and a $.10 dividend per share on Common stock. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X9.

Cash	$ 40,000	
Interest Income		$ 40,000

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To record surplus notes interest income from ABC Insurance Company for 20X9. ($500,000 * 8%)

Investment in ABC Surplus Notes	$ 5,000	
Investment in ABC Preferred Stock	$ 400,000	
Investment in ABC Common Stock	$ 130,000	
Unrealized Gain/Loss		$ 535,000

To record 20X9 unrealized gain on investment in ABC Common, Preferred and Surplus Notes. Components computed as follows:

Total Net Income net of preferred stock dividend and interest on surplus notes ($1,400,000 - $50,000 - $80,000)	$ 1,270,000
Less amount needed to restore investment in surplus notes	($ 10,000)
Amount available for preferred stock and common stock investment restoration	$ 1,260,000
Amount needed to restore preferred stock component	($ 1,000,000)
Amount available to restore common stock component	$ 260,000

Surplus Notes Component ($10,000 * 50%)	$ 5,000
Preferred Stock Component ($1,000,000 * 40%)	$ 400,000
Common Stock Component ($260,000 * 50%)	$ 130,000

Cash	$ 10,000	
Unrealized Gain/Loss	$ 10,000	
Dividend Income		$ 10,000
Investment in ABC Common Stock		$ 10,000

To record 20X9 dividend on ABC Common. (100,000 shares * $.10)

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Statement of Statutory Accounting Principles No. 100 – Revised

Fair Value

STATUS

Type of Issue	Common Area
Issued	December 5, 2009; Substantively revised November 6, 2017
Effective Date	December 31, 2010; Substantive revisions detailed in Issue Paper No. 157 effective January 1, 2018
Affects	Nullifies INT 09-04
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement defines fair value, establishes a framework for measuring fair value and establishes disclosure requirements about fair value.

SUMMARY CONCLUSION

2. This standard applies under other accounting pronouncements that require or permit fair value measurements, but this standard does not require any new fair value amendments. However, the application of this standard may change current practice. This standard does not eliminate the practicability exceptions to fair value measurements in accounting pronouncements within the scope of this standard.

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3. This standard applies under other statutory accounting pronouncements that require or permit fair value measurements, except as follows:

a. This standard does not eliminate the practicality exceptions to fair value measurements in accounting pronouncements within the scope of this standard.

b. This standard does not apply under *SSAP No. 22R—Leases* and other accounting pronouncements that address fair value measurements for purposes of lease classification to measurement under SSAP No. 22R. This scope exception does not apply to assets acquired or liabilities assumed in a business combination that are required to be measured at fair value under *SSAP No. 68—Business Combinations and Goodwill*, regardless of whether those assets and liabilities are related to leases. This standard does not apply to share-based payment transactions captured within *SSAP No. 104R—Share-Based Payments*.

Definition of Fair Value

4. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Components of the Fair Value Definition

5. Asset/Liability – A fair value measurement is for a particular asset or liability. Therefore, the measurement should consider attributes specific to the asset or liability, for example, the condition and/or location of the asset or liability and restrictions, if any, on the sale or use of the asset at the measurement date. The asset or liability might be a standalone asset or liability (for example, a financial instrument or an operating asset) or a group of assets and/or liabilities (for example, an asset group, a reporting unit, or a business).

6. Price – A fair value measurement assumes that the asset or liability is exchanged in an orderly transaction between market participants to sell the asset or transfer the liability at the measurement date. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction (for example, a forced liquidation or distress sale). The transaction to sell the asset or transfer the liability is a hypothetical transaction at the measurement date, considered from the perspective of a market participant that holds the asset or owes the liability. Therefore, the objective of a fair value measurement is to determine the price that would be received to sell the asset or paid to transfer the liability at the measurement date (an exit price).

7. Principal (or Most Advantageous) Market – A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The principal market is the market in which the reporting entity would sell the asset or transfer the liability with the greatest volume and level of activity for the asset or liability. The most advantageous market is the market in which the reporting entity would sell the asset or transfer the liability with the price that maximizes the amount that would be received for the asset or minimizes the amount that would be paid to transfer the liability, considering transaction costs in the respective market(s). In either case, the principal (or most advantageous) market (and thus, market participants) should be considered from the perspective of the reporting entity, thereby allowing for differences between and among entities with different activities. If there is a principal market for the asset or liability, the fair value measurement shall represent the price in that market (whether that price is directly observable or otherwise determined using a valuation technique), even if the price in a different market is potentially more advantageous at the measurement date.

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8. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. Transaction costs represent the incremental direct costs to sell the asset or transfer the liability in the principal (or most advantageous) market for the asset or liability. Transaction costs are not an attribute of the asset or liability; rather, they are specific to the transaction and will differ depending on how the reporting entity transacts. However, transaction costs do not include the costs that would be incurred to transport the asset or liability to (or from) its principal (or most advantageous) market. If location is an attribute of the asset or liability (as might be the case for a commodity), the price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall be adjusted for the costs, if any, that would be incurred to transport the asset or liability to (or from) its principal (or most advantageous) market.

9. Market Participants – Market participants are buyers and sellers in the principal (or most advantageous) market for the asset or liability that are:

a. Independent of the reporting entity; that is, they are not related parties;

b. Knowledgeable, having a reasonable understanding about the asset or liability and the transaction based on all available information, including information that might be obtained through due diligence efforts that are usual and customary;

c. Able to transact for the asset or liability; and

d. Willing to transact for the asset or liability; that is, they are motivated but not forced or otherwise compelled to do so.

10. The fair value of the asset or liability shall be determined based on the assumptions that market participants would use in pricing the asset or liability. In developing those assumptions, the reporting entity need not identify specific market participants. Rather, the reporting entity should identify characteristics that distinguish market participants generally, considering factors specific to (a) the asset or liability, (b) the principal (or most advantageous) market for the asset or liability, and (c) market participants with whom the reporting entity would transact in that market.

11. Application to Assets – A fair value measurement assumes the highest and best use of the asset by market participants, considering the use of the asset that is physically possible, legally permissible, and financially feasible at the measurement date. In broad terms, highest and best use refers to the use of an asset by market participants that would maximize the value of the asset or the group of assets within which the asset would be used. Highest and best use is determined based on the use of the asset by market participants, even if the intended use of the asset by the reporting entity is different.

12. The highest and best use of the asset establishes the valuation premise used to measure the fair value of the asset. Specifically:

a. In-use – The highest and best use of the asset is in-use if the asset would provide maximum value to market participants principally through its use in combination with other assets as a group (as installed or otherwise configured for use). For example, that might be the case for certain nonfinancial assets. If the highest and best use of the asset is in-use, the fair value of the asset shall be measured using an in-use valuation premise. When using an in-use valuation premise, the fair value of the asset is determined based on the price that would be received in a current transaction to sell the asset assuming that the asset would be used with other assets as a group and that those assets would be available to market participants. Generally, assumptions about the highest and best use of the asset should be consistent for all of the assets of the group within which it would be used.

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b. In-exchange – The highest and best use of the asset is in-exchange if the asset would provide maximum value to market participants principally on a standalone basis. For example, that might be the case for a financial asset. If the highest and best use of the asset is in-exchange, the fair value of the asset shall be measured using an in-exchange valuation premise. When using an in-exchange valuation premise, the fair value of the asset is determined based on the price that would be received in a current transaction to sell the asset standalone.

13. Because the highest and best use of the asset is determined based on its use by market participants, the fair value measurement considers the assumptions that market participants would use in pricing the asset, whether using an in-use or an in-exchange valuation premise.

14. Application to Liabilities – Consideration of non-performance risk (own credit-risk) should not be reflected in the fair value calculation for liabilities (including derivative liabilities) at subsequent measurement. At initial recognition, it is perceived that the consideration of own-credit risk may be inherent in the contractual negotiations resulting in the liability. The consideration of non-performance risk for subsequent measurement is inconsistent with the conservatism and recognition concepts as well as the assessment of financial solvency for insurers, as a decrease in credit standing would effectively decrease reported liabilities and thus seemingly increase the appearance of solvency. Furthermore, liabilities reported or disclosed at "fair value" shall not reflect any third-party credit guarantee of debt.

Equity Securities Subject to Contractual Sale Restrictions

15. An equity security that an entity cannot sell on the measurement date because of a contractual sale restriction shall be measured at fair value on the basis of the price in the principal (or most advantageous) market[1]. A contractual sale restriction does not change the market in which that equity security would be sold. A discount applied to the price of an equity security because of a contractual sale restriction is not a characteristic of the equity security. A contractual sale restriction is a characteristic of the reporting entity holding the equity security rather than a characteristic of the asset and, therefore, is not considered in measuring the fair value of an equity security. A contractual sale restriction prohibiting the sale of an equity security is a characteristic of the reporting entity holding the equity security and shall not be separately recognized as its own unit of account.

16. The effect on a fair value measurement arising from a restriction on the sale or use of an asset by a reporting entity will differ depending on whether the restriction would be taken into account by market participants when pricing the asset. When the restriction is a characteristic of the asset, the restriction should be considered in measuring the fair value of the asset. For example, an equity security issued through a private placement is not registered and is legally restricted from being sold on a national securities exchange or an over-the-counter market until the shares are registered or the conditions necessary for an exemption from registration have been satisfied. A market participant would sell the private placement equity securities in a different market than the market used for registered equity securities on the measurement date. Because that restriction would be a characteristic of the equity security, a market participant would consider the inability to resell the security on a national securities exchange or an over-the-counter market when pricing the equity security; therefore, the reporting entity that holds the Class A shares acquired through a private placement transaction would consider that restriction a characteristic of the asset, and the reporting entity should measure the fair value of the equity security on the basis of the market price of the similar unrestricted equity security adjusted to reflect the effect of the restriction[1].

[1] Refer to *SSAP No. 4—Assets and Nonadmitted Assets* for admissibility guidance for restricted equity securities.

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Fair Value at Initial Recognition

~~15.~~17. When an asset is acquired or a liability is assumed in an exchange transaction for that asset or liability, the transaction price represents the price paid to acquire the asset or received to assume the liability (an entry price). In contrast, the fair value of the asset or liability represents the price that would be received to sell the asset or paid to transfer the liability (an exit price). Conceptually, entry prices and exit prices are different. Entities do not necessarily sell assets at the prices paid to acquire them. Similarly, entities do not necessarily transfer liabilities at the prices received to assume them.

~~16.~~18. In many cases, the transaction price will equal the exit price and, therefore, represent the fair value of the asset or liability at initial recognition. In determining whether a transaction price represents the fair value of the asset or liability at initial recognition, the reporting entity shall consider factors specific to the transaction and the asset or liability. For example, a transaction price might not represent the fair value of an asset or liability at initial recognition if:

a. The transaction is between related parties.

b. The transaction occurs under duress or the seller is forced to accept the price in the transaction. For example, that might be the case if the seller is experiencing financial difficulty.

c. The market in which the transaction occurs is different from the market in which the reporting entity would sell the asset or transfer the liability, that is, the principal or most advantageous market. For example, those markets might be different if the reporting entity is a securities dealer that transacts in different markets, depending on whether the counterparty is a retail customer (retail market) or another securities dealer (inter-dealer market).

d. For liabilities, differences may exist as non-performance risk (own credit risk) is not reflected in the fair value (i.e., exit price) determination of all liabilities (including derivatives).

Valuation Techniques

~~17.~~19. Valuation techniques consistent with the market approach, income approach, and/or cost approach shall be used to measure fair value. Key aspects of those approaches are summarized below:

a. Market approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities (including a business). For example, valuation techniques consistent with the market approach often use market multiples derived from a set of comparables. Multiples might lie in ranges with a different multiple for each comparable. The selection of where within the range the appropriate multiple falls requires judgment, considering factors specific to the measurement (qualitative and quantitative). Valuation techniques consistent with the market approach include matrix pricing. Matrix pricing is a mathematical technique used principally to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities.

b. Income approach. The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. Those valuation techniques include present value techniques; option-pricing models, such as the Black-Scholes-Merton formula (a closed-form model) and a binomial model (a lattice model), which incorporate present value techniques; and

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the multiperiod excess earnings method, which is used to measure the fair value of certain intangible assets.

c. Cost approach. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (often referred to as current replacement cost). From the perspective of a market participant (seller), the price that would be received for the asset is determined based on the cost to a market participant (buyer) to acquire or construct a substitute asset of comparable utility, adjusted for obsolescence. Obsolescence encompasses physical deterioration, functional (technological) obsolescence, and economic (external) obsolescence and is broader than depreciation for financial reporting purposes (an allocation of historical cost) or tax purposes (based on specified service lives).

~~18.~~20. Valuation techniques that are appropriate in the circumstances and for which sufficient data are available shall be used to measure fair value. In some cases, a single valuation technique will be appropriate (for example, when valuing an asset or liability using quoted prices in an active market for identical assets or liabilities). In other cases, multiple valuation techniques will be appropriate (for example, as might be the case when valuing a reporting unit). If multiple valuation techniques are used to measure fair value, the results (respective indications of fair value) shall be evaluated and weighted, as appropriate, considering the reasonableness of the range indicated by those results. A fair value measurement is the point within that range that is most representative of fair value in the circumstances.

~~19.~~21. Valuation techniques used to measure fair value shall be consistently applied. However, a change in a valuation technique or its application (for example, a change in its weighting when multiple valuation techniques are used) is appropriate if the change results in a measurement that is equally or more representative of fair value in the circumstances. That might be the case if, for example, new markets develop, new information becomes available, information previously used is no longer available, or valuation techniques improve. Revisions resulting from a change in the valuation technique or its application shall be accounted for as a change in accounting estimate pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors*. The disclosure provisions of SSAP No. 3 for a change in accounting estimate are not required for revisions resulting from a change in a valuation technique or its application.

Inputs to Valuation Techniques

~~20.~~22. In this standard, inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk, for example, the risk inherent in a particular valuation technique used to measure fair value (such as a pricing model) and/or the risk inherent in the inputs to the valuation technique. Inputs may be observable or unobservable:

a. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity.

b. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

Valuation techniques used to measure fair value shall maximize the use of observable inputs and minimize the use of unobservable inputs.

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Fair Value Hierarchy

~~21.~~23. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. The level in the fair value hierarchy within which the fair value measurement in its entirety falls shall be determined based on the lowest level input that is significant to the fair value measurement in its entirety. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability.

~~22.~~24. The availability of inputs relevant to the asset or liability and the relative reliability of the inputs might affect the selection of appropriate valuation techniques. However, the fair value hierarchy prioritizes the inputs to valuation techniques, not the valuation techniques. For example, a fair value measurement using a present value technique might fall within Level 2 or Level 3, depending on the inputs that are significant to the measurement in its entirety and the level in the fair value hierarchy within which those inputs fall.

Level 1 Inputs

~~23.~~25. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available, except as discussed in paragraphs ~~24~~26 and ~~25~~27.

~~24.~~26. If the reporting entity holds a large number of similar assets or liabilities (for example, debt securities) that are required to be measured at fair value, a quoted price in an active market might be available but not readily accessible for each of those assets or liabilities individually. In that case, fair value may be measured using an alternative pricing method that does not rely exclusively on quoted prices (for example, matrix pricing) as a practical expedient. However, the use of an alternative pricing method renders the fair value measurement a lower level measurement.

~~25.~~27. In some situations, a quoted price in an active market might not represent fair value at the measurement date. That might be the case if, for example, significant events (principal-to-principal transactions, brokered trades, or announcements) occur after the close of a market but before the measurement date. The reporting entity should establish and consistently apply a policy for identifying those events that might affect fair value measurements. However, if the quoted price is adjusted for new information, the adjustment renders the fair value measurement a lower level measurement.

~~26.~~28. If the reporting entity holds a position in a single financial instrument (including a block) and the instrument is traded in an active market, the fair value of the position shall be measured within Level 1 as the product of the quoted price for the individual instrument times the quantity held. The quoted price shall not be adjusted because of the size of the position relative to trading volume (blockage factor). The use of a blockage factor is prohibited, even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

Level 2 Inputs

~~27.~~29. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term,

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a Level 2 input must be observable for substantially the full term of the asset or liability. Level 2 inputs include the following:

a. Quoted prices for similar assets or liabilities in active markets

b. Quoted prices for identical or similar assets or liabilities in markets that are not active, that is, markets in which there are few transactions for the asset or liability, the prices are not current, or price quotations vary substantially either over time or among market makers (for example, some brokered markets), or in which little information is released publicly (for example, a principal-to-principal market)

c. Inputs other than quoted prices that are observable for the asset or liability (for example, interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks, and default rates)

d. Inputs that are derived principally from or corroborated by observable market data by correlation or other means (market-corroborated inputs).

~~28.~~30. Adjustments to Level 2 inputs will vary depending on factors specific to the asset or liability. Those factors include the condition and/or location of the asset or liability, the extent to which the inputs relate to items that are comparable to the asset or liability, and the volume and level of activity in the markets within which the inputs are observed. An adjustment that is significant to the fair value measurement in its entirety might render the measurement a Level 3 measurement, depending on the level in the fair value hierarchy within which the inputs used to determine the adjustment fall.

~~29.~~31. The reporting entity should evaluate the following factors to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability when compared with normal market activity for the asset or liability (or similar assets or liabilities). The factors include, but are not limited to:

a. There are few recent transactions.

b. Price quotations are not based on current information.

c. Price quotations vary substantially either over time or among market makers (for example, some brokered markets).

d. Indexes that previously were highly correlated with the fair values of the asset or liability are demonstrably uncorrelated with recent indications of fair value for that asset or liability.

e. There is a significant increase in implied liquidity risk premiums, yields, or performance indicators (such as delinquency rates or loss severities) for observed transactions or quoted prices when compared with the reporting entity's estimate of expected cash flows, considering all available market data about credit and other nonperformance risk for the asset or liability.

f. There is a wide bid-ask spread or significant increase in the bid-ask spread.

g. There is a significant decline or absence of a market for new issuances (that is, a primary market) for the asset or liability or similar assets or liabilities.

h. Little information is released publicly (for example, a principal-to-principal market).

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The reporting entity shall evaluate the significance and relevance of the factors to determine whether, based on the weight of the evidence, there has been a significant decrease in the volume and level of activity for the asset or liability.

~~30.~~32. If the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability (or similar assets or liabilities), transactions or quoted prices may not be determinative of fair value (for example, there may be increased instances of transactions that are not orderly). Further analysis of the transactions or quoted prices is needed, and a significant adjustment to the transactions or quoted prices may be necessary to estimate fair value in accordance with this standard. Significant adjustments also may be necessary in other circumstances (for example, when a price for a similar asset requires significant adjustment to make it more comparable to the asset being measured or when the price is stale).

~~31.~~33. This standard does not prescribe a methodology for making significant adjustments to transactions or quoted prices when estimating fair value. Paragraphs ~~17-19~~19-21 discuss the use of valuation techniques in estimating fair value. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate (for example, the use of a market approach and a present value technique). When weighting indications of fair value resulting from the use of multiple valuation techniques, the reporting entity shall consider the reasonableness of the range of fair value estimates. The objective is to determine the point within that range that is most representative of fair value under current market conditions. A wide range of fair value estimates may be an indication that further analysis is needed.

~~32.~~34. Even in circumstances where there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. Determining the price at which willing market participants would transact at the measurement date under current market conditions if there has been a significant decrease in the volume and level of activity for the asset or liability depends on the facts and circumstances and requires the use of significant judgment. However, the reporting entity's intention to hold the asset or liability is not relevant in estimating fair value. Fair value is a market-based measurement, not an entity-specific measurement.

~~33.~~35. Even if there has been a significant decrease in the volume and level of activity for the asset or liability, it is not appropriate to conclude that all transactions are not orderly (that is, distressed or forced). Circumstances that may indicate that a transaction is not orderly include, but are not limited to:

a. There was not adequate exposure to the market for a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities under current market conditions.

b. There was a usual and customary marketing period, but the seller marketed the asset or liability to a single market participant.

c. The seller is in or near bankruptcy or receivership (that is, distressed), or the seller was required to sell to meet regulatory or legal requirements (that is, forced).

d. The transaction price is an outlier when compared with other recent transactions for the same or similar asset or liability.

The reporting entity shall evaluate the circumstances to determine whether the transaction is orderly based on the weight of the evidence.

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~~34.~~36. The determination of whether a transaction is orderly (or not orderly) is more difficult if there has been a significant decrease in the volume and level of activity for the asset or liability. Accordingly, the reporting entity shall consider the following guidance:

a. If the weight of the evidence indicates the transaction is not orderly, the reporting entity shall place little, if any, weight (compared with other indications of fair value) on that transaction price when estimating fair value or market risk premiums.

b. If the weight of the evidence indicates the transaction is orderly, the reporting entity shall consider that transaction price when estimating fair value or market risk premiums. The amount of weight placed on that transaction price when compared with other indications of fair value will depend on the facts and circumstances such as the volume of the transaction, the comparability of the transaction to the asset or liability being measured at fair value, and the proximity of the transaction to the measurement date.

c. If the reporting entity does not have sufficient information to conclude that the transaction is orderly or that the transaction is not orderly, it shall consider that transaction price when estimating fair value or market risk premiums. However, that transaction price may not be determinative of fair value (that is, that transaction price may not be the sole or primary basis for estimating fair value or market risk premiums). The reporting entity shall place less weight on transactions on which the reporting entity does not have sufficient information to conclude whether the transaction is orderly when compared with other transactions that are known to be orderly.

In its determinations, the reporting entity need not undertake all possible efforts, but shall not ignore information that is available without undue cost and effort. The reporting entity would be expected to have sufficient information to conclude whether a transaction is orderly when it is party to the transaction.

~~35.~~37. Regardless of the valuation technique(s) used, the reporting entity shall include appropriate risk adjustments. Risk-averse market participants generally seek compensation for bearing the uncertainty inherent in the cash flows of an asset or liability (risk premium). A fair value measurement should include a risk premium reflecting the amount market participants would demand because of the risk (uncertainty) in the cash flows. Otherwise, the measurement would not faithfully represent fair value. In some cases, determining the appropriate risk premium might be difficult. However, the degree of difficulty alone is not a sufficient basis on which to exclude a risk adjustment. Risk premiums should be reflective of an orderly transaction (that is, not a forced or distressed sale) between market participants at the measurement date under current market conditions.

~~36.~~38. When estimating fair value, this standard does not preclude the use of quoted prices provided by third parties, such as pricing services or brokers, when the reporting entity has determined that the quoted prices provided by those parties are determined in accordance with this standard. However, when there has been a significant decrease in the Volume or level of activity for the asset or liability, the reporting entity should evaluate whether those quoted prices are based on current information that reflects orderly transactions or a valuation technique that reflects market participant assumptions (including assumptions about risks). In weighting a quoted price as an input to a fair value measurement, the reporting entity should place less weight (when compared with other indications of fair value that are based on transactions) on quotes that do not reflect the result of transactions. Furthermore, the nature of the quote (for example, whether the quote is an indicative price or a binding offer) should be considered when weighting the available evidence, with more weight given to quotes based on binding offers.

Level 3 Inputs

~~37.~~39. Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for

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situations in which there is little, if any, market activity for the asset or liability at the measurement date. However, the fair value measurement objective remains the same, that is, an exit price from the perspective of a market participant that holds the asset or owes the liability. Therefore, unobservable inputs shall reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). Unobservable inputs shall be developed based on the best information available in the circumstances, which might include the reporting entity's own data. In developing unobservable inputs, the reporting entity need not undertake all possible efforts to obtain information about market participant assumptions. However, the reporting entity shall not ignore information about market participant assumptions that is reasonably available without undue cost and effort. Therefore, the reporting entity's own data used to develop unobservable inputs shall be adjusted if information is reasonably available without undue cost and effort that indicates that market participants would use different assumptions.

Inputs Based on Bid and Ask Prices

~~38.~~40. If an input used to measure fair value is based on bid and ask prices (for example, in a dealer market), the price within the bid-ask spread that is most representative of fair value in the circumstances shall be used to measure fair value, regardless of where in the fair value hierarchy the input falls (Level 1, 2, or 3). This standard does not preclude the use of mid-market pricing or other pricing conventions as a practical expedient for fair value measurements within a bid-ask spread.

Utilizing Net Asset Value Per Share as a Practical Expedient to Fair Value

~~39.~~41. A reporting entity may utilize net asset value per share (NAV)[2] as a practical expedient to fair value in either of the following situations, unless, as prescribed in paragraph ~~44~~46, it is probable that the reporting entity will sell the investment for an amount different from the net asset value per share (or its equivalent):

a. When a SSAP specifically identifies NAV as a permitted practical expedient.

b. When the conditions specified in paragraph ~~40~~42 are met.

~~40.~~42. Pursuant to paragraph ~~39~~41, a reporting entity is permitted to utilize NAV as a practical expedient to fair value when the investment meets both of the following criteria:

a. The investment does not have a readily determinable fair value as defined in paragraph ~~41~~43.

b. The investment is in an investment company or is an investment in a real estate fund for which it is industry practice to measure investment assets at fair value on a recurring basis and to issue financial statements consistent with the measurement principles of an investment company.

~~41.~~43. An equity security has a readily determinable fair value if it meets any of the following conditions:

a. The fair value of an equity security is readily determinable if sales prices or bid-and-asked quotations are currently available on a securities exchange registered with the U.S. Securities and Exchange Commission (SEC) or in the over-the-counter market, provided that those prices or quotations for the over-the-counter market are publicly reported by

[2] Net asset value per share is the amount of net assets attributable to each share of capital stock (other than senior equity securities, that is, preferred stock) outstanding at the close of the period. It excludes the effects of assuming conversion of outstanding convertible securities, whether or not their conversion would have a diluting effect. *(This footnote reflects the definition of Net Asset Value Per Share from the FASB Codification Master Glossary.)*

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the National Association of Securities Dealers Automated Quotations systems or by OTC Markets Group Inc. Restricted stock meets that definition if the restriction terminates within one year[3].

b. The fair value of an equity security traded only in a foreign market is readily determinable if that foreign market is of a breadth and scope comparable to one of the U.S. markets identified in paragraph ~~41~~43.a.

c. The fair value of an equity security that is an investment in a mutual fund or in a structure similar to a mutual fund (that is, a limited partnership or a venture capital entity) is readily determinable if the fair value per share (unit) is determined and published and is the basis for current transactions.

~~42.~~44. An entity is considered an investment company if it qualifies under the following assessments:

a. An entity regulated under the Investment Company Act of 1940.

b. An entity that is not regulated under the Investment Company Act of 1940, but that possesses all of the following fundamental characteristics:

i. The entity, 1) obtains funds from one or more investors and provides the investors with investment management services, and 2) commits to its investors that its business purpose and only substantive activities are investing the funds solely for returns from capital appreciation, investment income, or both.

ii. The entity or its affiliates do not obtain or have the objective of obtaining returns or benefits from an investee or its affiliates that are not normally attributable to ownership interests or that are other than capital appreciation or investment income.

c. The following characteristics are not required, but are typically found in an investment company. If the entity does not possess one or more of these typical characteristics, the reporting entity shall conduct further assessments to determine whether the entity's activities are consistent with those of an investment company:

i. The entity has more than one investment.

ii. The entity has more than one investor.

iii. The entity has investors that are not related parties of the parent or the investment manager.

iv. The entity has ownership interests in the form of equity or partnership interests.

v. The entity manages substantially all of its investments on a fair value basis.

~~43.~~45. If a reporting entity is permitted under paragraph ~~39~~41 to utilize NAV as a practical expedient, the reporting entity shall identify whether the holdings of the investment company, in determining NAV, are measured at fair value as of the reporting entity's measurement date. If the NAV of the investment obtained from the entity is not as of the reporting entity's measurement date, or is not based on a fair value measurement of the underlying investments, the reporting entity shall consider whether an adjustment to the most recent NAV is necessary. The objective of any adjustment is to estimate a net asset

[3] If an investment would otherwise have a readily determinable fair value, except that the investment has a restriction expiring in more than one year, the reporting entity is not permitted to use NAV for that investment.

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value per share for the investment that is calculated on the basis of underlying investments held at fair value.

~~44.~~46. A reporting entity shall decide on an investment-by-investment basis whether to apply the practical expedient in paragraph ~~39~~41 and shall apply that practical expedient consistently to the fair value measurement of the reporting entity's entire position in a particular investment, unless it is probable at the measurement date that the reporting entity will sell a portion of an investment at an amount different from NAV. In those situations, the reporting entity shall account for the portion of the investment that is being sold at fair value, as defined in paragraph 4, without use of the NAV practical expedient.

~~45.~~47. A reporting entity is not permitted to estimate the fair value of an investment (or a portion of the investment) using the NAV of the investment (or its equivalent) as a practical expedient if, as of the reporting entity's measurement date, it is probable that the reporting entity will sell the investment for an amount different from the net asset value per share (or its equivalent). A sale is considered probable only if all of the following criteria have been met as of the reporting entity's measurement date:

a. Management having the authority to approve the action commits to a plan to sell the investment.

b. An active program to locate a buyer and other actions required to complete the plan to sell the investment have been initiated.

c. The investment is available for immediate sale subject only to terms that are usual and customary for sales of such investments (for example, a requirement to obtain approval of the sale from the investee or a buyer's due diligence procedures).

d. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

~~46.~~48. An investment reported at NAV as a practical expedient pursuant to paragraph ~~39~~41, shall not be categorized within the fair value hierarchy. Although the investment is not categorized within the fair value hierarchy, a reporting entity shall separately identify NAV (or its equivalent) as required under paragraphs ~~48~~50.a. and ~~48~~50.b. to permit reconciliations.

Disclosures

~~47.~~49. The objective of the disclosure requirements is to provide information about assets and liabilities measured at fair value in the financial statements as well as fair value amounts disclosed in the notes to financial statements or reporting schedules. To meet these objectives, the reporting entity shall disclose the information in paragraphs ~~48~~50 through ~~57~~59.

~~48.~~50. For each class of assets and liabilities measured and reported[4] at fair value or NAV in the statement of financial position after initial recognition. The reporting entity shall determine appropriate classes of assets and liabilities in accordance with the annual statement instructions.

a. The fair value/NAV measurements at the reporting date.

[4] The term "reported" is intended to reflect the measurement basis for which the asset or liability is classified within its underlying SSAP. For example, a bond with an NAIC designation of 2 is considered an amortized cost measurement and is not included within this disclosure even if the amortized cost and fair value measurement are the same. An example of when such a situation may occur includes a bond that is written down as other-then-temporarily impaired as of the date of financial position. The amortized cost of the bond after the recognition of the other-than-temporary impairment may agree to fair value, but under SSAP No. 26R this security is considered to still be reported at amortized cost.

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b. The level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2 or 3). Investments reported at NAV shall not be captured within the fair value hierarchy, but shall be separately identified.

c. For fair value measurements categorized within Level 2 and Level 3 of the fair value hierarchy, a description of the valuation technique(s) and the inputs used in the fair value measurement. If there has been a change in the valuation technique (for example, changing from a market approach to an income approach or the use of an additional valuation technique), the reporting entity shall disclose that change and the reason(s) for making it.

d. For fair value measurements categorized within Level 3 of the fair value hierarchy a reconciliation from the opening balances to the closing balances disclosing separately changes during the period attributable to the following:

i. Total gains or losses for the period recognized in income or surplus.

ii. Purchases, sales, issues, and settlements (each type disclosed separately).

iii. The amounts of any transfers into or out of Level 3 and the reasons for those transfers. Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3.

e. A reporting entity shall consistently follow its policy for determining when transfers between levels are recognized. The policy about the timing of recognizing transfers shall be the same for transfers into Level 3 as that for transfers out of Level 3. Examples of policies for when to recognize the transfers are as follows:

i. The actual date of the event or change in circumstances that caused the transfer.

ii. The beginning of the reporting period.

iii. The end of the reporting period.

~~49.~~51. For derivative assets and liabilities, the reporting entity shall present both of the following:

a. The disclosures required by paragraphs ~~48~~50.a. and ~~48~~50.b. on a gross basis.

b. The reconciliation disclosures required by paragraph ~~48~~50.c., ~~48~~50.d. and ~~48~~50.e. on either a gross or net basis.

~~50.~~52. The quantitative disclosures required in paragraphs ~~48-49~~50-51 of this standard shall be presented using a tabular format.

~~51.~~53. The reporting entity shall disclose the fair value hierarchy and the method used to obtain the fair value measurement, or the use of NAV, for all items in which fair value is disclosed within the annual statement investment schedules. This disclosure is satisfied by the completion of the investment schedules in the Annual statement and is not required quarterly.

~~52.~~54. For investments measured using the NAV practical expedient pursuant to paragraph ~~39~~41, a reporting entity shall disclose information that helps users of its financial statements to understand the nature and risks of the investments and whether the investments, if sold, are probable of being sold at amounts different from net asset value per share. A reporting entity shall disclose the following information for instances in which the investment may be sold below NAV, or if there are significant restrictions in the liquidation of an investment held at NAV:

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a. The NAV along with a description of the investment/investment strategy of the investee.

b. If the investment that can never be redeemed with the investees, but the reporting entity receives distributions through the liquidation of the underlying assets of the investees, the period of time over which the underlying assets are expected to be liquidated by the investees if the investee has communicated the timing to the reporting entity or announced the timing publicly. If the timing is unknown, the reporting entity shall disclose that fact.

c. The amount of the reporting entity's unfunded commitments related to investments in the class.

d. A general description of the terms and conditions upon which the investor may redeem the investment.

e. The circumstances in which an otherwise redeemable investment in the class (or a portion thereof) might not be redeemable (for example, investments subject to a lockup or gate). Also, for those otherwise redeemable investments that are restricted from redemption as of the reporting entity's measurement date, the reporting entity shall disclose when the restriction from redemption might lapse if the investee has communicated that timing to the reporting entity or announced the timing publicly. If the timing is unknown, the reporting entity shall disclose that fact and how long the restriction has been in effect.

f. Any other significant restriction on the ability to sell investments in the class at the measurement date.

g. If a group of investments would otherwise meet the criteria in paragraph ~~45~~47 but the individual investments to be sold have not been identified (for example, if a reporting entity decides to sell 20% ~~percent~~ of its investments in private equity funds but the individual investments to be sold have not been identified), so the investments continue to qualify for the practical expedient in paragraph ~~39~~41, the reporting entity shall disclose its plans to sell and any remaining actions required to complete the sale(s).

~~53.~~55. The reporting entity is encouraged, but not required, to combine the fair value information disclosed under this standard with the fair value information disclosed under other accounting pronouncements (for example, disclosures about fair value of financial instruments) in the periods in which those disclosures are required, if practicable. The reporting entity also is encouraged, but not required, to disclose information about other similar measurements, if practicable.

Disclosures about Fair Value of Financial Instruments

~~54.~~56. A reporting entity shall disclose in the notes to the financial statements, as of each date for which a statement of financial position is presented in the quarterly or annual financial statements, the aggregate fair value or NAV for all financial instruments and the level within the fair value hierarchy in which the fair value measurements in their entirety fall. This disclosure shall be summarized by type of financial instrument, for which it is practicable to estimate fair value, except for certain financial instruments identified in paragraph ~~55~~57. Fair value disclosed in the notes shall be presented together with the related admitted values in a form that makes it clear whether the fair values and admitted values represent assets or liabilities and to which line items in the Statement of Assets, Liabilities, Surplus and Other Funds they relate. Unless specified otherwise in another SSAP, the disclosures may be made net of encumbrances, if the asset or liability is so reported. A reporting entity shall also disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments. If it is not practicable for an entity to estimate the fair value of the financial instrument or a class of financial instruments, and the investment

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does not qualify for the NAV practical expedient, the aggregate carrying amount for those items shall be reported as "not practicable" with additional disclosure as required in paragraph ~~48~~50.

~~55.~~57. The disclosures about fair value prescribed in paragraph ~~54~~56 are not required for the following:

a. Employers' and plans' obligations for pension benefits, other postretirement benefits including health care and life insurance benefits, postemployment benefits, employee stock option and stock purchase plans, and other forms of deferred compensation arrangements, as defined in *SSAP No. 12—Employee Stock Ownership Plans*, *SSAP No. 92—Postretirement Benefits Other Than Pensions*, *SSAP No. 102—Pensions* and *SSAP No. 104R—Share-Based Payments*.

b. Substantively extinguished debt subject to the disclosure requirements of *SSAP No. 103R—Transfer and Servicing of Financial Assets and Extinguishments of Liabilities*.

c. Insurance contracts, other than financial guarantees and deposit-type contracts .

d. Lease contracts as defined in *SSAP No. 22R—Leases.*

e. Warranty obligations and rights.

f. Investments accounted for under the equity method.

g. Equity instruments issued by the entity.

h. Deposit liabilities with no defined or contractual maturities.

~~56.~~58. If it is not practicable for an entity to estimate the fair value of a financial instrument or a class of financial instruments, and the investment does not qualify for the NAV practical expedient, the following shall be disclosed:

a. Information pertinent to estimating the fair value of that financial instrument or class of financial instruments, such as the carrying amount, effective interest rate, and maturity; and

b. The reasons why it is not practicable to estimate fair value.

~~57.~~59. In the context of this standard, practicable means that an estimate of fair value can be made without incurring excessive costs. It is a dynamic concept: what is practicable for one entity might not be for another; what is not practicable in one year might be in another. For example, it might not be practicable for an entity to estimate the fair value of a class of financial instruments for which a quoted market price is not available because it has not yet obtained or developed the valuation model necessary to make the estimate, and the cost of obtaining an independent valuation appears excessive considering the materiality of the instruments to the entity. Practicability, that is, cost considerations, also may affect the required precision of the estimate; for example, while in many cases it might seem impracticable to estimate fair value on an individual instrument basis, it may be practicable for a class of financial instruments in a portfolio or on a portfolio basis. In those cases, the fair value of that class or of the portfolio should be disclosed. Finally, it might be practicable for an entity to estimate the fair value only of a subset of a class of financial instruments; the fair value of that subset should be disclosed.

Relevant Literature

60. For equity securities that are subject to contractual sales, disclose the fair value of equity securities subject to contractual sale restrictions.

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~~58.~~61. This standard adopts with modification *FAS 157, Fair Value Measurements*; (FAS 157) *FSP FAS 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement Under Statement 13*, (FSP FAS 157-1) and *FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly* (FSP FAS 157-4). Modifications from FAS 157, FSP FAS 157-1 and FSP FAS 157-4 include:

a. This standard does not adopt the scope exclusions within paragraph 3 of FAS 157 for accounting pronouncements that require or permit measurements that are similar to fair value but that are not intended to measure fair value, including (a) accounting pronouncements that permit measurements that are based on, or otherwise use, vendor-specific objective evidence of fair value and (b) inventory pricing. These items are excluded as they are not prevalent within statutory accounting.

b. This standard does not adopt guidance from FAS 157 regarding the consideration of non-performance risk (own credit risk) in determining the fair value measurement of liabilities. The consideration of own credit-risk in the measurement of fair value liabilities is inconsistent with the statutory accounting concept of conservatism and the assessment of financial solvency for insurers. The fair value determination for liabilities should follow the guidance adopted from FAS 157, with the exception of the consideration of own-performance risk.

c. This standard includes revisions to reference statutory standards or terms instead of GAAP standards or terms.

d. This standard incorporates the guidance from SSAP No. 27 regarding disclosures about fair value of financial instruments. This incorporated SSAP No. 27 guidance was adopted from *FAS 107, Disclosures about Fair Value of Financial Instruments* (FAS 107) and was revised to adopt *FSP FAS 107-1 and APB-1, Interim Disclosures about Fair Value of Financial Instruments* (FSP FAS 107-1 and APB-1). For statutory purposes, the incorporation of this guidance within one standard results in having one comprehensive standard addressing fair value measurements and disclosures.

~~59.~~62. In August 2010, this statement adopted with modification the new and revised disclosure requirements within *ASU 2010-06, Fair Value Measurements and Disclosures – (Topic 820): Improving Disclosures about Fair Value Measurements* (ASU 2010-06). GAAP revisions within ASU 2010-06 that modify the FASB Codification on aspects originally added by *ASU 2009-05, Fair Value Measurements and Disclosures, Measuring Liabilities at Fair Value* (ASU 2009-05). These revisions are not adopted, as the underlying GAAP guidance within ASU 2009-05 has not been considered for statutory accounting. When ASU 2009-05 is reviewed for statutory accounting, the GAAP guidance considered will reflect the revisions from ASU 2010-06. Subsequent nonsubstantive revisions to the guidance adopted from ASU 2010-06 were incorporated within this statement in November 2010 to clarify the disclosure requirements for statutory accounting. These revisions removed the distinction between recurring and non-recurring fair value measurements and clarified disclosure requirements for assets and liabilities measured and reported at fair value in the statement of financial position. In April 2019 this statement adopted with modification disclosure revisions from *ASU 2018-13, Changes to the Disclosure Requirements for Fair Value Measurement.* Modifications to ASU 2018-13 incorporate revisions to previously adopted GAAP disclosures, and do not incorporate revisions related to disclosures not previously reflected for statutory accounting.

~~60.~~63. In November 2017, substantive revisions, as detailed in Issue Paper No. 157, were incorporated to this statement to adopt *ASU 2009-12, Investments in Certain Entities That Calculate Net Asset Value per Share (or Its* Equivalent*)* and *ASU 2015-07, Disclosures for Investments in Certain Entities that*

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Calculate Net Asset Value per Share (or Its Equivalent). These substantive revisions incorporated new guidance allowing reporting entities to utilize net asset value per share as a practical expedient to fair value when certain conditions are met.

64. Paragraphs ~~54-57~~56-59 of this statement adopt FAS 107 as amended by *FASB Statement No. 119, Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments* (FAS 119), except that paragraph 15(c) of FAS 119 relating to disclosure of financial instruments held or issued for trading is rejected and *FASB Emerging Issues Task Force No. 85-20, Recognition of Fees for Guaranteeing a Loan*. Financial instruments named within paragraph 8 of FAS 107 that are exempt from disclosure are adopted to the extent applicable for statutory accounting and are reflected in paragraph ~~55~~57 of this statement. This standard also adopts revisions to FAS 107 reflected in *FSP FAS 107-1 and APB-1, Interim Disclosures about Fair Value of Financial Instruments* (FSP FAS 107-1 and APB-1), and thus requires disclosure in both annual and quarterly financial statements. In addition, this standard rejects FASB Statement No. 126, Exemptions from Certain Required Disclosures about Financial Instruments for Certain Nonpublic Entities, an amendment of FAS 107. FAS 119 is addressed in SSAP No. 31.

~~61.~~65. This standard adopts *ASU 2022-03, Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions*, with modification to be consistent with statutory language in the respective statutory accounting statements.

~~62.~~66. This standard rejects *ASU 2019-05, Financial Instruments—Credit Losses: Targeted Transition Relief, ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, ASU 2013-03, Financial Instruments – Clarifying the Scope and Applicability of a Particular Disclosure to Nonpublic Entities* (ASU 2013-03), *ASU 2016-01, Financial Instruments – Overall* (ASU 2016-01), *FSP FAS 157-2: Effective Date of FASB Statement No. 157* (FSP FAS 157-2) and *FSP FAS 157-3: Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active* (FSP FAS 157-3).

Effective Date and Transition

~~63.~~67. This standard shall be effective for December 31, 2010, annual financial statements, with interim and annual financial statement reporting thereafter. Early adoption is permitted for December 31, 2009, annual financial statements, with interim and annual reporting thereafter. Nonsubstantive disclosure revisions adopted in August and November 2010 to paragraphs ~~48-49~~50-51 and the corresponding disclosure illustrations are initially effective for year-end 2010 financial statements, with interim and annual reporting thereafter. Nonsubstantive revisions adopted March 2011 to paragraphs ~~48~~50.a., ~~48~~50.d.ii., ~~51~~53 and ~~54~~56 of this statement are effective January 1, 2012, with interim and annual reporting thereafter as required in this statement. (Paragraph ~~51~~53 is satisfied by the annual statement investment schedules and is not required quarterly.) Revisions to adopt ASU 2009-12 and ASU 2015-07, and provide guidance for allowing net asset value per share as a practical expedient to fair value when certain conditions are met as detailed in Issue Paper No. 157, is effective January 1, 2018, with early adoption permitted.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 138—Fair Value Measurements*
- *Issue Paper No. 157—Use of Net Asset Value*

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Statement of Statutory Accounting Principles No. 101

Income Taxes

STATUS

Type of Issue	Common Area
Issued	August 31, 2011
Effective Date	January 1, 2012
Affects	Supersedes SSAP No. 10 and SSAP No. 10R; Nullifies INT 00-21, INT 00-22, INT 01-19 and INT 01-20
Affected by	No other pronouncements
Interpreted by	INT 01-18; INT 06-12; INT 18-03; INT 22-02; INT 23-03
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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EXHIBIT A – IMPLEMENTATION QUESTIONS AND ANSWERS **14**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for current and deferred federal and foreign income taxes and current state income taxes. This statement supersedes conclusions reached in *SSAP No. 10—Income Taxes* and *SSAP No. 10R—Income Taxes, A Temporary Replacement of SSAP No. 10.*

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SUMMARY CONCLUSION

2. For purposes of accounting for federal and foreign income taxes, reporting entities shall adopt *FASB Statement No. 109, Accounting for Income Taxes* (FAS 109) with modifications for state income taxes(INT 18-03), the realization criteria for deferred tax assets, and the recording of the impact of changes in deferred tax balances. One objective of accounting for income taxes is to recognize the estimated amount of taxes payable or refundable for the current year as a tax liability or asset. A second objective is to recognize deferred tax liabilities and assets for the future tax consequences of events that have been recognized in a reporting entity's statutory financial statements or tax returns. However, the second objective is realistically constrained because (a) the tax payment or refund that results from a particular tax return is a joint result of all the items included in that return, (b) taxes that will be paid or refunded in future years are the joint result of events of the current or prior years and events of future years, and (c) information available about the future is limited. As a result, financial statements will recognize current and deferred income tax assets and liabilities in accordance with the provisions of this statement based upon estimates and approximations. For purposes of this statement, only adjusted gross deferred tax assets that are more likely than not (a likelihood of more than 50% ~~percent~~) to be realized shall be considered in determining admitted adjusted gross deferred tax assets.

Current Income Taxes

3. "Income taxes incurred" shall include current income taxes, the amount of federal and foreign income taxes paid (recovered) or payable (recoverable) for the current year. Current income taxes are defined as:

a. Current year estimates (including quarterly estimates) of federal and foreign income taxes payable or refundable, based on tax returns for the current and prior years, except as addressed in paragraph 3.b., and tax loss contingencies (including related interest and penalties) for current and all prior years, computed in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* with the following modifications:

   i. The term "probable" as used in SSAP No. 5R shall be replaced by the term "more likely than not (a likelihood of more than 50% ~~percent~~)" for federal and foreign income tax loss contingencies only.

   ii. For purposes of the determination of a federal and foreign income tax loss contingency, it shall be presumed that the reporting entity will be examined by the relevant taxing authority that has full knowledge of all relevant information.

   iii. If the estimated tax loss contingency is greater than 50% of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% of the original tax benefit recognized.

b. Amounts incurred or received during the current year relating to prior periods, to the extent not previously provided, as such amounts are deemed to be changes in accounting estimates as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors*.

c. In determining when tax loss contingencies associated with temporary differences should be included in current income taxes under paragraph 3.a., and therefore included in deferred taxes under paragraph 7, a reporting entity is not required to "gross-up" its current and deferred taxes until such time as an event has occurred that would cause a re-evaluation of the contingency and its probability of assessment, e.g., the IRS has identified the item as one which may be adjusted upon audit. Such an event could be the reporting entity's (or its affiliate or parent in a consolidated income tax return) receipt of a Form 5701, Proposed Audit Adjustment, or could occur earlier upon receipt of an

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Information Document Request. At such time, the company must reassess the probability of an adjustment, reasonably re-estimate the amount of tax contingency as determined in accordance with paragraph 3.a., make any necessary adjustment to deferred taxes, and re-determine the admissibility of any adjusted gross deferred tax asset as provided in paragraph 11.

4. State taxes (including premium, income and franchise taxes) shall be computed in accordance with SSAP No. 5R and shall be limited to (a) taxes due as a result of the current year's taxable basis calculated in accordance with state laws and regulations and (b) amounts incurred or received during the current year relating to prior periods, to the extent not previously provided as such amounts are deemed to be changes in accounting estimates. Property and casualty insurance companies shall report state taxes as other underwriting expenses under the caption "Taxes, licenses, and fees." Life and accident and health insurance companies shall report such amounts as general expenses under the caption "Insurance taxes, licenses, and fees, excluding federal income taxes." Other health entities shall report such amounts as general administration expenses under the caption "Taxes, licenses, and fees." State tax recoverables that are reasonably expected to be recovered in a subsequent accounting period are admitted assets. State taxes are reasonably expected to be recovered if the refund is attributable to overpayment of estimated tax payments, errors, carrybacks, or items for which the reporting entity has authority to recover under a state regulation or statute.

Deferred Income Taxes

5. Because tax laws and statutory accounting principles differ in their recognition and measurement of assets, liabilities, equity, revenues, expenses, gains, and losses, differences arise between:

a. The amount of taxable income and pretax statutory financial income for a year, and

b. The tax bases of assets or liabilities and their reported amounts in statutory financial statements.

6. A reporting entity's balance sheet shall include deferred income tax assets (DTAs) and liabilities (DTLs) related to the estimated future tax consequences of temporary differences and carryforwards, generated by statutory accounting, as defined in paragraph 11 of FAS 109.

7. A reporting entity's deferred tax assets and liabilities are computed as follows:

a. Temporary differences are identified and measured using a "balance sheet" approach whereby statutory and tax basis balance sheets are compared;

b. Temporary differences include unrealized gains and losses and nonadmitted assets but do not include asset valuation reserve (AVR), interest maintenance reserve (IMR), Schedule F penalties and, in the case of a mortgage guaranty insurer, amounts attributable to its statutory contingency reserve to the extent that "tax and loss" bonds have been purchased;

c. Total DTAs and DTLs are computed using enacted tax rates;

d. A DTL is not recognized for amounts described in paragraph 31 of FAS 109; and

e. Gross DTAs are reduced by a statutory valuation allowance adjustment if, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50% ~~percent~~) that some portion or all of the gross DTAs will not be realized. The statutory

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valuation allowance adjustment[1], determined in a manner consistent with paragraphs 20-25 of FAS 109[2], shall reduce the gross DTAs to the amount that is more likely than not to be realized (the adjusted gross deferred tax assets).

8. Changes in DTAs and DTLs, including changes attributable to changes in tax rates and changes in tax status, if any, shall be recognized as a separate component of gains and losses in unassigned funds (surplus)[3]. Admitted adjusted gross DTAs and DTLs shall be offset and presented as a single amount on the statement of financial position.

Admissibility of Income Tax Assets

9. Current income tax recoverables shall include all current income taxes, including interest, reasonably expected to be recovered in a subsequent accounting period, whether or not a return or claim has been filed with the taxing authorities. Current income tax recoverables are reasonably expected to be recovered if the refund is attributable to overpayment of estimated tax payments, errors, carrybacks, as defined in paragraph 289 of FAS 109, or items for which the reporting entity has substantial authority, as that term is defined in Federal Income Tax Regulations.(INT 06-12)

10. Current income tax recoverables meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

11. The net admitted DTA shall not exceed the excess of the adjusted gross DTA, as determined under paragraph 7.e., over gross DTL. Adjusted gross DTAs shall be admitted based upon the three-component admission calculation at an amount equal to the sum of paragraphs 11.a., 11.b., and 11.c.:

a. Federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS

[1] The statutory valuation allowance adjustment is utilized strictly to calculate the "adjusted gross DTA". (Admittance criteria in paragraph 11 are applied to the "adjusted gross DTA".) In determining the amount of adjusted gross DTA, the reporting entity shall consider reversal patterns of temporary differences to the extent necessary to support establishing or not establishing a valuation allowance adjustment, determined in accordance with paragraphs 228 and 229 of FAS 109. For purposes of this accounting statement, consideration of reversal patterns does not require scheduling beyond that necessary to support establishing or not establishing a valuation allowance adjustment. The application of the statutory valuation allowance adjustment in this statement shall not result in a statutory valuation allowance reserve within the statutory financial statements, but rather should result in a reduction of the gross DTA.

[2] For purposes of determining the amount of adjusted gross DTA and the amount admitted under paragraph 11, the admission calculation shall be made on a separate company, reporting entity basis. A reporting entity that files a consolidated federal income tax return with its parent should look to the amount of taxes it paid (or were allocated to it) as a separate legal entity in determining the admitted DTA under paragraph 11.a. Furthermore, the DTA under this paragraph may not exceed the amount that the reporting entity could reasonably expect to have refunded by its parent. The taxes paid by the reporting entity represent the maximum DTA that may be admitted under paragraph 11.a., although the amount could be reduced pursuant to the group's tax allocation agreement. The amount of admitted adjusted gross DTA under paragraph 11.b.i. is limited to the amount that the reporting entity expects to realize within the applicable realization period, on a separate company basis. The reporting entity must estimate its separate company taxable income and the tax benefit that it expects to receive from reversing deductible temporary differences in the form of lower tax payments to its parent. A reporting entity that projects a tax loss in the applicable realization period cannot admit a DTA related to the loss under paragraph 11.b., even if the loss could offset taxable income of other members in the consolidated group and the reporting entity could expect to be paid for the tax benefit pursuant to its tax allocation agreement.

[3] Changes in DTAs and DTLs due to changes to tax rates and tax status shall be recorded as a "change in net deferred income tax," excluding any change reflected in unrealized capital gains. Tax effects previously reflected in unrealized capital gains (to present unrealized gains and losses "net of tax") shall be re-measured for the change in the tax rate in the same reporting line. Changes in net deferred tax shall not include changes in nonadmitted DTAs, as changes in nonadmittance are reported on a separate reporting line.

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tax loss carryback provisions[4], not to exceed three years, including any amounts established in accordance with the provision of SSAP No. 5R as described in paragraph 3.a. of this statement related to those periods.

b. If the reporting entity is subject to risk-based capital requirements or is required to file a Risk-Based Capital Report with the domiciliary state, the reporting entity shall use the *Realization Threshold Limitation Table – RBC Reporting Entities* (RBC Reporting Entity Table) in this component of the admission calculation. The RBC Reporting Entity Table's threshold limitations are contingent upon the ExDTA ACL RBC Ratio[5].

If the reporting entity is either a mortgage guaranty insurer or financial guaranty insurer that is not subject to risk-based capital requirements and is not required to file a Risk-Based Capital Report with the domiciliary state and the reporting entity meets the minimum capital and reserve requirements for the state of domicile, then the reporting entity shall use the *Realization Threshold Limitation Table – Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entities* (Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table) in this component of the admission calculation. The Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table's threshold limitations are contingent upon the following ratio: the numerator is equal to the sum of 1) surplus to policyholders, 2) less the amount of the admitted DTA in paragraph 11.a. (ExDTA Surplus) plus, 3) contingency reserves. The denominator is equal to the required amount of minimum aggregate capital required to be maintained under the applicable NAIC model law or state variation thereof based on the risk characteristics and the amount of insurance in force (Required Aggregate Risk Capital)[6].

If the reporting entity (1) is not subject to risk-based capital requirements, (2) is not required to file a Risk-Based Capital Report with the domiciliary state, (3) is not a mortgage guaranty or financial guaranty insurer, and (4) meets the minimum capital and reserve requirements, then the reporting entity shall use the *Realization Threshold Limitation Table – Other Non-RBC Reporting Entities* (Other Non-RBC Reporting Entity Table). The Other Non-RBC Reporting Entity Table's threshold limitations are contingent upon the ratio of adjusted gross DTA (Adjusted gross DTA less the amount of DTA admitted in paragraph 11.a.) to adjusted capital and surplus[7].

[4] For example, under the Federal Internal Revenue Code, ordinary losses can be carried back two years for entities taxed as nonlife insurance companies, while capital losses for entities taxed both as nonlife and life insurance companies can be carried back three years. For losses arising in tax years after 2017, entities taxed as life insurance companies are not permitted to carryback ordinary losses.

[5] The December 31 Risk-Based Capital ratio is calculated based on the Authorized Control Level RBC for the current reporting period, which is in the process of being filed with the state of domicile, and computed without net deferred tax assets (ExDTA ACL RBC). The interim period (March 31, June 30, and September 30) ExDTA ACL RBC ratio numerator shall use the Total Adjusted Capital (TAC) with current quarter surplus ExDTA and current quarter TAC adjustments. The interim period denominator shall use the Authorized Control Level RBC as filed for the most recent calendar year.

[6] If the reporting entity is a mortgage guaranty insurer, this ratio is based on the requirements of Section 12 of the NAIC Mortgage Guaranty Insurance Model Law and state laws that, based on the risk characteristics and amount of insurance in force, require aggregate capital to be maintained in a risk-to-capital ratio of not less than 25 to 1. If the reporting entity is a financial guaranty insurer, this ratio is based on the requirements of Section 4C of the NAIC Financial Guaranty Insurance Model Guideline 1626 and state laws that require aggregate capital to be maintained based on the risk characteristics and amount of insurance in force.

[7] Consistent with the requirements of paragraph 11.b.ii., adjusted statutory capital and surplus used in this calculation component is based on statutory capital and surplus for the current reporting period excluding any net DTA, EDP equipment and operating system software and any net positive goodwill.

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Realization Threshold Limitation Table – RBC Reporting Entities

ExDTA ACL RBC (%)	11.b.i.	11.b.ii.
Greater than 300%	3 years	15%
200 – 300%	1 year	10%
Less than 200%	0 years	0%

Realization Threshold Limitation Table – Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entities

(See paragraph 11.b.) Ex DTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital (%)	11.b.i.	11.b.ii.
Greater than 115%	3 years	15%
100% to 115%	1 year	10%
Less than 100%	0 years	0%

Realization Threshold Limitation Table – Other Non-RBC Reporting Entities

Adjusted Gross DTA / Adjusted Capital & Surplus (%)	11.b.i.	11.b.ii.
Less than 50%	3 years	15%
50% to 75%	1 year	10%
Greater than 75%	0 years	0%

The reporting entity shall admit:

i. The amount of adjusted gross DTAs, after the application of paragraph 11.a.[8], expected to be realized within the applicable period (refer to the 11.b.i. column of the applicable Realization Threshold Limitation Table above; the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) following the balance sheet date limited to the amount determined in paragraph 11.b.ii.

ii. An amount that is no greater than the applicable percentage (refer to the 11.b.ii. column of the applicable Realization Threshold Limitation Table above: the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) of statutory capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for the current reporting period's statement filed with the domiciliary state commissioner adjusted to exclude any net DTAs, EDP equipment and operating system software and any net positive goodwill.(INT 01-18) For financial guaranty or mortgage guaranty non-RBC reporting entities, the amount of statutory capital and surplus utilized for this part of the calculation does not include contingency reserves.

[8] Under the Federal Internal Revenue Code, entities taxed as life insurance companies are not permitted to carryback ordinary losses arising in tax years after 2017. As such, admittance of ordinary DTAs for such entities will be limited to paragraph 11.b. and paragraph 11.c. for reporting periods ending with and subsequent to December 31, 2017.

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c. The amount of adjusted gross DTAs, after application of paragraphs 11.a. and 11.b. that can be offset against existing gross DTLs. The reporting entity shall consider the character (i.e., ordinary versus capital) of the DTAs and DTLs such that offsetting would be permitted in the tax return under existing enacted federal income tax laws and regulations. Additionally, for purposes of this component, the reporting entity shall consider the reversal patterns of temporary differences; however, this consideration does not require scheduling beyond that required in paragraph 7.e.

12. In computing a reporting entity's admitted adjusted gross DTA pursuant to paragraph 11;

a. For purposes of paragraph 11.a., existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, shall be determined in accordance with paragraphs 228 and 229 of FAS 109;

b. In determining the amount of federal income taxes that can be recovered through loss carrybacks, the amount and character (i.e., ordinary versus capital) of the loss carrybacks and the impact, if any, of the Alternative Minimum Tax shall be determined in accordance with the provisions of the Internal Revenue Code, and regulations thereunder;

c. The amount of carryback potential that may be considered in calculating the admitted adjusted gross DTAs of a reporting entity in paragraph 11.a. that files a consolidated income tax return with one or more affiliates, may not exceed the amount that the reporting entity could reasonably expect to have refunded by its parent; and

d. The phrases "reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years," "realized within one year of the balance sheet date" and "realized within three years of the balance sheet date" are intended to accommodate interim reporting dates and reporting entities that file on an other than calendar year basis for federal income tax purposes.

Realization of Tax Benefits and Tax Planning Strategies

13. Future realization of the tax benefit of an existing deductible temporary difference or carryforward ultimately depends on the existence of sufficient taxable income of the appropriate character (for example, ordinary income or capital gain) within the carryback, carryforward period available under the tax law. The following four possible sources of taxable income may be available under the tax law to realize a tax benefit for deductible temporary differences and carryforwards:

a. Future reversals of existing taxable temporary differences.

b. Future taxable income exclusive of reversing temporary differences and carryforwards.

c. Taxable income in prior carryback year(s) if carryback is permitted under the tax law.

d. Tax-planning strategies in paragraph 14 that would, if necessary, be implemented to, for example:

i. Accelerate taxable amounts to utilize expiring carryforwards;

ii. Change the character of taxable or deductible amounts from ordinary income or loss to capital gain or loss; and

iii. Switch from tax-exempt to taxable investments.

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Evidence available about each of those possible sources of taxable income will vary for different tax jurisdictions and, and possibly, from year to year. To the extent evidence about one or more sources of taxable income is sufficient to support a conclusion that the reporting entity will realize the full or a partial amount of its adjusted gross deferred tax assets, other sources need not be considered. Consideration of each source is required, however, to determine the amount of the statutory valuation allowance adjustment that is recognized for gross deferred tax assets under paragraph 7.e.

14. In some circumstances, there are tax-planning strategies (including elections for tax purposes) that (a) are prudent and feasible, (b) a reporting entity ordinarily might not take, but would take to prevent an operating loss or tax credit carryforward from expiring unused, and (c) would result in realization of deferred tax assets. A reporting entity shall consider tax-planning strategies in determining the amount of the statutory valuation allowance adjustment necessary under paragraph 7.e. Consideration of tax planning strategies for the realization of deferred tax assets when determining admission under paragraph 11 is not required; however, such strategies shall not conflict with the tax planning strategies used when computing the statutory valuation allowance. Any significant potential expenses to implement a tax-planning strategy or any significant losses that would be recognized if that strategy were implemented (net of any recognizable tax benefits associated with those expenses or losses) shall reduce the amount of admission under paragraph 11.

15. When a prudent and feasible tax-planning strategy is contemplated, and management determines this strategy would more likely than not enable the reporting entity to realize the full or a partial amount of its adjusted gross deferred tax assets, paragraph 3 of this statement related to tax loss contingencies shall be applied in determining admissibility of deferred tax assets under paragraph 11 of this statement.

Intercompany Income Tax Transactions

16. In the case of a reporting entity that files a consolidated income tax return with one or more affiliates, income tax transactions (including payment of tax contingencies to its parent) between the affiliated parties shall be recognized if:

a. Such transactions are economic transactions as defined in *SSAP No. 25—Affiliates and Other Related Parties*;

b. Are pursuant to a written income tax allocation agreement; and

c. Income taxes incurred are accounted for in a manner consistent with the principles of FAS 109, as modified by this statement.

17. Amounts owed to a reporting entity pursuant to a recognized transaction shall be treated as a loan or advance, and nonadmitted, pursuant to SSAP No. 25, to the extent that the recoverable is not settled within 90 days of the filing of a consolidated income tax return, or where a refund is due the reporting entity's parent, within 90 days of the receipt of such refund.

Intraperiod Tax Allocation

18. In accordance with paragraph 35 of FAS 109, a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL. The amount allocated shall be computed in a manner consistent with paragraph 38 of FAS 109.

19. Income taxes incurred shall be allocated to net income and realized capital gains or losses in a manner consistent with paragraph 38 of FAS 109. Furthermore, income taxes incurred or received during the current year attributable to prior years shall be allocated, to the extent not previously provided, to net income in accordance with SSAP No. 3 unless attributable, in whole or in part, to realized capital gains or losses, in which case, such amounts shall be apportioned between net income and realized capital gains and losses, as appropriate.

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Interim Periods

20. Income taxes incurred in interim periods shall be computed using an estimated annual effective current tax rate for the annual period in accordance with the methodology described in paragraphs 19 and 20 of *Accounting Principles Board Opinion No. 28, Interim Financial Reporting*. Estimates of the annual effective tax rate at the end of interim periods are, of necessity, based on estimates and are subject to subsequent refinement or revision. If a reliable estimate cannot be made, the actual effective tax rate for the year-to-date may be the best estimate of the annual effective tax rate. If a reporting entity is unable to estimate a part of its "ordinary" income (or loss) or the related tax (or benefit) but is otherwise able to make a reliable estimate, the tax (or benefit) applicable to the item that cannot be estimated shall be reported in the interim period in which the item is reported.

Disclosures

21. Statutory financial statement disclosures shall be made in a manner consistent with the provisions of paragraphs 43-45 and 48 of FAS 109. However, required disclosures with regard to a reporting entity's GAAP valuation allowance shall be replaced with disclosures relating to the statutory valuation allowance adjustment and the nonadmittance of some portion or all of a reporting entity's DTAs. The financial statements shall include the disclosures required by paragraph 47 of FAS 109 for non-public companies. Paragraphs 22-28 describe the disclosure requirements as modified for the difference between the requirements of FAS 109 and those prescribed by this statement.

22. The components of the net DTA or DTL recognized in a reporting entity's financial statements shall be disclosed as follows:

a. The total of all DTAs (gross, adjusted gross, admitted and nonadmitted) by tax character;

b. The total of all DTLs by tax character;

c. The total DTAs nonadmitted as the result of the application of paragraph 11;

d. The net change during the year in the total DTAs nonadmitted;

e. The amount of each result or component of the calculation, by tax character of paragraphs 11.a., 11.b.i., 11.b.ii., and 11.c., and the ExDTA ACL RBC Ratio, the ExDTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital Ratio, or the Adjusted Gross DTA/Adjusted Capital and Surplus Ratio used in the applicable *Realization Threshold Limitation Table* (the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) in paragraph 11.b., as applicable; and

f. The impact of tax-planning strategies on the determination of adjusted gross DTAs and the determination of net admitted DTAs, by percentage and by tax character, and whether the tax-planning strategies include the use of reinsurance-related tax planning strategies.

23. To the extent that DTLs are not recognized for amounts described in paragraph 31 of FAS 109, the following shall be disclosed:

a. A description of the types of temporary differences for which a DTL has not been recognized and the types of events that would cause those temporary differences to become taxable;

b. The cumulative amount of each type of temporary difference;

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c. The amount of the unrecognized DTL for temporary differences related to investments in foreign subsidiaries and foreign corporate joint ventures that are essentially permanent in duration if determination of that liability is practicable or a statement that determination is not practicable; and

d. The amount of the DTL for temporary differences other than those in paragraph 23.c. that is not recognized in accordance with the provisions of paragraphs 31 of FAS 109.

24. The significant components of income taxes incurred (i.e., current income tax expense) and the changes in DTAs and DTLs shall be disclosed. Those components would include, for example:

a. Current tax expense or benefit;

b. The change in DTAs and DTLs (exclusive of the effects of other components listed below);

c. Investment tax credits;

d. The benefits of operating loss carryforwards;

e. Adjustments of a DTA or DTL for enacted changes in tax laws or rates or a change in the tax status of the reporting entity; and

f. Adjustments to gross deferred tax assets because of a change in circumstances that causes a change in judgment about the realizability of the related deferred tax asset, and the reason for the adjustment and change in judgment.

25. Additionally, to the extent that the sum of a reporting entity's income taxes incurred and the change in its DTAs and DTLs is different from the result obtained by applying the federal statutory rate to its pretax net income, a reporting entity shall disclose the nature of the significant reconciling items.

26. A reporting entity shall also disclose the following:

a. The amounts, origination dates and expiration dates of operating loss and tax credit carryforwards available for tax purposes;

b. The amount of federal income taxes incurred in the current year and each preceding year, which are available for recoupment in the event of future net losses; and

c. The aggregate amount of deposits admitted under Section 6603 of the Internal Revenue Service Code.

27. For any federal or foreign income tax loss contingencies as determined in accordance with paragraph 3.a. for which it is reasonably possible that the total liability will significantly increase within 12 months of the reporting date, the reporting entity shall disclose an estimate of the range of the reasonably possible increase or a statement that an estimate of the range cannot be made.

28. If a reporting entity's federal income tax return is consolidated with those of any other entity or entities, the following shall be disclosed:

a. A list of names of the entities with whom the reporting entity's federal income tax return is consolidated for the current year; and

b. The substance of the written agreement, approved by the reporting entity's Board of Directors, which sets forth the manner in which the total combined federal income tax for

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all entities is allocated to each entity which is a party to the consolidation. (If no written agreement has been executed, explain why such an agreement has not been executed.) Additionally, the disclosure shall include the manner in which the entity has an enforceable right to recoup federal income taxes in the event of future net losses which it may incur or to recoup its net losses carried forward as an offset to future net income subject to federal income taxes.

29. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

30. This statement adopts the provisions of FAS 109 except as modified in paragraph 2 of this statement which results in paragraphs 29-30, 36-37, 39, 41-42, 46, and 49-59 of FAS 109 being rejected, inasmuch as they are not applicable to reporting entities subject to this statement or are inconsistent with other statutory accounting principles. Paragraph 47 of FAS 109 is adopted with modification to provide for the disclosures required for non-public reporting entities. This statement rejects *ASU 2016-16, Intra-Entity Transfers of Assets Other than Inventory*.

31. This statement rejects *ASU 2013-11, Income Taxes: Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists, ASU 2015-17 Balance Sheet Classification of Deferred Taxes*, *FASB Interpretation No. 18, Accounting for Income Taxes in Interim Periods…an interpretation of APB Opinion No. 28* and *FIN 48: Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109*.

32. The following lists FASB Staff Positions that are adopted or rejected by this statement:

a. *FASB Staff Position FAS 109-1, Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004* is adopted in its entirety.

b. FASB *Staff Position FAS 109-2, Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004* is rejected in its entirety.

c. *FASB Staff Position FIN 48-2, Effective Date of FIN 48 for Certain Nonpublic Enterprises* is rejected in its entirety.

d. *FASB Staff Position FIN 48-3, Effective Date of FIN 48 for Certain Nonpublic Enterprises* is rejected in its entirety.

33. The following lists Accounting Principles Board Opinions that are adopted or rejected by this statement:

a. *Accounting Principles Board Opinion No. 2, Accounting for the "Investment Credit,"* paragraphs 9-15 are adopted with modification to utilize the cost reduction method only and rejects all other paragraphs;

b. *Accounting Principles Board Opinion No. 4 (Amending No. 2), Accounting for the "Investment Credit,"* is rejected in its entirety;

c. *Accounting Principles Board Opinion No. 10, Omnibus Opinion—1966,* paragraph 6 is adopted;

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d. *Accounting Principles Board Opinion No. 23, Accounting for Income Taxes—Special Areas,* paragraphs 1-3, 5-9, 12-13, and 15-18 are adopted, and paragraphs 19-25, and 31-33 are rejected;

e. *Accounting Principles Board Opinion No. 28, Interim Financial Reporting,* paragraphs 19 and 20 are adopted and all other paragraphs rejected.

34. The following lists FASB Technical Bulletins that are adopted or rejected by this statement:

a. *FASB Technical Bulletin No. 79-9, Accounting in Interim Periods for Changes in* Income *Tax Rates* is rejected in its entirety;

b. FASB *Technical Bulletin No. 82-1, Disclosure of the Sale or Purchase of Tax Benefits through Tax Leases* is adopted in its entirety.

35. The following lists FASB Emerging Issues Task Force Issues that are adopted or rejected by this statement:

a. FASB *Emerging Issues Task Force No. 91-8, Application of FASB Statement No. 96 to a State Tax Based on the Greater of a Franchise Tax or an Income Tax,* is rejected in its entirety;

b. *FASB Emerging Issues Task Force No. 92-8, Accounting for the Income Tax Effects* under *FASB Statement No. 109 of a Change in Functional Currency When an Economy Ceases to Be Considered Highly Inflationary*, is adopted in its entirety;

c. FASB *Emerging Issues Task Force No. 93-13, Effect of a Retroactive Change in Enacted Tax Rates That Is Included in Income from Continuing Operations*, is rejected in its entirety;

d. *FASB Emerging Issues Task Force No. 93-16, Application of FASB Statement No. 109 to* Basis *Differences within Foreign Subsidiaries That Meet the Indefinite Reversal Criterion of APB Opinion No. 23*, is rejected in its entirety;

e. FASB *Emerging Issues Task Force No. 93-17, Recognition of Deferred Tax Assets for a Parent Company's Excess Tax Basis in the Stock of a Subsidiary That Is Accounted for as a Discontinued Operation*, is adopted in its entirety;

f. *FASB Emerging Issues Task Force No. 94-10, Accounting by a Company for the* Income *Tax Effects of Transactions among or with Its Shareholders under FASB Statement No. 109*, is rejected in its entirety;

g. FASB *Emerging Issues Task Force No. 95-9, Accounting for Tax Effects of Dividends in France in Accordance with FASB Statement No. 109*, is rejected in its entirety;

h. FASB *Emerging Issues Task Force No. 95-10, Accounting for Tax Credits Related to Dividend Payments in Accordance with FASB Statement No. 109*, is rejected in its entirety;

i. *FASB Emerging Issues Task Force No. 95-20, Measurement in the Consolidated Financial Statements of a Parent of the Tax Effects Related to the Operations of a* Foreign *Subsidiary That Receives Tax Credits Related to Dividend Payments*, is rejected in its entirety.

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36. This statement rejects AICPA Accounting Interpretations, Accounting for the Investment Credit: Accounting Interpretations of APB Opinion No. 4 in its entirety.

Effective Date and Transition

37. This statement shall be effective for years beginning January 1, 2012. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Revisions adopted in August 2019 to Exhibit A – Implementation Questions and Answers which update the exhibit in response to changes from the federal Tax Cuts and Jobs Act and to clarify deferred tax asset and deferred tax liability offsetting under paragraph 11.c., are effective for financial accounting years ending December 31, 2019. Any change in income tax balances resulting from the August 2019 revisions are accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 83—Accounting for Income Taxes*

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EXHIBIT A – IMPLEMENTATION QUESTIONS AND ANSWERS

The National Association of Insurance Commissioners issued *SSAP No. 101—Income Taxes*, with a corresponding implementation question and answer exhibit, with an effective date of January 1, 2012. Further nonsubstantive revisions were developed to update the Q&A for the revised corporate federal income tax rate and certain other federal tax law changes primarily under the Tax Cuts and Jobs Act enacted in December 2017 and to clarify deferred tax asset and deferred tax liability offsetting under SSAP No. 101, paragraph 11.c. These revisions to the implementation guidance are effective for financial accounting years ending December 31, 2019. Any change in income tax balances resulting from the August 2019 revisions are accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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Question No.	Question	SSAP No. 101 Paragraph Reference	Page Number
12	How do you present deferred taxes in the annual statement?	8, 18 and 21-28	52
13	How are tax-planning strategies to be considered in determining adjusted gross DTAs and admitted adjusted gross DTAs?	11.a., 11.b.i., 14 and 15	61

1. Q – What are the primary differences between the accounting for income taxes pursuant to FAS 109 and SSAP No. 101? [No specific paragraph reference]

1.1 A – SSAP No. 101 establishes statutory accounting principles for current and deferred federal and foreign income taxes and current state income taxes. In general, SSAP No. 101 adopts the concepts of FAS 109, with modifications. The primary differences and modifications are summarized below:

1.2 State Income Tax

- FAS 109 – State income taxes should be included as "income taxes incurred." Deferred state income taxes are recognized.

- SSAP No. 101 – State income taxes should be included as "Taxes, Licenses, and Fees" by property and casualty insurers and as "Insurance taxes, licenses, and fees, excluding federal income taxes" by life and accident and health insurers. No deferred state income taxes are recognized.

1.3 Valuation Allowance

- FAS 109 – Gross deferred tax assets (DTAs) are reduced by a valuation allowance if it is more likely than not that some portion or all of the DTAs will not be realized. The valuation allowance should be sufficient to reduce the DTA to the amount that is more likely than not to be realized.

- SSAP No. 101 – Gross DTAs are reduced by a statutory valuation allowance adjustment that is determined on a separate company, reporting entity basis. Pursuant to paragraphs 2 and 7.e. of SSAP No. 101, gross DTAs are adjusted to an amount that is more likely than not to be realized (a likelihood of more than 50% ~~percent~~). Only adjusted gross DTAs shall be considered in determining admitted adjusted gross DTAs. See Question 2 for further discussion of the statutory valuation allowance adjustment. See Question 4 for a further discussion of the admissibility test. See Question 12 for further discussion of presentation and disclosure of the statutory valuation allowance adjustment.

1.4 Unique Statutory Accounting Items

- FAS 109 – In general, the effects of all temporary differences must be reflected with limited exceptions provided in FAS 109 paragraphs 31-34 (relating to items specified in Accounting Principles Board Opinion No. 23) and for temporary differences related to goodwill for which amortization is not deductible for tax purposes.

- SSAP No. 101 – In addition to the exceptions provided in FAS 109, temporary differences do not include asset valuation reserve (AVR), interest maintenance reserve (IMR), Schedule F penalties and, in the case of a mortgage guaranty insurer, amounts attributable to its statutory contingency reserve to the extent that "tax and loss" bonds have been purchased.

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1.5 Changes in Deferred Tax Assets and Liabilities

- FAS 109 – Changes in DTAs and deferred tax liabilities (DTLs) are included in income tax expense or benefit and are allocated to continuing operations, discontinued operations, extraordinary items and items charged directly to shareholders' equity.

- SSAP No. 101 – Changes in DTAs and DTLs are recognized as a separate component of gains and losses in surplus, except to the extent allocated to changes in unrealized gains and losses.

1.6 Regulated Enterprises

- FAS 109 – Regulated enterprises that meet the criteria for application of FAS 71, *Accounting for* the *Effects of Certain Types of Regulation*, are not exempt from the requirements of FAS 109. However, assets are reported on a net-of-tax basis (see paragraphs 29, 57, 58 and 59 of FAS 109).

- SSAP No. 101 – These special paragraphs do not apply pursuant to paragraph 30 of SSAP No. 101.

1.7 Business Combinations

- FAS 109 – Paragraphs 30 and 53-56 of FAS 109 provide certain guidance regarding the treatment of business combinations. In general, a deferred tax asset or liability is recognized for the differences between the assigned values and the tax bases of the assets and liabilities recognized in a purchased business combination. If financial statements for prior years are restated, all purchase business combinations that were consummated in those prior years shall be remeasured in accordance with FAS 109.

- SSAP No. 101 – These special paragraphs do not apply pursuant to paragraph 30 of SSAP No. 101.

1.8 Intraperiod Tax Allocation

- FAS 109 – Income tax expense or benefit is allocated among continuing operations, discontinued operations, extraordinary items, and items charged or credited directly to shareholders' equity pursuant to paragraphs 36 and 37 of FAS 109.

- SSAP No. 101 – These paragraphs of FAS 109 do not apply pursuant to paragraph 30 of SSAP No. 101. Instead, paragraphs 18 and 19 of SSAP No. 101 provide special rules for statutory accounting. See Question 10 for a further discussion of these rules.

1.9 Certain Quasi-Reorganizations

- FAS 109 – Paragraph 39 provides special rules relating to the treatment of deductible temporary differences and carryforwards as of the date of a quasi-reorganization.

- SSAP No. 101 – Paragraph 39 of FAS 109 does not apply pursuant to paragraph 30 of SSAP No. 101.

1.10 Financial Statement Classification of DTAs and DTLs

- FAS 109 – Pursuant to paragraphs 41 and 42 of FAS 109, DTAs and DTLs are to be classified separately as either current or noncurrent, depending on the classification of the

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related asset or liability. Furthermore, current DTAs and DTLs and noncurrent DTAs and DTLs are netted within the classification and with the net amount reported.

- SSAP No. 101 – These paragraphs do not apply to statutory accounting pursuant to paragraph 30 of SSAP No. 101. The net admitted DTA, or the net DTL, should be reported in the statutory financial statements.

1.11 Accounting for Uncertainty in Income Taxes

- FAS 109 – Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 (FIN 48) provides accounting and reporting guidance for uncertain tax positions under GAAP.

- SSAP No. 101 – FIN 48 is rejected for statutory accounting pursuant to paragraph 31 of SSAP No. 101. *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* provides guidance in determining the amount of federal and foreign income tax loss contingencies with the following modifications. The term "probable" as used in SSAP No. 5R is replaced by the term "more likely than not (a likelihood of more than 50% ~~percent~~)". In determining the amount of a federal or foreign income tax loss contingency, it shall be assumed that the reporting entity will be examined by the tax authority that has full knowledge of all relevant information. If the estimated tax loss contingency is greater than 50% of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% of the original tax benefit recognized. See Question 9 for further discussion of income tax loss contingencies.

1.12 Classification of Interest and Penalties

- FAS 109 – FIN 48 allows interest on tax assessments to be reported as either income taxes or interest expense and penalties to be reported as either income taxes or another expense classification, based on the accounting policy election of the enterprise.

- SSAP No. 101 – Interest and penalties related to foreign or federal income tax are included in income taxes pursuant to paragraph 3.a. of SSAP No. 101.

1.13 Financial Statement Disclosures

- FAS 109 – Paragraphs 43-45 and 47-48 of FAS 109 provide various requirements for providing information in the financial statements regarding the income taxes of the reporting entity. In general, the reporting entity is to provide certain information regarding the components of its DTAs and DTLs, the amount of and changes in its valuation allowance, significant components of income tax expense, differences between the expected amount of income tax expense using current tax rates and the amount of reported income tax expense, and tax attributes being carried over. In addition, FIN 48 includes specific disclosures related to uncertain tax positions.

- SSAP No. 101 – In general, paragraphs 21-29 of SSAP No. 101 follow the disclosure requirements provided by FAS 109, but with the following modifications and additions:

  - The disclosures regarding valuation allowance are replaced with disclosures relating to the statutory valuation allowance adjustment and the nonadmitted portion of the DTA.

  - The amount of the gross DTA, adjusted gross DTA, DTL, admitted and nonadmitted DTA is required to be separately disclosed, by tax character (ordinary or capital).

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- Disclose the amount of each result or component of the admission calculation, by tax character, for paragraphs 11.a, 11.b.i, 11.b.ii, and 11.c. In addition, disclose the ExDTA Authorized Control Level (ACL) RBC Ratio, the ExDTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital Ratio (see paragraph 11.b.), or the Adjusted Gross DTA/Adjusted Capital and Surplus Ratio used in the applicable Realization Threshold Limitation Table (the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) in paragraph 11.b., as applicable.

- The impact of tax-planning strategies on the determination of adjusted gross DTAs and the determination of net admitted adjusted gross DTAs, by percentage and by tax character, must be disclosed. In addition, disclose whether tax-planning strategies include the use of reinsurance-related tax planning strategies.

- FIN 48 and the associated disclosure requirements are rejected for statutory accounting purposes and replaced with the following disclosure. For any federal or foreign income tax loss contingencies for which it is reasonably possible that the total liability will significantly increase within 12 months of the reporting date, a disclosure of an estimate of the range of the reasonably possible increase is required. If determination of a reasonable range of the significant increase is not possible, the reporting entity is to provide a statement that an estimate cannot be made.

- The disclosures relating to deferred income tax expense or benefit are replaced with certain disclosures relating to the reporting entity's "change in DTAs and DTLs."

- Only the nature of significant reconciling items between the reported amount and "expected" amount of income tax expense and change in DTAs and DTLs are to be disclosed. This generally follows the disclosure requirements of FAS 109 for nonpublic entities.

- See Question 12 for a more detailed discussion of the disclosure requirements of SSAP No. 101.

2. Q – How should an entity measure its adjusted gross deferred tax assets and its gross deferred tax liabilities? [Paragraph 7]

2.1 A – An enterprise shall record a gross deferred tax liability or asset for all temporary differences and operating loss, capital loss and tax credit carryforwards. Temporary differences include unrealized gains and losses and nonadmitted assets but do not include AVR, IMR, Schedule F penalties and, in the case of a mortgage guaranty insurer, amounts attributable to its statutory contingency reserve to the extent that "tax and loss" bonds have been purchased. In general, temporary differences produce taxable income or result in tax deductions when the related asset is recovered or the related liability is settled. A deferred tax asset or liability represents the increase or decrease in taxes payable or refundable in future years as a result of temporary differences and carryforwards at the end of the current year. Additionally, gross DTAs are reduced by a statutory valuation allowance adjustment if, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50% ~~percent~~) that some portion or all of the gross DTAs will not be realized. The statutory valuation allowance adjustment, determined in a manner consistent with paragraphs 20-25 of FAS 109, shall reduce gross DTAs to the amount that is more likely than not to be realized (the adjusted gross deferred tax assets).[9] This answer only addresses the recognition of adjusted gross DTAs and gross DTLs and does not address the admissibility of such amounts. See Question 4 for a discussion of the admissibility criteria of SSAP No. 101.

[9] SSAP No. 101 requires the statutory valuation allowance adjustment to be presented in the annual statement as a direct reduction in the gross DTA. It is not included in non-admitted DTA.

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2.2 Paragraph 7 of SSAP No. 101 states that temporary differences are identified and measured using a "balance sheet" approach whereby the statutory balance sheet and the tax basis balance sheet are compared. Operating loss, capital loss and tax credit carryforwards are computed in accordance with the applicable Internal Revenue Code.

2.3 The following illustrates the recognition and measurement of a typical book to tax difference for an insurance company:

Illustration

Assumptions:

1/1/X2 Purchase 100 shares of Darby/Allyn Corp. stock for $25 a share
3/31/X2 Fair Value of Darby/Allyn Corp. stock has increased to $35 a share
3/31/X2 Tax basis reserves are computed and determined to be 80% of the statutory basis reserves

Balance Sheet at 3/31/X2:

	Statutory Basis	Tax Basis	Basis Difference	Tax Effect DTA (DTL) (21%)[10]
Common Stock	$3,500	$2,500	($1,000) [11]	($210)
Reserves	$100,000	$80,000	$20,000 [12]	$4,200

Journal Entries:

1/1/X2	DR	Common stock	$2,500
	CR	Cash	($2,500)
		Acquisition of common stock at $25 per share	

3/31/X2	DR	Common stock	$1,000
	CR	Change in unrealized capital gains and losses	($1,000)
		Adjust carrying value to FV of $35 per share at end of quarter	

3/31/X2	DR	Change in reserves or unpaid losses	$100,000
	CR	Reserves or Unpaid losses	($100,000)
		Recognition of reserves computed on a statutory basis	
3/31/X2	DR	Deferred tax asset	$4,200
	CR	Change in deferred income taxes	($3,990)
	CR	Deferred tax liability	($210)
		Recognition of deferred taxes	

[10] See Question 3 for a discussion of "enacted rates."

[11] The carrying value of the stock on the statutory balance sheet reflects the fair value of the common stock per *SSAP No. 30R—Unaffiliated Common Stock* whereas the carrying value of the stock for tax purposes is its original cost. This difference is defined as temporary in that the $1,000 appreciation in value will be recognized in the tax return when the stock is disposed of. The difference is a deferred tax liability in that the reversal of this temporary difference will increase future taxable income.

[12] The reserve difference arises because, even though tax reserves are based on statutory reserves, they generally are reduced below statutory reserves pursuant to various provisions of the Internal Revenue Code. This amount is a temporary difference in that the entity will recognize the difference between statutory and tax carrying values over the life of the reserve or upon settlement of the claim or payment of the reserve. The difference is a deferred tax asset in that the reversal of this temporary difference will decrease future taxable income.

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NOTE: Presentation of deferred tax amounts and unrealized gain or losses net of tax is addressed in Question 12.

2.4 As depicted in the Illustration, the deferred tax assets and liabilities are tracked gross in the entity's ledger and not netted until after consideration of the statutory valuation allowance adjustment, if any (see below), and the admissibility of deferred tax assets.

Statutory Valuation Allowance Adjustment

2.5 SSAP No. 101 paragraph 7.e., provides that gross DTAs are reduced by a statutory valuation allowance *adjustment* if, based on the weight of available evidence, it is more likely than not that some portion or all of the gross DTAs will not be realized. The statutory valuation allowance adjustment is determined on a separate company, reporting entity basis. The determination of whether gross DTAs will be realized is based on the existence of sufficient taxable income of the appropriate character (ordinary income or capital gain) within the carryback, carryover period available under the tax law. Paragraph 13.a. through 13.d. of SSAP No. 101 identifies four sources of taxable income to be considered in evaluating the existence of sufficient taxable income. These sources are identical to those to be considered under FAS 109 paragraph 21. FAS 109 paragraph 20 provides that "all available evidence, both positive and negative, should be considered to determine whether, based on the weight of that evidence, a valuation allowance is needed. Information about an enterprise's current financial position and its results of operations for the current and preceding years ordinarily is readily available. That historical information is supplemented by all currently available information about future years. Sometimes, however, historical information may not be available (for example, start-up operations) or it may not be as relevant (for example, if there has been a significant, recent change in circumstances) and special attention is required." A reporting entity is not required to consider all four sources of taxable income in determining the need for a statutory valuation allowance adjustment if one or more sources are alone sufficient to support the conclusion that the entity will realize the tax benefits of its gross deferred tax assets (i.e., a conclusion that no valuation allowance is necessary). However, the reporting entity is required to consider all of the potential sources of taxable income to determine the amount of the adjustment if a conclusion is reached that a statutory valuation allowance adjustment is necessary. SSAP No. 101 modifies FAS 109 related to admission of DTAs. Admission of DTAs is calculated irrespective of the conclusion reached in establishing or not establishing a statutory valuation allowance adjustment. See Question 4.13 for discussion regarding consideration of reversal patterns specific to paragraph 11.c. of the admissibility test.

2.6 Footnote 1 to paragraph 7.e. of SSAP No. 101 indicates that a reporting entity shall consider reversal patterns of temporary differences, and might be required to schedule such differences:

> …to the extent necessary to support establishing or not establishing a valuation allowance adjustment, determined in accordance with paragraphs 228 and 229 of FAS 109. For purposes of this accounting statement, consideration of reversal patterns does not require scheduling beyond that necessary to support establishing or not establishing a valuation allowance adjustment.

Paragraph 228 of FAS 109 generally holds that a company may need to schedule its temporary differences to determine the particular years in which the reversal of temporary differences is expected to occur. As discussed in Question 5b, paragraph 229 of FAS 109 indicates that future originating temporary differences and their subsequent reversal should be considered in determining the existence of future taxable income.

2.7 Although a reporting entity may need to consider the reversal pattern of temporary differences in evaluating the need for a statutory valuation allowance adjustment, scheduling the reversal pattern of such differences is not required in every instance. Under SSAP No. 101 and consistent with FAS 109, a general understanding of reversal patterns is, in many cases, relevant in assessing the need for a valuation allowance. Judgment is crucial in making this assessment. The amount of scheduling, if any, that will be

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required will depend on the facts and circumstances of each situation. For example, a reporting entity which relies upon future taxable income exclusive of reversing temporary differences and carryforwards[13] for realization of DTAs is not required to schedule the reversal pattern of its existing temporary differences. This is consistent with guidance provided by the Financial Accounting Standards Board (FASB) in its answer to question 2 of *A Guide to Implementation of Statement 109 on Accounting for Income Taxes: Question and Answers* (Special Report on Statement 109) which states that scheduling of existing temporary differences is unnecessary for purposes of determining the need for a valuation allowance "where it can be easily demonstrated that future taxable income will more likely than not be adequate to realize future tax benefits of existing deferred tax assets." In contrast, a reporting entity which relies upon the future reversal of existing taxable temporary differences to realize the tax benefits of its deductible temporary differences and carryforwards may be required to consider the reversal patterns of its taxable temporary differences.[14] The degree of scheduling required, however, depends on the facts and circumstances of each situation and the relative magnitude of the taxable and deductible temporary differences. In certain situations, the ability to reasonably conclude that reversing taxable temporary differences will more likely than not create sufficient taxable income to realize reversing deductible temporary differences can be done without detailed scheduling.[15]

2.8 If scheduling is considered necessary, the amount of scheduling required will depend on the particular facts and circumstances and be subject to judgment. There may be more than one acceptable approach. The FASB's answer to question 1 of the Special Report on Statement 109 indicates that the following concepts underlie the determination of reversal patterns under Statement 109:

a. The particular years in which temporary differences result in taxable or deductible amounts generally are determined by the timing of the recovery of the related asset or settlement of the related liability' (paragraph 228).

b. The tax law determines whether future reversals of temporary differences will result in taxable and deductible amounts that offset each other in future years' (paragraph 227).

In addition, the FASB noted that "minimizing complexity is an appropriate consideration in selecting a method for determining reversal patterns"[16], but that the methods used must be systematic and logical and should be consistently applied for all similarly categorized temporary differences and from year to year. Furthermore, the same method should be utilized in determining the reversal patterns in every taxing jurisdiction for which the temporary difference exists.

[13] One of the four possible sources of taxable income that can be used to realize a tax benefit. See paragraph 13.b. of SSAP No. 101.

[14] For example, due to the relatively short loss carryback periods (or, in the case of entities taxed as life insurance companies, no carryback of operating losses) under current tax law, such consideration may be appropriate when taxable temporary differences are expected to reverse in a short number of future years while the deductible temporary differences are expected to reverse over a long number of future years. In addition, for "indefinite-lived" intangible assets (i.e., intangible assets like those discussed in paragraph 11 of FAS 142 for which no legal, regulatory, contractual, competitive, economic, or other factors limit their useful lives), predicting reversal of temporary differences related to such assets would be inconsistent with financial reporting assertions that the assets are indefinite-lived. In such a case, the reversal of taxable temporary differences with respect to such indefinite-lived intangible assets should not be considered a source of future taxable income when determining the statutory valuation allowance adjustment for entities taxed as non-life insurance companies. On the other hand, entities taxed as life insurance companies may, under current tax law, carry forward operating losses with no expiration period, subject to a utilization limit of 80% of taxable income (before the loss carry forward) in the carry forward year. In such case, the reversal of taxable temporary differences with respect to indefinite-lived intangible assets may be considered a source of taxable income, subject to the applicable tax law limitations.

[15] Q&A 2 from the Special Report on Statement 109 published by the FASB.

[16] Q&A 1 from the Special Report on Statement 109 published by the FASB.

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Grouping of Assets and Liabilities for Measurement

2.9 The manner in which an entity groups its assets and liabilities for measurement shall be conducted in a reasonable and consistent manner. For instance, an entity may group its invested assets into annual statement classifications (stocks, bonds, preferred stocks, etc.) or other reasonable groupings (lines of business for grouping its reserves). Entities have the option of recognizing the DTA and DTL within each grouping on a net or gross basis. For instance, a portfolio of common stocks will have both unrealized gain and unrealized losses associated with them. The reporting entity may elect to combine the unrealized gains and losses and compute a single DTA or DTL or it may elect to segregate the unrealized gains from the unrealized losses and compute separate DTAs and DTLs. This option might also arise with respect to depreciable assets. Regardless of which method an entity elects, it is crucial that consistency is maintained to and within each grouping from period to period. An entity shall retain internal documentation to support its grouping in addition to the methodologies employed to arrive at such. An entity is permitted to modify its groupings should events or circumstances change from a previous period. Examples include a change in materiality of underlying assets and liabilities, administrative costs associated with detailing groupings increases or changes in the computer systems that allow more specificity. Entities that modify their groupings should be prepared to rationalize these changes. These entities should also disclose that a modification was made and general reason for such in the notes to the financial statements.

Measurement of Nonadmitted Assets

2.10 As noted in paragraph 7.b. of SSAP No. 101, temporary differences include nonadmitted assets. The measurement of these types of assets is not addressed in FAS 109 in that the concept of nonadmission is unique to statutory accounting. For assets that are nonadmitted for statutory accounting purposes, DTAs and DTLs should be measured after nonadmission.

Illustration:

	Statutory Before Nonadmit (Info Purpose)	**Statutory After Nonadmit**	**Tax**	**Basis Difference**[17]	**Tax Effect DTA (DTL) (**21%**)**
Furniture Fixtures and Equipment	$1,000	0	$1,000		
Accumulated Depreciation	200	0	400		
Basis	$800	0	$600	$600	$126

2.11 The effect of this illustration is a reduction of surplus by $674 ($800 decrease for nonadmitted asset and $126 increase for DTA), provided the resulting DTA meets the admissibility test in paragraph 11 of SSAP No. 101.

3. Q – A reporting entity's deferred tax assets and liabilities are computed using "enacted tax rates." What is **the meaning of the term "enacted tax rates"? [Paragraph 7.c.]**

3.1 A – Paragraph 7.c. of SSAP No.101 provides that total DTAs and DTLs are computed using enacted tax rates.

3.2 Consistent with FAS 109, SSAP No. 101 further requires that deferred tax assets and liabilities be measured using the enacted tax rate that is expected to apply to taxable income in the periods in which the

[17] Difference is computed from the "Statutory After Nonadmit" balance.

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deferred tax asset or liability is expected to be settled or realized. The effects of future changes in tax rates are not anticipated in the measurement of deferred tax assets and liabilities. Deferred tax assets and liabilities are adjusted for changes in tax rates and other changes in the tax law, and the effects of those changes are recognized at the time the change is enacted.

3.3 Tax laws may apply different tax rates to ordinary income and capital gains. In instances where the enacted tax law provides for different rates on income of different character, deferred tax assets and liabilities should be measured by applying the appropriate enacted tax rate based on the type of taxable or deductible amounts expected to be realized from the reversal of existing temporary differences.

4a. Q – How should a reporting entity calculate the amount of its admitted adjusted gross DTAs? [Paragraph 11]

4.1 A – After a reporting entity has calculated the amount of its adjusted gross DTAs and gross DTLs pursuant to paragraph 7, it must determine the amount of its adjusted gross DTAs that can be admitted under paragraph 11, not to exceed the amount of total adjusted gross DTAs. The amount of adjusted gross DTAs is not recalculated under paragraph 11; rather, some or all of the adjusted gross DTA may not be currently admitted. As noted in paragraph 11, the net admitted DTA shall not exceed the excess of the adjusted gross DTAs over gross DTLs.

4.2 Paragraphs 11.a., 11.b. and 11.c. require three interdependent calculations or components that when added together equal the amount of the reporting entity's admitted adjusted gross DTAs. Each of the calculations starts with the total of the reporting entity's adjusted gross DTAs, and determines the amount of such adjusted gross DTAs that can be admitted under that part. For example, the consideration of existing temporary differences in the calculation of admitted adjusted gross DTAs under paragraph 11.a., does not prevent the reconsideration of the same temporary differences in the paragraph 11.b.i. calculation. However, to avoid duplication of admitted adjusted gross DTAs when adding the three parts together, the amount of admitted adjusted gross DTAs under paragraph 11.a. must be subtracted from the amount of adjusted gross DTAs in the paragraph 11.b.i. calculation. Similarly, the amount of admitted adjusted gross DTAs under paragraphs 11.a. and 11.b. must be subtracted from the total adjusted gross DTAs in the paragraph 11.c. calculation. For illustrations of the paragraph 11 DTA admission calculations, see Question 4.16 through Question 4.25.

First Component – Admission Based on Previously Paid Taxes [Paragraph 11.a.]

4.3 Under paragraphs 11.a. and 12.b., a reporting entity can admit adjusted gross DTAs to the extent that it would be able to recover federal income taxes paid in the carryback period, by treating existing temporary differences that reverse during a timeframe corresponding with Internal Revenue Code tax loss carryback provisions[18], not to exceed three years as ordinary or capital losses that originated in each such subsequent year. The reversing temporary differences are specific to each year in which they reverse, and in turn, to the specific year(s) to which they can be carried back corresponding with tax loss carryback provisions. Reversing temporary differences for unrealized losses and nonadmitted assets are treated as capital or ordinary losses depending on their character for tax purposes. The entity is not required to project an actual net operating loss in future periods. This first component of admission is available to all entities, regardless of whether they meet any of the threshold limitations in paragraph 11.b. for reversals expected to be realized against future taxable income.

4.4 Paragraph 12.b. limits the amount of federal income taxes recoverable under paragraph 11.a. to the amount that would be refunded to the reporting entity if a carryback claim was filed with the Internal

[18] For example, under the Federal Internal Revenue Code, ordinary losses can be carried back two years for entities taxed as nonlife insurance companies, while capital losses for entities taxed both as nonlife and life insurance companies can be carried back three years. For losses arising in tax years after 2017, entities taxed as life insurance companies are not permitted to carryback ordinary losses.

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Revenue Service (IRS). If some amount of taxes paid in the carryback period is not recovered because of limitations imposed by the Alternative Minimum Tax system in effect in taxable years prior to 2018, the resulting AMT credit is not treated as a newly created DTA. Paragraph 12.c. further limits the amount of federal income taxes recoverable under paragraph 11.a. for a reporting entity that files a consolidated income tax return with one or more affiliates, to the amount that the reporting entity could reasonably expect to have refunded by its parent. See Question 8 for a further discussion of the impact of filing a consolidated federal income tax return.

Second Component – Admission Based On Projected Future Tax Savings [Paragraph 11.b.]

4.5 The amount of a reporting entity's adjusted gross DTAs that can be admitted pursuant to paragraph 11.b. is in part, dependent on the amount of the reporting entity's adjusted capital and surplus. Accordingly, a reporting entity must determine which Realization Threshold Limitation Table set forth in paragraph 11.b. is applicable to the reporting entity and then, based on its respective facts, determine what applicable period to apply under paragraph 11.b.i. and applicable percentage to use under paragraph 11.b.ii.

4.6 If the reporting entity is subject to risk-based capital requirements or is required to file a Risk-Based Capital Report with the domiciliary state, it should use the RBC Reporting Entity Table set forth in paragraph 11.b. Threshold limitations for this table are contingent upon the ExDTA ACL RBC ratio. See Question 4b for a discussion on the ExDTA ACL RBC ratio.

4.7 If the reporting entity is (1) either a mortgage guaranty insurer or financial guaranty insurer that is not subject to risk-based capital requirements, (2) is not required to file a Risk-Based Capital Report with the domiciliary state, and (3) the reporting entity meets the minimum capital and reserve requirements[19] for the state of domicile, then it should use the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table set forth in paragraph 11.b. Threshold limitations for this table are contingent upon the ratio of ExDTA Surplus plus contingency reserves divided by the minimum aggregate capital required (see further detail in paragraph 11.b.).

4.8 If the reporting entity (1) is not subject to risk-based capital requirements, (2) is not required to file a Risk-Based Capital Report with the domiciliary state, (3) is not a mortgage guaranty or financial guaranty insurer, and (4) meets the minimum capital and reserve requirements[19], it should use the Other Non-RBC Reporting Entity Table set forth in paragraph 11.b. Threshold limitations for this table are contingent upon the ratio of adjusted gross DTA less the amount of adjusted gross DTA admitted in paragraph 11.a. to adjusted capital and surplus.

4.9 The amount of admitted adjusted gross DTAs under paragraph 11.b.i., is limited to the amount that the reporting entity expects to realize within the applicable period as determined using the applicable Realization Threshold Limitation Table following the balance sheet date. See Question 6 for a further discussion of the meaning of "expected to be realized." See Question 4.2 regarding the amount of adjusted gross DTAs considered in the paragraph 11.b.i. calculation. The amount of admitted adjusted gross DTAs under the paragraph 11.a. calculation is subtracted from the amount of adjusted gross DTAs under paragraph 11.b.i., to prevent the counting of the same admitted adjusted gross DTAs more than once. If the reporting entity expects to realize an amount of adjusted gross DTAs under paragraph 11.b.i. that is equal to or less than the admitted adjusted gross DTAs calculated under paragraph 11.a., then the resulting admitted adjusted gross DTAs under paragraph 11.b.i. will be zero.

4.10 The reference to applicable period following the balance sheet date in 4.9 refers to the paragraph 11.b.i. column of the applicable Realization Threshold Limitation Table, the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table or the Other Non-RBC Reporting Entity Table.

[19] If a reporting entity is not at the minimum capital and reserve requirements, the admitted adjusted gross DTA for this component is zero.

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4.11 The amount of admitted adjusted gross DTAs under paragraph 11.b.i. is also limited to an amount that is no greater than the applicable percentage of adjusted statutory capital and surplus specified in paragraph 11.b.ii. See Question 4c for a discussion of the meaning of "an amount that is no greater than".

4.12 The reference to an amount no greater than the applicable percentage of statutory capital and surplus in 4.11 refers to the 11.b.ii. column of the applicable Realization Threshold Limitation Table; the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table or the Other Non-RBC Reporting Entity Table.

Third Component – Admission Based On Offset Against DTL [Paragraph 11.c.]

4.13 Under paragraph 11.c., a reporting entity can admit adjusted gross DTAs as an offset against gross DTLs in an amount equal to the lesser of: (1) its adjusted gross DTAs, after subtracting the amount of admitted adjusted gross DTAs under paragraphs 11.a. and 11.b., or (2) its gross DTLs. See Question 4.2 regarding the amount of adjusted gross DTAs considered in the paragraph 11.c. calculation. In determining the amount of adjusted gross DTAs that can be offset against existing gross DTLs in the paragraph 11.c. calculation, the character (i.e., ordinary versus capital) of the DTAs and DTLs must be taken into consideration such that offsetting would be permitted in the tax return under existing enacted federal income tax laws and regulations. For example, an adjusted gross DTA related to unrealized capital losses could not be offset against an ordinary income DTL. Ordinary DTAs can be admitted by offset with ordinary DTLs and/or capital DTLs. However, capital DTAs can only be admitted by offset with capital DTLs. In addition, for reporting entities that consider reversal of existing temporary differences in determining the need for a statutory valuation allowance adjustment, significant and relevant historical and/or currently available information may exist specific to the remaining amount of total adjusted gross DTAs and gross DTLs must also be taken into consideration in the determination of the admission of adjusted gross DTAs under paragraph 11.c. However, for those reporting entities, no scheduling is required beyond that necessary in determining the need for a statutory valuation allowance adjustment. As stated in paragraph 11.c., "for purposes of this component, the reporting entity shall consider the reversal patterns of temporary differences; however, this consideration does not require scheduling beyond that required in paragraph 7.e." See Question 2.5 through Question 2.8 for further discussion of scheduling for purposes of determining the reporting entity's statutory valuation allowance adjustment.) This consideration requires a scheduling exercise if scheduling is needed for determination of the statutory valuation allowance adjustment and, as a result, should be consistent with the determination of any statutory valuation allowance adjustment, which occurs prior to performing the admissibility calculations.[20] However, as noted in Question 2.7, scheduling reversal patterns of temporary differences in evaluating the need for a statutory valuation allowance adjustment where a reporting entity relies on sources of future taxable income, exclusive of reversals of temporary differences, is not required. In such case, that reporting entity is not required to schedule reversal patterns of temporary differences for purposes of paragraph 11.c. of SSAP No. 101. This is the case even if the reversal pattern of the temporary difference is readily determinable, such as straight-line amortization of a fixed amount. It also is the case if, for example, the reporting entity in determining its statutory valuation allowance adjustment has considered a source of future income reversal of existing temporary differences that are capital in character, but not those that are ordinary in character. In such case, the reporting entity is not required to schedule reversal patterns of ordinary temporary differences for purposes of paragraph 11.c.

[20] Footnote 1 of SSAP No. 101 provides that a reporting entity "shall consider reversal patterns of temporary differences *to the extent necessary* to support establishing or not establishing a valuation allowance adjustment." (Emphasis added).

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Other Considerations

4.14 In certain situations, a reporting entity's expected federal income tax rate on its reversing temporary differences are expected to be less than the enacted tax rate used in the determination of its gross DTAs and DTLs. Examples of such entities include: Blue Cross-Blue Shield Organizations with section 833(b) deductions, reporting entities projecting a tax loss, and entities that file in a consolidated federal income tax return that cannot realize the full amount of their adjusted gross DTAs under the existing intercompany tax sharing or tax allocation agreement. Pursuant to paragraphs 231, 232 and 238 of FAS 109, such entities are required to report their gross DTLs at the enacted tax rate, and cannot take into consideration the impact of other adjustments such as the section 833(b) deduction to reduce their gross DTLs.

4.15 For those entities, the amount of admitted adjusted gross DTAs calculated under paragraph 11.a. will reflect the actual tax rate in the carryback period under paragraph 11.a. which takes into consideration the impact in the carryback years of the AMT and special deductions, as well as the provisions of the intercompany tax sharing or allocation agreement. Likewise, the amount of admitted adjusted gross DTAs calculated under paragraph 11.b. will reflect the expected tax rate in the applicable period as discussed in paragraph 4.14, which takes into consideration the impact of special deductions and the provisions of the intercompany tax sharing or allocation agreement. See Question 6 for further discussion of this issue. As such, the entity's admitted adjusted gross DTAs under paragraphs 11.a. and 11.b. may be less than its adjusted gross DTAs on temporary differences at the enacted rate. Any unused amount of DTAs resulting from this differential under paragraphs 11.a. and 11.b. can be used under paragraph 11.c. to offset existing DTLs.

4.16 The above principles can be illustrated by the following examples:

4.17 Facts:

RBC Reporting Entity Example

1. Life Insurance Company ABC[21] has $9,500,000 of deductible temporary differences ($6,000,000 ordinary and $3,500,000 capital) at 12-31-20X2 that generate $1,995,000 of gross DTAs ($1,260,000 ordinary, $735,000 capital), at the enacted federal income tax rate of 21%%. ABC has sufficient evidence of projected future taxable income exclusive of reversing temporary differences and carryforwards to support a conclusion that it will realize the full amount of its ordinary gross DTAs, and it was unnecessary in reaching that conclusion (i.e., that no valuation allowance adjustment need be established for ordinary DTAs) to consider reversal patterns of temporary differences. However, management has concluded, after considering all four sources of taxable income described in paragraph 13 of SSAP No. 101, that a statutory valuation allowance adjustment should be recognized for $168,000 of capital DTAs, reducing capital DTAs from $735,000 to $567,000. Thus, in total, management has concluded that ABC will more likely than not realize gross DTAs of $1,827,000 ($1,260,000 ordinary, $567,000 capital) related to its $9,500,000 of deductible temporary differences. ABC also has $4,000,000 of taxable temporary differences ($2,800,000 ordinary and $1,200,000 capital) resulting in $840,000 ($588,000 ordinary, $252,000 capital) of gross DTLs.

2. ABC has determined that $2,000,000 of its $6,000,000 existing deductible ordinary temporary differences will reverse in 20X3, another $1,500,000 will reverse in 20X4, and another $2,000,000 will reverse in 20X5. The remaining $500,000 of ABC's existing deductible ordinary temporary differences will reverse in years 20X6 or later. ABC has determined that $200,000, $300,000, and $400,000 of its $3,500,000 deductible capital

[21] Please note the results in this example may be different due to differences in the applicable carryback periods if ABC was taxed as a non-life insurance company.

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temporary differences are expected to reverse in 20X3, 20X4, and 20X5, respectively, and the remaining $2,600,000 will reverse in years 20X6 or later.

3. ABC reported $400,000 ($300,000 ordinary, $100,000 capital) and $1,000,000 ($800,000 ordinary, $200,000 capital) of taxable income in 20X0 and 20X1, respectively. ABC reported $84,000 ($63,000 ordinary, $21,000 capital) and $210,000 ($168,000 ordinary, $42,000 capital) of tax expense on its 20X0 and 20X1 federal income tax returns, respectively. It has also projected taxable income of $1,500,000 ($1,200,000 ordinary, $300,000 capital) and $315,000 ($252,000 ordinary, $63,000 capital) of federal income taxes for 20X2 that have been reflected in its current statutory income tax provision calculation.

4. ABC expects to realize[22] a federal income tax benefit of 21% from 20X3 through 20X5 related to reversing ordinary temporary differences. ABC does not anticipate any capital gain income in 20X3 through 20X5.

5. ABC has an ExDTA ACL RBC Ratio at 12-31-20X2 of 600%. Adjusted statutory capital and surplus under paragraph 11.b.ii. is $7,000,000 at 12-31-20X2, and was computed by subtracting the admitted balances of net DTA's, goodwill and EDP from the current period statutory surplus. Statutory surplus is defined in paragraph 2 of SSAP No. 72.

6. The above facts are summarized in the following table:

	Ordinary	Capital	Total
20X2 – Current Year Taxable Income & Tax:			
Taxable Income in CY	$ 1,200,000	$ 300,000	$ 1,500,000
Tax Provision @ 21%	$ 252,000	$ 63,000	$ 315,000
Deductible Temporary Differences	$ 6,000,000	$ 3,500,000	$ 9,500,000
DTA @21%	$ 1,260,000	$ 735,000	$ 1,995,000
Taxable Temporary Differences	$ 2,800,000	$ 1,200,000	$ 4,000,000
DTL @21%	$ 588,000	$ 252,000	$ 840,000
Valuation Allowance		$ 168,000	$ 168,000
Carryback Taxable Income & Tax:			
20X0 Taxable Income	$ 300,000	$ 100,000	$ 400,000
Tax	$ 63,000	$ 21,000	$ 84,000
20X1 Taxable Income	$ 800,000	$ 200,000	$ 1,000,000
Tax	$ 168,000	$ 42,000	$ 210,000
Reversal of Deductible Temp Differences:			
20X3	$ 2,000,000	$ 200,000	$ 2,200,000
20X4	$ 1,500,000	$ 300,000	$ 1,800,000
20X5	$ 2,000,000	$ 400,000	$ 2,400,000
20X6 and later	$ 500,000	$ 2,600,000	$ 3,100,000
Total (before valuation allowance)	$ 6,000,000	$ 3,500,000	$ 9,500,000

4.18 Calculation of ABC's Admitted Adjusted Gross DTAs:

1. Paragraph 11.a. calculation. ABC cannot admit any ordinary adjusted gross DTAs under paragraph 11.a., because entities taxed as life insurance companies are not permitted to carry back ordinary tax losses under existing Federal income tax law. However, ABC can admit

[22] See Question 6 for discussion on the admittance calculation under paragraph 11.b.i. and what is meant by the phrase: "expected to be realized."

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capital adjusted gross DTAs of $126,000 under paragraph 11.a. because all capital losses are permitted a 3-year carryback under existing Federal income tax law and ABC paid taxes on capital gains in each year 20X0-20X2.

a. ABC first carries $100,000 of the hypothetical capital loss[23] of $200,000 from 20X3 back to 20X0 recovering $21,000 in taxes paid. The remaining $100,000 of the 20X3 hypothetical capital loss ($200,000 – $100,000) is available for utilization in years 20X1 and 20X2.

b. ABC would carry the remaining $100,000 of the hypothetical capital loss from 20X3 back to 20X1 recovering $21,000 in taxes paid. In addition, ABC would carry back $100,000 of hypothetical capital loss from 20X4 to 20X1 to recover another $21,000 of taxes paid.[24]

c. ABC would carry the remaining $200,000 of the hypothetical capital loss from 20X4 plus an additional $100,000 of the hypothetical capital loss from 20X5 back to 20X2, recovering $63,000 in taxes projected to be paid.

2. Paragraph 11.b. calculation. ABC can admit $1,050,000 of adjusted gross DTAs under paragraph 11.b. Since ABC has an ExDTA ACL RBC ratio of 600%, the Realization Threshold Limitation Table provides that the company can use the thresholds of 3 years for projected realization and 15% of adjusted capital and surplus. The company expects to realize a federal income tax benefit of $1,155,000 ($5,500,000 X 21%) in 20X3 through 20X5 related to its reversing ordinary deductible temporary differences and $126,000 ($600,000 X 21%) in 20X3 through 20X5 related to its reversing capital deductible temporary differences (through carryback to 20X0-20X2).[25] The $1,281,000 amount ($1,155,000 + $126,000) must be reduced by the $126,000 of admitted adjusted gross DTAs under paragraph 11.a. to prevent double counting of the same income tax benefit. As a result, ABC has projected adjusted gross DTAs available for admission under this component of $1,155,000 ($1,281,000 – $126,000), all of which are ordinary in tax character. However, 15% of adjusted capital and surplus is a limiting factor in this example. As such, even though ABC has sufficient sources of future taxable income exclusive of reversing taxable temporary differences to realize a federal income tax benefit of $1,155,000 in 20X3 through 20X5 related to its reversing ordinary deductible temporary differences, admission of those temporary differences is limited to $1,050,000 ($7,000,000 X 15%).

3. Paragraph 11.c. calculation. ABC can admit $462,000 ($210,000 ordinary, $252,000 capital) of adjusted gross DTAs under paragraph 11.c. ABC has $1,827,000 of total adjusted gross DTAs available for admission under paragraph 11. These DTAs are made up of $1,260,000 ordinary DTAs and $567,000 of capital DTAs. To prevent double counting of admitted adjusted gross DTAs, the $1,260,000 of ordinary DTAs must be reduced by the $1,050,000 admitted under paragraph 11.b., leaving $210,000 for admission under paragraph 11.c. Likewise, the $567,000 of capital DTAs must be reduced by the $126,000 admitted under paragraph 11.a., leaving $441,000 for admission under paragraph 11.c. There are $588,000 of ordinary DTLs available to offset against the $210,000 of ordinary DTAs. There are $252,000 of

[23] It should be noted that if ABC's hypothetical 20X3 carryback was insufficient to fully offset all capital gain income in 20X0, the company would not be allowed to carryback any of the hypothetical loss from 20X4 or 20X5 to 20X0 per paragraph 11.a., as 20X0 is outside of the timeframe corresponding with capital loss carryback provisions for an insurance company.

[24] If ABC would not have had sufficient hypothetical capital loss from 20X4 to carryback to 20X1, the company would not have been able to carryback its hypothetical capital loss of $400,000 from 20X5 back to 20X1 pursuant to the applicable tax loss carryback provisions.

[25] Because ABC projects no capital gain income in 20X3 through 20X5, it is not able to realize a federal income tax benefit on the remaining $300,000 of capital temporary differences reversing in that 3-year period.

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capital DTLs available to offset against the $441,000 capital DTAs. However, the tax character of the DTAs and DTLs becomes a limiting factor for this component. While ordinary DTAs can be offset against both ordinary and capital DTLs, the reverse is not allowed in the tax return (see Question 4.13). Because ABC did not consider reversal of existing temporary differences in determining that no valuation allowance was necessary for gross ordinary DTAs, it need not consider reversal patterns of temporary differences for admission of ordinary DTAs in its paragraph 11.c. calculation. On the other hand, because ABC was required to consider all four sources of taxable income specified in paragraph 13 of SSAP No. 101(including future reversals of existing taxable capital temporary differences) in establishing a valuation allowance for gross capital DTAs, it is required to consider reversal patterns of temporary differences for admission of capital DTAs in its paragraph 11.c. calculation, but this consideration does not require scheduling beyond that required by paragraph 7.e. of SSAP No. 101 (again see Question 4.13). In this situation, after the required consideration, ABC can admit $210,000 and $252,000 of its ordinary and capital DTAs, respectively.

4.19 Summary of ABC's Admitted Gross DTA Calculation:

	Ordinary	Capital	Total
Gross DTAs at Enacted Tax Rate	$1,260,000	$735,000	$1,995,000
Less: Statutory Valuation Allowance		$168,000	$168,000
Adjusted Gross DTAs at Enacted Tax Rate	$1,260,000	$567,000	$1,827,000
Admitted Gross DTAs (paragraph 11.a.)	0	$126,000	$126,000
Admitted Gross DTAs (paragraph 11.b.)	$1,050,000	0	$1,050,000
Admitted Gross DTAs (paragraph 11.c.)	$210,000	$252,000	$462,000
Total Admitted Adjusted Gross DTAs (sum of 11.a, 11.b., and 11.c)	$1,260,000	$378,000	$1,638,000
Nonadmitted Adjusted Gross DTAs	0	$239,000	$239,000
Admitted DTA	$1,260,000	$378,000	$1,638,000
Gross DTL	$(588,000)	$(252,000)	$(840,000)
Net Admitted DTA/DTL	$672,000	$126,000	$798,000

4.20 Facts:

Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Example

1. Financial Guaranty Insurance Company DEF has the same facts as Life Insurance Company ABC except:

a. DEF is not an RBC reporting entity and therefore does not calculate an RBC percentage. DEF is a financial guaranty insurer and has an ExDTA Surplus plus Contingency Reserve/Required Aggregate Risk Capital ratio of 105%. This ratio represents the sum of surplus to policyholders (excluding any admitted DTA from 11.a.) plus contingency reserves divided by the minimum aggregate capital required.

b. DEF reported $1,000,000 of taxable income and $210,000 of tax expense on its 20X1 federal income tax return. It has also projected taxable income of $1,500,000 and $315,000 of federal income taxes for 20X2 that has been reflected in its current statutory income tax provision calculation. DEF recognized no capital gain income in 20X1 or 20X2, so all of its taxable income in those years was ordinary in character. But DEF has $1,000,000 less deductible capital temporary differences than ABC and so, after considering all four sources

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of taxable income specified in paragraph 13 of SSAP No. 101, DEF establishes the same valuation allowance against gross capital DTAs as ABC. After the valuation allowance, DEF has $357,000 ($2,500,000 gross capital DTAs x 21% = $525,000 less $168,000 valuation allowance = $357,000) of adjusted gross capital DTAs.

4.21 Calculation of DEF's Admitted Adjusted Gross DTAs:

1. Paragraph 11.a. calculation. DEF can admit $525,000 ($210,000 + $315,000) of adjusted gross DTAs under paragraph 11.a, all of which are ordinary in tax character.

a. As an entity taxed as a nonlife insurance company, DEF, unlike ABC, is permitted to carry back ordinary tax losses. DEF first carries $1,000,000 of the hypothetical net operating loss[26] of $2,000,000 from 20X3 back to 20X1 recovering $210,000 in taxes paid. The remaining $1,000,000 of the hypothetical net operating loss ($2,000,000 – $1,000,000) is available for utilization in 20X2.

b. DEF would carry the remaining $1,000,000 of the hypothetical net operating loss from 20X3 plus an additional $500,000 of the hypothetical net operating loss from 20X4 back to 20X2 recovering $315,000 in taxes projected to be paid.[27]

2. Paragraph 11.b. calculation. DEF cannot admit any additional adjusted gross DTAs under paragraph 11.b. Since DEF has an ExDTA Surplus/Policyholders and Contingency Reserves ratio of 105%, the Realization Threshold Limitation Table provides that the company can use the thresholds of 1 year for projected realization and 10% of adjusted capital and surplus. The company expects to realize a federal income tax benefit of $420,000 ($2,000,000 X 21%) in 20X3 related to its reversing deductible temporary differences. The $420,000 amount must be reduced by the $525,000 of admitted adjusted gross DTAs under paragraph 11.a. to prevent double counting of the same income tax benefit. DEF admitted $105,000 ($525,000 - $420,000) more adjusted gross DTAs based on carryback of hypothetical net operating losses under paragraph 11.a. than is projected to be realized within the 1- year applicable threshold limitation. As a result, there is $0 of expected additional reversing deductible differences available for admission under paragraph 11.b.

3. Paragraph 11.c. calculation. DEF can admit $840,000 ($588,000 ordinary, $252,000 capital) of adjusted gross DTAs under paragraph 11.c. DEF has $1,617,000 of total adjusted gross DTAs available for admission under paragraph 11. These DTAs are made up of $1,260,000 ordinary DTAs and $357,000 of capital DTAs. To prevent double counting of admitted adjusted gross DTAs, the $1,260,000 of ordinary adjusted gross DTAs must be reduced by the $525,000 admitted under paragraph 11.a., leaving $735,000 for admission under paragraph 11.c. There are $588,000 of ordinary DTLs to offset against the $735,000 of ordinary DTAs. There are $252,000 of capital DTLs to offset against the $357,000 capital DTAs. However, the tax character of the DTAs and DTLs must be considered as a potential limiting factor for this component because while ordinary DTAs can be offset against both ordinary and capital DTLs, the reverse is not allowed in the tax return (see Question 4.13). In this situation, DEF can admit $588,000 and $252,000 of its ordinary and capital DTAs,

[26] It should be noted that if DEF's hypothetical 20X3 carryback was insufficient to fully offset all positive taxable income in 20X1, the company would not be allowed to carryback any of the hypothetical loss from 20X4 or 20X5 to 20X1 per paragraph 11.a., as 20X1 is outside of the timeframe corresponding with the tax loss carryback provisions for a non-life insurance company.

[27] If DEF would not have had sufficient hypothetical NOL from 20X4 to carryback to 20X2, the company would not have been able to carryback is hypothetical NOL of $2,000,000 from 20X5 back to 20X2 as 20X2 is outside of the timeframe corresponding with the tax loss carryback provisions for a nonlife insurance company.

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respectively.28 If DEF's adjusted gross DTAs, after reduction for the amount of adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., were less than $840,000 in this example, DEF would be limited to the balance of its adjusted gross DTAs in the paragraph 11.c. calculation, subject to the rules of offset under existing enacted federal income tax laws and regulations.

4.22 Summary of DEF's Admitted Gross DTA Calculation:

	Ordinary	Capital	Total
Gross DTAs at Enacted Tax Rate	$1,260,000	$525,000	$1,785,000
Less: Statutory Valuation Allowance		$168,000	$168,000
Adjusted Gross DTAs at Enacted Tax Rate	$1,260,000	$357,000	$1,617,000
Admitted Gross DTAs (paragraph 11.a.)	$525,000	$0	$525,000
Admitted Gross DTAs (paragraph 11.b.)	$0	0	$0
Admitted Gross DTAs (paragraph 11.c.)	$588,000	$252,000	$840,000
Total Admitted Adjusted Gross DTAs (sum of 11.a, 11.b., and 11.c)	$1,113,000	$252,000	$1,365,000
Nonadmitted Adjusted Gross DTAs	$147,000	$105,000	$352,000
Admitted DTA	$1,113,000	$252,000	$1,365,000
Gross DTL	$(588,000)	$(252,000)	$(840,000)
Net Admitted DTA/DTL	$525,000	$0	$525,000

4.23 Facts:

Other Non-RBC Reporting Entity Example

1. Title Insurance Company GHI has the same facts as Life Insurance Company ABC except:

a. GHI is not a RBC reporting entity and therefore does not calculate a RBC percentage. GHI is also not a financial guaranty or mortgage guaranty insurer. As such, GHI must use the Other Non-RBC Reporting Entity Threshold Limitation Table under paragraph 11.b.

b. GHI reported $1,000,000 of taxable income and $210,000 of tax expense on its 20X1 federal income tax return. It has also projected taxable income of $1,500,000 and $315,000 of federal income taxes for 20X2 that has been reflected in its current statutory income tax provision calculation. GHI recognized no capital gain income in 20X1 or 20X2, so all of its taxable income in those years was ordinary in character. But GHI has $1,000,000 less deductible capital temporary differences than ABC and so, after considering all four sources of taxable income specified in paragraph 13 of SSAP No. 101, GHI establishes the same valuation allowance against gross capital DTAs as ABC. After the valuation allowance, DEF has $357,000 ($2,500,000 gross capital DTAs x 21% = $525,000 less $168,000 valuation allowance = $357,000) of adjusted gross capital DTAs.

[28] DEF's required consideration of reversal patterns of temporary differences is the same as ABC's. See Question 4.18.3.

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4.24 Calculation of GHI's Admitted Adjusted Gross DTAs:

1. Paragraph 11.a. calculation. GHI can admit $525,000 ($210,000 + $315,000) of adjusted gross DTAs under paragraph 11.a, all of which are ordinary in tax character.

a. As an entity taxed as a nonlife insurance company, GHI, unlike ABC, is permitted to carry back ordinary tax losses. GHI first carries $1,000,000 of the hypothetical net operating loss[29] of $2,000,000 from 20X3 back to 20X1 recovering $210,000 in taxes paid. The remaining $1,000,000 of the hypothetical net operating loss ($2,000,000 – $1,000,000) is available for utilization in 20X2.

b. GHI would carry the remaining $1,000,000 of the hypothetical net operating loss from 20X3 plus an additional $500,000 of the hypothetical net operating loss from 20X4 back to 20X2 recovering $315,000 in taxes projected to be paid.[30]

2. Paragraph 11.b. calculation. GHI can admit $630,000 of adjusted gross DTAs under paragraph 11.b. Since GHI has an Adjusted Gross DTA to Adjusted Capital and Surplus ratio of 15.6% ($1,092,000/$7,000,000), the Realization Threshold Limitation Table provides that the company can use the thresholds of 3 years for projected realization and 15% of adjusted capital and surplus. The company expects to realize a federal income tax benefit of $1,155,000 ($5,500,000 X 21%) in 20X3 through 20X5 related to its reversing deductible temporary differences. The $1,155,000 amount must be reduced by the $525,000 of admitted adjusted gross DTAs under paragraph 11.a. to prevent double counting of the same income tax benefit. As a result, GHI has projected adjusted gross DTAs available for admission under this component of $630,000 ($1,155,000 – $525,000), all of which is ordinary in tax character. 15% of adjusted capital and surplus ($7,000,000 X 15% = $1,050,000) is not a limiting factor in this example. As such, admission of reversing deductible temporary differences that are projected to be realized during 20X3 through 20X5 is $630,000.

3. Paragraph 11.c. calculation. GHI can admit $357,000 ($105,000 ordinary, $252,000 capital) of adjusted gross DTAs under paragraph 11.c. GHI has $1,617,000 of total adjusted gross DTAs available for admission under paragraph 11. These DTAs are made up of 1,260$,000 ordinary DTAs and $357,000 of capital DTAs. To prevent double counting of admitted adjusted gross DTAs, the $1,260,000 of ordinary adjusted gross DTAs must be reduced by the $525,000 admitted under paragraph 11.a. and the $630,00 admitted under paragraph 11.b., leaving $105,000 for admission under paragraph 11.c. There is $588,000 of ordinary DTLs available to offset against the $105,000 of ordinary DTAs. There is $252,000 of capital DTLs to offset against the $357,000 capital DTAs. Accordingly, the tax character of the DTAs and DTLs becomes a limiting factor for this component. While ordinary DTAs can be offset against both ordinary and capital DTLs, the reverse is not allowed in the tax return (see Question 4.13). In this situation, GHI can admit $105,000 and $252,000 of its ordinary and capital DTAs, respectively[31].

[29] It should be noted that if GHI's hypothetical 20X3 carryback was insufficient to fully offset all positive taxable income in 20X1, the company would not be allowed to carryback any of the hypothetical loss from 20X4 or 20X5 to 20X1 per paragraph 11.a., as 20X1 is outside of the timeframe corresponding with the tax loss carryback provisions for a non-life insurance company.

[30] If GHI would not have had sufficient hypothetical NOL from 20X4 to carryback to 20X2, the company would not have been able to carryback is hypothetical NOL of $2,000,000 from 20X5 back to 20X2 as 20X2 is outside of the timeframe corresponding with the tax loss carryback provisions for a nonlife insurance company.

[31] GHI's required consideration of reversal patterns of temporary differences is the same as ABC's. See Question 4.18.3.

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4.25 Summary of GHI's Admitted Gross DTA Calculation:

	Ordinary	Capital	Total
Gross DTAs at Enacted Tax Rate	$1,260,000	$525,000	$1,785,000
Less: Statutory Valuation Allowance		$168,000	$168,000
Adjusted Gross DTAs at Enacted Tax Rate	$1,260,000	$357,000	$1,617,000
Admitted Gross DTAs (paragraph 11.a.)	$525,000	$0	$525,000
Admitted Gross DTAs (paragraph 11.b.)	$630,000	0	$630,000
Admitted Gross DTAs (paragraph 11.c.)	$105,000	$252,000	$357,000
Total Admitted Adjusted Gross DTAs (sum of 11.a, 11.b., and 11.c)	$1,260,000	$252,000	$1,512,000
Nonadmitted Adjusted Gross DTAs	$0	$105,000	$352,000
Admitted DTA	$1,260,000	$252,000	$1,512,000
Gross DTL	$(588,000)	$(252,000)	$(840,000)
Net Admitted DTA/DTL	$ 672,000	$0	$672,000

4b. Q – How is the ExDTA ACL RBC ratio calculated? [Paragraph 11.b.i.]

4.26 A – The December 31 ExDTA ACL RBC ratio is calculated in the same manner as in the ACL RBC Ratio computed in the Annual RBC Report, where Total Adjusted Capital (TAC) is divided by ACL RBC. However, for purposes of paragraph 11.b.i., TAC does not include any DTAs of the reporting entity. The ACL RBC would be the amount calculated in the Annual RBC Report.

4.27 The interim period (March 31, June 30, and September 30) ExDTA ACL RBC ratio calculation is discussed in 4.29-4.33.

4.28 For all companies, the TAC will include current period capital and surplus, excluding any DTAs of the reporting entity. Other TAC adjustments are dependent on whether the company is a Life, P&C or Health insurer.

4.29 For life companies, the AVR adjustment is calculated as a required part of the development of capital and surplus each quarter and is one of the major adjustments to TAC (added back to surplus). As noted on the illustrative interim TAC calculation in 4.33 for life companies, there are other TAC adjustments such as subsidiaries' dividend liabilities, etc., that are drawn from the quarterly statement.

4.30 For P&C and Health companies, except for the AVR and life subsidiaries' dividend liability amounts (both of which are only applicable to P&C companies with life subsidiaries), which are readily available on the quarter, the prior year's annual TAC adjustments should be used in the current quarter's TAC calculation. The P&C and Health interim TAC illustrations in 4.33 provide example details of various interim RBC TAC adjustments.

4.31 The ACL RBC used for the interim RBC calculation is the ACL RBC from the most recently filed annual statement for the most recent calendar year. For example, for June 30, 20X3, the ACL for the interim RBC calculation is taken from the 20X2 RBC Report based on the 20X2 annual statement.

4.32 In most instances, the prior year's annual ACL RBC will suffice. A company should only revise its interim ACL RBC for a material change in its risk profile when requested to do so by its domiciliary state or subject to domiciliary state approval.

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4.33 The above principles are illustrated below:

Interim Life RBC Example			
Based on the 2018 Life RBC Report page LR033			
		Reported	Interim Period
	SOURCE OF THE DATA	12/31/20X2	3/31/20X3
Capital and Surplus	P3, L38	$1,800,000,000	$1,700,000,000
Adjustments:			
AVR	P3, L24.01	60,000,000	65,000,000
Dividend Liability	P3, L6.1, L6.2 in part	0	0
Sub AVR	P3, L24.01 of subs	5,000,000	4,500,000
Sub Dividend Liability	P3, L6.1, L6.2 in part of subs	0	0
P&C Non-Tabular Discounts and/or Alien Insurance Subsidiary: Other	P&C Subs P3, L1 & L3 in part	0	0
Hedging Fair Value Adjustment	Company Records	0	0
Credit for Capital Notes	P3, L24.11	0	0
Total Adjusted Capital (TAC)	5-Year Historical Data, P22, C1, L30	1,865,000,000	1,769,500,000
Less: Deferred Tax Asset	P2, C3, L18.2	190,000,000	200,000,000
TAC ExDTA		$1,675,000,000	$1,569,500,000
Authorized Control Level RBC	5-Year Historical Data	$175,000,000	$175,000,000*
Total Adjusted Capital ExDTA/Authorized Control Level RBC		957%	897%
*ACL RBC amount for interim period is the 12/31/20X2 amount			

Interim P&C RBC Example			
(Based on the 2018 P&C RBC Report page PR026			
		Reported	Interim Period
	SOURCE OF THE DATA	12/31/20X2	3/31/20X3
Capital and Surplus	P3, C1, L37 (Ann. & Qtrly. Stmt.)	$850,000,000	$765,000,000
Adjustments:			
Non-Tabular Discount-Losses	SCHEDULE P P1-SUM C32, L12 (Ann. Stmt. Only)	(800,000)	(800,000)
Non-Tabular Discount-Expense	SCHEDULE P P1-SUM C33. L12 (Ann. Stmt. Only)	(60,000)	(60,000)
Discount on Medical Loss Reserves Reported as Tabular in Schedule P	Company Records	0	0

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Discount on Medical Expense Reserves Reported as Tabular in Schedule P	Company Records	0	0
P&C Subs Non-Tabular Discount-Losses	SCHEDULE P P1-SUM C32, L12 (Ann. Stmt. Only)	0	0
P&C Subs Non-Tabular Discount-Expenses	SCHEDULE P P1-SUM C33, L12 (Ann. Stmt. Only)	0	0
P&C Subs Discount on Medical Loss Reserves Reported as Tabular in Schedule P	Subs' Company Records	0	0
P&C Subs Discount on Medical Expense Reserves Reported as Tabular in Schedule P	Subs' Company Records	0	0
AVR - Life Subs	Subs P3, C1, L24.01 (Ann. & Qtrly. Stmt.)	5,000,000	6,000,000
Dividend Liability - Life Subs	Subs P3 C1 L6.1 + L6.2 (Ann. & Qtrly. Stmt.)	0	0
Total Adjusted Capital	5-Year Historical Data P17, C1, L28	854,140,000	770,140,000
	(Annual/Current calc. on Qtr.)		
Less: Deferred Tax Asset	P2, C3, L18.2 (Ann. & Qtrly. Stmt.)	82,000,000	72,000,000
Total Adjusted Capital ExDTA	PR026 (Annual RBC Report/Current Calc. on Qtr.)	772,140,000	698,140,000
Authorized Control Level Risk-Based Capital	5-Year Historical Data P17, C1, L29 (Annual)	171,000,000	171,000,000*
Total Adjusted Capital ExDTA/ Authorized Control Level Risk-Based Capital		452%	408%
*ACL RBC amount for interim period is the 12/31/20X2 amount			

Interim Health RBC Example			
(Based on the 2018 Health RBC Report page XR024			
		Reported	Interim Period
	SOURCE OF THE DATA	12/31/20X2	3/31/20X3
Capital and Surplus	P3, C3, L33 (Ann. & Qtrly. Stmt.)	$850,000,000	$765,000,000
Adjustments:			
AVR – Life Subs	Subs' Company Records	0	0
Dividend Liability – Life Subs	Subs' Company Records	0	0
Tabular Discounts – P&C subs	Subs' Company Records	0	0
Non-Tabular Discounts – P&C Subs	Subs' Company Records	0	0

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Total Adjusted Capital	5-Year Historical Data P28, C1, L14 (Annual/ Current calc. on Qtr.)	850,000,000	765,000,000
Less: Deferred Tax Asset	P2, C3, L18.2 (Ann. & Qtrly. Stmt.)	82,000,000	72,000,000
Total Adjusted Capital ExDTA	XR 24 (Annual RBC Report/Current Calc. on Qtr.)	768,000,000	693,000,000
Authorized Control Level Risk-Based Capital	5-Year Historical Data P28, C1, L15 (Annual)	171,000,000	171,000,000*
Total Adjusted Capital ExDTA/ Authorized Control Level Risk-Based Capital		449%	405%
*ACL RBC amount for interim period is the 12/31/20X2 amount			

4c. Q – What is meant by the phrase "an amount that is no greater than"? [Paragraph 11.b.ii.]

4.34 A – As discussed in question 4.11 the amount of admitted adjusted gross DTAs under paragraph 11.b.i. is also limited to an amount that is no greater than the applicable percentage of statutory capital and surplus test specified in paragraph 11.b.ii. For purposes of this test, statutory capital and surplus as shown on the statutory balance sheet of the reporting entity for the current period's statement filed with the domiciliary state commissioner is adjusted to exclude any net DTAs, EDP equipment and operating system software and any net positive goodwill.

4.35 The phrase "an amount that is no greater than" in paragraph 11.b.ii. allows an entity to utilize an amount lower (e.g., from the reporting entity's most recently filed statement) than what would be allowed if it utilized the amount of statutory capital and surplus adjusted to exclude any net DTAs, EDP equipment and operating system software and any net positive goodwill as required to be shown on the statutory balance sheet of the reporting entity for the current period's statement filed with the domiciliary state commissioner. This ability to utilize a lower amount is for administrative ease if a reporting entity's surplus is increasing.

4.36 For example, at 12/31/20X2 if adjusted capital and surplus is $100M and at 9/30/20X2 it was $80M, the entity may utilize the $80M amount from the prior quarter.

4.37 If instead 12/31/20X2 adjusted capital and surplus were $60M, the entity may not utilize the $80M amount from the prior quarter as that would overstate the limitation under paragraph 11.b.ii.

4.38 If at 12/31/20X2 an entity's adjusted capital and surplus was initially determined to be $150M, the entity can still utilize that amount under paragraph 11.b.ii., if there is a late accounting adjustment that increases that amount to $160M.

5a. Q – How is the timing of reversals of temporary differences and carryforwards determined for SSAP No. 101 purposes? [Paragraphs 7, 11.a., 11.b.i. and 12.a.]

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5.1 A – The timing of temporary difference reversals is critical in determining the amount of admitted adjusted gross DTAs. Determining the reversal of temporary differences impacts the adjusted gross DTA admitted pursuant to paragraphs 11.a., 11.b.i. and potentially 11.c. of SSAP No. 101. For purposes of paragraph 11.c., determining the reversal of temporary differences is necessary only to the extent required by paragraph 7.e. as discussed in Question 4.13.

5.2 Paragraph 12.a. of SSAP No. 101 states that "For purposes of paragraph 11.a., existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, shall be determined in accordance with paragraphs 228 and 229 of FAS 109." The timing of reversals of temporary differences and carryforwards for purposes of paragraph 11.b. of SSAP No. 101 shall be determined under similar principles.

5.3 Paragraph 228 of FAS 109 states, in pertinent part, that "[t]he particular years in which temporary differences result in taxable or deductible amounts generally are determined by the timing of the recovery of the related asset or settlement of the related liability." Question 1 of the FASB's Special Report on Statement 109 provides additional guidance on scheduling. It defines "scheduling" as the analysis performed to determine the pattern and timing of the reversal of temporary differences. The FASB's Special Report also provides certain scheduling guidelines to be followed, including the need for the method employed to be systematic and logical, that a consistent method be used for each category of temporary differences, and that a change in the method used be considered a change in accounting principle.

5.4 Assume Company A purchases its only asset for $1,000, an asset that is admissible for statutory accounting purposes and depreciated over five years on a straight-line basis. Assume also that the asset is depreciated over seven years for tax purposes using the Modified Accelerated Cost Recovery System (MACRS). The following table summarizes the statutory and tax basis of the asset at the end of each year.

Year	Cost	Statutory Depreciation	Statutory Basis	Tax Depreciation	Tax Basis	Deductible/ (Taxable) Temporary Difference
1	$1,000	$200	$800	$143	$857	$57
2	-	200	600	245	612	12
3	-	200	400	175	437	37
4	-	200	200	125	312	112
5	-	200	-	89	223	223
6	-	-	-	89	134	134
7	-	-	-	89	45	45
8	-	-	-	45[32]	-	-

5.5 At the end of year one, the Company would conclude that $45 ($57 - $12) of the $57 outstanding deductible temporary difference would reverse within one year, leaving a temporary difference of $12 at the end of year two. However, for computing a two or three-year reversal, the Company would not project a reversal of the temporary difference by the end of year three or four as the deductible temporary difference is scheduled to increase (from $12 to $37 and from $37 to $112, respectively). If the Company had decided to sell the asset in year two, it may be appropriate to conclude that the outstanding deductible temporary difference of $57 would reverse in year two.

[32] Due to the mid-year convention applicable to most asset acquisitions for tax purposes, the asset is treated as acquired in mid-year, meaning that a seven (7) year asset is depreciated over eight (8) tax years.

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5.6 A similar rationale would apply in the instance of a nonadmitted asset. Assume the same facts as aforementioned, except that the asset is nonadmitted for statutory accounting purposes. The results are summarized in tabular form below.

Year	Cost	Statutory Charge to Surplus	Statutory Basis	Tax Depreciation	Tax Basis	Deductible/ (Taxable) Temporary Difference
1	$1,000	$1,000	-	$143	$857	$857
2	-	-	-	245	612	612
3	-	-	-	175	437	437
4	-	-	-	125	312	312
5	-	-	-	89	223	223
6	-	-	-	89	134	134
7	-	-	-	89	45	45
8	-	-	-	45	-	-

5.7 In this example, the Company has a steady decline in the deductible temporary difference that is not complicated by competing depreciation regimes. This is due to the fact that the Company took the large surplus charge when the asset was nonadmitted, thereby creating a significant deductible temporary difference. The Company would project a $245 temporary difference reversal in year two (from $857 to $612), a $175 temporary difference reversal in year three (from $612 to $437), and a $125 temporary difference reversal in year four (from $437 to $312). Although the Company will take income statement charges for depreciation on the nonadmitted asset, the statutory basis is nonetheless zero from the moment the asset was nonadmitted. Future statutory depreciation deductions will not impact the statutory basis and have no impact on the analysis.

5.8 The above examples assume a single asset. However, the analysis becomes more complicated when the Company has hundreds or thousands of assets within its fixed asset pool. In this instance, it is expected that management will make its best estimate of the expected reversal pattern determined in a manner consistent with the grouping for measurement (see question 2 for more discussion about grouping).

5.9 As indicated above, the timing of the reversal of a particular balance sheet item will depend on the expected recovery of the related asset and liability. For example, the temporary difference associated with property & casualty loss reserves would be expected to reverse in a manner consistent with the payout pattern ("development") of the underlying loss reserves. Historical loss development triangles may be useful in substantiating a reversal pattern. For instance, assume Company A writes two types of property and casualty policies: auto liability and workers' compensation. The following table details the components of the statutory and tax reserves for Company A as of December 31, 20X2.[33]

Private Passenger Auto Liability	Statutory Reserves	Tax Reserves	Temporary Difference
AY + 0	$1,000	$900	$100
AY + 1	850	690	160
AY + 2	700	580	120
AY + 3	550	490	60
AY + 4	400	385	15
AY + 5	300	275	25
AY + 6	200	175	25
AY + 7	100	90	10

[33] Under current tax law, the loss payment period extends for more years, but the concepts illustrated herein are unchanged.

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AY + 8	80	75	5
AY + 9	70	65	5
Prior	50	45	5
Total	$4,300	$3,770	$530

Workers' Compensation	Statutory Reserves	Tax Reserves	Temporary Difference
AY + 0	$1,000	$825	$175
AY + 1	900	800	100
AY + 2	850	770	80
AY + 3	790	695	95
AY + 4	725	610	115
AY + 5	695	600	95
AY + 6	655	575	80
AY + 7	605	545	60
AY + 8	575	505	70
AY + 9	550	495	55
Prior	505	450	55
Total	$7,850	$6,870	$980

5.10 One option in analyzing the reversal of the temporary difference would be to calculate the historical loss development patterns for the two lines of business by accident year for each year in the applicable reversal period. By applying these development patterns to the individual temporary differences, the Company could estimate the expected reversal of the temporary difference as a whole for each year in the applicable reversal period.

5.11 Another option would be to apply the average development factor by line of business to each reserve for each year in the applicable reversal period. If the average one-year development factor for all accident years for auto liability and workers' compensation were 70% and 35%, respectively, the one-year temporary difference reversal would be $371 ($530 x 70%) for auto liability and $343 ($980 x 35%) for workers' compensation. The same approach could be used in determining the reversal for any other year in the applicable reversal period.

5.12 The temporary difference related to property and casualty unearned premiums is typically ~~twenty percent (~~20%~~)~~ of the outstanding statutory unearned premium reserve. If a company issues only one-year policies, it is reasonable to assume that the entire temporary difference will reverse in one year. If a company writes multi-year contracts, management will be required to estimate the percentage of the unearned premium that will be earned within each year of the applicable reversal period and apply these percentages to the outstanding temporary difference.

5.13 The reversal of the temporary difference related to life insurance reserves may require actuarial assistance, normally involving anticipated development of the statutory and tax reserves for policies issued prior to the end of the current reporting year. In computing the anticipated development, it would be expected that reasonable assumptions be used, which may include cash-flow modeling of the entity's reserves. Deferred acquisition costs on life insurance policies are amortized over prescribed periods pursuant to federal tax law. The amortization schedules should provide management with the ability to estimate the reversal for each year in the applicable reversal period with reasonable accuracy.

5.14 For those temporary differences that do not have a defined reversal period, such as unrealized losses on common stock or deferred compensation liabilities, management will need to determine when the temporary difference is "expected" to reverse. For instance, assume a company has an unrealized loss

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of $200 in its equity portfolio and that, on average, the portfolio turns over ~~twenty percent (~~20%~~)~~ per year. It would be appropriate for the company to conclude that $40 of the temporary difference will reverse in each year in the applicable reversal period. When determining when the temporary difference would be "expected" to reverse, management should normally consider events that are likely to occur using information, facts and circumstances in existence as of the reporting date. The estimates used in this circumstance should not be extended to other tests of impairment. For instance, when the entity assumed a 20% turnover in its equity portfolio, it is not involuntarily required to record an impairment in accordance with paragraph ~~10~~11 of *SSAP No. 30R—Unaffiliated Common Stock*.

5.15 In summary, the methodology used to develop the reversal pattern should be consistent, systematic, and rational. Although consistency is encouraged, business conditions may dictate that certain factors be given more or less weight than in previous periods. Factors to be considered include historical patterns, recent trends, and the likely impact of future initiatives (without regard to future originating temporary differences). For instance, if a company has migrated to a more efficient claims management system, outstanding reserves may be settled more quickly than historical payment patterns may indicate. A company that expects to enter into a loss portfolio transfer reinsurance transaction should consider the implications of that treaty in determining the reversal of the loss reserve temporary difference.

5b. Q – How should future originating differences impact the scheduling of temporary difference reversals during the applicable period? [Paragraphs 11.a., 11.b.i., 11.c. and 12.a]

5.16 A – Future originating differences, and their subsequent reversals, are considered in assessing the existence of future taxable income. However, they should not impact the scheduling of existing temporary difference reversals during the applicable period. Paragraph 229 of FAS 109 provides the following:

> 229. For some assets or liabilities, temporary differences may accumulate over several years and then reverse over several years. That pattern is common for depreciable assets. Future originating differences for existing depreciable assets and their subsequent reversals are a factor to be considered when assessing the likelihood of future taxable income (paragraph 21(b)) for realization of a tax benefit for existing deductible temporary differences and carryforwards.

6. Q – What is meant by the phrase "expected to be realized"? [Paragraph 11.b.i.]

6.1 A – A reporting entity calculates the amount of its adjusted gross DTAs and gross DTLs under paragraph 7 using the enacted tax rate. The amount of adjusted gross DTAs and gross DTLs is not recalculated under paragraph 11. The purpose of paragraph 11 is to determine the amount of adjusted gross DTAs that can be admitted in the reporting period.

6.2 An excerpt of SSAP No. 4 – *Assets and Nonadmitted Assets* indicates:

> 2. For purposes of statutory accounting, an asset shall be defined as: probable[34] future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.

6.3 The phrase "expected to be realized" encompasses a reasonable expectation as to the value of the DTAs consistent with SSAP No. 4. This means that if a reporting entity's management expects that deductible temporary differences that reverse in the applicable period will produce a federal income tax benefit at a rate that is lower than the enacted rate, the expected rate should be taken into consideration in the determination of the amount of admitted adjusted gross DTAs under paragraph 11.b.i. In other words, available evidence causes the reporting entity to expect the asset to be realized at less than the enacted

[34] *FASB Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements* (CON 6) states, "Probable is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in FASB Statement No. 5, Accounting for Contingencies, par. 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved."

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rate. In such cases, it would not be appropriate to calculate the amount of admitted adjusted gross DTAs under paragraph 11.b.i. on the basis of reversing deductible temporary differences at the enacted tax rate.

6.4 The following examples illustrate situations where the amount of admitted adjusted gross DTAs under paragraph 11.b.i. would be less than the adjusted gross DTAs calculated using deductible temporary differences reversing in the applicable period at the enacted income tax rate. The approach in these examples is to determine the tax savings that the company would expect to realize from its reversing deductible temporary differences. This is accomplished through a calculation of the company's income tax liability "with and without" these temporary differences. It is assumed that in these examples there are no prudent and feasible tax-planning strategies that would cause the entity to expect the asset to be realized at a rate different than that presented in the examples.

Example 1:

6.5 BCBS is a Blue Cross/Blue Shield Organization that expects to fully offset its regular taxable income with available section 833 (b) deductions in 20X2. Prior to considering the section 833 (b) deduction, BCBS projects $8,000,000 of taxable income in 20X3, which includes $3,000,000 of reversing deductible temporary differences that were part of its def erred inventory at 12/31/X2. The Company's ExDTA ACL RBC percentage is 250% and therefore it is required to use the one-year applicable period under paragraph 11.b.i.

20X3	Without Reversing Temporary Differences	With Reversing Temporary Differences
Taxable Income Before 833(b)	$11,000,000	$11,000,000
Reversing Temporary Differences		(3,000,000)
Net	11,000,000	8,000,000
Section 833 (b) Deduction	(11,000,000)	(8,000,000)
Taxable Income	C 0	0
Tax	0	0

6.6 BCBS has a 0% effective tax rate on taxable income in 20X3Its regular taxable income is $0, both "with and without" the $3,000,000 reversing deductible temporary differences since the section 833 (b) deduction changes by an equal amount. Therefore, BCBS would admit zero adjusted gross DTAs under paragraph 11.b.i., before reduction for any adjusted gross DTAs admitted under paragraph 11.a. The unused amount of adjusted gross DTAs related to the 21% rate differential under paragraph 11.b.i. would be taken into account under paragraph 11.c. as part of the amount of adjusted gross DTAs, after reduction for adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., that can be offset against existing gross DTLs. The same approach would be used in 20X4 and 20X5 if the Company instead qualified for the three-year applicable period under paragraph 11.b.i.

Example 2:

6.7 ABC, a company taxed as a nonlife insurance company, is projecting an income tax loss in 20X3 of $20,000,000, which includes $5,000,000 of reversing deductible temporary differences that were part of its deferred inventory at 12/31/X2. ABC expects to pay $0 federal income taxes in 20X3 as a result of its tax loss. The Company's ExDTA ACL RBC percentage is 250% and therefore, it is required to use the one-year applicable period under paragraph 11.b.i.

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20X3	Without Reversing Temporary Differences	With Reversing Temporary Differences
Taxable Income (Loss)	($15,000,000)	($15,000,000)
Reversing Temporary Differences		(5,000,000)
Taxable Income (Loss)	(15,000,000)	(20,000,000)
Tax	0	0

6.8 In 20X3, ABC expects to realize no tax benefit related to the $5,000,000 of reversing deductible temporary differences since they simply increase the amount of an NOL. Its expected income tax rate for 20X3 would be 0% and ABC would have $0 admitted adjusted gross DTAs under paragraph 11.b.i. However, if some or all of the reversing temporary differences could be absorbed in the carryback period, ABC would have an admitted adjusted gross DTA under paragraph 11.a.[35] The adjusted gross DTAs of $1,050,000 ($5,000,000 x 21%), related to ABC's reversing temporary differences, would also be available as part of its total adjusted gross DTAs, after reduction for adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., that can be offset against gross DTLs in the paragraph 11.c. calculation.

6.9 If a company qualified to utilize the three-year applicable period under paragraph 11.b.i. and within that applicable period forecasted a taxable loss in one or more of the years and taxable income in the other years, the loss may be utilized in determining the with and without calculation. This loss utilization must be within the applicable period and would be limited to the amount allowed to be carried back or carried forward under applicable tax law.

7. Q – SSAP No. 101 provides that a reporting entity may admit deferred tax assets in an amount equal to federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, including any amounts established in accordance with the provisions of SSAP No. 5R as described in paragraph 3.a. of this statement related to those periods. What is the meaning of the term "taxes paid"? [Paragraph 11.a.]

7.1 A – Under paragraph 11.a. of SSAP No. 101, the term "taxes paid" means the total tax (not including interest and penalties), that was or will be reported on the reporting entity's federal income tax returns for the applicable carryback period including any amounts established in accordance with the provision of SSAP No. 5R as described in paragraph 3.a. of SSAP No. 101 related to those periods. If a federal income tax return in the applicable carryback period has been amended, or adjusted by the IRS, "taxes paid" would reflect the impact of the amended tax return, or settlement with the IRS.

7.2 In applying the term "taxes paid" to a reporting entity that is party to a consolidated federal income tax return, the term "taxes paid" means the total federal income tax that was paid, or is expected to be paid to the common parent of the reporting entity's affiliated group, in accordance with the intercompany tax sharing agreement, with respect to the income tax years included in the applicable carryback period. "Taxes paid" includes amounts established in accordance with the provision of SSAP No. 5R as described in paragraph 3.a. of SSAP No. 101 related to those periods, including current federal income taxes payable (i.e., accrued in the entity's financial statements) related to the applicable carryback period. The ability of the reporting entity to recover (through loss or credit carrybacks) taxes that were paid to its common parent is generally governed by the terms and provisions of the affiliated group's intercompany tax sharing or tax allocation agreement.

7.3 For purposes of paragraphs 7.1 and 7.2, "taxes paid" includes both regular tax and alternative minimum tax for taxable years beginning before January 1, 2018. For taxable years beginning after

[35] For purposes of determining the amount of admitted adjusted gross DTAs under paragraph 11.a., ABC would look to the amount of existing temporary differences that reverse during a timeframe corresponding with the tax loss carryback provisions allowed by the applicable tax law, in this case 2 years, notwithstanding that it is limited to a one-year applicable period for purposes of paragraph 11.b.i.

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December 31, 2017, the applicable carryback periods are two years for ordinary losses for entities taxed as nonlife insurance companies, and three years for capital losses for entities taxed both as nonlife and life insurance companies. Entities taxed as life insurance companies are not permitted to carryback ordinary losses arising in tax years after 2017.

8. Q – How is a company's computation of adjusted gross and admitted adjusted gross deferred tax assets impacted if it joins in the filing of a consolidated federal income tax return? [paragraphs 7, 11, 12 and 16]

8.1 A – For purposes of determining the amount of DTAs and the amount admitted under paragraph 11, the calculation should be made on a separate company, reporting entity basis. Under paragraph 7, a reporting entity's gross deferred tax assets and liabilities are determined by identifying its temporary differences. These temporary differences are measured using a "balance sheet" approach by comparing statutory and tax basis balance sheets for that entity. Once a reporting entity determines its gross DTAs, they are reduced for any statutory valuation allowance adjustment that may be necessary to determine the adjusted gross DTAs. The amount of adjusted gross DTAs that are admitted is determined in accordance with paragraph 11.

8.2 Under paragraph 11.a., an entity shall determine the amount of "federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years." Such amount shall include any amounts established for tax loss contingencies in accordance with paragraph 3.a. Consistent with guidance promulgated in other EAIWG interpretations, a reporting entity that files a consolidated federal income tax return with its parent should look to the amount of taxes it paid (or were allocable to it) as a separate legal entity in determining the admitted adjusted gross DTAs under paragraph 11.a. Furthermore, the admitted adjusted gross DTAs under paragraph 11.a. may not exceed the amount that the entity could reasonably expect to have refunded by its parent (paragraph 12.c.). The taxes paid by the reporting entity represent the maximum DTAs that may be admitted under paragraph 11.a., although the amount could be reduced pursuant to the group's tax allocation agreement.

8.3 The amount of admitted adjusted gross DTAs under paragraph 11.b.i. is limited to the amount that the reporting entity expects to realize within the applicable period (refer to the 11.b.i. column of the applicable Realization Threshold Limitation Table in paragraph 11.b.) following the balance sheet date on a separate company basis. The entity must estimate its separate company taxable income and the tax benefit that it expects to receive from reversing deductible temporary differences in the form of lower tax payments to its parent. If the reporting entity has reversing adjusted gross DTAs during the applicable period for which it does not expect to realize a benefit under paragraph 11.b. on a separate company basis, the reporting entity cannot admit an amount related to such DTAs under paragraph 11,b., even though the reporting entity may be paid a tax benefit for such items pursuant to its tax allocation agreement.

8.4 The following examples reflect this analysis and assume that the surplus limitation of paragraph 11.b.ii. is not applicable:

Example 1:

8.5 Assume Company A, an entity taxed as a nonlife insurance company, joins in the filing of a consolidated federal income tax return. Consolidated taxes paid in prior carryback years total $150, of which Company A paid $100. Company A has existing temporary differences that reverse by the end of the second calendar year following the balance sheet date[36] that, on a separate company reporting entity

[36] Corresponds to the timeframe permitted by the Internal Revenue Code for carrybacks of tax losses for a nonlife insurance company. For tax years beginning after 2017, entities taxed as life insurance companies are not permitted to carry back ordinary tax losses. However, entities taxed both as life insurance and nonlife insurance companies are permitted to carry back capital losses three taxable years. Accordingly, if this example involved a capital loss, it could apply either to an entity taxed as a life insurance company or as a nonlife insurance company.

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basis and following the applicable carryback provisions of the Internal Revenue Code for each year in which temporary differences reverse, would give rise to a tax recovery of $125.

8.6 Under paragraph 11.a., Company A could record an admitted DTA of $100, equal to the taxes it paid. Due to the consolidated return filing, the $100 admitted under paragraph 11.a. could only be admitted provided this amount could reasonably be expected to be refunded by the parent [paragraph 12.c.] and would be available pursuant to a written income tax allocation agreement [paragraph 16.b.]. Additionally, assume Company A's ExDTA ACL RBC exceeds 300%, and that it expects to realize $175 from 3 years of DTA reversals, based on its separate company analysis. A 3-year period is applicable for paragraph 11.b.i., notwithstanding that only 2 years of DTA reversals may be taken int account under paragraph 11.a. due to tax limitations on operating loss carrybacks. In such case, Company A could admit an additional $75 under paragraph 11.b.i. ($175 less the $100 admitted under paragraph 11.a.).

Example 2:

8.7 Assume the same facts as in Example 1, except consolidated taxes paid in prior carryback years that could be recovered are $70 and, pursuant to a written income tax allocation agreement, taxes recoverable through loss carrybacks may not exceed consolidated taxes paid in prior carryback years.

8.8 In this situation, Company A would admit a DTA of $70 under paragraph 11.a. (recoverable taxes limited to consolidated taxes paid which could be refunded by the parent). In addition, $105 ($175-$70) of DTA may be admitted under paragraph 11.b.i., on the basis of Company A's separate company estimated taxable income and temporary differences that are expected to be realized within the applicable 3-year period following the balance sheet date.

Example 3:

8.9 Parent Company P files a consolidated federal income tax return with its nonlife insurance subsidiaries, R, S and T. Assume consolidated taxes that could be recovered through loss carryback total $450. However, in the prior carryback years $200 was paid by each of the subsidiaries, R, S and T. The difference between the amount paid by the subsidiaries ($600) and the amount available through loss carryback ($150) is attributable to interest expense incurred by Company P. Pursuant to the group's written income tax allocation agreement, in the case of loss carrybacks, taxes recoverable are limited to the consolidated taxes paid in the carryback years.

8.10 Because the adjusted gross DTA admitted under paragraph 11.a. for each reporting entity cannot exceed what each entity paid and could reasonably be expected to be refunded by P, no more than $450 in total may be admitted by the subsidiaries (under paragraph 11.a.). If the adjusted gross DTA associated with the subsidiaries' temporary differences that reverse in the 11.a. period exceed the $450 of taxes recoverable through loss carryback on a consolidated basis, the adjusted gross DTA admitted by the insurance subsidiaries under paragraph 11.a. should be allocated among the subsidiaries, consistent with the principles of its written income tax allocation agreement. This allocation would, in most instances, be based on each subsidiary's share of reversing temporary differences.

8.11 Under paragraph 11.c., an entity may admit its adjusted gross DTAs, after application of paragraphs 11.a. and 11.b., based upon offset against its own existing gross DTLs and not against gross DTLs of other members of the affiliated or consolidated group.

9a. Q – Current income taxes are defined by paragraph 3.a. to include tax loss contingencies for current and all prior years, computed in accordance with SSAP No. 5R, including the modifications in paragraphs 3.a.i, 3.a.ii. and 3.a.iii. How does the modification provided in paragraph 3.a.iii. impact the calculation of the tax contingencies recorded?

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9.1 A – Paragraph 3.a.iii. provides the following rule: If the estimated tax loss contingency is greater than 50% of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% of the original tax benefit recognized.

9.2 For example, assume that a company claimed a deduction in its current year federal income tax return that resulted in a $100 permanent tax benefit37. Management must assume that the tax position will be examined by a taxing authority that has full knowledge of all relevant information (paragraph 3.a.ii.). In addition, management has determined that the probability of a liability is more likely than not (a likelihood of more than 50% pursuant to paragraph 3.a.i.) and that the liability can be reasonably estimated. Management's best estimate of the loss of the tax benefit is $40 (an amount not greater than 50% of the tax benefit originally recognized). Under these facts, the company would establish a current tax liability in the amount of $40, increasing its current income tax expense by $40.

DR	Current income tax expense	$40	
CR	Liability for current income tax		$40

9.3 Assume the same facts as 9.2, except that management determines the best estimate of the liability to be $60 (an amount greater than 50% of the tax benefit originally recorded). Under paragraph 3.a.iii., the company would be required to record a tax contingency of $100 offsetting the entire original tax benefit recorded. Under these facts, the company would establish a current tax liability in the amount of $100, increasing its current income tax expense by $100.

DR	Current income tax expense	$100	
CR	Liability for current income tax		$100

9b. Q – What impact, if any, does the inclusion of tax contingencies as a component of current income taxes have on the determination of deferred income taxes? [Paragraph 3.c.]

9.4 A – The purpose of this interpretation is to address when such contingencies should be "grossed-up" and reflected in the calculation of both statutory current and deferred federal income taxes.

9.5 Gross deferred tax assets and liabilities are determined in accordance with paragraph 7 of SSAP No. 101 and reflect the changes in temporary differences considered in estimating taxes currently payable and are manifested in the enterprise's tax basis balance sheet. If gross tax loss contingencies associated with temporary differences have been included in taxes currently payable, a corresponding adjustment must be made to the tax basis balance sheet used in the determination of gross deferred tax assets and liabilities. Deferred tax assets and liabilities are not adjusted for tax contingencies not associated with temporary differences (i.e. permanent differences).

9.6 For example, assume that a company determines, in accordance with SSAP No. 5R, including the modifications in paragraph 3.a. of SSAP No. 101, a tax loss contingency is required to be established for a $100 deduction claimed in a prior year federal income tax return. Assuming a 21% tax rate, the company would establish a current tax liability in the amount of $21, increasing its current income tax expense by $21.

DR	Current income tax expense	$21	
CR	Liability for current income tax		$21

[37] The treatment of tax contingencies related to temporary differences is discussed in Question 9b.

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9.7 If the $100 deduction was associated with a temporary difference such as reserves, the company would make a corresponding adjustment to deferred taxes. The company would increase its gross deferred tax asset for reserves by $21 to reflect the future tax benefit associated with that reserve deduction. Any gross deferred tax asset recorded would still be subject to the admissibility requirements of paragraph 11.

DR	Gross deferred tax asset	$21	
CR	Change in net deferred tax (surplus)		$21

9.8 If the $100 deduction was associated with a permanent item such as meals and entertainment expenses, the company would make no corresponding adjustment to the deferred tax assets.

9.9 In determining the timing of when a tax loss contingency for a temporary item should be grossed up, paragraph 3.c. of SSAP No. 101 provides the following guidance:

> 3.c. In determining when tax loss contingencies associated with temporary differences should be included in current income taxes under Paragraph 3.a., and therefore included in deferred taxes under paragraph 7, a reporting entity is not required to "gross-up" its current and deferred taxes until such time as an event has occurred that would cause a re-evaluation of the contingency and its probability of assessment, e.g., the IRS has identified the item as one which may be adjusted upon audit. Such an event could be the reporting entity's (or its affiliate or parent in a consolidated income tax return) receipt of a Form 5701, Proposed Audit Adjustment, or could occur earlier upon receipt of an Information Document Request. At such time, the company must reassess the probability of an adjustment, reasonably re-estimate the amount of tax contingency as determined in accordance with paragraph 3.a., make any necessary adjustment to deferred taxes, and re-determine the admissibility of any adjusted gross deferred tax asset as provided in paragraph 11.

10a. Q – If the reporting entity adjusts the amount of regular taxable income and capital gains reported on a prior year income tax return from the amount originally determined for financial reporting purposes, how is the effect of the change reported in the current year? [Paragraph 19]

10.1 A – Paragraph 19 of SSAP No. 101 indicates that "income taxes incurred or received during the current year attributable to prior years shall be allocated, to the extent not previously provided, to net income in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* unless attributable, in whole or in part, to realized capital gains or losses, in which case, such amounts shall be apportioned between net income and realized capital gains and losses, as appropriate". Paragraph 19 also indicates that income taxes incurred are to be allocated to ordinary income and realized capital gains consistent with paragraph 38 of FAS 109. Paragraph 38 of FAS 109 provides, in general, that the portion of the total income tax expense remaining after allocation to ordinary income would be allocated to realized capital gains or losses.

10.2 In accordance with paragraph 19, the amount of additional federal income taxes incurred in the current year with respect to the prior year would be allocated between ordinary income and realized capital gain items. The amount of additional federal income tax expense allocated to ordinary income should be determined by comparing the amount of additional tax expense actually incurred to the amount of tax expense that would have been incurred had the adjustment to ordinary income been zero (a "with and without" computation). The remaining amount of additional federal income tax expense would then be allocated to realized capital gains. The amounts of additional federal income tax expense allocated to ordinary income and realized capital gains would be included in the current period's federal income tax expense and not as a direct adjustment to surplus.

10.3 As an example, assume Company X files its 20X1 federal income tax return and reports $1,000,000 of taxable income comprised of $800,000 of ordinary income and $200,000 of capital gain

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income. Since the company is subject to taxation at a 21% ~~percent~~ tax rate on all its income, it incurred federal income tax expense of $210,000. In preparing its 20X1 statutory income tax provision, the company estimated that its liability for 20X1 federal income tax would be $147,000 based on $600,000 of ordinary income and $100,000 realized capital gains.

10.4 In determining the amount of "income taxes incurred" for its 20X2 financial statement, Company X must include the additional $63,000 of income tax expense incurred on its 20X1 federal income tax return ($210,000 actual tax incurred less $147,000 originally reported) in net income for 20X2 pursuant to paragraph 19 of SSAP No. 101 and not as a surplus adjustment. The $63,000 additional expense would be allocated to federal income taxes on net income and realized capital gains and losses as follows:

Total additional income tax expense	$63,000
Tax expense allocated to operations ($200,000 additional income x 34%)	42,000
Tax expense allocated to realized gains	$21,000

The tax expense allocated to operations was determined as follows:

Total recomputed tax expense	$210,000
Tax expense with only capital gain changes	168,000
Tax expense allocated to operations	$42,000

10.5 For all purposes of computing and allocating federal income taxes between operations and capital gains and losses, the character of the income or loss item as determined for statutory accounting purposes should be followed. Thus, if an income item is treated as a capital gain for statutory accounting purposes but as ordinary income for tax purposes, the federal income tax allocable to such income would be considered tax expense attributable to capital gains.

10b. Q – What is meant by the phrase in paragraph 18 "a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL"? [Paragraph 18]

10.6 A – Pursuant to Paragraph 18 of SSAP No. 101, a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL in accordance with paragraph 35 of FAS 109. Paragraph 35 of FAS 109 indicates that income taxes incurred are to be allocated between various items, including gains from operations and items charged or credited directly to shareholders' equity, such as the change in unrealized gains and losses.

10.7 To the extent a reporting entity's admitted DTA or its DTL changes during the year, the portion of such change allocable to changes in unrealized gains and losses during the year should be determined. The portion so allocable would be reported with, and netted against, the related change in unrealized gains and losses reported as a component of changes in surplus. The remaining portion of the change in DTA or DTL allocable to other temporary differences should be reported as a separate component of changes in surplus and/or change in nonadmitted assets.

10.8 For example, assume the reporting entity has DTAs of $1,000 relating to temporary differences other than unrealized losses, and a $100 DTL relating to unrealized gains as of the beginning of the year. Since the entity is subject to tax at 21% ~~percent~~ and all of its DTAs are expected to reverse within one year, the entity recorded a $900 net admitted DTA as of the beginning of the year.

10.9 During the current year, the DTAs relating to temporary differences other than unrealized losses did not change, but the DTL relating to the entity's unrealized gains increased by $100 (unrealized gains increased by $476 during the year). As a result, the amount of the entity's net admitted DTAs decreased by $100.

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10.10 Pursuant to paragraph 18 of SSAP No. 101, the $100 decrease in the DTA during the year is to be allocated between changes attributable to temporary differences other than unrealized gains and losses and those attributable to unrealized gains and losses. Since the DTA relating to temporary differences other than unrealized gains and losses did not change during the year, the entire decrease is allocable to the change in unrealized gains. Therefore, the $100 decrease is to be allocated and netted against the $476 change in unrealized gains reported in change in surplus, resulting in a $376 net increase in surplus relating to its unrealized gains. If a portion of the unrealized loss DTA is determined to be nonadmitted, that amount is not recorded separately from the operating differences DTA. The change in the total nonadmitted DTA from period to period is recorded in surplus as a Change in Nonadmitted Assets.

11. Q – How are current and deferred income taxes to be accounted for in interim periods? [Paragraphs 12.d. and 20]

11.1 A – In setting forth the methodology for the computation of current income taxes (income taxes incurred) in interim periods, paragraph 20 states:

> 20. Income taxes incurred in interim periods shall be computed using an estimated annual effective current tax rate for the annual period in accordance with the methodology described in paragraphs 19 and 20 of *Accounting Principles Board Opinion No. 28, Interim Financial Reporting*. Estimates of the annual effective tax rate at the end of interim periods are, of necessity, based on estimates and are subject to subsequent refinement or revision. If a reliable estimate cannot be made, the actual effective tax rate for the year-to-date may be the best estimate of the annual effective tax rate. If an insurer is unable to estimate a part of its "ordinary" income (or loss) or the related tax (or benefit) but is otherwise able to make a reliable estimate, the tax (or benefit) applicable to the item that cannot be estimated shall be reported in the interim period in which the item is reported.

11.2 As a result, to the extent a reliable estimate can be made of an expected annual effective tax rate, reporting entities should apply this rate to net income before federal and foreign income taxes, in the case of property and casualty insurers and health insurers, and net income and realized capital gains before federal and foreign income taxes in the case of life insurers. If a reliable estimate of the expected annual effective tax rate cannot be made, reporting entities should compute current and deferred taxes at interim reporting dates using the most reliable information that is available.

11.3 The following examples illustrate the estimation process for income taxes incurred using the estimated annual effective rate:

Projected statutory net income[38] for current year		$10,000,000
Estimated annual permanent differences		(2,800,000)
Estimated annual temporary differences:		2,000,000
Projected taxable income for current year		$9,200,000
Projected federal tax for current year (at 21%)		$1,932,000
Estimated annual effective tax rate		19.322%

[38] For all examples in Question 11, statutory net income represents operating and capital gain income before federal and foreign income taxes.

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11.4 As a result, assuming that during the calendar year the reporting entity's expectations as to its statutory and taxable income do not change, income tax incurred will be recorded on a quarterly basis as follows:

Quarter	Statutory Income (Loss)	Income Taxes Incurred
1	$(2,000,000)	$(386,400)
2	4,000,000	772,800
3	6,000,000	1,159,200
4	2,000,000	386,400
Total	$10,000,000	$1,932,000

11.5 If the reporting entity's expectations as to its statutory and taxable income change in the second quarter so that it expects that its annual effective rate will increase from 19.32% to 20%, it will record income taxes incurred in the second quarter of $786,400 (cumulative statutory income at end of the second quarter of $2,000,000 at 20% or $400,000 less $386,400 tax benefit recorded in first quarter).

11.6 As noted above, life insurers must estimate their annual effective tax rate and record income taxes incurred based on net income and realized capital gains before federal and foreign income taxes. With regard to intraperiod tax allocation, paragraph 19 states in relevant part:

> 19. Income taxes incurred shall be allocated to net income and realized capital gains or losses in a manner consistent with paragraph 38 of FAS 109.

11.7 As a result of the above and where the reporting entity expects realized capital gains or losses for the annual period, income taxes incurred must be allocated using a "with and without" methodology to net income before taxes and realized capital gains (see Question 10.4 for further discussion).

11.8 An example of this "with and without" methodology is as follows:

Projected statutory net income for current year		$10,000,000
Realized gains included above		(1,000,000)
		9,000,000
Estimated annual permanent differences:		(2,800,000)
Estimated annual temporary differences:		2,000,000
Projected ordinary taxable income for current year		$8,200,000
Projected ordinary federal tax for current year (at 21%)		$1,722,000
Projected capital gain federal tax for current year (at 21%)		210,000
Projected total federal tax for current year		$1,932,000
Estimated ordinary annual effective tax rate ($1,722,000 / $9,000,000)		19.13%
Estimated capital gain annual effective tax rate ($210,000 / $1,000,000)		21.0%
Estimated total annual effective tax rate ($1,932,000 / $10,000,000)		19.32%

11.9 As a result, assuming that during the calendar year the reporting entity's expectations as to its statutory and taxable income (including the amounts of ordinary and capital income) do not change, income tax incurred will be recorded on a quarterly basis as follows:

Quarter	Ordinary Income (Loss)	Capital Income (Loss)	Ordinary Taxes Incurred	Capital Taxes Incurred
1	$(1,000,000)	$(1,000,000)	$(191,333)	$(210,000)
2	3,000,000	1,000,000	573,999	210,000
3	5,000,000	1,000,000	956,667	210,000
4	2,000,000	0	383,667	0
Total	$9,000,000	$1,000,000	$1,722,000	$210,000

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11.10 With respect to the recording of deferred taxes on an interim basis paragraph 12.d. states:

> 12.d. The phrases "reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years," "realized within one year of the balance sheet date" and "realized within three years of the balance sheet date" are intended to accommodate interim reporting dates and reporting entities that file on an other than calendar year basis for federal income tax purposes.

11.11 When considered in the context of paragraph 20, this paragraph requires the use of the annual effective rate when determining deferred taxes at an interim reporting date. As such, a reporting entity's admitted adjusted gross DTAs are determined in accordance with paragraph 11 by reference to the adjusted gross DTAs that will reverse each year in the applicable period. Note however, that due to the inherent unpredictability, and general inability to project changes in capital gains and losses on a quarter by quarter basis, the deferred tax implications of the changes in unrealized gains and losses should be recorded on a discrete period basis (i.e., based on the change in the amounts on a quarter by quarter basis). For example, in determining its admitted adjusted gross DTAs at March 31, 20X2, the reversal period referred to above is calendar years 20X3, 20X4 and 20X5 (i.e., expected adjusted gross DTAs at December 31, 20X2 that are expected to reverse in 20X3, 20X4 and 20X5).

11.12 This methodology is illustrated by the following example:

In this example, XYZ Co. is a nonlife insurance company[39] that has a two-year carryback potential and also has an ExDTA ACL RBC percentage of 700%.

Projected statutory net income for 20X3		$10,000,000
Estimated annual permanent differences:		(2,800,000)
Estimated annual temporary differences:		2,000,000
Projected ordinary taxable income for current year		$9,200,000
Temporary differences at December 31, 20X2:		$5,000,000
Estimated temporary differences at December 31, 20X3:		$7,000,000
Taxable income in carryback period (taxes paid at 21%):		
Year ended December 31, 20X1	2,000,000	(420,000)
Year ended December 31, 20X2	3,000,000	(630,000)
Year ended December 31, 20X3	$9,200,000	($1,932,000)

Note: Year ended December 31, 20X3 taxable income and taxes paid considered in the calculation of its interim tax accruals are based on the reporting entity's estimate of its annual taxable income and taxes to be paid. This amount may differ from the quarterly federal income tax estimates it expects to make during the year.

	Reversing Period		
	20X3	**20X4**	**20X5**
December 31, 20X2 Temporary difference reversals:	$2,000,000	$1,500,000	$1,500,000
	20X4	20X5	20X6
December 31, 20X3 Temporary difference reversals:	$3,000,000	$2,000,000	$2,000,000

[39] Please note the results in this example could be different if XYZ Co. was a life insurance company because, under current Federal income tax law, life insurance companies are not permitted to carry back net operating losses. In such case, XYZ would not admit any deferred tax assets under paragraph 11.a. However, if XYZ were able to admit deferred tax assets for all of its 20X3-20X5 temporary difference reversals at December 31, 20X2 and for all of its 20X4-20X6 temporary difference reversals at December 31, 20X3 under paragraph 11.b. (based on adequate sources of projected taxable income in those reversal periods), then the results in this example would be unchanged.

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Admitted deferred tax assets at December 31, 20X2:				
	Paragraph 11.a.			
		20X1	$2,000,000	
		20X2	1,500,000	
			3,500,000	
		Taxes paid at 21%		$735,000
	Paragraph 11.b.			315,000
	Paragraph 11.c.			0
	Total admitted			$1,050,000
Note: The recovery of federal income taxes paid in prior years under paragraph 11.a. is calculated in this example by carrying back 20X3's temporary difference reversals of $2,000,000 to offset 20X1's taxable income of $2,000,000; then carrying back 20X4's temporary difference reversals of $1,500,000 to offset $1,500,000 of 20X2's taxable income of $3,000,000 XYZ's projected taxable income for 20X3 ($9,200,000) is more than adequate to allow the remaining $315,000 of the $1,050,000 expected to be realized from temporary difference reversals in 20X3-20X5 ($5,000,000 x 21% = $1,050,000) to be recognized under paragraph 11.b.				
Admitted deferred tax assets at December 31, 20X3:				
	Paragraph 11.a.			
		20X2	$3,000,000	
		20X3	2,000,000	
			5,000,000	
		Taxes paid at 21%		$1,050,000
	Paragraph 11.b.			420,000
	Paragraph 11.c.			0
	Total admitted			$1,470,000
Note: The recovery of federal income taxes paid in prior years under paragraph 11.a. is calculated in this example by carrying back 20X4's temporary difference reversals of $3,000,000 to offset 20X2's taxable income of $3,000,000; then carrying back 20X5's temporary difference reversals of $2,000,00 to offset $2,000,000 of 20X3's taxable income. It is assumed for this example that XYZ has more than adequate amounts of projected income for 20X4-20X6 to allow the remaining $420,000 of the $1,470,000 expected to be realized from temporary difference reversals in 20X4-20X6 ($7,000,000 x 21% = $1,470,000) to be recognized under paragraph 11.b.				
Total estimated federal taxes for 20X3:				
	Income taxes incurred (current tax) ($9,200,000 X 21%)			$1,932,000
	Change in deferred tax ($1,050,000 – $1,470,000)			(420,000)
				$1,512,000

11.13 As a result of the above, the annual effective tax rate for current and deferred income taxes is as follows:

Current ($3,220,000/$10,000,000)	19.32%
Deferred (($700,000)/$10,000,000)	(4.2)%
Total annual effective rate	15.12%

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Quarter	Statutory Income (Loss)	Income Taxes Incurred	Deferred Taxes
1	$(2,000,000)	$(386,400)	$84,000
2	4,000,000	772,800	(168,000)
3	6,000,000	1,159,200	(252,000)
4	2,000,000	386,400	(84,000)
Total	$10,000,000	$1,932,000	$(420,000)

11.14 To the extent that a reporting entity's estimated year end[40] admitted adjusted gross deferred tax assets are limited by its surplus pursuant to paragraph 11.b.ii., the annual effective deferred tax rate must be adjusted to consider the impact of this limitation on a quarterly basis.

12. Q – How do you present deferred taxes in the Annual Statement? [Paragraphs 8, 18, 21-28 and 36]

12.1 A – This answer is divided into three different parts.

Unrealized Capital Gains and Losses

12.2 SSAP No. 101 paragraph 18 states:

> 14. In accordance with paragraph 35 of FAS 109, a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL. The amount allocated shall be computed in a manner consistent with paragraph 38 of FAS 109.

12.3 The following illustrates the presentation of such requirement in the annual statement:

Illustration A Assumptions:

12.4 Entity grouped its investments in a reasonable and consistent manner and calculated the following gross amounts attributable to appreciation and depreciation in the fair value of its common stocks during 20X2 (see question 2 regarding grouping of assets and liabilities for measurement):

	Gross	Carrying Value	Rate	Tax Effected DTA (DTL)
Common stock carrying value 1/1/X2		$800,000		
Unrealized (loss)	($714,286)		21%	$150,000
Unrealized gain	571,429		21%	(120,000)
Net (loss) gain		(142,857)		$30,000
Common stock carrying value 12/31/X2		$657,143		

12.5 The journal entries need to present unrealized losses and gains net of tax are:

12/31/X2	DR	Change in unrealized capital gains and losses	$142,857
	CR	Common stock	($142,857)
	Recognition of net depreciation in FV of common stock		

12/31/X2	DR	Deferred tax asset	$150,000
	CR	Deferred tax liability	($120,000)
	CR	Change in deferred income taxes	($30,000)
	Recognition of gross deferred tax amounts		

[40] In the previous example, year-end is December 31, 20X3.

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12/31/X2	DR	Change in deferred income taxes	$30,000
	CR	Change in unrealized capital gains and losses	($30,000)
	Reclass tax effect of net unrealized loss per paragraph 18 of SSAP No. 101		

12.6 Condensed 12/31/X2 Balance Sheet:

ASSETS	20X2	20X1	LIABILITIES, SURPLUS AND OTHER FUNDS	20X2	20X1
Common Stock	$657,143	$800,000	Surplus:		
Net deferred tax asset	30,000		Beginning of year	$800,000	
			Change in UNL	(112,857)[41]	
Total Assets	$687,143	$800,000	**Liabilities & Surplus**	$687,143	$800,000

Annual Statement Presentation

12.7 In accordance with SSAP No. 101, DTAs and DTLs shall be offset and presented as a single amount on the statement of financial position. The following illustrates this requirement:

Illustration B Assumptions:

12.8 The entity had the following balances:

	1/1/X2	12/31/X2	Change
Gross DTA	$200,000	$510,000	$310,000
Statutory Valuation Allowance Adjustment	0	10,000	10,000
Adjusted Gross DTA	200,000	500,000	300,000[42]
DTA Nonadmitted	25,000	150,000	125,000
Admitted Adjusted Gross DTA	175,000	350,000	175,000
Gross DTL	100,000	200,000	100,000
Net Admitted Adjusted Gross DTA	$75,000	$150,000	$75,000
Current FIT Recoverable	**$18,000**	**$20,000**	**$2,000**

12.9 Illustrative 12/31/X2 Balance Sheet for Illustration B:

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
Current Federal and foreign income tax recoverable and interest thereon	$20,000	$0	$20,000	$18,000
Net deferred tax asset	$300,000	$150,000	$150,000	$75,000

[41] Computed at $142,857 (total change in UNG/UNL) - $30,000 tax effect.

[42] Includes $30,000 resulting from net unrealized losses as shown in Illustration A. As such the change in net deferred income taxes at 12/31/X2 is $170,000 ($300,000 (gross change in DTA) – $100,000 (gross change in DTL) – $30,000 reclass to net unrealized capital gains (losses)).

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12.10 Illustrative 12/31/X2 Income Statement for Illustration B:

STATEMENT OF INCOME (P/C) SUMMARY OF OPERATIONS (Life & Health) STATEMENT OF REVENUES AND EXPENSES (Health)	1 Current Year	2 Prior Year
Gains and (losses) in surplus		
Change in net unrealized capital gains (losses) less capital gains tax of $30,000	$112,857	0
Change in net deferred income tax	$170,000	0
Change in nonadmitted assets	($125,000)	0

12.11 Illustrative 12/31/X2 Exhibit of Nonadmitted Assets for Illustration B:

	1 End of Current Year	2 End of Prior Year	3 Changes for Year (Increase) Decrease
Net deferred tax asset	$150,000	$25,000	($125,000)
Total	$150,000	$25,000	($125,000)

Illustration C Assumptions:

12.12 The entity had the following balances (1/1/X2 balances carried forward from Illustration B):

	1/1/X2	**12/31/X2**	**Change**
Gross DTA	$200,000	$510,000	$310,000
Statutory Valuation Allowance Adjustment	0	10,000	10,000
Adjusted Gross DTA	200,000	500,000	300,000[43]
DTA Nonadmitted	25,000	150,000	125,000
Net Admitted Adjusted Gross DTA	175,000	350,000	175,000
Gross DTL	100,000	200,000	100,000
Net Admitted Adjusted Gross DTA	$75,000	$150,000	$75,000
Current FIT Liability	**$7,000**	**$12,000**	**$5,000**

12.13 Illustrative 12/31/X2 Balance Sheet for Illustration C:

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
Net deferred tax asset	$300,000	$150,000	$150,000	75,000

LIABILITIES, SURPLUS AND OTHER FUNDS	1 Current Year	2 Prior Year
Current Federal and foreign income taxes (including $0 on realized capital gains (Losses))	$12,000	$7,000

[43] Includes $30,000 resulting from net unrealized losses as shown in Illustration A. As such the change in net deferred income taxes at 12/31/X2 is $170,000 ($300,000 (gross change in DTA) – $100,000 (gross change in DTL) – $30,000 reclass to net unrealized capital gains (losses)).

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12.14 Illustrative 12/31/X2 Income Statement for Illustration C:

STATEMENT OF INCOME (P/C) **SUMMARY OF OPERATIONS (Life & Health)** **STATEMENT OF REVENUES AND EXPENSES (Health)**	1 Current Year	2 Prior Year
Gains and (losses) in surplus		
Change in net unrealized capital gains (losses) less capital gains tax of $30,000	$112,857	0
Change in net deferred income tax	$170,000	0
Change in nonadmitted assets	($125,000)	0

12.15 Illustrative 12/31/X2 Exhibit of Nonadmitted Assets for Illustration C:

	1 End of Current Year	2 End of Prior Year	3 Changes for Year (Increase) Decrease
Net deferred tax asset	$150,000	$25,000	($125,000)
Total	$150,000	$25,000	($125,000)

Notes to the Financial Statements Disclosures:

12.16 SSAP No. 101 paragraphs 21-28 include extensive disclosure requirements. Although some of these amounts are presented on the face of the financial statements or in schedules or exhibits to the annual statement, they will be included in the Notes to the Financial Statements both in the annual statement and in the annual audited financial statements.

12.17 This section provides specific examples that illustrate the disclosures required in SSAP No. 101. The formats in the illustrations are not requirements. Some of the disclosure paragraphs of SSAP No. 101 are not specific as to whether the entity should disclose the nature of certain items or whether the entity should disclose specific amounts. The illustrations included herein use a combination of each method. The NAIC encourages a format that provides the information in the most understandable manner in the specific circumstances. The following illustrations are for a single hypothetical insurance enterprise, referred to as AlphaBeta Property & Casualty Insurance Company. All of the disclosures would be completed in the year-end annual statement and audited statutory financial statements.

12.18 Selected AlphaBeta P/C Company Financial Data at December 31, 20X2 (Balance Sheet information carried forward from Illustration B):

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
Current federal and foreign income tax recoverable and interest thereon	$20,000	$0	$20,000	$18,000
Net deferred tax asset	$300,000	$150,000	$150,000	$75,000

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CAPITAL AND SURPLUS ACCOUNT	1 Current Year	2 Prior Year
Change in net unrealized capital gains (losses) less capital gains tax of $30,000	($112,857)	0
Change in net deferred income tax	$170,000	0
Change in nonadmitted assets	($125,000)	0

EXHIBIT OF NONADMITTED ASSETS	1 End of Current Year	2 End of Prior Year	3 Changes for Year (Increase) Decrease
Net deferred tax asset	$150,000	$25,000	($125,000)

STATEMENT OF INCOME	20X2
UNDERWRITING INCOME	
Premiums earned	$5,250,000
DEDUCTIONS:	
Losses incurred	3,550,000
Loss adjustment expenses incurred	1,750,000
Other underwriting expenses incurred	525,000
Net underwriting gain (loss)	(575,000)
INVESTMENT INCOME	
Net investment gain (loss)	1,350,000
OTHER INCOME	
Total other income	125,000
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	900,000
Dividends to policyholders	200,000
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	700,000
Federal and foreign income taxes incurred	220,000
Net income	$480,000

Paragraph 22 Illustration:

12.19 The components of the net DTA recognized in the Company's Assets, Liabilities, Surplus and Other Funds are as follows:

	12/31/20X2			12/31/20X1			Change		
	Ordinary	Capital	Total	Ordinary	Capital	Total	Ordinary	Capital	Total
Gross Deferred Tax Assets	$375,000	$135,000	$510,000	$93,000	$107,000	$200,000	$282,000	$28,000	$310,000
Statutory Valuation Allowance Adjustments	0	10,000	10,000	0	0	0	0	10,000	10,000
Adjusted Gross Deferred Tax Assets	375,000	125,000	500,000	93,000	107,000	200,000	282,000	18,000	300,000
Deferred Tax Assets Nonadmitted	150,000	0	150,000	20,000	5,000	25,000	130,000	(5,000)	125,000
Subtotal Net Admitted Deferred Tax Asset	225,000	125,000	350,000	73,000	102,000	175,000	152,000	23,000	175,000
Deferred Tax Liabilities	21,000	179,000	200,000	15,000	85,000	100,000	6,000	94,000	100,000
Net Admitted Deferred Tax Asset/(Net Deferred Tax Liability)	$204,000	($54,000)	$150,000	$58,000	$17,000	$75,000	$146,000	($71,000)	$75,000
Admission Calculation Components SSAP No. 101 (Paragraph 11)									

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	12/31/20X2			12/31/20X1			Change		
	Ordinary	Capital	Total	Ordinary	Capital	Total	Ordinary	Capital	Total
a. Federal Income Taxes Paid In Prior Years Recoverable Through Loss Carrybacks.	$85,000	$5,000	$90,000	$45,000	$5,000	$50,000	$40,000	0	$40,000
b. Adjusted Gross Deferred Tax Assets Expected To Be Realized (Excluding The Amount Of Deferred Tax Assets From a, above) After Application of the Threshold Limitation. (The Lesser of b.i. and b.ii. Below)	50,000	10,000	60,000	13,000	12,000	25,000	37,000	(2,000)	35,000
i. Adjusted Gross Deferred Tax Assets Expected to be Realized Following the Balance Sheet Date.	**NA**	**NA**	**60,000**	**NA**	**NA**	**25,000**	**NA**	**NA**	**35,000**
ii. Adjusted Gross Deferred Tax Assets Allowed per Limitation Threshold.	**NA**	**NA**	**900,000**	**NA**	**NA**	**750,000**	**NA**	**NA**	**150,000**
c. Adjusted Gross Deferred Tax Assets (Excluding the Amount Of Deferred Tax Assets From a. and b. above) Offset by Gross Deferred Tax Liabilities.	90,000	110,000	200,000	15,000	85,000	100,000	75,000	25,000	100,000
Deferred Tax Assets Admitted as the result of application of SSAP No. 101.Total (a. + b. + c.)	$225,000	$125,000	$350,000	$73,000	$102,000	$175,000	$152,000	$23,000	$175,000

	20X2 Percentage	20X1 Percentage
Ratio Percentage Used to Determine Recovery Period and Threshold Limitation Amount[44]	600%	500%
Amount of Adjusted Capital and Surplus Used to Determine Recovery Period And Threshold Limitation[45]	$6,000,000	$5,000,000

The Company's tax-planning strategies include the use of reinsurance-related tax-planning strategies.

Impact of Tax Planning Strategies	12/31/20X2			12/31/20X1			Change		
	Ordinary Percent	Capital Percent	Total Percent[46]	Ordinary Percent	Capital Percent	Total Percent	Ordinary Percent	Capital Percent	Total Percent
Adjusted Gross DTAs (% of Total Adjusted Gross DTAs)	6%	7%	13%	7%	7%	14%	-1%	0%	-1%
Net Admitted Adjusted Gross DTAs (% of Total Net Admitted Adjusted Gross DTAs)	14%	15%	29%	15%	15%	30%	-1%	0%	-1%

Paragraph 23 Illustration:

12.20 The Company has not recognized a deferred tax liability of approximately $30,000 of foreign withholding taxes for the undistributed earnings of its 100% ~~percent~~ owned foreign subsidiaries that arose in 20X2 and prior years because the Company does not expect those unremitted earnings to

[44] Disclose the ratio used by the reporting entity from the applicable Realization Threshold Limitation Table in paragraph 11.b. of SSAP No. 101 to determine the appropriate limitations of paragraph 11.b. In the event that late immaterial modifications to a reporting entity's statutory financial statements occur subsequent to initial completion of the statutory financial statements but prior to filing or similar deadline, these immaterial changes do not need to be reflected in this ratio if such modifications do not cause the reporting entity to change the threshold limitation from the applicable Realization Threshold Limitation Table.

[45] Provide the amount of adjusted capital and surplus used to calculate the limitation under paragraph 11.b.ii.

[46] The total percentage should be separately calculated and is not intended to be a summation of the percentages by tax character.

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reverse and become taxable to the Company in the foreseeable future. A deferred tax liability will be recognized when the Company expects that it will recover those undistributed earnings in a taxable manner, such as through receipt of dividends or sale of the investments. As of December 31, 20X2, the undistributed earnings of these subsidiaries were approximately $200,000.

Paragraph 24 Illustration:

12.21 The provisions for incurred taxes on earnings for the years ended December 31 are:

	20X2	20X1
Federal	$180,000	$135,000
Foreign	40,000	15,000
	220,000	150,000
Federal income tax on net capital gains	52,000	36,000
Utilization of capital loss carry-forwards	(52,000)	(36,000)
Federal and foreign income taxes incurred	$220,000	$150,000

12.22 The tax effects of temporary differences that give rise to significant[47] portions of the deferred tax assets and deferred tax liabilities are as follows:

	12/31/20X2	12/31/20X1	Change
Deferred Tax Assets:			
Ordinary			
Discounting of unpaid losses	30,000	10,000	20,000
Unearned premium reserve	235,000	50,000	185,000
Investments	25,000	15,000	10,000
Pension accrual	65,000	15,000	50,000
Other (including items <5% of total ordinary tax assets)	20,000	3,000	17,000
Subtotal	375,000	93,000	282,000
Statutory valuation allowance adjustment	0	0	0
Nonadmitted	150,000	20,000	130,000
Admitted ordinary deferred tax assets	225,000	73,000	152,000
Capital			
Investments	125,000	45,000	80,000
Net capital loss carry-forward	10,000	62,000	(52,000)
Other (including items <5% of total capital tax assets)	0	0	0
Subtotal	135,000	107,000	28,000
Statutory valuation allowance adjustment	10,000	0	10,000
Nonadmitted	0	5,000	(5,000)
Admitted capital deferred tax assets	125,000	102,000	23,000
Admitted deferred tax assets	350,000	175,000	175,000
Deferred Tax Liabilities:			
Ordinary			
Investments	10,000	5,000	5,000
Fixed assets	6,000	5,000	1,000
Other (including items <5% of total ordinary tax liabilities)	5,000	5,000	0
Subtotal	21,000	15,000	6,000

[47] Significant is defined as any amount in excess of 5% of the total applicable DTAs or DTLs.

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Capital:			
Investments	110,000	55,000	55,000
Real estate	64,000	25,000	39,000
Other (including items <5% of total capital tax liabilities)	5,000	5,000	
Subtotal	179,000	85,000	94,000
Deferred tax liabilities	200,000	100,000	100,000
Net deferred tax assets/liabilities	150,000	75,000	75,000

12.23 The change in net deferred income taxes is comprised of the following (this analysis is exclusive of nonadmitted assets as the Change in Nonadmitted Assets is reported separately from the Change in Net Deferred Income Taxes in the surplus section of the annual statement):

	Dec. 31, 20X2	Dec. 31, 20X1	Change
Adjusted gross deferred tax assets	$500,000	$200,000	$300,000
Total deferred tax liabilities	200,000	100,000	100,000
Net deferred tax assets (liabilities)	$300,000	$100,000	200,000
Tax effect of unrealized gains (losses)			(30,000)
Change in net deferred income tax			$170,000

Paragraph 25 Illustration[48]:

12.24 The provision for federal and foreign income taxes incurred is different from that which would be obtained by applying the statutory Federal income tax rate to income before income taxes. The significant items causing this difference are as follows:

	Dec. 31, 20X2	Effective Tax Rate
Provision computed at statutory rate	$147,000	21.0%
Tax exempt income deduction	(61,000)	(8.7)
Dividends received deduction	(50,000)	(7.1)
Tax differentials on foreign earnings	(21,000)	(3.0)
Change in statutory valuation allowance adjustment	10,000	1.4
Nondeductible goodwill	8,000	1.1
Other	7,000	2.4
Total	$50,000	7.1%
Federal and foreign income taxes incurred	$220,000	31.4%
Change in net deferred income taxes[49]	(170,000)	(24.3)
Total statutory income taxes	$50,000	7.1%

Paragraph 26 Illustration:

12.25 The Company has net capital loss carryforwards which expire as follows: 20X5, $9,000; 20X6; $1,000.

[48] This illustration includes both the rate reconciliation and the tax effected amounts although only one of these is required to be disclosed under SSAP No. 101.

[49] As reported in the surplus section of the annual statement. The change in net deferred income taxes is before nonadmission of any DTA. The change in nonadmitted DTA is reported together with the total change in nonadmitted assets and presented as a separate component of surplus.

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Paragraph 27 Illustration:

12.26 The Company believes it is reasonably possible that the liability related to any federal or foreign tax loss contingencies may significantly increase within the next 12 months. However, an estimate of the reasonably possible increase cannot be made at this time.

Paragraph 28 Illustration:

12.27 The Company is included in a consolidated federal income tax return with its parent company, Alpha Corporation. The Company has a written agreement, approved by the Company's Board of Directors, which sets forth the manner in which the total combined federal income tax is allocated to each entity which is a party to the consolidation. Pursuant to this agreement, the Company has the enforceable right to recoup federal income taxes paid in prior years in the event of future net losses, which it may incur, or to recoup its net losses carried forward as an offset to future net income subject to federal income taxes.

13. Q – How are tax-planning strategies to be considered in determining adjusted gross DTAs [Paragraph 7.e.] and admitted adjusted gross DTAs [Paragraphs 11.a., 11.b.i., 14 and 15]?

Overview:

13.1 A – Paragraph 14 of SSAP No. 101 states:

> In some circumstances, there are tax-planning strategies (including elections for tax purposes) that (a) are prudent and feasible, (b) a reporting entity ordinarily might not take, but would take to prevent an operating loss or tax credit carryforward from expiring unused, and (c) would result in realization of deferred tax assets. A reporting entity shall consider tax-planning strategies in (1) determining the amount of the statutory valuation allowance adjustment necessary under paragraph 7.e. and (2) the realization of deferred tax assets when determining admission under paragraph 11…

13.2 Paragraph 248 of FAS 109 additionally states that:

> Tax-planning strategies also may shift the estimated pattern and timing of future reversals of temporary differences. A tax-planning strategy to accelerate the reversal of deductible temporary differences in time to offset taxable income that is expected in an early future year might be the only means to realize a tax benefit for those deductible temporary differences if they otherwise would reverse and provide no tax benefit in some later future year(s).

13.3 As also provided in paragraph 14 of SSAP No. 101, if a tax-planning strategy is used to accelerate the reversal or realization of an item, any significant net-of-tax potential costs or losses associated with the implementation of the strategy should reduce the adjusted gross or admitted DTA.

13.4 When considering a prudent and feasible tax-planning strategy that is more likely than not to enable realization of all or part of an adjusted gross DTA or admitted DTA, paragraph 15 of SSAP No. 101 states that "paragraph 3 of this statement related to tax loss contingencies shall be applied in determining admissibility of deferred tax assets under paragraph 11 of this statement." Accordingly, a reporting entity must evaluate the likelihood, if a tax-planning strategy were implemented, of whether a tax loss contingency would be required to be recorded under paragraph 3.a. If so, the admitted tax benefit of a tax-planning strategy must be reduced by the amount of tax loss contingency so required. For example, if a tax-planning strategy provided a $100 admitted DTA, but the reporting entity estimated that a tax loss contingency reserve of $40 would be required if the strategy was implemented, the admitted DTA resulting from the tax-planning strategy would be reduced by $40. Since the admitted DTA would be net of any applicable tax loss contingencies, no separate tax loss contingencies would actually be recorded for these items.

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Statutory Valuation Allowance Adjustment:

13.5 As discussed in Question 2.5, future realization of gross DTAs ultimately depends on the existence of sufficient taxable income of the appropriate character within the carryback or carryforward period available under the tax law. In determining adjusted gross DTAs, a reporting entity shall consider the four sources of taxable income that may be available under the tax law, one of which is tax-planning strategies[50]. As noted in paragraph 13 of SSAP No. 101, a reporting entity is not required to consider all four sources of taxable income if one or more sources are alone sufficient to support the conclusion that the entity will realize the tax benefits of its adjusted gross DTAs (i.e., a conclusion that no statutory valuation allowance is necessary). Accordingly, tax-planning strategies need not be considered if the other sources of taxable income are sufficient to realize the benefits of reversing existing DTAs. However, the reporting entity is required to consider the impact of tax planning strategies to determine the amount of the adjustment if a conclusion is reached that a statutory valuation allowance adjustment is necessary.

Tax-Planning Strategies for Admission of DTAs:

13.6 In order for a tax-planning strategy to support admission of adjusted gross DTAs under paragraph 11, the reporting entity must demonstrate that (1) the admitted DTAs would be realized either within a period that would give rise to a carryback of tax losses under the Internal Revenue Code, not to exceed three years (for admission under paragraph 11.a.), or within the applicable period (refer to the 11.b.i. column of the applicable Realization Threshold Limitation Table in paragraph 11) and (2) it would have the ability to implement the strategy. In such circumstances an entity may recognize, as admitted assets, the related DTAs that are realizable as a result of the available tax-planning strategy in accordance with paragraphs 11.a., 11.b.i. and 11.c. of SSAP No. 101. Using tax-planning strategies in determining the admissible DTA is analogous to the use of tax-planning strategies in determining the amount of the statutory valuation allowance adjustment required under paragraph 7.e. of SSAP No. 101 and paragraph 22 of FAS 109. Although a reporting entity may use tax-planning strategies in determining the portion of its adjusted gross DTAs that are admissible, it is not required to do so.

13.7 The requirement in paragraph 11.a. and 11.b.i. of SSAP No. 101 to consider only those DTAs that reverse or are realized within a period that would give rise to a carryback of losses under the Internal Revenue Code not to exceed three years (paragraph 11.a.) or within the applicable period following the balance sheet date (paragraph 11.b.i.) causes those DTAs which would otherwise reverse beyond such period to potentially provide no tax benefit (unless admitted under paragraph 11.c.). The potential reversal beyond the appropriate period is comparable to an expiring operating loss or tax credit carryforward, in that the deduction would not provide a tax benefit under SSAP No. 101. Thus, to the extent prudent and feasible tax-planning strategies exist to accelerate the reversal or realization of these DTAs, these strategies are comparable to those contemplated in paragraph 248 of FAS 109 above.

13.8 An example of a prudent and feasible tax-planning strategy is as follows:

13.9 Company A, a property/casualty insurance company for federal income tax purposes, has paid federal income taxes of $500,000 in each of calendar years 20X1 and 20X2. The company has an ExDTA ACL RBC percentage of 250% and, therefore, is required to use the one-year applicable period under paragraph 11.b.i. of SSAP No. 101. It has capital and surplus for purposes of paragraph 11.b.ii. of SSAP No. 101 of $20,000,000. Company A has an obligation to provide post-retirement health benefits to its employees. At December 31, 20X2, Company A has included a liability for $1,000,000 on its statutory- basis financial statements for post-retirement health benefits. This liability is not currently deductible for federal income tax purposes, and only $25,000 reverses within each of the next two calendar years. This is Company A's only DTA under SSAP No. 101, and there are no DTLs. Company

[50] See paragraph 13 of SSAP No. 101 and paragraph 21 of FAS 109. Examples of tax-planning strategies as provided in paragraph 13.d. are (1) accelerate taxable amounts to utilize expiring carryforward, (2) change the character of taxable or deductible amounts from ordinary income or loss to capital gain or loss, and (3) switch from tax-exempt to taxable investments.

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A, absent any tax- planning strategies, would compute a DTA of $210,000 ($1,000,000 X 21%), and would admit $10,500 ($50,000 X 21%) under paragraph 11.a., and has no additional admitted DTA under paragraph 11.b.

13.10 Company A could implement a welfare benefit fund for tax purposes and contribute assets to the fund to cover qualifying welfare benefits. The contribution, subject to limitations, would be deductible for federal income tax purposes, and would have the effect of accelerating the deduction for Company A's post-retirement health benefits. Company A has computed that $300,000 could be contributed during 20X3 to the welfare benefit fund, and to implement this strategy, it would cost $15,000 on an after-tax basis. Company A management believe that this strategy is prudent and feasible, and the Company would be able to implement this strategy if necessary. Company A would be able to admit an additional $48,000 of DTAs ($300,000 X 21%, or $63,000, less $15,000 in costs) under paragraph 11.a., with no additional admitted DTA under paragraph 11.b.

13.11 A tax-planning strategy would not be considered prudent or feasible if use of the strategy would be inconsistent with assumptions inherent in statutory or other accounting basis financial statements. For instance, a tax-planning strategy to sell securities identified as "held to maturity" for GAAP-basis financial statements at a loss would not be prudent or feasible. Additionally, if a potential tax planning strategy were to involve selling debt securities at a loss, it would not be prudent or feasible if the securities had not been identified as impaired and the loss recognized for statutory-basis financial statements. Additionally, a tax-planning strategy that could not be implemented to realize a tax benefit within the requisite period following the balance sheet date or is inconsistent with management's business plan objectives would not be prudent and/or feasible.

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Statement of Statutory Accounting Principles No. 102

Pensions

STATUS

Type of Issue	Common Area
Issued	Finalized March 3, 2012
Effective Date	January 1, 2013
Affects	Supersedes SSAP No. 89; Nullifies INT 99-26, INT 01-16, INT 03-18, INT 04-03, INT 04-12 and INT 13-03
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **2**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles and related reporting for employers' pension obligations.

2. This statement establishes financial accounting and reporting standards for an insurer that offers pension benefits to its employees. Ordinarily, such benefits are periodic pension payments to retired employees or their survivors, but they may also include benefits payable as a single lump sum and other types of benefits, such as death benefits provided through a pension plan. (This statement does not apply to life insurance benefits provided outside a pension plan or postretirement health and welfare benefits.) Arrangements to provide pension benefits may take a variety of forms and may be financed in different ways. This statement applies to any arrangement that is similar in substance to a pension plan regardless of form or financing. This statement applies to a written plan and to a plan whose existence may be implied from a well-defined, although perhaps unwritten, practice of paying postretirement benefits. This statement supersedes the guidance in *SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8*, nullifies and incorporates the guidance in *INT 99-26: Offsetting Pension Assets and Liabilities,* and *INT 04-12: Determining the Classification and Benefit Attribution Method for a "Cash Balance" Pension Plan*, and nullifies *INT 01-16: Measurement Date for SSAP No. 8 Actuarial Valuations*, *INT 03-18: Accounting for a Change in the Additional Minimum Liability in SSAP No. 8—Pensions* and *INT 04-03: Clarification for Calculating the Additional Minimum Pension Liability under SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8, paragraph 16.f.*. This statement also modifies *INT 04-17: Impact of Medicare Modernization on Postretirement Benefits* to remove reference to pensions as this interpretation only addresses postretirement benefits other than pensions.

SUMMARY CONCLUSION

Defined Benefit Plans

Single-Employer Defined Benefit Pension Plans

3. A defined benefit pension plan is one that defines an amount of pension benefit to be provided, usually as a function of one or more factors such as age, years of service, or compensation. (Hybrid pension plans that refer to an account balance, rather than a monthly annuity at retirement (also known as cash balance plans) are considered defined benefit plans for purposes of applying this statement.) For defined benefit plans, reporting entities shall adopt *FAS 158: Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (FAS 158) and *FASB Staff Position FAS 136(R)-1, Employers' Disclosures about Postretirement Benefit Plan Assets* (FSP FAS 136(R)-1) with modifications as discussed within paragraph 87.

4. A pension benefit is part of the compensation paid to an employee for services. In a defined benefit pension plan, the employer promises to provide, in addition to current wages, retirement income payments in future years after the employee retires or terminates service. Generally, the amount of benefit to be paid depends on a number of future events that are incorporated in the plan's benefit formula, often including how long the employee and any survivors live, how many years of service the employee renders, and the employee's compensation in the years immediately before retirement or termination. In

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most cases, services are rendered over a number of years before an employee retires and begins collecting the pension. Even though the services rendered by an employee are complete and the employee has retired, the total amount of benefit that the employer has promised and the cost to the employer of the services rendered are not precisely determinable but can only be estimated using the benefit formula and estimates of the relevant future events, many of which the employer cannot control.

Elements of Pension Accounting

5. Net periodic pension cost is made up of several components that reflect different aspects of the employer's financial arrangements as well as the cost of benefits earned by employees. The cost of a benefit can be determined without regard to how the employer decides to finance the plan. The service cost component of net periodic pension cost is the actuarial present value of benefits attributed by the plan's benefit formula to services rendered by employees during the period. The service cost component is conceptually the same for an unfunded plan, a plan with minimal funding, and a well-funded plan. The other components of net periodic pension cost are interest cost (interest on the projected benefit obligation, which is a discounted amount), actual[1] return on plan assets, amortization of any prior service cost or credit included in unassigned funds (surplus), and gain or loss, which includes, to the extent recognized, amortization of the net gain or loss included in unassigned funds (surplus) (refer to paragraph 24).

6. The projected benefit obligation is the actuarial present value of all benefits attributed by the plan's benefit formula to employee service rendered prior to that date. The projected benefit obligation is measured using an assumption as to future compensation levels if the pension benefit formula is based on those future compensation levels. The projected benefit obligation is a measure of benefits attributed to service to date assuming that the plan continues in effect and that estimated future events (including compensation increases, turnover, and mortality) occur.

7. The accumulated benefit obligation is the actuarial present value of benefits attributed by the pension benefit formula to employee service rendered prior to that date and based on current and past compensation levels. The accumulated benefit obligation differs from the projected benefit obligation in that it includes no assumption about future compensation levels. For plans with flat-benefit or non-pay-related pension benefit formulas, the accumulated benefit obligation and the projected benefit obligation are the same.

8. Plan assets are assets that have been segregated and restricted to provide for pension benefits. The amount of plan assets includes amounts contributed by the employer and amounts earned from investing the contributions, less benefits paid. Assets not segregated in a trust or otherwise effectively restricted so that they cannot be used by the employer for other purposes are not considered plan assets even though it may be intended that such assets be used to provide for pension benefits. Amounts accrued by the employer but not yet paid to the plan are also not considered plan assets. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

Recognition of Net Periodic Pension Cost

9. The following components shall be included in the net pension cost for a period by an employer sponsoring a defined benefit pension plan: a) Service cost; b) Interest cost; c) Actual return on plan assets;

[1] To address a question on how the expected return on plan assets affects the determination of net periodic pension cost if the actual return on plan assets for a period is a component of net periodic pension cost, it is noted that the expected return on plan assets generally will be different from the actual return on plan assets for the year. This statement provides for recognition of that difference (a net gain or loss) in unassigned funds in the period it arises. The amount recognized in unassigned funds is also a component of net periodic pension cost for the current period. Thus, the amount recognized in unassigned funds and the actual return on plan assets, when aggregated, equal the expected return on plan assets. The amount recognized in unassigned funds affects future net periodic pension cost through subsequent amortization, if any, of the net gain or loss. (This footnote reflects guidance included in E12 of FSP FAS 158-1.)

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d) Amortization of any prior service cost or credit included in unassigned funds (surplus); e) Gain or loss (including the effects of changes in assumptions) to the extent recognized; and f) Amortization of any net transition asset or obligation existing at the date of initial application of this statement and remaining in unassigned funds (surplus).

Service Cost

10. The service cost component recognized in a period shall be determined as the actuarial present value of benefits attributed by the pension benefit formula to employee service (including both vested and nonvested employees) during that period.

11. The prior service cost for nonvested employees not previously recognized[2] is not required to be included in net periodic pension cost entirely in the year this standard is adopted. Unrecognized prior service cost for nonvested employees shall be amortized as a component of net periodic pension cost by assigning an equal amount to each expected future period of service before vesting occurs for nonvested employees active at the date of the amendment. Unassigned funds (surplus) is adjusted each period as prior service cost is amortized ~~(refer to paragraphs 91-93 for transition guidance related to the recognition of the prior service cost for nonvested employees though unassigned surplus)~~.

Interest Cost

12. The interest cost component recognized in a period shall be determined as the increase in the projected benefit obligation due to the passage of time. Measuring the projected benefit obligation as a present value requires accrual of an interest cost at rates equal to the assumed discount rates.

Actual Return on Plan Assets

13. For a funded plan, the actual return on plan assets shall be determined based on the fair value of plan assets at the beginning and the end of the period, adjusted for contributions and benefit payments.

Prior Service Cost

14. Plan amendments (including initiation of a plan) often include provisions that grant increased benefits based on services rendered in prior periods. Because plan amendments are granted with the expectation that the employer will realize economic benefits in future periods, the cost of providing such retroactive benefits (prior service cost) is not required to be included in net periodic pension cost entirely in the year of the amendment but provides for recognition during the future service periods of those employees active at the date of the amendment who are expected to receive benefits under the plan.

15. A plan amendment that retroactively increases benefits (including benefits that are granted to retirees) increases the projected benefit obligation. The cost of the benefit improvement shall be recognized as a charge to unassigned funds (surplus) at the date of the amendment. Except as specified in paragraphs 16-17, that prior service cost shall be amortized as a component of net periodic pension cost by assigning an equal amount to each future period of service of each employee active at the date of the amendment who is expected to receive benefits under the plan. If all or almost all of a plan's participants are inactive, the cost of retroactive plan amendments affecting benefits of inactive participants shall be amortized based on the remaining life expectancy of those participants instead of based on the remaining service period. Unassigned funds (surplus) is adjusted each period as prior service cost is amortized.

[2] The previous statutory accounting guidance in *SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8* excluded nonvested employees from the service cost calculation. This exclusion has been eliminated with the issuance of this SSAP.

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16. Consistent use of an alternative approach that more rapidly amortizes the cost of retroactive amendments is acceptable. For example, a straight-line amortization of the cost over the average remaining service period of employees expected to receive benefits under the plan is acceptable. The alternative method used shall be disclosed.

17. In some situations, a history of regular plan amendments and other evidence may indicate that the period during which the employer expects to realize economic benefits from an amendment granting retroactive benefits is shorter than the entire remaining service period of the active employees. Identification of such situations requires an assessment of the individual circumstances and the substance of the particular plan situation. In those circumstances, the amortization of prior service cost shall be accelerated to reflect the more rapid expiration of the employer's economic benefits and to recognize the cost in the periods benefited.

18. A plan amendment that retroactively reduces, rather than increases, benefits decreases the projected benefit obligation. The reduction in benefits shall be recognized as a credit (prior service credit) to unassigned funds (surplus) that shall be used first to reduce any remaining prior service cost included in unassigned funds (surplus). Any remaining prior service credit shall be amortized as a component of net periodic pension cost on the same basis as the cost of a benefit increase.

Gains and Losses

19. Gains and losses are changes in the amount of either the projected benefit obligation or plan assets resulting from experience different from that assumed and from changes in assumptions. This statement does not distinguish between those sources of gains and losses. Gains and losses include amounts that have been realized, as well as amounts that are unrealized. Because gains and losses may reflect refinements in estimates as well as real changes in economic values and because some gains in one period may be offset by losses in another or vice versa, recognition of gains and losses as components of net pension cost of the period in which they arise is not required. Gains and losses that are not recognized immediately as a component of net periodic pension cost shall be recognized as increases or decreases in unassigned funds (surplus) as they arise.

20. The expected return on plan assets shall be determined based on the expected long-term rate of return on plan assets and the fair value of plan assets.

21. Asset gains and losses are differences between the actual return on assets during a period and the expected return on assets for that period. Asset gains and losses include changes reflected in the fair value of assets.

22. As a minimum, amortization of a net gain or loss included in unassigned funds (surplus) shall be included as a component of net pension cost for a year if, as of the beginning of the year, that net gain or loss exceeds 10% ~~percent~~ of the greater of the projected benefit obligation or the fair value of plan assets. If amortization is required, the minimum amortization shall be that excess divided by the average remaining service period of active employees expected to receive benefits under the plan. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants shall be used instead of average remaining service.

23. Any systematic method of amortizing gains or losses may be used in lieu of the minimum specified in paragraph 22 provided that (a) the minimum is used in any period in which the minimum amortization is greater (reduces the net balance included in unassigned funds (surplus) by more), (b) the method is applied consistently, (c) the method is applied similarly to both gains and losses, and (d) the method used is disclosed.

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24. The gain or loss component of net periodic pension cost shall consist of (a) the difference between the actual return on plan assets and the expected return on plan assets and (b) amortization of the net gain or loss included in unassigned funds (surplus).

Recognition of Liabilities and Assets

25. If the projected benefit obligation (considering both vested and nonvested participants) exceeds the fair value of plan assets, the employer shall recognize in its statement of financial position a liability that equals the unfunded projected benefit obligation. If the fair value of plan assets exceeds the projected benefit obligation, the employer shall recognize in its statement of financial position an asset that equals the overfunded projected benefit obligation. This prepaid asset resulting from the excess of the fair value of plan assets over the projected benefit obligation shall be nonadmitted.

26. If multiple single-employer plans exist, the employer shall aggregate the statuses of all overfunded plans and recognize that amount as an asset in its statement of financial position. It also shall aggregate the statuses of all underfunded plans and recognize that amount as a liability in its statement of financial position. It is not acceptable statutory accounting practice to offset pension or postretirement benefits other than pensions liability generated by one plan against the prepaid assets of another plan.

27. The asset or liability that is recognized pursuant to paragraph 25 may result in a temporary difference, as defined in *SSAP No. 101—Income Taxes*. The deferred tax effects of any temporary differences shall be recognized in income tax expense or benefit for the year and shall be allocated pursuant to SSAP No. 101.

28. If a new determination of the funded status of a plan to be recognized as an asset or a liability in the employer's statement of financial position is made, or when net gains or losses, prior service costs or credits, or the net transition asset or obligation existing at the date of initial application of this statement are amortized as components of net periodic pension cost, the related balances for those net gains or losses, prior service costs or credits, and transition asset or obligation in unassigned funds (surplus) shall be adjusted as necessary and reported in unassigned funds (surplus).

Measurement of Cost and Obligations

29. The service component of net periodic pension cost, the projected benefit obligation, and the accumulated benefit obligation are based on an attribution of pension benefits to periods of employee service and on the use of actuarial assumptions to calculate the actuarial present value of those benefits. Actuarial assumptions reflect the time value of money (discount rate) and the probability of payment (assumptions as to mortality, turnover, early retirement, and so forth).

Attribution

30. Pension benefits ordinarily shall be attributed to periods of employee service based on the plan's benefit formula to the extent that the formula states or implies an attribution. In some situations a history of regular increases and other evidence may indicate that an employer has a present commitment to make future amendments and that the substance of the plan is to provide benefits attributable to prior service that are greater than the benefits defined by the written terms of the plan. In those situations, the substantive commitment shall be the basis for the accounting, and the existence and nature of the commitment to make future amendments shall be disclosed.

31. In some situations a history of regular increases in non-pay-related benefits or benefits under a career-average-pay plan and other evidence may indicate that an employer has a present commitment to make future amendments and that the substance of the plan is to provide benefits attributable to prior service that are greater than the benefits defined by the written terms of the plan. In those situations, the

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substantive commitment shall be the basis for the accounting, and the existence and nature of the commitment to make future amendments shall be disclosed.

32. Some plans may have benefit formulas that attribute all or a disproportionate share of the total benefits provided to later years of service, thereby achieving in substance a delayed vesting of benefits. For such plans the total projected benefit shall be considered to accumulate in proportion to the ratio of the number of completed years of service to the number that will have been completed when the benefit is first fully vested. If a plan's benefit formula does not specify how a particular benefit relates to services rendered, the benefit shall be considered to accumulate as follows:

a. For benefits of a type includable in vested benefits, in proportion to the ratio of the number of completed years of service to the number that will have been completed when the benefit is first fully vested.

b. For benefits of a type not includable in vested benefits, in proportion to the ratio of completed years of service to total projected years of service.

Assumptions

33. Each significant actuarial assumption used shall reflect the best estimate solely with respect to that individual assumption. All assumptions shall presume that the plan will continue in effect in the absence of evidence that it will not continue.

34. Assumed discount rates shall reflect the rates at which the pension benefits could be effectively settled. It is appropriate in estimating those rates to look to available information about rates implicit in current prices of annuity contracts that could be used to effect settlement of the obligation. In making those estimates, employers may also look to rates of return on high-quality fixed-income investments currently available and expected to be available during the period to maturity of the pension benefits. Assumed discount rates are used in measurements of the projected, accumulated, and vested benefit obligations and the service and interest cost components of net periodic pension cost.

35. The objective of selecting assumed discount rates using the method noted in paragraph 34 is to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments, would provide the necessary future cash flows to pay the pension benefits when due. Notionally, that single amount, the projected benefit obligation, would equal the fair value of a portfolio of high-quality zero-coupon bonds whose maturity dates and amounts would be the same as the timing and amount of the expected future benefit payments. Because cash inflows would equal cash outflows in timing and amount, there would be no reinvestment risk in the yields to maturity of the portfolio. However, in other than a zero coupon portfolio, such as a portfolio of long-term debt instruments that pay semiannual interest payments or whose maturities do not extend far enough into the future to meet expected benefit payments, the assumed discount rates (the yield to maturity) need to incorporate expected reinvestment rates available in the future. Those rates shall be extrapolated from the existing yield curve at the measurement date. The determination of the assumed discount rate is separate from the determination of the expected rate of return on plan assets whenever the actual portfolio differs from the hypothetical portfolio above. Assumed discount rates shall be reevaluated at each measurement date. If the general level of interest rates rises or declines, the assumed discount rates shall change in a similar manner.

36. Interest rates vary depending on the duration of investments; for example, U.S. Treasury bills, 7-year bonds and 30-year bonds have different interest rates. Thus, the weighted-average discount rate (interest rate) inherent in the prices of annuities (or a dedicated bond portfolio) will vary depending on the length of time remaining until individual benefit payment dates. A plan covering only retired employees would be expected to have significantly different discount rates from one covering a work force of 30-

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year-olds. A properly weighted average rate can be used for aggregate computations such as the service cost and interest cost component of net pension cost for the period.

37. In addition to a properly weighted average rate, as stated in paragraph 36, an entity may elect to measure the service cost and interest cost components of net periodic benefit cost by using individual spot rates derived from an acceptable high-quality corporate bond yield curve and matched with separate cash flows for each future year (also known as the spot rate approach). If the election is made to switch from a weighted-average approach to the spot rate approach, this approach shall be consistently applied to all defined benefit plans and to the measurement of both service and interest cost. This change shall be reflected as a change in estimate as prescribed in *SSAP No. 3—Accounting Changes and Corrections of Errors* and once changed; the company should not revert back to the weighted-average discount rate in future periods. This change in estimate shall be appropriately disclosed in accordance with this statement, SSAP No. 3 and the Preamble.

38. An insurance company deciding on the price of an annuity contract will consider the rates of return available to it for investing the premium received and the rates of return expected to be available to it for reinvestment of future cash flows from the initial investment during the period until benefits are payable. That consideration is indicative of a relationship between rates inherent in the prices of annuity contracts and rates available in investment markets. It would be appropriate for employers to consider that relationship and information about investment rates in estimating the discount rates required for application of this statement.

39. The expected long-term rate of return on plan assets shall reflect the average rate of earnings expected on the funds invested or to be invested to provide for the benefits included in the projected benefit obligation. In estimating that rate, appropriate consideration should be given to the returns being earned by the plan assets in the fund and the rates of return expected to be available for reinvestment. The expected long-term rate of return on plan assets is used to compute the expected return on assets.

40. The service cost component of net periodic pension cost and the projected benefit obligation shall reflect future compensation levels to the extent that the pension benefit formula defines pension benefits wholly or partially as a function of future compensation levels. Future increases for which a present commitment exists shall be similarly considered. Assumed compensation levels shall reflect an estimate of the actual future compensation levels of the individual employees involved, including future changes attributed to general price levels, productivity, seniority, promotion, and other factors. All assumptions shall be consistent to the extent that each reflects expectations of the same future economic conditions, such as future rates of inflation. Measuring service cost and the projected benefit obligation based on estimated future compensation levels entails considering indirect effects, such as changes under existing law in social security benefits or benefit limitations that would affect benefits provided by the plan.

41. The accumulated benefit obligation shall be measured based on employees' history of service and compensation without an estimate of future compensation levels. Excluding estimated future compensation levels also means excluding indirect effects of future changes such as increases in the social security wage base. In measuring the accumulated benefit obligation, projected years of service shall be a factor only in determining employees' expected eligibility for particular benefits, such as:

a. Increased benefits that are granted provided a specified number of years of service are rendered

b. Early retirement benefits

c. Death benefits

d. Disability benefits

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42. Automatic benefit increases specified by the plan (for example, automatic cost-of-living increases) that are expected to occur shall be included in measurements of the projected, accumulated, and vested benefit obligations, and the service cost component. Also, retroactive plan amendments shall be included in the computation of the projected and accumulated benefit obligations once they have been contractually agreed to, even if some provisions take effect only in future periods.

Measurement of Plan Assets

43. Plan investments, whether equity or debt securities, real estate, or other, shall be measured at their fair value as of the measurement date. The fair value of an investment shall be reduced by brokerage commissions and other costs normally incurred in a sale, if those costs are significant (similar to fair value less costs to sell).

44. Plan assets used in plan operations (for example, buildings, equipment, furniture and fixtures, and leasehold improvements) shall be measured at cost less accumulated depreciation or amortization for all purposes.

45. The measurements of plan assets and benefit obligations shall be as of the date of the employer's fiscal year-end statement of financial position. Requiring that the pension measurements be as of a particular date is not intended to require that all procedures be performed after that date. As with other financial statement items requiring estimates, much of the information can be prepared as of an earlier date and projected forward to account for ~~subsequent~~ events occurring between the most recent valuation date and the plan's year end (for example, employee service and benefit payments). Unless a business entity remeasures both its plan assets and benefit obligations during the fiscal year, the funded status it reports in its interim-period statement of financial position shall be the same asset or liability recognized in the previous year-end statement of financial position adjusted for (1) subsequent accruals of net periodic pension cost that exclude the amortization of amounts previously recognized in other unassigned funds (surplus) (for example, subsequent accruals of service cost, interest cost, and return on plan assets) and (2) contributions to a funded plan, or benefit payments. Sometimes, a business entity remeasures both plan assets and benefit obligations during the fiscal year. That is the case, for example, when a significant event such as a plan amendment, settlement, or curtailment occurs that calls for a remeasurement. Upon remeasurement, a business entity shall adjust its statement of financial position in a subsequent interim period to reflect the overfunded or underfunded status of the plan consistent with that measurement date.

46. If a significant event caused by the employer (such as a plan amendment, settlement, or curtailment) that requires an employer to re-measure both plan assets and benefit obligations does not coincide with a month-end, the employer may elect to re-measure plan assets and benefit obligations using the month-end that is closest to the date of the significant event. This re-measurement would not eliminate the requirement for a year-end measurement of plan assets and benefit obligations required in paragraph 45.

47. If an employer re-measures plan assets and benefit obligations during the fiscal year in accordance with paragraph 46, the employer shall adjust the fair value of plan assets and the actuarial present value of benefit obligations for any effects of the significant event that may or may not be captured in the month-end measurement (for example, if the closest month-end is before the date of a partial settlement, then the measurement of plan assets may include assets that are no longer part of the plan). An employer shall not adjust the fair value of plan assets and the actuarial present value of benefit obligations for other events occurring between the month-end date used to re-measure plan assets and benefit obligations and the employer's fiscal year-end that may be significant to the measurement of defined benefit plan assets and obligations, but are not caused by the employer (for example, changes in market prices or interest rates).

48. Measurements of net periodic pension cost for both interim and annual financial statements shall be based on the assumptions used for the previous year-end measurements unless more recent

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measurements of both plan assets and obligations are available or a significant event occurs, such as a plan amendment, that would ordinarily call for such measurements.

Employers with Two or More Plans

49. An employer that sponsors two or more separate defined benefit pension plans shall determine net periodic pension cost, liabilities, and assets by separately applying the provisions of this statement to each plan. In particular, unless an employer clearly has a right to use the assets of one plan to pay benefits of another, a liability required to be recognized for one plan shall not be reduced or eliminated because the employer has recognized an asset for another plan that has assets in excess of its projected benefit obligation. (As noted within paragraph 26, overfunded plans shall be aggregated for asset reporting (nonadmitted) and underfunded plans shall be aggregated for liability reporting.)

Annuity Contracts

50. An annuity contract is a contract in which an insurance company unconditionally undertakes a legal obligation to provide specified benefits to specific individuals in return for a fixed consideration or premium. An annuity contract is irrevocable and involves the transfer of significant risk from the employer to the insurance company. Some annuity contracts ~~(participating annuity contracts)~~include participation rights (participating annuity contract), which provide that the purchaser (either the plan or the employer) may participate in the experience of the insurance company. Under those contracts, the insurance company ordinarily pays dividends to the purchaser. If the substance of a participating annuity contract is such that the employer remains subject to all or most of the risks and rewards associated with the benefit obligation covered and the assets transferred to the insurance company, that contract is not an annuity contract for purposes of this statement.

51. To the extent that benefits currently earned are covered by annuity contracts, the cost of those benefits shall be the cost of purchasing the contracts, except as provided in paragraph 54. That is, if all the benefits attributed by the plan's benefit formula to service in the current period are covered by nonparticipating annuity contracts, the cost of the contracts determines the service cost component of net pension cost for that period.

52. Benefits provided by the pension benefit formula beyond benefits provided by annuity contracts (for example, benefits related to future compensation levels) shall be accounted for according to the provisions of this statement applicable to plans not involving insurance contracts.

53. Benefits covered by annuity contracts shall be excluded from the projected benefit obligation and the accumulated benefit obligation. Except as provided in paragraph 54, annuity contracts shall be excluded from plan assets.

54. Some annuity contracts provide that the purchaser (either the plan or the employer) may participate in the experience of the insurance company. Under those contracts, the insurance company ordinarily pays dividends to the purchaser, the effect of which is to reduce the cost of the plan. The purchase price of a participating annuity contract ordinarily is higher than the price of an equivalent contract without participation rights. The difference is the cost of the participation right. The cost of the participation right shall be recognized at the date of purchase as a nonadmitted asset. In subsequent periods, the participation right shall be nonadmitted and measured at its fair value if the contract is such that fair value is reasonably estimable. Otherwise, the participation right shall be measured at its amortized cost (not in excess of its net realizable value), and the cost shall be amortized systematically over the expected dividend period under the contract.

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Other Contracts with Insurance Companies

55. Insurance contracts that are in substance equivalent to the purchase of annuities shall be accounted for as such. Other contracts with insurance companies shall be accounted for as investments and measured at fair value. For some contracts, the best available evidence of fair value may be contract value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value.

Defined Benefit Plans – Settlements and Curtailments

56. A settlement is defined as a transaction that (a) is an irrevocable action, (b) relieves the employer (or the plan) of primary responsibility for a pension benefit obligation, and (c) eliminates significant risks related to the obligation and the assets used to effect the settlement. Examples of transactions that constitute a settlement include (a) making lump-sum cash payments to plan participants in exchange for their rights to receive specified pension benefits and (b) purchasing nonparticipating annuity contracts to cover vested benefits.

57. A transaction that does not meet all of the above three criteria does not constitute a settlement for purposes of this statement. For example, investing in a portfolio of high-quality fixed-income securities with principal and interest payment dates similar to the estimated payment dates of benefits may avoid or minimize certain risks. However, that does not constitute a settlement because the investment decision can be reversed, and such a strategy does not relieve the employer (or the plan) of primary responsibility for a pension obligation nor does it eliminate significant risks related to the obligation.

58. The definition of an annuity contract is included in paragraph 50. If the substance of a participating annuity contract is such that the employer remains subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance company, the purchase of the contract does not constitute a settlement.

Curtailment

59. A curtailment is an event that significantly reduces the expected years of future service of present employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future services. Curtailments include:

a. Termination of employees' services earlier than expected, which may or may not involve closing a facility or discontinuing a component of an entity.

b. Termination or suspension of a plan so that employees do not earn additional defined benefits for future services. In the latter situation, future service may be counted toward vesting of benefits accumulated based on past service.

Relationship of Settlements and Curtailments to Other Events

60. A settlement and a curtailment may occur separately or together. If benefits to be accumulated in future periods are reduced but the plan remains in existence and continues to pay benefits, to invest assets, and to receive contributions, a curtailment has occurred but not a settlement. If an employer purchases nonparticipating annuity contracts for vested benefits and continues to provide defined benefits for future service, either in the same plan or in a successor plan, a settlement has occurred but not a curtailment. If a plan is terminated (that is, the obligation is settled and the plan ceases to exist) and not replaced by a successor defined benefit plan, both a settlement and a curtailment have occurred (whether or not the employees continue to work for the employer).

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Accounting for Settlement of the Pension Obligation

61. The maximum gain or loss subject to recognition in earnings when a pension obligation is settled is the net gain or loss remaining in unassigned funds (surplus) plus any transition asset remaining in unassigned funds (surplus) from initial application of SSAP No. 89. That maximum amount includes any gain or loss first measured at the time of settlement. The maximum amount shall be recognized in earnings if the entire projected benefit obligation is settled. If only part of the projected benefit obligation is settled, the employer shall recognize in earnings a pro rata portion of the maximum amount equal to the percentage reduction in the projected benefit obligation.

62. If the purchase of a participating annuity contract constitutes a settlement, the maximum gain (but not the maximum loss) shall be reduced by the cost of the participation right before determining the amount to be recognized in earnings.

63. If the cost of all settlements in a year is less than or equal to the sum of the service cost and interest cost components of net periodic pension cost for the plan for the year, gain or loss recognition is permitted but not required for those settlements. However, the accounting policy adopted shall be applied consistently from year to year.

Accounting for a Plan Curtailment

64. The prior service cost included in unassigned funds (surplus) associated with years of service no longer expected to be rendered as the result of a curtailment is a loss. For example, if a curtailment eliminates half of the estimated remaining future years of service of those who were employed at the date of a prior plan amendment and were expected to receive benefits under the plan, then the loss associated with the curtailment is half of the prior service cost included in unassigned funds (surplus) related to that amendment that has not been amortized as a component of net periodic pension cost. For purposes of applying the provisions of this paragraph, prior service cost includes the cost of retroactive plan amendments and any transition obligation remaining in unassigned funds (surplus) from initial application of SSAP No. 89.

65. The projected benefit obligation may be decreased (a gain) or increased (a loss) by a curtailment.

a. To the extent that such a gain exceeds any net loss included in unassigned funds (surplus) (or the entire gain, if a net gain exists), it is a curtailment gain.

b. To the extent that such a loss exceeds any net gain included in unassigned funds (surplus) (or the entire loss, if a net loss exists), it is a curtailment loss.

For purposes of applying the provisions of this paragraph, any transition asset remaining in unassigned funds (surplus) from initial application of SSAP No. 89 shall be treated as a net gain and shall be combined with the net gain or loss arising subsequent to transition to SSAP No. 89.

66. If the sum of the effects identified in paragraphs 64 and 65 is a net loss, it shall be recognized in earnings when it is probable that a curtailment will occur, and the effects described are reasonably estimable. If the sum of those effects is a net gain, it shall be recognized in earnings when the related employees terminate, or the plan suspension or amendment is adopted.

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Termination Benefits

67. An employer may provide benefits to employees in connection with their termination of employment. They may be either special termination benefits offered only for a short period of time or contractual termination benefits required by the terms of a plan only if a specified event, such as a plant closing, occurs. An employer that offers special termination benefits to employees shall recognize a liability and a loss when the employees accept the offer and the amount can be reasonably estimated. An employer that provides contractual termination benefits shall recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated. Termination benefits may take various forms including lump-sum payments, periodic future payments, or both. They may be paid directly from an employer's assets, an existing pension plan, a new employee benefit plan, or a combination of those means. The cost of termination benefits recognized as a liability and a loss shall include the amount of any lump-sum payments and the present value of any expected future payments. A situation involving termination benefits may also involve a curtailment to be accounted for under paragraphs 64-66.

Disclosures – Single-Employer Defined Benefit Plans

68. An employer that sponsors one or more defined benefit pension plans or one or more other defined benefit postretirement plans shall provide the following information, separately for pension plans and other postretirement benefit plans. Amounts related to the employer's results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer's statement of financial position, shall be disclosed as of the date of each statement of financial position presented.

a. A reconciliation of beginning and ending balances of the benefit obligation showing separately, if applicable, the effects during the period attributable to each of the following: service cost, interest cost, contributions by plan participants, actuarial gains and losses, foreign currency exchange rate changes, benefits paid, plan amendments, business combinations, divestitures, curtailments, settlements, and special termination benefits.

b. A reconciliation of beginning and ending balances of the fair value of plan assets showing separately, if applicable, the effects during the period attributable to each of the following: actual return on plan assets, foreign currency exchange rate changes, contributions by the employer, contributions by plan participants, benefits paid, business combinations, divestitures, and settlements.

c. The funded status of the plans and the amounts recognized in the statement of financial position, showing separately the assets and liabilities recognized.

d. The objectives of the disclosures about postretirement benefit plan assets are to provide users of financial statements with an understanding of:

    i. How investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies

    ii. The classes of plan assets

    iii. The inputs and valuation techniques used to measure the fair value of plan assets

    iv. The effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period

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v. Significant concentrations of risk within plan assets.

An employer shall consider those overall objectives in providing the following information about plan assets:

(a) A narrative description of investment policies and strategies, including target allocation percentages or range of percentages considering the classes of plan assets disclosed pursuant to (b) below, as of the latest statement of financial position presented (on a weighted-average basis for employers with more than one plan), and other factors that are pertinent to an understanding of those policies and strategies such as investment goals, risk management practices, permitted and prohibited investments including the use of derivatives, diversification, and the relationship between plan assets and benefit obligations. For investment funds disclosed as classes as described in (b) below, a description of the significant investment strategies of those funds shall be provided.

(b) The fair value of each class of plan assets as of each date for which a statement of financial position is presented. Asset classes shall be based on the nature and risks of assets in an employer's plan(s). Examples of classes of assets could include, but are not limited to, the following: cash and cash equivalents; equity securities, (segregated by industry type, company size, or investment objective); debt securities, issued by national, state, and local governments; corporate debt securities; asset-backed securities; structured debt; derivatives on a gross basis (segregated by type of underlying risk in the contract, for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, and other contracts); investment funds (segregated by type of fund); and real estate. Those examples are not meant to be all inclusive. An employer should consider the overall objectives in paragraph 68.d. in determining whether additional classes of plan assets or further disaggregation of classes should be disclosed.

(c) A narrative description of the basis used to determine the overall expected long-term rate-of-return-on-assets assumption, such as the general approach used, the extent to which the overall rate-of-return-on-assets assumption was based on historical returns, the extent to which adjustments were made to those historical returns in order to reflect expectations of future returns, and how those adjustments were determined. The description should consider the classes of assets described in (b) above, as appropriate.

(d) Information that enables users of financial statements to assess the inputs and valuation techniques used to develop fair value measurements of plan assets at the reporting date. For fair value measurements using significant unobservable inputs, an employer shall disclose the effect of the measurements on changes in plan assets for the period. To meet those objectives, the employer shall disclose the following information for each class of plan assets disclosed pursuant to (b) above for each annual period:

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(1) The level within the fair value hierarchy in which the fair value measurements in their entirety fall,[3] segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3)

(2) Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.

e. For defined benefit pension plans, the accumulated benefit obligation.

f. The benefits (as of the date of the latest statement of financial position presented) expected to be paid in each of the next five fiscal years, and in the aggregate for the five fiscal years thereafter. The expected benefits should be estimated based on the same assumptions used to measure the company's benefit obligation at the end of the year and should include benefits attributable to estimated future employee service.

g. The employer's best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the next fiscal year beginning after the date of the latest statement of financial position presented. Estimated contributions may be presented in the aggregate combining (1) contributions required by funding regulations or laws, (2) discretionary contributions, and (3) noncash contributions.

h. The amount of net benefit cost recognized, showing separately the service cost component, the interest cost component, the expected return on plan assets for the period, the gain or loss component, the prior service cost or credit component, the transition asset or obligation component, and the gain or loss recognized due to settlements or curtailments.

i. Separately the net gain or loss and net prior service cost or credit recognized in unassigned funds (surplus) for the period pursuant to paragraphs 15 and 19 and reclassification adjustments of unassigned funds (surplus) for the period, as those amounts, including amortization of the net transition asset or obligation, are recognized as components of net periodic benefit cost.

j. The amounts in unassigned funds (surplus) that have not yet been recognized as components of net periodic benefit cost, showing separately the net gain or loss, net prior service cost or credit, and net transition asset or obligation.

k. On a weighted-average basis, the following assumptions used in the accounting for the plans: discount rates, rates of compensation increase (for pay-related plans), expected long-term rates of return on plan assets specifying, in a tabular format, the assumptions used to determine the benefit obligation and the assumptions used to determine net benefit cost, and interest crediting rates (for cash balance plans and other plans with promised crediting rates).

[3] In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. The level in the fair value hierarchy within which the fair value measurement in its entirety falls shall be determined based on the lowest level input that is significant to the fair value measurement in its entirety. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability.

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l. If applicable, the amounts and types of securities of the employer and related parties included in plan assets.

m. If applicable, any alternative method used to amortize prior service amounts or net gains and losses pursuant to paragraphs 16 and 23.

n. If applicable, any substantive commitment, such as past practice or a history of regular benefit increases, used as the basis for accounting for the benefit obligation.

o. If applicable, the cost of providing special or contractual termination benefits recognized during the period and a description of the nature of the event.

p. An explanation of the following information:

i. The reasons for significant gains and losses related to changes in the defined benefit obligation for the period.

ii. Any other significant change in the benefit obligation or plan assets not otherwise apparent in the other disclosures required by this statement.

Disclosures – Employers with Two or More Defined Benefit Plans

69. The disclosures required by this statement shall be aggregated for all of an employer's defined benefit pension plans and for all of an employer's other defined benefit postretirement plans unless disaggregating in groups is considered to provide useful information or is otherwise required by this paragraph and paragraph 70. Disclosures shall be as of the date of each statement of financial position presented. Disclosures about pension plans with assets in excess of the accumulated benefit obligation generally may be aggregated with disclosures about pension plans with accumulated benefit obligations in excess of assets. The same aggregation is permitted for other postretirement benefit plans. If aggregate disclosures are presented, an employer shall disclose, as of the date of each financial statement position presented:

a. The projected benefit obligation and fair value of plan assets for plans with projected benefit obligations in excess of plan assets.

b. The accumulated benefit obligation and fair value of plan assets for pension plans with accumulated benefit obligations in excess of plan assets.

70. A U.S. reporting entity may combine disclosures about pension plans or other postretirement benefit plans outside the United States with those for U.S. plans unless the benefit obligations of the plans outside the United States are significant relative to the total benefit obligation and those plans use significantly different assumptions.

Interim Financial Disclosures –Defined Benefit Plans

71. The following shall be disclosed within interim financial statements that include a statement of income:

a. The amount of net periodic benefit cost recognized, for each period for which a statement of income is presented, showing separately the service cost component, the interest cost component, the expected return on plan assets for the period, the gain or loss component, the amount of prior service cost or credit component, the transition asset or obligation component, and the gain or loss recognized due to a settlement or curtailment.

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b. The total amount of the employer's contributions paid, and expected to be paid, during the current fiscal year, if significantly different from amounts previously disclosed pursuant to paragraph 68.g. Estimated contributions may be presented in the aggregate combining (1) contributions required by funding regulations or laws, (2) discretionary contributions, and (3) noncash contributions.

Defined Contribution Plans

72. A defined contribution pension plan is a plan that provides pension benefits in return for services rendered, provides an individual account for each participant, and has terms that specify how contributions to the individual's account are to be determined rather than the amount of pension benefits the individual is to receive. Under a defined contribution plan, the pension benefits a participant will receive depend only on the amount contributed to the participant's account, the returns earned on investments of those contributions, and forfeitures of other participants' benefits that may be allocated to the participant's account.

73. To the extent that a plan's defined contributions to an individual's account are to be made for periods in which that individual renders services, the net pension cost for a period shall be the contribution called for in that period. If a plan calls for contributions for periods after an individual retires or terminates, the estimated cost shall be accrued during the employee's service period.

74. A pension plan having characteristics of both a defined benefit plan and a defined contribution plan requires careful analysis. If the substance of the plan is to provide a defined benefit, as may be the case with some "target benefit" plans, the accounting requirements shall be determined in accordance with the provisions applicable to a defined benefit plan and the disclosure requirements within paragraph 68 shall be followed.

Disclosures - Defined Contribution Plans

75. An employer shall disclose the amount of cost recognized for defined contribution pension plans and for other defined contribution postretirement benefit plans for all periods presented separately from the amount of cost recognized for defined benefit plans. The disclosures shall include a description of the nature and effect of any significant changes during the period affecting comparability, such as a change in the rate of employer contributions, a business combination, or a divestiture.

Multiemployer Plans

76. A multiemployer plan is a pension plan to which two or more unrelated employers contribute, usually pursuant to one or more collective-bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer.

77. A reporting entity participating in a multiemployer plan shall recognize as net pension cost the required contribution for the period and shall recognize as a liability any contributions due and unpaid.

78. In some situations, withdrawal from a multiemployer plan may result in a reporting entity having an obligation to the plan for a portion of its unfunded benefit obligations. If withdrawal under circumstances that would give rise to an obligation is either probable or reasonably possible, the provisions of *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets* shall apply.

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Disclosures - Multiemployer Plans

79. A reporting entity shall disclose the amount of contributions to multiemployer plans for each annual period for which a statement of income is presented. A reporting entity may disclose total contributions to multiemployer plans without disaggregating the amounts attributable to pension plans and other postretirement benefit plans. The disclosures shall include a description of the nature and effect of any changes affecting comparability, such as a change in the rate of employer contributions, a business combination, or a divestiture. This disclosure shall identify whether the contributions represent more than 5% ~~percent~~ of total contributions to the plan as indicated in the plan's most recently available annual report.

80. In addition to the requirements of paragraph 79, the following information shall be disclosed:

a. Whether a funding improvement plan or rehabilitation plan had been implemented or is pending.

b. Whether the reporting entity paid a surcharge to the plan.

c. A description of minimum contributions required for future periods, if applicable.

d. A qualitative description of the extent to which the employer could be responsible for the obligations of the plan, including benefits earned by employees during employment with another employer.

81. In some situations, withdrawal from a multiemployer plan may result in a reporting entity having an obligation to the plan for a portion of the unfunded benefit obligation of the pension plans and other postretirement benefit plans. If withdrawal under circumstances that would give rise to an obligation is either probable or reasonably possible, the provisions of SSAP No. 5R shall apply. If it is either probable or reasonably possible that (a) an employer would withdraw from the plan under circumstances that would give rise to an obligation or (b) an employer's contribution to the fund would be increased during the remainder of the contract period to make up a shortfall in the funds necessary to maintain the negotiated level of benefit coverage (a "maintenance of benefits" clause), the employer shall apply the provisions and disclosures of SSAP No. 5R.

Multiple-Employer Plans

82. Some pension plans to which two or more unrelated employers contribute are not multiemployer plans. Rather, they are in substance aggregations of single-employer plans combined to allow participating employers to pool their assets for investment purposes and to reduce the costs of plan administration. Those plans ordinarily do not involve collective-bargaining agreements. They may also have features that allow participating employers to have different benefit formulas, with the employer's contributions to the plan based on the benefit formula selected by the employer. Such plans shall be considered single-employer plans rather than multiemployer plans, and each reporting entity's accounting shall be based on its respective interest in the plan.

Non-U.S. Pension Plans

83. Except for its effective date, this statement includes no special provisions applicable to pension arrangements outside the United States. To the extent that those arrangements are in substance similar to pension plans in the United States, they are subject to the provisions of this statement. The substance of an arrangement is determined by the nature of the obligation and by the terms or conditions that define the amount of benefits to be paid, not by whether (or how) a plan is funded, whether benefits are payable at intervals or as a single amount, or whether the benefits are required by law or custom or are provided under a plan the employer has elected to sponsor.

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84. It is customary or required in some countries to provide benefits in the event of a voluntary or involuntary severance of employment (also called termination indemnities). If such an arrangement is in substance a pension plan (for example, if the benefits are paid for virtually all terminations), it is subject to the provisions of this statement.

Business Combinations

85. When an employer is acquired in a business combination and that employer sponsors a single-employer defined benefit pension plan, the assignment of the purchase price to individual assets acquired and liabilities assumed shall include a liability for the projected benefit obligation in excess of plan assets or an asset for plan assets in excess of the projected benefit obligation, thereby eliminating any previously existing net gain or loss, prior service cost or credit, or transition asset or obligation recognized in unassigned funds (surplus). If it is expected that the plan will be terminated or curtailed, the effects of those actions shall be considered in measuring the projected benefit obligation.

Consolidated/Holding Company Plans

86. The employees of many reporting entities are members of a plan sponsored by a parent company or holding company. A reporting entity who participates in these plans and is not directly liable for obligations under the plan shall recognize pension expense equal to its allocation from the holding company or parent company of the required contribution to the plan for the period. A liability shall be established for any such contributions due and unpaid. Furthermore, the reporting entity shall disclose in the notes to the financial statements that its employees participate in a plan sponsored by the holding company for which the reporting entity has no legal obligation. The amount of expense incurred, and the allocation methodology utilized by the provider of such benefits shall also be disclosed. If the reporting entity is directly liable for obligations under the plan, then the requirements outlined above in paragraphs 1-85 and 90-101 of this statement shall be applied.

Relevant Literature

87. This statement adopts with modification paragraphs 1-7 and 16-17 as well as Appendix C – Amendments to Statements 87 and 88 and Appendix E – Amendments to Statement 132(R) of *FASB Statement No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)* (FAS 158). Paragraphs 8-10 providing specific guidance for not-for-profit organizations is rejected. Paragraphs 11-15 regarding the effective dates for FAS 158 is rejected and paragraph 19 providing an alternative method for remeasuring plan assets and benefits obligations as of the fiscal year the measurement date provisions are applied is also rejected. Appendix D – Amendments to Statement 106 has not been incorporated within this statutory statement as it will be considered in accordance with revisions to *SSAP No. 14—Postretirement Benefits Other Than Pensions*. Disclosures included within FAS 132(R), as amended by FAS 158, pertaining to health care (paragraphs 5.l. and 5.m.) have been rejected for inclusion within this standard, but will also be considered in accordance with revisions to SSAP No. 14. This statement adopts the revisions to paragraph 5.d. of FAS 132(R) as amended by *FASB Staff Position FAS 132(R)-1, Employers' Disclosures about Postretirement Benefit Plan Assets* (FSP FAS 132(R)-1) and *ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASU 2010-06). Other revisions to disclosures requirements as amended by FSP FAS 132(R)-1 relate to nonpublic entities and are rejected. This statement adopts by reference revisions to ASC 715-80 as detailed in *ASU 2011-09, Compensation – Retirement Benefits – Multiemployer Plans* with limited additional disclosures required within statutory financial statements. This statement adopts by reference *FSP FASB 158-1, Conforming Amendments to the Illustrations in FASB Statements No. 87, No. 88, and No. 106 and to the Related Staff Implementation Guides* (FSP FAS 158-1) to the extent that the examples and related implementation guides comply with the adopted GAAP guidance previously identified within this statement, as modified for statutory accounting. This statement adopts with modification the

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disclosure revisions reflected in *ASU 2018-14, Changes to the Disclosure Requirements for Defined Benefit Plans,* consistent with the modifications from the adoption of FAS 158 and FAS 106. The following modifications from the adopted paragraphs of FAS 158 have been incorporated within this standard:

a. All references to 'other comprehensive income' or 'accumulated other comprehensive income' within FAS 158 have been revised to reflect unassigned funds (surplus).

b. Any prepaid asset resulting from the excess of the fair value of plan assets over the projected benefit obligation shall be nonadmitted. Furthermore, any asset recognized from the cost of a 'participation right' of an annuity contract per paragraph 54 shall also be nonadmitted.

c. Provisions within paragraph 30 of FAS 87, as amended by FAS 158, permitting a market-related value of plan assets have been eliminated with only the fair value measurement method for plan assets being retained.

d. The reduced disclosure requirements for nonpublic entities described in paragraph 8 of FAS 132(R), as amended by FAS 158, are rejected. All reporting entities shall follow the disclosure requirements included in paragraph 5 of FAS 132(R) as amended by FAS 158.

e. Clarification has been included within this standard to ensure both vested and nonvested employees are included within the recognition of net periodic pension cost and in the pension benefit obligation. Although this is consistent with GAAP, this is a change from previous statutory accounting. As nonvested employees were excluded from statutory accounting under SSAP No. 89, guidance has been included to indicate that the unrecognized prior service cost attributed to nonvested individuals is not required to be included in net periodic pension cost entirely in the year this standard is adopted. The unrecognized prior service cost for nonvested employees shall be amortized as a component of net periodic pension cost by assigning an equal amount to each expected future period of service before vesting occurs for nonvested employees active at the date of the amendment. Unassigned funds (surplus) is then adjusted each period as prior service cost is amortized. (Guidance is included within the transition related to the recognition of the prior service cost for nonvested employees through unassigned funds (surplus).)

f. Conclusion of *Interpretation 04-12: EITF 03-4: Determining the Classification and Benefit Attribution Method for a "Cash Balance" Pension Plan* indicating that 'cash balance' plans are considered defined benefit plans has been incorporated within paragraph 3 of this statement.

g. Conclusion of *Interpretation 99-26: Offsetting Pension Assets and Liabilities* prohibiting the offset of defined benefit liabilities of one plan with prepaid assets of another plan has been incorporated within paragraph 26 of this statement.

h. Provisions within paragraph 36 of FAS 87, as amended by FAS 158, regarding the classification of underfunded liabilities as current or noncurrent liabilities and the classification of assets from overfunded plans as noncurrent assets has been rejected as inconsistent with statutory accounting.

i. Provisions within paragraph 49 of FAS 87, as amended by FAS 158, defining the fair value of investments have been rejected. Fair value definitions and measurement for investments shall be determined in accordance with statutory accounting guidance.

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j. Provisions within paragraph 52 of FAS 87, as amended by FAS 158, regarding the plan assets measurement date for consolidating subsidiaries or entities utilizing the equity method under APB Opinion No. 18 has been rejected. For statutory accounting, all entities shall follow the measurement date guidance within paragraph 45 of this statement.

k. Transition under FAS 158 is different from this statement. FAS 158 requires entities with publicly traded equity securities to initially apply the requirement to recognize the funded status of a benefit plan; the gains/losses, prior service costs/credits and transition obligations/assets that have not yet been included in net periodic benefit cost; and the disclosure requirements as of the end of the fiscal year ending after December 15, 2006. ~~Transition guidelines for statutory accounting are defined in paragraphs 90-101.~~

l. FAS 158 provided two approaches for an employer to transition to a fiscal year-end measurement date. For purposes of statutory accounting, the second approach permitting reporting entities to use earlier measurements determined for year-end reporting as of the fiscal year immediately preceding the year that the measurement date provisions is rejected. For consistency purposes, all reporting entities shall follow the first approach and remeasure plan assets and benefit obligations as of the beginning of the fiscal year that the measurement date provisions are applied.

88. This statement adopts the revisions to ASC 715-30 as it relates to interim re-measurement due to a *significant* event as detailed in *ASU 2015-04, Practical Expedient for the Measurement Date of An Employer's Defined Benefit Obligation and Plan Assets*. Other revisions are rejected as statutory accounting requires the annual measurement of benefit obligations and plan assets to be measured as of a year-end measurement date.

89. This statement rejects *ASU 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. Existing statutory disclosures on the components of pension costs shall be completed.

Effective Date and Transition

90. Reporting entities are required to disclose the projected benefit obligation, the accumulated benefit obligation and the fair value of plan assets for defined benefit pension plans in the first reporting period after the effective date of this standard and in each subsequent reporting period. This disclosure shall specifically note the funded/underfunded status of the pension plan based on the projected benefit obligation. Reporting entities shall also specifically note the surplus impact necessary, at each reporting date, to reflect the full projected benefit obligation within the financial statements.

91. This statement is effective for quarterly and annual reporting periods beginning on or after January 1, 2013 (transition date) with early adoption permitted. Any unfunded defined benefit pension amounts, as determined when the projected benefit obligation exceeds the fair value of plan assets, is a liability under SSAP No. 5R and shall be reported in the first quarter statutory financial statements after the transition date with a corresponding entry to unassigned funds (surplus). If the fair value of plan assets exceeds the projected benefit obligation, the asset shall be considered a nonadmitted asset. Net periodic pension cost shall include a component for unrecognized prior service cost for nonvested employees beginning in 2013.

~~92. Gains or losses, prior service costs or credits (including prior service costs for non-vested participants pursuant to paragraph 11), and remaining transition assets or obligations from prior application of SSAP No. 89 (collectively referred to as "unrecognized items") that have not yet been~~

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~~included in net periodic benefit cost as of December 31, 2012[4] shall be recognized as components of the balance of unassigned funds (surplus), net of tax, as of January 1, 2013 (provided that alternative transition is not elected per paragraph 93.b.). The offset to unassigned funds is reported separately as an "Aggregate Write-In for Other Than Invested Assets" or as an "Aggregate Write-In for Other Liabilities." After recognition, the full unfunded or overfunded status of the plan shall be reflected within the financial statements.[5] Any prepaid asset resulting from an overfunded plan shall be nonadmitted.~~

~~93. Due to the potential impact to surplus as a result of immediately applying the accounting guidance in paragraph 92, reporting entities may elect one of the following two methods, on an individual plan basis, to recognize the transition surplus impact:~~

~~a. Reporting entities may elect to recognize the entire transition surplus impact calculated from applying paragraph 92, on an individual plan basis, as of January 1, 2013.~~

~~b. Alternatively, reporting entities may elect to recognize the entire surplus impact from applying paragraph 92, on an individual plan basis, over a period not to exceed ten (10) years. The surplus impact initially recognized as of January 1, 2013, under this transition option, and subsequently over the transition period, shall be the greater of:~~

~~i. Ten percent of the calculated surplus impact as of the transition date;~~

~~ii. Amortization[6] of the "unrecognized items" (defined in paragraph 92) into net periodic pension cost, including any accelerated amortization of these items from curtailments or settlements that occur after the transition date. (If the amortization cannot be determined at transition, at a minimum, the amount amortized for "unrecognized items" during the prior year shall be utilized for this component of the calculation. If the amount recognized for transition (greater of all three components in paragraph 93.b.) is subsequently determined to be less than what is amortized for the year (paragraph 93.b.ii.), the difference between what was recognized for transition, and what is amortized must immediately be recognized as an adjustment to the transition impact to unassigned funds (surplus);~~

~~[4] The intent of the guidance is to recognize the unrecognized amounts as of December 31, 2012, annual statements, even if new actuarial projections (accumulated benefit obligation/projected benefit obligation amounts) are calculated as of January 1, 2013. (These projections would be considered in the recognition of the 2013 pension cost.)~~

~~[5] Upon the effective date of this statement, reporting entities are required to reflect the full unfunded or overfunded status of their defined benefit pension plans. As such, the concept of an "additional minimum liability" previously reflected in *SSAP No. 89—Pensions* is not incorporated within this statement. If an additional minimum liability (and a corresponding intangible asset) had been recognized under SSAP No. 89, such items shall be eliminated with the implementation of this statement, and the guidance in paragraph 93 shall be followed. The elimination of any additional minimum liability and corresponding intangible asset shall also occur if the entity elects the transition option reflected in paragraph 93.b.~~

~~[6] Unless otherwise impacted from the provisions within this statement or in accordance with changes to the pension plan, the amortization of the unrecognized items into net periodic pension cost shall continue to follow the existing amortization schedules in effect on the transition date.~~

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iii. Amount necessary to establish a total liability that is equal to any unfunded accumulated benefit obligation (the accumulated benefit obligation less the fair value of plan assets).[7]

94. If the surplus deferral (paragraph 93.b.) is elected at the transition date, subsequently, starting with the 2014 year-end financial statement, the reporting entity shall annually recognize the remaining surplus impact (collectively referred to as the "transition liability"[8]) on a systematic basis over a period not to exceed nine years. The minimum amount recognized each subsequent year shall be an amount that reflects the conditions within paragraph 93.b. Reporting entities that elect the transition option in paragraph 93.b. are permitted to recognize the remaining transition liability, or an amount in excess of the minimum requirement, at any time after the transition date.

95. Reporting entities that elect the transition option in paragraph 93.b. must recognize any remaining transition liability to the extent that the plan reflects a prepaid benefit cost. (For example, if changes in circumstances have resulted with the plan reflecting an overfunded status, the remaining transition liability must be recognized to the extent that the plan is overfunded.) The transition guidance in paragraph 93.b. is not intended (on a net basis for each plan) to result in more favorable, subsequent surplus pension positions when there are remaining unrecognized liabilities as a result of the reporting entity's initial election for surplus deferral. Therefore, if there is a plan curtailment, settlement, or other plan amendment resulting in a reduction of benefit obligations, or net benefit obligation gains due to revisions in assumptions (e.g., discount rates) or plan experience differing from assumptions, or plan asset gains due to the actual return on plan assets exceeding the expected return on plan assets, a corresponding amount of unrecognized liability from the surplus deferral shall be recognized. For this purpose, net gains, if any, are the net aggregation of all gains and losses (excluding plan amendments that increase benefit obligations) from factors such as those listed above, determined as of a measurement or remeasurement date. This shall occur regardless if the impact from the change results with the plan being in an overfunded state, or whether the gain is recognized in earnings. The transition guidance was to provide surplus relief from the immediate surplus impact from adopting SSAP No. 102, but in no instance should changes (on a net basis for each plan) attributed to pension plans result in more favorable, subsequent surplus positions when there are unrecognized liabilities remaining as a result of the reporting entity's initial election for surplus deferral. The guidance in this paragraph was originally contained within *INT 13-03: Clarification of Surplus Deferral in SSAP No. 92 & SSAP No. 102* and was effective December 15, 2013.

96. The transition guidance in paragraphs 92-95 is specific to the transition surplus impact from initially applying this statement on January 1, 2013. Thus, this transition guidance does not apply to additional liability calculated from subsequent comparison of the fair value of plan assets to the projected benefit obligation, or the impact of subsequent plan amendments.

97. Reporting entities electing to apply the transition guidance in paragraph 93.b. must disclose the full transition surplus impact calculated from applying paragraph 92 in the first quarter statutory financial statements after the transition date and each reporting period thereafter. This disclosure shall include the

[7] The intent of this standard is to ensure that under the deferral option the liability initially recognized for an unfunded plan reflects the minimum liability previously recognized under SSAP No. 89. For any instances in which an additional minimum liability recognized under SSAP No. 89 is greater than the unfunded ABO at transition, an amount equal to the previously recognized additional minimum liability shall be used in determining this component of paragraph 93.b.iii. The deferral option under this standard is not intended to allow a surplus benefit to be recognized at initial transition for an unfunded plan.

[8] If the surplus deferral from paragraph 93.b. is elected, the deferred liability, although comprised of the previous "unrecognized items" shall be collectively referred to as the "transition liability." Although reporting entities will need to continue to track the unrecognized items for amortization into net periodic cost (offset through unassigned funds), reporting entities shall not allocate the recognized surplus impact from transition to these categories. As noted in paragraph 93.b.ii., the minimum amount of liability recognized under the deferral option must cover the annual amortization of the "unrecognized items" into net periodic pension cost to prevent a surplus benefit.

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~~initial "transition liability" calculated under paragraph 92, the annual amortization amount of the "unrecognized items" into net periodic pension cost, the amount of the unfunded accumulated benefit obligation, and the remaining unrecognized transition impact. This disclosure shall include a schedule of the entity's anticipated recognition of the remaining surplus impact over the transition period.~~

~~98.~~92. The requirement to measure plan assets and benefit obligations as of the date of the reporting entity's financial statement year-end is effective for financial statement years beginning January 1, 2014. (The measurement date change will be initially reflected in the December 31, 2014 financial statements.)

~~99.~~93. In order to transition to a fiscal year-end measurement date, the reporting entity shall remeasure plan assets and benefit obligations as of the beginning of the fiscal year that the measurement date provisions are applied. The reporting entity shall use those new measurements to determine the effects of the measurement date change as of the beginning of the fiscal year that the measurement date provisions are applied.

~~100.~~94. The reporting entity shall measure plan assets and benefit obligations as of the beginning of the fiscal year that the measurement date provisions are applied. This would result with the following:

a. Net periodic benefit cost for the period between the measurement date that is used for the immediately preceding fiscal year-end and the beginning of the fiscal year that the measurement date provisions are applied, exclusive of any curtailment or settlement gain or loss, shall be recognized, net of tax, as a separate adjustment of the opening balance unassigned funds (surplus). That is, the pretax amount recognized as an adjustment to unassigned funds (surplus) is the net periodic benefit cost that without a change in measurement date otherwise would have been recognized on a delayed basis during the first interim period for the fiscal year that the measurement date provisions are applied.

b. Any gain or loss arising from a curtailment or settlement between the measurement date that is used for the immediately preceding fiscal year-end and the beginning of the fiscal year that the measurement date provisions are applied shall be recognized in earnings in that period and not as an adjustment to unassigned funds (surplus). This provision prohibits a reporting entity from early application of the measurement date provisions when the reporting entity has issued financial statements for the prior year without recognition of such a settlement or curtailment.

c. Other changes in the fair value of plan assets and the benefit obligations (for example, gains or losses) for the period between the measurement date that is used for the immediately preceding fiscal year-end and the beginning of the fiscal year that the measurement date provisions are applied shall be recognized, net of tax, as a separate adjustment of the opening balance of unassigned funds (surplus) for the fiscal year that the measurement date provisions are applied.

~~101.~~95. Earlier application of the recognition or measurement date provisions is encouraged, however, early applications must be for all of the reporting entity's benefit plans. If early application is elected, the transition date shall reflect the January 1st of the year in which this standard is initially applied. Retrospective application is not permitted.

REFERENCES

Other

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- *SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8*

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Relevant Issue Papers

- *Issue Paper No. 8—Accounting for Pensions*
- *Issue Paper No. 123—Accounting for Pensions, A Replacement of SSAP No. 8*
- *Issue Paper No. 132—Accounting for Pensions, A Replacement of SSAP No. 89*

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~~EXHIBIT A - IMPLEMENTATION GUIDE~~

~~*Note: After transition, new "unrecognized" amounts will be reflected in the year-end funded status, but not yet reflected in unassigned funds. Therefore, additional entries will be needed at the end of each year to recognize these new "unrecognized" amounts in unassigned funds. (An example includes gains and losses that will be included in unassigned funds (surplus), but not recognized in net periodic pension cost if they do not exceed 10% of the greater of the projected benefit obligation or the fair value of plan assets.) The entries in the implementation guide focus on the transition impact, and subsequent entries for "unrecognized" items have not been included within the illustrations.*~~

~~Transition Implementation~~

~~1. Overfunded Plan with Prepaid Benefit Cost~~

~~*Consideration of contributions or tax effects are not reflected in this example.*~~

~~Example 1~~	~~Dec. 31, 2012~~	~~Jan. 1, 2013~~
~~Accumulated Benefit Obligation~~	~~$(6,240)~~	~~$(6,240)~~
~~Plus: Non-Vested Liability~~	~~(100)*~~	~~(100)~~
~~Total Accumulated Benefit Obligation~~	~~$(6,340)~~	~~$(6,340)~~
~~Projected Benefit Obligation~~	~~$(6,437)~~	~~$(6,437)~~
~~Plus: Non-Vested Liability~~	~~(100)~~	~~(100)~~
~~Total PBO~~	~~$(6,537)~~	~~$(6,537)~~
~~Plan Assets at Fair Value~~	~~$9,268~~	~~$9,268~~
~~Funded Status~~	~~$2,731~~	~~$2,731~~
~~Transition Obligation / (Asset)~~	~~$36~~	
~~Prior Service Cost~~	~~214~~	

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~~Prior Service Cost (Non-Vested)~~	~~100~~	
~~Unrecognized Losses / (Gains)~~	~~2,465~~	
~~Total Unrecognized Items~~	~~$2,815~~	~~–~~
~~Net Overfunded Plan Asset / (Liability for Benefits)~~	~~$5,546~~	~~$2,731~~

~~*The amount shown for December 31, 2012 reflects the non-vested liability, which must be considered at transition under SSAP No. 102. However, the non-vested liability is not a factor in the December 31, 2012, financial statements under SSAP No. 89.~~

~~Overfunded Plan Asset and Liability for Benefits are terms to reflect the overfunded and unfunded status of the plan. For the amounts shown as of December 31, 2012, immediately prior to the effective date of the new standard, these terms reflect the balance sheet position. As overfunded plan assets are not admitted, these prepaids shall be reflected within Aggregate Write-Ins for Other-Than-Invested Assets. Transition liabilities recognized that have not been reflected through expense shall be reflected within Aggregate Write-Ins for Liabilities.~~

~~1a. January 1, 2013 – Transition Date - Recognize "Unrecognized Items"~~

~~1. Unassigned Funds – Transition Obligation 36~~

~~Unassigned Funds – Prior Service Cost 214~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 100~~

~~Unassigned Funds – Unrecognized Losses 2,465~~

~~Overfunded Plan Asset 2,815~~

~~*(Aggregate Write-Ins for Other-Than-Invested Assets)*~~

~~*For this plan, which is overfunded by more than the unrecognized liabilities, the entry at transition will be netted against the existing prepaid with an offset to unassigned funds.*~~

~~2. Change in Nonadmitted - Overfunded Plan Asset 2,815~~

~~*(Aggregate Write-Ins for Other-Than-Invested Assets)*~~

~~Unassigned Funds 2,815~~

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~~*This entry illustrates the impact to the "change in nonadmitted" as a result of the decline in overfunded plan assets. For this particular example, with the transition entry to unassigned funds and the impact to nonadmitted assets, there is no surplus impact at transition.*~~

~~1b. December 31, 2013 – Recognition of Periodic Pension Cost~~

~~After transition, recognition of net periodic pension cost includes: 1) service cost, 2) interest cost, 3) expected return on plan assets, 4) amortization of prior service cost included in unassigned funds, 5) amortization of gains and losses, and 6) amortization of any transition asset or obligation remaining in unassigned funds.~~

~~*(Per paragraph 93, if surplus deferral is elected at transition, beginning with 2014 annual financials, the entity shall recognize the remaining surplus impact on a systematic basis over a period not to exceed the remaining nine years. As, this illustration is in an overfunded status, there is no surplus deferral. Recognition of net periodic cost, including amortization of the "unrecognized items" will occur each year regardless if surplus deferral is elected.)*~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2013~~
~~Service Cost~~	~~550~~
~~Interest Cost~~	~~150~~
~~Expected Return on Plan Assets~~	~~(250)~~
~~*Total*~~	~~*450*~~
~~Amortization of:~~	
~~○ Transition Obligation~~	~~7.2~~
~~○ Prior Service Cost~~	~~42.8~~
~~○ Prior Service Cost (nonvested)~~	~~20~~
~~○ Unrecognized Losses~~	~~493~~
~~*Total*~~	~~*563*~~

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~~Total Net Periodic Pension Cost~~	~~1,013~~

~~1. Net Periodic Pension Cost 1,013~~

~~Prepaid Benefit Cost 1,013~~

~~*(Aggregate Write-Ins for Other-Than-Invested Assets)*~~

~~*This entry recognizes the periodic pension cost with an offset to the prepaid pension asset. (A prepaid benefit cost is created when cumulative contributions to a pension plan exceed cumulative net periodic pension costs. Thus, a prepaid benefit cost can only be reduced through the recognition of pension cost.)*~~

~~2. Overfunded Plan Asset 563~~

~~*(Aggregate Write-Ins for Other-Than-Invested Assets)*~~

~~Unassigned Funds – Transition Obligation 7.2~~

~~Unassigned Funds – Prior Service Cost 42.8~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 20~~

~~Unassigned Funds – Unrecognized Losses 493~~

~~*This entry recognizes the transition amounts amortized through net periodic pension cost. The offset is to unassigned funds (as unassigned funds was used for the initial recognition of the unrecognized items). As this plan continues to be overfunded, these amounts are offset to overfunded plan assets.*~~

~~3. Change in Nonadmitted - Prepaid Benefit Cost 1,013~~

~~*(Aggregate Write-Ins for Other-Than-Invested Assets)*~~

~~Unassigned Funds 1,013~~

~~*This entry illustrates the impact of the change in nonadmitted prepaid benefit cost to unassigned funds.*~~

~~4. Unassigned Funds 563~~

~~Change in Nonadmitted – Overfunded Plan Asset 563~~

~~*(Aggregate Write-Ins for Other-Than-Invested Assets)*~~

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~~*This entry illustrates the impact of the change in nonadmitted overfunded plan asset to unassigned funds.*~~

~~1c. December 31, 2014 – Recognition of Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2014~~
~~Service Cost~~	~~2500~~
~~Interest Cost~~	~~1000~~
~~Expected Return on Plan Assets~~	~~(500)~~
~~*Total*~~	~~*3000*~~
~~Amortization of:~~	
~~o Transition Obligation~~	~~7.2~~
~~o Prior Service Cost~~	~~42.8~~
~~o Prior Service Cost (nonvested)~~	~~20~~
~~o Unrecognized Losses~~	~~493~~
~~*Total*~~	~~*563*~~
~~Total Net Periodic Pension Cost~~	~~3,563~~

~~*Note – This example was purposely completed to show a significant amount of periodic pension cost to create an underfunded plan status. This was done strictly for illustration purposes and is not intended to indicate that such significant changes would be expected, although they could occur.*~~

~~1. Net Periodic Pension Cost 3,563~~

~~Prepaid Benefit Cost 3,563~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

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~~2. Overfunded Plan Asset 1,282~~

~~Unassigned Funds – Transition Obligation 7.2~~

~~Unassigned Funds – Prior Service Cost 42.8~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 20~~

~~Unassigned Funds – Unrecognized Losses 493~~

~~Liability for Pension Benefits 719~~

~~*(Aggregate Write-In for Other Liabilities)*~~

~~*This entry recognizes the transition amounts that have been recognized through net periodic pension cost, with an offset to unassigned funds. The overfunded plan asset is initially offset, until the plan reaches an unfunded status, which is then reflected through a liability for pension benefits (aggregate write-in for other liabilities).*~~

~~3. Change in Nonadmitted - Prepaid Benefit Cost 3,563~~

~~Unassigned Funds 3,563~~

~~4. Unassigned Funds 1,282~~

~~Change in Nonadmitted - Overfunded Plan Asset 1,282~~

~~*These entries illustrate the impact of the change in nonadmitted to unassigned funds.*~~

~~Illustration 1 – Example Paragraph 97 Note Disclosure:~~

~~SSAP No. 102 became effective January 1, 2013. This SSAP requires that any underfunded defined benefit pension amounts, as determined when the projected benefit obligation exceeds the fair value of plan assets, to be recognized as a liability under SSAP No. 5R. Such liability is required to be reported in the first quarter statutory financial statement after the transition date with a corresponding entry to unassigned funds. The adoption of SSAP No. 102 did not have a surplus impact on ABC entity as the pension plan was overfunded by more than the transition liabilities. At transition, ABC entity recognized $2,815 in unrecognized transition obligations, prior service costs, and unrecognized losses as components of the ending balance of unassigned funds as of January 1, 2013. This recognition resulted in a financial presentation which reflects the actual $2,731 overfunded status of the plan (fair value of plan assets exceeds the projected benefit obligation) as of January 1, 2013. As required under SSAP No. 102, overfunded plan assets are nonadmitted.~~

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~~***For purposes of this example, tax effects are not reflected. However, the amount recognized at transition as components of the unassigned funds shall be net of tax.***~~

~~**The following provides the status of the pension plan as of December 31, 2012, and the transition date (January 1, 2013):**~~

~~Example 1~~	~~Dec. 31, 2012~~	~~Jan. 1, 2013~~
~~Accumulated Benefit Obligation~~	~~$(6,240)~~	~~$(6,240)~~
~~Plus: Non-Vested Liability~~	~~(100)~~	~~(100)~~
~~Total Accumulated Benefit Obligation~~	~~$(6,340)~~	~~$(6,340)~~
~~Projected Benefit Obligation~~	~~$(6,437)~~	~~$(6,437)~~
~~Plus: Non-Vested liability~~	~~(100)~~	~~(100)~~
~~Total PBO~~	~~$(6,537)~~	~~$(6,537)~~
~~Plan Assets at Fair Value~~	~~$9,268~~	~~$9,268~~
~~Funded Status~~	~~$2,731~~	~~$2,731~~
~~Transition Obligation / (Asset)~~	~~$36~~	
~~Prior Service Cost~~	~~214~~	
~~Prior Service Cost (Non-Vested)~~	~~100~~	
~~Unrecognized Losses / (Gains)~~	~~2,465~~	
~~Total Unrecognized Items~~	~~$2,815~~	~~–~~
~~Net Overfunded Plan Asset / (Liability for Benefits)~~	~~$5,546~~	~~$2,731~~

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~~In the March 31, 2013, financial statements, the $2,731 overfunded plan assets was reflected as follows:~~

- ~~Prepaid Benefit Cost $5,546 (nonadmitted)~~
- ~~Overfunded Plan Asset $(2,815) (nonadmitted)~~

~~These amounts are reported net in Aggregate Write-Ins for Other-Than-Invested Assets: $2,731~~

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~~Illustration of Example 1 – Overfunded Plan with Prepaid Benefit Cost~~

	~~Aggregate Write-In for Other-Than-Invested Assets~~		~~Nonadmitted Assets~~	~~Unassigned Funds~~	~~Periodic Pension Cost~~	~~Aggregate Write-In for Other Liabilities~~
	~~Prepaid Benefit Cost~~	~~Overfunded Plan Asset~~				
~~Existing Balances 12/31/2012~~	~~5,546DR~~		~~5,546CR~~			
~~Transition Entries – 1/1/2013~~						
~~A~~		~~2,815CR~~		~~2,815DR~~		
~~B~~			~~2,815DR~~	~~2,815CR~~		
~~After Transition~~	~~5,546DR~~	~~2,815CR~~	~~2,731CR~~	~~–~~		
~~After Transition - Net~~	~~2,731DR~~		~~2,731CR~~	~~–~~		
~~A – Recognize "unrecognized items" existing at 1/1/13 transition date (gains or losses, prior service costs or credits, and transition assets or obligations). For this plan, which is overfunded by more than the unrecognized liabilities, the entry at transition will be netted against the existing overfunded plan asset with an offset to unassigned funds.~~						
~~B – Illustrates the impact to the "change in nonadmitted" as a result of the decline in overfunded plan assets. For this particular example, with the transition entry to unassigned funds and the impact to nonadmitted assets, there is no surplus impact at transition. At transition, the net balance in aggregate write-ins reflects the overfunded state of the plan.~~						
~~Recognition of Net Periodic Pension Cost – 12/31/2013~~						
~~C~~	~~1,013CR~~				~~1,013DR~~	~~———~~
~~D~~		~~563DR~~		~~563CR~~		
~~E~~			~~1,013DR~~	~~1,013CR~~		
~~F~~			~~563CR~~	~~563DR~~		
~~Net Impact~~	~~450CR~~		~~450DR~~	~~1,013CR~~	~~1,013DR~~	
~~Ending~~	~~4,533 DR~~	~~2,252CR~~	~~2,281CR~~	~~1,013CR~~	~~1,013DR~~	
~~Ending Balances-Net~~	~~2,281DR~~		~~2,281CR~~	~~–~~		
~~C – Reflects the periodic pension cost with an offset to the prepaid pension asset.~~						

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~~D – Recognizes the transition amounts amortized through net periodic pension cost. The offset it to unassigned funds (as that was how the "unrecognized items" were recognized at transition).~~

~~E/F – Reflects the change in nonadmitted assets to unassigned funds.~~

~~Recognition of Net Periodic Pension Cost – 12/31/2014~~

~~G~~	~~3,563CR~~				~~3,563DR~~	
~~H~~		~~1,282DR~~		~~563CR~~		~~719CR~~
~~I~~			~~3,563DR~~	~~3,563CR~~		
~~J~~			~~1,282CR~~	~~1,282DR~~		
~~Net Impact~~	~~2,281CR~~		~~2,281DR~~	~~2,844CR~~	~~3,563DR~~	~~719CR~~
~~Ending Balances~~	~~970 DR~~	~~970 CR~~	~~–~~	~~2,844CR~~	~~3,563DR~~	
~~Ending Balances - Net~~	~~–~~		~~–~~	~~719DR~~		~~719CR~~

~~G/H – Reflects the periodic pension cost with an offset to the prepaid pension asset. As no contributions have been made, the 2014 pension cost moves the plan from an overfunded to underfunded state. The overfunded plan asset credit is reduced to equally offset the remaining prepaid benefit cost of $970. The underfunded status is then reflected through a liability for pension benefits (aggregate write-in for other liabilities).~~

~~I/J – Reflects the change in nonadmitted assets to unassigned funds.~~

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~~2. Underfunded Plan with Accrued Benefit Cost~~

~~*Consideration of contributions or tax effects are not reflected in this example.*~~

~~Example 2~~	~~Dec. 31, 2012~~	~~Jan. 1, 2013~~
~~Accumulated Benefit Obligation~~	~~$(2,015)~~	~~$(2,015)~~
~~Plus: Non-Vested Liability~~	~~(60)*~~	~~(60)~~
~~Total Accumulated Benefit Obligation~~	~~$(2,075)~~	~~$(2,075)~~
~~Projected Benefit Obligation~~	~~$(2,268)~~	~~$(2,268)~~
~~Plus: Non-Vested Liability~~	~~(60)~~	~~(60)~~
~~Total PBO~~	~~$(2,328)~~	~~$(2,328)~~
~~Plan Assets at Fair Value~~	~~$1,992~~	~~$1,992~~
~~Funded Status~~	~~$(336)~~	~~$(336)~~
~~Transition Obligation / (Asset)~~	~~$(544)~~	
~~Prior Service Cost / (Credit)~~	~~(494)~~	
~~Prior Service Cost (Non-Vested)~~	~~60~~	
~~Unrecognized Losses / (Gains)~~	~~926~~	
~~Total Unrecognized Items~~	~~$(52)~~	~~–~~
~~Net Overfunded Plan Asset / (Liability for Benefits)~~	~~$(388)~~	~~$(336)~~

~~*The amount shown for December 31, 2012, reflects the non-vested liability, which must be considered at transition under SSAP No. 102. However, the non-vested liability is not a factor in the December 31, 2012, financial statements under SSAP No. 89.~~

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~~*Overfunded Plan Asset and Liability for Benefits are terms to reflect the overfunded and underfunded status of the plan. For the amounts shown as of December 31, 2012, immediately prior to the effective date of the new standard, these terms reflect the balance sheet position. As overfunded plan assets are not admitted, these prepaids shall be reported within Aggregate Write-Ins for Other-Than-Invested Assets. Transition liabilities recognized that have not been reflected through expense shall be reported within Aggregate Write-Ins for Liabilities.*~~

~~2a. January 1, 2013 – Transition Date - Recognize "Unrecognized Items"~~

~~1. Liability for Pension Benefits 52~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 60~~

~~Unassigned Funds – Unrecognized Losses 926~~

~~Unassigned Funds – Transition Asset 544~~

~~Unassigned Funds – Prior Service Credit 494~~

~~*For this plan, which is underfunded but has a net unrecognized asset, at transition the entity will improve their surplus presentation by $52 through a contra-liability. Use of the contra-liability is necessary, as if the item were recorded as an asset, it would be nonadmitted and result in a surplus reduction. Although there is a net unrecognized asset, this plan is in an underfunded state.*~~

~~2b. December 31, 2013 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2012~~
~~Service Cost~~	~~250~~
~~Interest Cost~~	~~100~~
~~Expected Return on Plan Assets~~	~~(50)~~
~~*Total*~~	~~*300*~~
~~Amortization of:~~	
~~o Transition Obligation (Asset)~~	~~(272)~~

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~~o Prior Service Cost / (Credit)~~	~~(247)~~
~~o Prior Service Cost (nonvested)~~	~~30~~
~~o Unrecognized Losses~~	~~463~~
~~*Total*~~	~~*(26)*~~
~~Total Net Periodic Pension Cost~~	~~274~~

~~1. Unassigned Funds – Transition Asset 272~~

~~Unassigned Funds – Prior Service Credit 247~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 30~~

~~Unassigned Funds – Unrecognized Losses 463~~

~~Liability for Pension Benefits 26~~

~~*(Aggregate Write-In for Liabilities)*~~

~~*This entry occurs to amortize the transition items. Due to the nature of the unrecognized items (net asset – recorded as a contra-liability), this entry reverses the original entry to remove the portion that will be amortized into periodic pension cost for the current period.*~~

~~2. Net Periodic Pension Cost 274~~

~~Accrued Benefit Cost 274~~

~~*This entry recognizes the net periodic pension cost for the service cost, interest cost, expected return on plan assets and the amortization of the unrecognized items.*~~

~~Note: All references to "accrued benefit cost" represent an unpaid expense liability, these amounts wills be reflected within general expenses due and accrued (life) or LAE/Other Underwriting expenses (p/c).~~

~~Note: This example uses a 2-year amortization period of the "unrecognized items." In actuality, amortization periods of each item will vary. Disclosures shall continue to separately present these items.~~

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~~2c. December 31, 2014 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2014~~
~~Service Cost~~	~~2500~~
~~Interest Cost~~	~~1000~~
~~Expected Return on Plan Assets~~	~~(500)~~
~~*Total*~~	~~*3,000*~~
~~Amortization of:~~	
~~○ Transition Obligation / (Asset)~~	~~(272)~~
~~○ Prior Service Cost / (Credit)~~	~~(247)~~
~~○ Prior Service Cost (nonvested)~~	~~30~~
~~○ Unrecognized Losses~~	~~463~~
~~*Total*~~	~~*(26)*~~
~~Total Net Periodic Pension Cost~~	~~2,974~~

~~1. Unassigned Funds – Transition Asset 272~~

~~Unassigned Funds – Prior Service Credit 247~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 30~~

~~Unassigned Funds – Unrecognized Losses 463~~

~~Liability for Pension Benefits 26~~

~~*(Aggregate Write-In for Liabilities)*~~

~~*This entry occurs to amortize the transition items. Due to the nature of the unrecognized items (net asset – recorded as a contra-liability), this entry reverses the original entry to remove the portion that will be amortized into periodic pension cost for the current period.*~~

~~2. Net Periodic Pension Cost 2,974~~

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~~Accrued Benefit Cost 2,974~~

~~*This entry recognizes the net periodic pension cost for the service cost, interest cost, expected return on plan assets and the amortization of the unrecognized items.*~~

~~Illustration 2 – Paragraph 97 Example Note Disclosure:~~

~~SSAP No. 102 became effective January 1, 2013. This SSAP requires that any underfunded defined benefit pension amounts, as determined when the projected benefit obligation exceeds the fair value of plan assets, to be recognized as a liability under SSAP No. 5R. Such liability is required to be reported in the first quarter statutory financial statement after the transition date with a corresponding entry to unassigned funds. At transition, ABC entity recognized a net $52 asset from unrecognized transition obligations/assets, prior service costs/credits, and unrecognized gains/losses as a component of the ending balance of unassigned funds as of January 1, 2013. This net impact was reflected as a contra-liability as the plan is in an underfunded state.~~

~~***For purposes of this example, tax effects are not reflected. However, the amount recognized at transition as components of the unassigned funds shall be net of tax.*~~

~~The following provides the status of the pension plan as of December 31, 2012, and the transition date (January 1, 2013):~~

~~Example 2~~	~~Dec. 31, 2012~~	~~Jan. 1, 2013~~
~~Accumulated Benefit Obligation~~	~~$(2,015)~~	~~$(2,015)~~
~~Plus: Non-Vested Liability~~	~~(60)~~	~~(60)~~
~~Total Accumulated Benefit Obligation~~	~~$(2,075)~~	~~$(2,075)~~
~~Projected Benefit Obligation~~	~~$(2,268)~~	~~$(2,268)~~
~~Plus: Non-Vested Liability~~	~~(60)~~	~~(60)~~
~~Total PBO~~	~~$(2,328)~~	~~$(2,328)~~
~~Plan Assets at Fair Value~~	~~$1,992~~	~~$1,992~~

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Funded Status	$(336)	$(336)
Transition Obligation / (Asset)	$(544)	
Prior Service Cost / (Credit)	(494)	
Prior Service Cost (Non-Vested)	60	
Unrecognized Losses / (Gains)	926	
Total Unrecognized Items	$(52)	–
Net Overfunded Plan Asset / (Liability for Benefits)	$(388)	$(336)

In the March 31, 2013, financial statements, underfunded pension obligations were reflected as follows:

- Accrued Benefit Cost - $388
- Liability for Pension Benefits (Aggregate Write-In for Liabilities) - ($52)

Illustration of Example 2 – Underfunded Plan with Accrued Benefit Cost

	Net Periodic Cost (Expense Recognition)	Unassigned	Aggregate Write-In	
Existing Balance – 12/31/2012		388DR		388CR
Transition Entries – 1/1/2013				
A		52CR	52DR	
After Transition		336DR	52DR	388CR
A. Recognize "unrecognized" items at transition. The above entry reflects the "net" impact, resulting with an unrecognized net asset (contra-liability) and an increase to the surplus presentation. (This unrecognized net asset is reflected as a contra-liability as it does not reflect a prepaid for the overfunding of plan assets. If this was reflected as an asset, it would be nonadmitted.)				

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~~Recognition of Net Periodic Pension Cost – 12/31/2013~~				
~~B~~ ~~C~~	 ~~274 DR~~	~~26 DR~~	~~26 CR~~	 ~~274 CR~~
~~B. Entry amortizes the transition items (entry is shown net.) Due to the nature of the unrecognized items, (net asset, recorded as a contra-liability), this entry reverses the original entry to remove the portion that will be amortized into net periodic pension cost for the current period.~~ ~~C. Entry recognizes the net periodic pension cost, interest cost, expected return on plan assets, and the amortization of the unrecognized items.~~				
~~Recognition of Net Periodic Pension Cost – 12/31/2014~~				
~~D~~ ~~E~~	 ~~2,974 DR~~	~~26 DR~~	~~26 CR~~	 ~~2,974 CR~~
~~D. Entry occurs to amortize the transition items (entry is shown net). Due to the nature of the unrecognized items, (net asset, recorded as a contra-liability), this entry reverses the original entry to remove the portion that will be amortized into net periodic pension cost for the current period.~~ ~~E. Entry recognizes net periodic pension cost the service cost, interest cost, expected return on plan assets and the amortization of the unrecognized items.~~				

~~3. Underfunded Plan with Accrued Benefit Cost with Surplus Deferral Elected~~

~~*Consideration of contributions or tax effects are not reflected in this example.*~~

~~Example 3~~	~~Dec. 31, 2012~~	~~Jan. 1, 2013~~
~~Accumulated Benefit Obligation~~	~~$(1,819)~~	~~$(1,819)~~
~~Plus: Non-Vested Liability~~	~~(103)*~~	~~(103)~~
~~Total Accumulated Benefit Obligation~~	~~$(1,922)~~	~~$(1,922)~~

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~~Projected Benefit Obligation~~	~~$(2,099)~~	~~$(2,099)~~
~~Plus: Non-Vested Liability~~	~~(103)~~	~~(103)~~
~~Total PBO as of January 1, 2012~~	~~$(2,202)~~	~~$(2,202)~~
~~Plan Assets at Fair Value~~	~~$0~~	~~$0~~
~~Funded Status~~	~~$(2,202)~~	~~$(2,202)~~
~~Transition Obligation / (Asset)~~	~~$0~~	
~~Prior Service Cost~~	~~0~~	
~~Prior Service Cost (Non-Vested)~~	~~103~~	
~~Unrecognized Losses / (Gains)~~	~~440~~	
~~Total Unrecognized Items~~	~~543~~	~~–~~
~~Net Overfunded Plan Asset / (Liability for Benefits)~~	~~$(1,659)~~	~~$(1,922)~~

~~* The amount shown for December 31, 2012, reflects the non-vested liability, which must be considered at transition under SSAP No. 102. However, the non-vested liability is not a factor in the December 31, 2012, financial statements under SSAP No. 89.~~

~~*Overfunded Plan Asset and Liability for Benefits are terms to reflect the overfunded and underfunded status of the plan. For the amounts shown as of December 31, 2012, immediately prior to the effective date of the new standard, these terms reflect the balance sheet position. As overfunded plan assets are not admitted, these prepaids shall be reflected within Aggregate Write-Ins for Other-Than-Invested Assets. Transition liabilities recognized that have not been reflected through expense shall be reflected within Aggregate Write-Ins for Liabilities.*~~

~~*As illustrated above, the liability for pension benefits as of January 1, 2013, does not equal the underfunded plan status as the entity elected the transition deferral. Rather, the liability for pension benefits equals, at a minimum, the accumulated benefit obligation (ABO) less the plan asset at fair value. (Minimum transition liability that equals the ABO is required in accordance with paragraph 93.) After the transition period, the net overfunded plan asset / (liability for benefits) should equal the funded status of the plan.*~~

~~3a. January 1, 2013 – Transition Date - Recognize "Unrecognized Items"~~

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~~In accordance with paragraph 93, the surplus impact initially recognized as of January 1, 2013 under the transition option, and subsequently over the transition period, shall be the greater of:~~

	~~Minimum Transition Liability~~	
~~93.b.i.~~	~~10% of Calculated Surplus Impact~~	~~54.3~~
~~93.b.ii.~~	~~Anticipated Annual Amortization of "Unrecognized Items" (Assumes 5-year Uniform Amortization)~~	~~108.6~~
~~93.b.iii.~~	~~Difference Between ABO and Accrued Benefit Cost~~	~~263~~
	~~Transition Liability~~	~~263~~

~~*Note: Amortization of the unrecognized items (paragraph 93.b.ii.) may not be determinable at transition. If the amortization amount that will be recognized year-end 2013 is unknown at the transition date, at a minimum, the amount amortized for "unrecognized items" during the prior year shall be utilized for the component in paragraph 93.b.ii. of the minimum transition liability. If the amount recognized for transition (greater of all three components in paragraph 93.b.) is subsequently determined to be less than what is amortized for the year (paragraph 93.b.ii.), the difference between what was recognized for transition, and what is amortized must immediately be recognized as an adjustment to the transition impact to unassigned funds – surplus.)*~~

~~January 1, 2013 – Transition Date:~~

~~*Reversal of Additional Minimum Liabilities/Intangible Plan Assets*: As this plan has an unfunded ABO, following the guidance under SSAP No. 89, the entity had recognized an additional minimum liability and corresponding admitted intangible asset. As the concept of an additional minimum liability has been eliminated from SSAP No. 102, at transition these amounts are eliminated, with the determination of the overfunded/unfunded projected benefit obligation calculated subsequent to the elimination.~~

~~Balances as of 12/31/2012 under SSAP No. 89:~~

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~~Accumulated Benefit Obligation: $1,819~~

~~Accrued Liability: $1,659~~

~~SSAP No. 89 Additional Minimum Liability: $160~~

~~SSAP No. 89 Admitted Intangible Asset: $160~~

~~Unassigned Funds 160~~

~~Intangible Asset 160~~

~~Additional Minimum Liability 160~~

~~Unassigned Funds 160~~

~~*Application of SSAP No. 102 – Recognition of Unfunded Status with Surplus Deferral:*~~

~~1. Unassigned Funds – Transition Liability 263~~

~~Liability for Pension Benefits 263~~

~~*(Aggregate Write-In for Liabilities)*~~

~~*This entry represents the minimum transition liability required to be recognized at the transition date. As noted within the transition guidance, an entity may elect to transition the surplus impact over a period not to exceed 10 years. Paragraph 93 provides the specifications on the minimum liability recognized at transition. As this transition liability amount has yet to be recognized through expense (periodic cost), the liability is reflected through "aggregate write-ins for liabilities."*~~

~~3b. December 31, 2013 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2013~~
~~Service Cost~~	~~250~~
~~Interest Cost~~	~~100~~
~~Expected Return on Plan Assets~~	~~(50)~~

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~~*Total*~~	~~*300*~~
~~Amortization of:~~	
~~○ Prior Service Cost (nonvested)~~	~~20.6~~
~~○ Unrecognized Losses~~	~~88~~
~~*Total*~~	~~*108.6*~~
~~Total Net Periodic Pension Cost~~	~~408.6~~

~~1. Liability for Pension Benefits 108.6~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 20.6~~

~~Unassigned Funds – Unrecognized Losses 88~~

~~*This entry occurs prior to amortization of the transition items. This entry reverses a portion of the original transition entry for the amount that will be amortized into periodic pension cost for the current period.*~~

~~2. Net Periodic Pension Cost 408.6~~

~~Accrued Benefit Cost 408.6~~

~~*This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the unrecognized items.*~~

~~Note: Although the entity elected the transition option for surplus deferral, and the guidance allows up to 10 years for deferral, an entity must continue to recognize a minimum amount of the transition liability as determined in accordance with paragraph 93.b. This requires the entity to recognize an amount that is at the greater of either 10% of the initial surplus impact or the amortization of the unrecognized items in effect at transition.~~

~~In this example, the entity will only receive a 3-year deferral – This illustration assumes 5-year uniform amortization of the transition amounts into expense for illustration purposes only. In practice, the minimum transition liability amounts may not be determinable until the expense is calculated in each future year:~~

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~~Surplus Impact at Transition~~		~~Prior Service Cost~~	~~Unrealized Losses~~	
~~Transition Liability:~~	~~543~~	~~103~~	~~440~~	
~~Amount Recognized Jan. 1, 2013~~	~~(263)~~			
~~Remaining Transition Liability~~	~~280~~			
				~~Remaining~~
~~Minimum Transition Liability:~~		~~Anticipated Amortization:~~		~~Transition Liability~~
~~2014~~	~~108.6~~	~~20.6~~	~~88~~	~~171.4~~
~~2015~~	~~108.6~~	~~20.6~~	~~88~~	~~62.8~~
~~2016~~	~~62.8~~	~~12~~	~~50.8~~	~~–~~

~~3c. December 31, 2014 – Recognition of Transition Liability:~~

~~1. Unassigned Funds – Transition Liability 108.6~~

~~Liability for Pension Benefits 108.6~~

~~*(Aggregate Write-In for Liabilities)*~~

~~*This entry represents the minimum transition liability required to be recognized at the subsequent date.*~~

~~3d. December 31, 2014 – Recognition of Net Periodic Benefit Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2014~~
~~Service Cost~~	~~50~~
~~Interest Cost~~	~~30~~
~~Expected Return on Plan Assets~~	~~(35)~~

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~~*Total*~~	~~*45*~~
~~Amortization of:~~	
~~o Prior Service Cost (nonvested)~~	~~20.6~~
~~o Unrecognized Losses~~	~~88~~
~~*Total*~~	~~*108.6*~~
~~Total Net Periodic Pension Cost~~	~~153.6~~

~~1. Liability for Pension Benefits 108.6~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 20.6~~

~~Unassigned Funds – Unrecognized Losses 88~~

~~2. Net Periodic Pension Cost 153.6~~

~~Accrued Benefit Cost 153.6~~

~~*This entry illustrates the December 2014 entries. The first removes the liability recognized for transition so that it could be recycled through expense, with the second recognizing net periodic cost (including the amortization of the unrecognized items.)*~~

~~3e. December 31, 2015 – Activity within the pension plan has resulted with an overfunded plan.~~

~~As required under paragraph 93, if the fair value of plan assets had changed so that the plan was in an overfunded status, the transition liability would also be impacted with accelerated recognition to the extent the plan is in an overfunded status:~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2015~~
~~Service Cost~~	~~100~~
~~Interest Cost~~	~~75~~

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~~Expected Return on Plan Assets~~	~~(50)~~
~~*Total*~~	~~*125*~~
~~Amortization of:~~	
~~○ Prior Service Cost (nonvested)~~	~~20.6~~
~~○ Unrecognized Losses~~	~~88~~
~~*Total*~~	~~*108.6*~~
~~Total Net Periodic Pension Cost~~	~~233.6~~

~~Recognition of Remaining Transition Liability and Net Periodic Pension Cost:~~

~~1. Unassigned Funds – Transition Liability 171.40~~

~~Liability for Pension Benefits 171.40~~

~~*(Aggregate Write-In for Liabilities)*~~

~~*This entry illustrates the immediate recognition of the remaining transition liability*~~

~~2. Liability for Pension Benefits 108.6~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Prior Service Cost (Nonvested) 20.6~~

~~Unassigned Funds – Unrecognized Losses 88~~

~~*This entry reflects the amortization into net periodic pension cost of the "unrecognized items" within unassigned funds. Amortization has not changed with the recognition of the remaining transition liability.*~~

~~3. Net Periodic Pension Cost 233.60~~

~~Accrued Benefit Cost 233.60~~

~~*Recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets, and the amortization of unrecognized items.*~~

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4. Accrued Benefit Cost 2,456

Prepaid Benefit Cost 844

(Aggregate Write-In – Assets)

Cash – Contribution 3,300

This entry recognizes the cash contribution, the elimination of the accrued benefit cost and the establishment of the prepaid benefit cost from the contribution.

5. Liability for Pension Benefits 217

Overfunded Plan Asset 217

Since the plan is now in a net overfunded status, the liability for pension benefits is reduced to zero, and offset to the overfunded pension asset (contra-asset).

6. Unassigned Funds (Change in Nonadmitted) 844

Prepaid Benefit Cost (Nonadmitted) 844

This entry recognizes the prepaid benefit cost that is nonadmitted and the underlying impact on unassigned funds.

7. Overfunded Plan Asset (Nonadmitted) 217

Unassigned Funds (Change in Nonadmitted) 217

This entry illustrates the impact of the change in nonadmitted overfunded plan asset to unassigned funds.

Example 3 - Comprehensive Illustration

Consideration of contributions or tax effects are not reflected in the example.

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~~Underfunded Plan With Accrued Benefit Cost - Surplus Deferral Elected~~

		~~12/31/2012~~	~~1/1/2013~~	~~12/31/2013~~	~~12/31/2014~~	~~12/31/2015~~
~~ABO~~		~~(1,819)~~	~~(1,819)~~	~~(2,019)~~	~~(2,049)~~	~~(2,079)~~
~~Non-Vested Liability~~		~~(103)~~	~~(103)~~	~~(103)~~	~~(103)~~	~~(103)~~
~~Total ABO~~	~~A~~	~~(1,922)~~	~~(1,922)~~	~~(2,122)~~	~~(2,152)~~	~~(2,182)~~
~~PBO~~	~~B~~	~~(2,099)~~	~~(2,099)~~	~~(2,399)~~	~~(2,444)~~	~~(2,569)~~
~~Non-Vested Liability~~	~~C~~	~~(103)~~	~~(103)~~	~~(103)~~	~~(103)~~	~~(103)~~
~~Total PBO~~	~~D~~	~~(2,202)~~	~~(2,202)~~	~~(2,502)~~	~~(2,547)~~	~~(2,672)~~
~~Plan Assets at Fair Value~~	~~E~~	~~–~~	~~–~~	~~–~~	~~–~~	~~3,300~~
~~Funded Status~~	~~F~~	~~(2,202)~~	~~(2,202)~~	~~(2,502)~~	~~(2,547)~~	~~628~~
~~*Items Not Recognized in Unassigned Funds*~~						
~~Transition Obligation (Asset)~~		~~–~~	~~–~~	~~–~~	~~–~~	~~–~~
~~Prior Service Cost~~		~~–~~	~~–~~	~~–~~	~~–~~	~~–~~
~~Prior Service Cost Non-Vested~~	~~G~~	~~103~~	~~–~~	~~–~~	~~–~~	~~–~~
~~Unrecognized Losses (Gains)~~	~~H~~	~~440~~	~~–~~	~~–~~	~~–~~	~~–~~
~~Total Unrecognized Items~~	~~I~~	~~543~~	~~–~~	~~–~~	~~–~~	~~–~~
~~Transition Items - Aggregate WI~~	~~J~~		~~(263)~~		~~(109)~~	~~(171)~~
~~Unassigned Funds - Transition~~	~~K~~			~~109~~	~~109~~	~~109~~
~~Periodic Pension Cost~~	~~L~~			~~(300)~~	~~(45)~~	~~(125)~~
~~Periodic Pension Cost - Amort.~~	~~M~~			~~(109)~~	~~(109)~~	~~(109)~~
~~Contribution~~	~~N~~		~~–~~	~~–~~	~~–~~	~~3,300~~
~~Overfunded Plan Asset~~	~~O~~	~~(1,659)~~	~~(1,922)~~	~~(2,222)~~	~~(2,376)~~	~~628~~
~~(Liability for Benefits)~~						
~~Unrecognized Transition Items~~	~~P~~		~~(280)~~	~~(280)~~	~~(171)~~	~~–~~

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Funded Status	Q		(2,202)	(2,502)	(2,547)	628
Liability Reported Beg of Year	R		(1,659)	(1,922)	(2,222)	(2,375)
Recognized Transition Items	S		(263)		(109)	(171)
Unassigned Funds	T			109	109	109
Net Periodic Pension Cost	U		–	(409)	(154)	(235)
Contribution	V		–	–		3,300
Accrued/Prepaid End of Year	W	(1,659)	(1,922)	(2,222)	(2,375)	628
Unrecognized Items	X		(280)	(280)	(171)	0
Funded Status	Y		(2,202)	(2,502)	(2,547)	628
Reporting Lines:	-					
Accrued Benefit Cost	Z	1,659	1,659	2,068	2,221	0
Aggregate WI – Net Asset	AA					628
Aggregate WI - Liability	BB		263	154	154	0
Total Liability/(Asset) Reported	CC	1,659	1,922	2,222	2,376	(628)
Unfunded/(Overfunded) Status	DD		2,202	2,502	2,547	(628)
Liability Not Reported	EE		280	280	171	0

Underfunded Plan with Accrued Benefit Cost - Surplus Deferral Elected

Jan. 1, 2013 - Transition

Entry A - Recognize Minimum Transition Liability

Unassigned Funds 263

Liability for Pension Benefits 263

(Aggregate Write-In for Liabilities)

Dec. 31, 2013 - Recognize Periodic Pension Cost

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~~*Entry A - Reverses portion of transition entry for the amount that will be amortized into periodic cost for the period.*~~

~~Liability for Pension Benefits 109~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds 109~~

~~*Entry B - Recognize net periodic cost*~~

~~Net Periodic Cost 409~~

~~Accrued Benefit Cost 409~~

~~Dec. 31, 2014 - Recognize Transition and Periodic Pension Cost~~

~~*Entry A - Recognize transition liability*~~

~~Unassigned Funds 109~~

~~Liability for Pension Benefits 109~~

~~*(Aggregate Write-In for Liabilities)*~~

~~*Entry B - Reverses portion of transition entry for the amount that will be amortized into periodic cost for the period.*~~

~~Liability for Pension Benefits 109~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds 109~~

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Entry C - Recognize net periodic cost

Net Periodic Cost	154	
Accrued Benefit Cost		154

Dec. 31, 2015 - Recognize Transition and Periodic Pension Cost

Entry A - Recognize transition liability

Unassigned Funds	171	
Liability for Pension Benefits		171
(Aggregate Write-In for Liabilities)		

Entry B - Reverses portion of transition entry for the amount that will be amortized into periodic cost for the period.

Liability for Pension Benefits	109	
(Aggregate Write-In for Liabilities)		
Unassigned Funds		109

Entry C - Recognize net periodic cost

Net Periodic Cost	234	
Accrued Benefit Cost		234

Entry D - Recognize Cash Contribution

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Accrued Benefit Cost	2,456	
Prepaid Benefit Cost	844	
(Aggregate Write-In Assets)		
Cash Contribution		3,300

Entry E – Reduce Liability to Zero and Record Overfunded Plan Asset

Liability for Pension Benefits	217	
Overfunded Plan Asset		217

Entry F – Recognize Nonadmitted Asset – Prepaid Benefit Cost

Unassigned Funds	844	
(Change in Nonadmitted)		
Prepaid Benefit Cost (Nonadmitted)		844

Entry G – Recognize Nonadmitted Asset – Overfunded Plan Asset

Overfunded Plan Asset (Nonadmitted)	217	
Unassigned Funds (Change in Nonadmitted)		217

Illustration 3 – Paragraph 97 Example Note Disclosure – March 31, 2013:

SSAP No. 102 became effective January 1, 2013. This SSAP requires that any underfunded defined benefit pension amounts, as determined when the projected benefit obligation exceeds the fair value of plan assets, to be recognized as a liability under SSAP No. 5R. Such liability is required to be reported in the first quarter statutory

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~~financial statement after the transition date with a corresponding entry to unassigned funds. ABC entity elected to utilize the minimum transition option reflected in paragraph 93 of SSAP No. 102. The SSAP requires initial transition liability to be the greater of paragraphs 93.b.i, 93.b.ii., and 93.b.iii.:~~

	~~Minimum Transition Liability~~	
~~93.b.i.~~	~~10% of Calculated Surplus Impact~~	~~54.3~~
~~93.b.ii.~~	~~Annual Amortization of "Unrecognized Items"~~ ~~(Assumes 5-year Uniform Amortization)~~	~~108.6~~
~~93.b.iii.~~	~~Difference Between ABO and Accrued Benefit Cost~~	~~263~~
	~~Minimum Transition Liability~~	~~263~~

~~*Note - Amortization of the unrecognized items (paragraph 93.b.ii.) may not be determinable at transition. If the amortization amount that will be recognized year-end 2013 is unknown at the transition date, at a minimum, the amount amortized for "unrecognized items" during the prior year shall be utilized for the component in paragraph 93.b.ii. of the minimum transition liability. If the amount recognized for transition (greater of all three components in paragraph 93.b.) is subsequently determined to be less than what is amortized for the year (paragraph 93.b.ii.), the difference between what was recognized for transition, and what is amortized must immediately be recognized as an adjustment to the transition impact to unassigned funds – surplus.*~~

~~Although the entity elected the transition option for surplus deferral, and SSAP No. 102 allows up to 10 years for deferral, an entity must continue to recognize a minimum amount of the transition liability as determined in accordance with paragraph 93.b. This requires the entity to recognize each year an amount that is at least equal to the amortization of the unrecognized items in effect at transition. Although the amortization of the transition items into future expenses (paragraph 93.b.ii.) may not be fully determinable at the time of transition (as they are dependent on the future expense calculations), the reporting entity anticipates that the remaining $280 surplus impact from the election of the transition deferral in SSAP No. 102 will be recognized over a 3-year* period.~~

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~~* This is a reporting entity projection and may be revised based on future expenses and activity.~~

~~Recognized Surplus Impact at Transition & Remaining Transition Liability~~		~~Prior Service Cost~~	~~Unrealized Losses~~
~~Transition Liability:~~	~~543~~	~~103~~	~~440~~
~~Amount Recognized Jan. 1, 2013~~	~~(263)~~		
~~Remaining Transition Liability~~	~~280~~		

~~The following provides the status of the pension plan as of December 31, 2012, and the transition date (January 1, 2013):~~

~~Example 3~~	~~Dec. 31, 2012~~	~~Jan. 1, 2013~~
~~Accumulated Benefit Obligation~~	~~$(1,922)~~	~~$(1,922)~~
~~Projected Benefit Obligation~~	~~$(2,099)~~	~~$(2,099)~~
~~Plus: Non-Vested Liability~~	~~(103)~~	~~(103)~~
~~Total PBO~~	~~$(2,202)~~	~~$(2,202)~~
~~Plan Assets at Fair Value~~	~~0~~	~~0~~
~~Funded Status~~	~~($2,202)~~	~~($2,202)~~
~~Transition Obligation / (Asset)~~	~~0~~	
~~Prior Service Cost~~	~~0~~	
~~Prior Service Cost (Non-Vested)~~	~~103~~	
~~Unrecognized Losses / (Gains)~~	~~440~~	
~~Total Unrecognized Items~~	~~543~~	~~–~~

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~~Overfunded Plan Asset / (Liability for Benefits)~~	~~(1,659)~~	~~(1,922)~~

~~In the March 31, 2013, financial statements, the $1,922 liability for pension benefits was reflected in the financial statements as follows:~~

- ~~Aggregate Write-Ins for Liabilities: $263~~
- ~~Accrued Benefit Cost: $1,659~~
- ~~Surplus Deferral - Unrecognized Transition Liability - $280~~

~~*(Note – This disclosure shall be completed on a quarterly and annual basis, with updated financial information reflecting the current and prior reporting periods, until the plan is fully funded without any transition liability remaining.)*~~

~~Illustration 3 – Paragraph 97 Example Note Disclosure – December 31, 2015 – After Overfunded Contribution:~~

~~At December 31, 2015, ABC entity contributed $3,300 towards the pension plan. This contribution resulted in the plan being in an overfunded status. Pursuant to the requirements of SSAP No. 102, ABC immediately recognized the remaining transition liability ($171.40). Although the transition liability has been fully-recognized to unassigned funds, the amortization of the liability into net periodic pension cost has not changed.~~

~~Although the entity elected the transition option for surplus deferral, and SSAP No. 102 allows up to 10 years for deferral, with the contribution resulting in an overfunded-plan status, ABC entity was restricted to a 3-year transition schedule as follows:~~

~~January 1, 2013 (Transition) $263.00~~

~~December 31, 2014 $108.60~~

~~December 31, 2015 $171.40~~

~~Total Transition Liability $543.00~~

~~In the December 31, 2015, annual financial statements, pension obligations were reflected as follows:~~

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- ~~Prepaid Benefit Cost - $844 (Nonadmitted)~~
- ~~Overfunded Plan Asset - $(217) (Nonadmitted)~~

~~These amounts are both reported as Aggregate Write-Ins for Other-Than-Invested Assets resulting in a net $628.~~

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~~4. Underfunded Plan with Prepaid Benefit Cost – No Surplus Deferral Elected~~

~~*Consideration of contributions or tax effects are not reflected in this example.*~~

~~Example 4~~	~~Dec. 31, 2012~~[9]	~~Jan. 1, 2013~~	~~Dec. 31, 2013~~	~~Jan. 1, 2014~~	~~Dec. 31, 2014~~
~~Accumulated Benefit Obligation~~	~~(1,532)~~	~~(1,532)~~	~~(1,732)~~	~~(1,732)~~	~~(1,957)~~
~~Plus: Non-Vested Liability~~	~~(100)~~	~~(100)~~	~~(100)~~	~~(100)~~	~~(100)~~
~~Total Accumulated Benefit Obligation~~	~~$ (1,632)~~	~~$ (1,632)~~	~~(1,832)~~	~~(1,832)~~	~~(2,057)~~
~~Projected Benefit Obligation~~	~~$(1,752)~~	~~$(1,752)~~	~~(2,052)~~	~~(2,052)~~	~~(2,277)~~
~~Plus: Non-Vested liability~~	~~(100)~~	~~(100)~~	~~(100)~~	~~(100)~~	~~(100)~~
~~Total PBO~~	~~$(1,852)~~	~~$(1,852)~~	~~(2,152)~~	~~(2,152)~~	~~(2,377)~~
~~Plan Assets at Fair Value~~	~~1,600~~	~~1,600~~	~~1,600~~	~~2,500~~	~~2,500~~
~~Funded Status~~	~~($252)~~	~~($252)~~	~~(552)~~	~~348~~	~~123~~
~~Transition Obligation / (Asset)~~	~~0~~	~~0~~	~~0~~	~~0~~	~~0~~
~~Prior Service Cost~~	~~48~~	~~0~~	~~0~~	~~0~~	~~0~~
~~Prior Service Cost (Non-Vested)~~	~~100~~	~~0~~	~~0~~	~~0~~	~~0~~
~~Unrecognized Losses / (Gains)~~	~~600~~	~~0~~	~~0~~	~~0~~	~~0~~
~~Total Unrecognized Items~~	~~748~~	~~0~~	~~0~~	~~0~~	~~0~~
~~Net Overfunded Plan Asset / (Liability for Benefits)~~	~~496~~	~~(252)~~	~~(552)~~	~~348~~	~~123~~

~~Overfunded Plan Asset and Liability for Benefits are terms to reflect the overfunded and unfunded status of the plan. For the amounts shown as of December 31, 2012 immediately prior to the effective date of the new standard, these terms reflect the~~

~~[9] The amount shown for December 31, 2012, reflects the non-vested liability, which must be considered at transition under SSAP No. 102. However, the non-vested liability is not a factor in the December 31, 2012, financial statements under SSAP No. 89.~~

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~~balance sheet position. As overfunded plan assets are not admitted, these prepaids shall be reflected within Aggregate Write-Ins for Other-Than-Invested Assets. Transition liabilities recognized that have not been reflected through expense shall be reflected within Aggregate Write-Ins for Liabilities.~~

~~January 1, 2013 – Transition Date, Recognize "Unrecognized Items"~~

~~A. Unassigned Funds – Prior Service Cost 48~~

~~Unassigned Funds – Prior Service Cost (Non-vested) 100~~

~~Unassigned Funds – Unrecognized Losses 600~~

~~Liability for Plan Benefits 252~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Overfunded Plan Asset 496~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~B. Change in Nonadmitted – Overfunded Plan Asset 496~~

~~Unassigned Funds 496~~

~~Prepaid Benefit Cost and Overfunded Plan Assets are both reflected as Aggregate Write-Ins for Other-Than-Invested Assets. However, Prepaid Benefit Cost can only be reduced with a corresponding income statement impact. Entry A, which uses a contra-asset, effectively results with a net elimination of the assets reported for the plan and establishes the appropriate liability to reflect the unfunded status. (Reporting entities will need to continue to track these categories separately.)~~

~~December 31, 2013 – Recognition of Net Periodic Pension Cost~~

~~After transition, recognition of net periodic pension cost includes: 1) service cost, 2) interest cost, 3) expected return on plan assets, 4) amortization of prior service cost included in unassigned funds, 5) amortization of gains and losses and 6) amortization of any transition asset or obligation remaining in unassigned funds.~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2013~~
~~Service Cost~~	~~250~~
~~Interest Cost~~	~~100~~

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~~Expected Return on Plan Assets~~	~~(50)~~
~~Total~~	~~300~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~
~~o Prior Service Cost (nonvested)~~	~~2.50~~
~~o Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~318.70~~

~~C. Liability for Pension Benefits 18.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Transition Liability 18.70~~

~~This entry occurs prior to amortization of the items recognized at transition. This entry reverses a portion of the original transition entry for the amount that will be amortized into periodic pension cost for the current period.~~

~~D. Net Periodic Pension Cost 318.70~~

~~Prepaid Benefit Cost 318.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the noted items. As the plan has a prepaid benefit cost, the prepaid benefit cost will be reduced with the recognition of periodic cost.~~

~~E. Overfunded Plan Asset 318.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds 318.70~~

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~~Entry reflects a reduction in the contra-asset recognized at transition at an amount equal to the reduction of prepaid benefit cost.~~

~~F. Change in Nonadmitted – Prepaid Benefit Cost 318.70~~

~~Unassigned Funds 318.70~~

~~G. Unassigned Funds 318.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 318.70~~

~~Entries to reflect the change in nonadmitted assets for both entries "D" and "E." These entries offset.~~

~~H. Unassigned Funds 318.70~~

~~Liability for Pension Benefits 318.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Entry recognizes the unfunded liability from the 2013 net periodic costs. This entry assumes no additional changes in the PBO or Fair Value of Plan Assets at year-end. In practice, there will always be changes in the year-end PBO due to changes in the discount rate used to calculate the PBO, actuarial demographics different than expected, etc. An additional variation is actual return on plan assets different from expected return on plan assets. All of these factors will impact the year-end funded status, and will also need to be recorded as part of entry "H" at year-end.~~

~~January 1, 2014 – Contribution~~

	~~Jan. 1, 2014~~
~~Contribution~~	~~$900~~

~~I. Prepaid Benefit Cost 900~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Cash 900~~

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~~J. Liability for Pension Benefits 552~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Overfunded Plan Asset 552~~

~~With the cash contribution, the plan becomes overfunded with a prepaid benefit cost. The contribution directly increases the Prepaid Benefit Cost. The liability for pension benefits is eliminated, with an offset to the Overfunded Plan asset. The plan now has a NET overfunded plan asset of $348.~~

~~K. Unassigned Funds 900~~

~~Change in Nonadmitted - Prepaid Benefit Cost 900~~

~~L. Change in Nonadmitted- Overfunded Plan Asset 552~~

~~Unassigned Funds 552~~

~~Entries recognize the impact as a result of the nonadmitted overfunded plan asset from entry "I" and "J."~~

~~December 31, 2014 – Recognition of Net Periodic Pension Cost~~

~~After transition, recognition of net periodic pension cost includes: 1) service cost, 2) interest cost, 3) expected return on plan assets, 4) amortization of prior service cost included in unassigned funds, 5) amortization of gains and losses, and 6) amortization of any transition asset or obligation remaining in unassigned funds.~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2014~~
~~Service Cost~~	~~200~~
~~Interest Cost~~	~~75~~
~~Expected Return on Plan Assets~~	~~(50)~~
~~Total~~	~~225~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~

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~~○ Prior Service Cost (nonvested)~~	~~2.50~~
~~○ Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~243.70~~

~~This example assumes no changes in the amortization timeframe. As noted in footnote 6 of SSAP No. 102, unless otherwise impacted from SSAP No. 102, or in accordance with changes to the pension plan, the amortization of the unrecognized items into net periodic pension cost shall continue to follow the existing amortization schedules in effect on the transition date.~~

~~Although the amortization of Prior Service Cost (assuming no additional changes) and non-vested Prior Service Cost will typically follow a straight-line amortization into Net Periodic Pension Cost, this is not the case for the Unrecognized Gains/Losses. The total amount of unrecognized gains/losses subject to amortization will continuously change due to changes in the discount rates, actuarial assumptions, differences between expected and actual return on assets, etc. In addition, unrecognized gains/losses are amortized into expense only to the extent that they exceed the 10% corridor (SSAP 102, paragraph 22). The 10% corridor is based on the greater of the PBO or the Fair Value of Plan assets, and these amounts are also continuously changing. Therefore, the amortization of the gain/loss will never occur on a straight-line basis using the corridor method described in paragraph 22. There is no "amortization schedule" in effect at transition date for the unrecognized gains/losses.~~

~~M. Overfunded Plan Assets 18.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds – Transition Liability 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the original transition entry made to unassigned funds for the amount that will be amortized into periodic pension cost for the current period. Since the plan is currently overfunded, this is offset by overfunded plan asset.~~

~~N. Unassigned Funds 18.70~~

~~Change in Nonadmitted - Overfunded Plan Asset 18.70~~

~~This entry reflects the change in nonadmitted from entry "M."~~

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~~O. Net Periodic Pension Cost 243.70~~

~~Prepaid Benefit Cost 243.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the noted items. As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost. Once that amount is exhausted, an accrued liability would be recorded.~~

~~P. Change in Nonadmitted - Prepaid Benefit Cost 243.70~~

~~Unassigned Funds 243.70~~

~~Entries to reflect the change in nonadmitted assets for entry "O."~~

~~Example 4 - Underfunded Plan with Prepaid Benefit Cost – No Surplus Deferral Elected:~~

	~~Aggregate Write-In For Other-Than-Invested Assets~~		~~Change in Nonadmitted Assets~~	~~Net Periodic Cost~~	~~Unassigned Funds~~	~~Liability for Pension Benefits~~	~~Cash~~
	~~Overfunded Plan Asset~~	~~Prepaid Benefit Cost~~					
~~Existing Balance 12/31/2012~~		~~496 DR~~	~~496 CR~~[10]	~~–~~	~~496 CR~~ ~~496 DR~~	~~–~~	
~~Transition Entries~~ ~~1/1/2013~~ ~~A~~ ~~B~~	~~496 CR~~		~~496 DR~~		~~748 DR~~ ~~496 CR~~	~~252 CR~~	
~~Jan. 1, 2013~~	~~496 CR~~	~~496 DR~~	~~–~~	~~–~~	~~252 DR~~	~~252 CR~~	
~~Jan. 1, 2013 - Net~~	~~–~~		~~–~~	~~–~~	~~252 DR~~	~~252 CR~~	~~–~~
~~Dec. 31, 2013:~~							

~~[10] This reflects the change reported in prior years.~~

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C D E F G H	318.70 DR	318.70 CR	318.70 DR 318.70 CR	318.70 DR[11]	18.70 CR 318.70 CR 318.70 CR 318.70 DR 318.70 DR	18.70 DR 318.70 CR	
Dec. 31, 2013	177.30 CR	177.30 DR	–		552 DR	552 CR	
Dec. 31, 2013 - Net	–		–	–	552 DR	552 CR	
Jan. 1, 2014 Contribution I J K L	552 CR	900 DR	900 CR 552 DR		900 DR 552 CR	552 DR	900 CR
After Contribution	729.30 CR	1077.30 DR	348 CR		900 DR	–	900 CR
Jan. 1, 2014 - Net	348 DR		348 CR		900 DR	–	900 CR
Dec. 31, 2014: M N O P	18.70 DR	243.70 CR	18.70 CR 243.70 DR	243.70 DR[11]	18.70 CR 18.70 DR 243.70 CR		
Dec. 31, 2014	710.60 CR	833.60 DR	123 CR		900 DR	–	900 CR
Dec. 31, 2014 - Net	123 DR		123 CR		900 DR		900 CR

5. Underfunded Plan with Prepaid Benefit Cost – Surplus Deferral, Funded ABO

Consideration of contributions or tax effects are not reflected in this example.

[11] Since Net Periodic Cost closes to unassigned funds at the end of each year, the balance does not carry forward.

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Example 5	Dec. 31, 2012[12]	Jan. 1, 2013	Dec. 31, 2013	Dec. 31, 2014	Jan, 1, 2015	Dec. 31, 2015
Accumulated Benefit Obligation	$(1,032)	$(1,032)	$(1,232)	$(1,457)	$(1,457)	$(1,657)
Plus: Non-Vested Liability	(100)	(100)	(100)	(100)	(100)	(100)
Total Accumulated Benefit Obligation	$(1,132)	$ (1,132)	(1,332)	(1,557)	(1,557)	(1,757)
Projected Benefit Obligation	$(1,752)	$(1,752)	(2,052)	(2,177)	(2,177)	(2,377)
Plus: Non-Vested liability	(100)	(100)	(100)	(100)	(100)	100
Total PBO	$(1,852)	$(1,852)	(2,152)	(2,277)	(2,277)	(2,477)
Plan Assets at Fair Value	1,600	1,600	1,600	1,600	2,500	2,500
Funded Status	($252)	($252)	(552)	(677)	223	23
Transition Obligation/(Asset)	0	0	0	0	0	
Prior Service Cost	48	0	0	0	0	
Prior Service Cost (Non-Vested)	100	0	0	0	0	
Unrecognized Losses/(Gains)	600	0	0	0	0	
Total Unrecognized Items	748	0	0	0	0	
Net Overfunded Plan Asset/ (Liability for Benefits)	496	(25.20)	(325.20)	(475.40)	223	23
Surplus Impact Deferred		(226.80)	(226.80)	(201.60)	-	-

Surplus Impact – The transition guidance in SSAP No. 92 and SSAP No. 102 requires a minimum of 10% of the surplus impact on the transition date. If a systematic 10-year allocation was applied to the total "unrecognized items" rather than the surplus impact,

[12] The amount shown for December 31, 2012, reflects the non-vested liability, which must be considered at transition under SSAP No. 102. However, the non-vested liability is not a factor in the December 31, 2012, financial statements under SSAP No. 89.

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~~there would be a number of years in which a prepaid asset would still be reflected without any impact to surplus even though the plan is underfunded. This is because a reduction in overfunded plan assets alone has a corresponding change to nonadmitted assets, resulting in a net zero surplus impact.~~

~~Determine the initial transition surplus impact under the deferral election:~~

~~In accordance with paragraph 93.b. of SSAP No. 102, the surplus impact initially recognized as of January 1, 2013 under the transition option, and subsequently over the transition period, shall be the greater of:~~

	~~Minimum Transition Liability~~	
~~93.b.i.~~	~~10% of Calculated Surplus Impact~~	~~25.20~~
~~93.b.ii.~~	~~Anticipated Annual Amortization of "Unrecognized Items" (Assume 40-year Uniform Amortization)~~	~~18.70~~
~~93.b.iii.~~	~~Difference Between unfunded ABO and Accrued Benefit Cost. (In this example, ABO is fully funded.)~~	~~–~~
	~~Transition Liability~~	~~25.20~~

~~*93.b.ii. Note: If the amortization cannot be determined at transition, at a minimum, the amount amortized for unrecognized items during the prior year shall be utilized for this calculation. If the amount recognized for transition (greater of all three components) is subsequently determined to be less than what was amortized for the year, the difference between what was recognized for transition and what is amortized must immediately be recognized as an adjustment to the transition impact to unassigned funds – surplus.*~~

~~January 1, 2013 – Transition Date~~

~~2. Unassigned Funds 496~~

~~Overfunded Plan Asset 496~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~3. Change in Nonadmitted – Overfunded Plan Asset 496~~

~~Unassigned Funds 496~~

~~4. Unassigned Funds – Transition Liability 25.20~~

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~~Liability for Plan Benefits 25.20~~

~~*(Aggregate for Write-In Liability)*~~

~~Prepaid Benefit Cost and Overfunded Plan Assets are both reflected as Aggregate Write-Ins for Other-Than-Invested Assets. However, Prepaid Benefit Cost can only be reduced with a corresponding income statement impact. Entry A, which uses a contra-asset, effectively results with a net elimination of the assets reported for the plan. (Reporting entities will need to continue to track these categories separately.) The first two entries (Entry A & B) have a ZERO surplus impact and the third entry recognizes a liability for 10% of the surplus impact calculated at transition as that is the greatest element from paragraph 93.b.~~

~~December 31, 2013 – Recognition of Net Periodic Pension Cost~~

~~After transition, recognition of net periodic pension cost includes: 1) service cost, 2) interest cost, 3) expected return on plan assets, 4) amortization of prior service cost included in unassigned funds, 5) amortization of gains and losses, and 6) amortization of any transition asset or obligation remaining in unassigned funds.~~

~~As noted in paragraph 93.b., if surplus deferral is elected at the transition date, subsequently, starting with the 2014 year-end financial statement, the reporting entity shall annually recognize the remaining surplus impact. As such, unless the entity elects to recognize the remaining surplus impact early (which is permitted under SSAP No. 102), there is no additional surplus impact from transition recognized as of December 31, 2013.~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2013~~
~~Service Cost~~	~~250~~
~~Interest Cost~~	~~100~~
~~Expected Return on Plan Assets~~	~~(50)~~
~~Total~~	~~300~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~
~~o Prior Service Cost (nonvested)~~	~~2.50~~
~~o Unrecognized Losses~~	~~15.00~~

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~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~318.70~~

~~Note – This example assumes no changes in the amortization timeframe. As noted in footnote 5 of SSAP No. 102, unless otherwise impacted from SSAP No. 102, or in accordance with changes to the pension plan, the amortization of the unrecognized items into net periodic pension cost shall continue to follow the existing amortization schedules in effect on the transition date. Although the amortization of Prior Service Cost (assuming no additional changes) and non-vested Prior Service Cost will typically follow a straight-line amortization into Net Periodic Pension Cost, this is not the case for the Unrecognized Gains/Losses. The total amount of unrecognized gains/losses subject to amortization will continuously change due to changes in the discount rates, actuarial assumptions, differences between expected and actual return on assets, etc. In addition, unrecognized gains/losses are amortized into expense only to the extent that they exceed the 10% corridor (SSAP No. 102, paragraph 22). The 10% corridor is based on the greater of the PBO or the Fair Value of Plan assets, and these amounts are also continuously changing. Therefore, the amortization of the gain/loss will never occur on a straight-line basis using the corridor method described in paragraph 22. There is no "amortization schedule" in effect at transition date for the unrecognized gains/losses.~~

~~D. Liability for Pension Benefits 18.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Transition Liability 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the original transition entry for the amount that will be amortized into periodic pension cost for the current period.~~

~~E. Net Periodic Pension Cost 318.70~~

~~Prepaid Benefit Cost 318.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the unrecognized items. (As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost.)~~

~~F. Overfunded Plan Asset 318.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

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~~Unassigned Funds 318.70~~

~~Entry reflects a reduction in the contra-asset recognized at transition at an amount equal to the reduction of prepaid benefit cost.~~

~~G. Change in Nonadmitted – Prepaid Benefit Cost 318.70~~

~~Unassigned Funds 318.70~~

~~H. Unassigned Funds 318.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 318.70~~

~~Entries to reflect the change in nonadmitted assets for both entries "E" and "F." These entries offset.~~

~~I. Unassigned Funds 318.70~~

~~Liability for Pension Benefits 318.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Entry reflects the unfunded liability from the 2013 plan-related costs. This entry assumes no additional changes in the PBO or Fair Value of Plan Assets at year-end. In practice, there will always be changes in the year-end PBO due to changes in the discount rate used to calculate the PBO, actuarial demographics different than expected, etc. An additional variation is actual return on plan assets different from expected return on plan assets. All of these factors will impact the year-end funded status, and will also need to be recorded as part of entry "I" at year-end.~~

~~December 31, 2014 – Recognition of Deferred Transition Impact~~

~~J. Unassigned Funds – Transition Liability 25.20~~

~~Liability for Pension Benefits 25.20~~

~~*(Aggregate Write-In for Liabilities)*~~

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~~Per paragraph 93, if surplus deferral is elected at transition, beginning with 2014 annual financials, the entity shall recognize the remaining surplus impact on a systematic basis over a period not to exceed the remaining nine years. This entry represents the minimum transition liability to be recognized subsequent to transition. Since it is assumed that there is no change in the amortization expectations, and ABO is still funded, this entry reflects 10% of the transition surplus impact.~~

~~December 31, 2014 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2014~~
~~Service Cost~~	~~100~~
~~Interest Cost~~	~~75~~
~~Expected Return on Plan Assets~~	~~(50)~~
~~Total~~	~~125~~
~~Amortization of:~~	
~~○ Prior Service Cost~~	~~1.20~~
~~○ Prior Service Cost (nonvested)~~	~~2.50~~
~~○ Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~143.70~~

~~Note – This example assumes no changes in the amortization timeframe. As noted in footnote 5 of SSAP No. 102, unless otherwise impacted from SSAP No. 102, or in accordance with changes to the pension plan, the amortization of the unrecognized items into net periodic pension cost shall continue to follow the existing amortization schedules in effect on the transition date. Although the amortization of Prior Service Cost (assuming no additional changes) and non-vested Prior Service Cost will typically follow a straight-line amortization into Net Periodic Pension Cost, this is not the case for the Unrecognized Gains/Losses. The total amount of unrecognized gains/losses subject to amortization will continuously change due to changes in the discount rates, actuarial assumptions, differences between expected and actual return on assets, etc. In addition, unrecognized gains/losses are amortized into expense only to the extent that they exceed the 10% corridor (SSAP No. 102, paragraph 22). The 10% corridor is based on the greater of the PBO or the Fair Value of Plan assets, and these amounts are also continuously changing. Therefore, the amortization of the gain/loss will never occur on a straight-line basis using the corridor method described in paragraph 22. There is no "amortization schedule" in effect at transition date for the unrecognized gains/losses.~~

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~~K. Liability for Pension Benefits 18.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Transition Liability 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the original transition entry for the amount that will be amortized into periodic pension cost for the current period.~~

~~L. Net Periodic Pension Cost 143.70~~

~~Prepaid Benefit Cost 143.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the noted items. (As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost.)~~

~~M. Overfunded Plan Asset 143.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds 143.70~~

~~Entry reflects the change in overfunded plan assets as a reduction in the contra-asset from initial transition.~~

~~N. Change in Nonadmitted – Prepaid Benefit Cost 143.70~~

~~Unassigned Funds 143.70~~

~~O. Unassigned Funds 143.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 143.70~~

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~~Entries reflect the change in nonadmitted assets for both entries "L" and "M." These entries offset.~~

~~P. Unassigned Funds 143.70~~

~~Liability for Pension Benefits 143.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Entry reflects the unfunded liability from the 2014 plan-related costs. This entry assumes no additional changes in the PBO or Fair Value of Plan Assets at year-end. In practice, there will always be changes in the year-end PBO due to changes in the discount rate used to calculate the PBO, actuarial demographics different than expected, etc. An additional variation is actual return on plan assets different from expected return on plan assets. All of these factors will impact the year-end funded status and will also need to be recorded as part of entry "P" at year-end.~~

~~January 1, 2015 – Recognition of Cash Contribution~~

	~~Jan. 1, 2015~~
~~Contribution~~	~~$900~~

~~Q. Prepaid Benefit Cost 900.00~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Cash 900.00~~

~~R. Liability for Pension Benefits 475.40~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Overfunded Plan Asset 475.40~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~S. Unassigned Funds 900.00~~

~~Change in Nonadmitted – Prepaid Benefit Cost 900.00~~

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~~T. Change in Nonadmitted – Overfunded Plan Asset 475.40~~

~~Unassigned Funds 475.40~~

~~With the cash contribution, the plan becomes overfunded with a prepaid benefit cost. The contribution directly increases the Prepaid Benefit Cost. The liability for pension benefits is eliminated, with an offset to the Overfunded Plan asset. The plan now has a NET overfunded plan asset of $223.~~

~~U. Unassigned Funds 201.60~~

~~Overfunded Plan Asset 201.60~~

~~Since the plan is in an overfunded status, per paragraph 93.b. of SSAP No. 102, the entity is required to recognize the deferred surplus impact from initial transition to the extent that the plan is overfunded. As the plan is overfunded by more than the remaining transition surplus impact, this entry recognizes the full remaining surplus impact deferred at transition.~~

~~V. Change in Nonadmitted – Overfunded Plan Assets 201.60~~

~~Unassigned Funds 201.60~~

~~Entry reflects the change in nonadmitted assets from entry "U."~~

~~December 31, 2015 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2015~~
~~Service Cost~~	~~100~~
~~Interest Cost~~	~~175~~
~~Expected Return on Plan Assets~~	~~(75)~~
~~Total~~	~~200~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~

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~~○ Prior Service Cost (nonvested)~~	~~2.50~~
~~○ Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~218.70~~

~~(Previous notes on amortization continue to apply.)~~

~~W. Overfunded Plan Asset 18.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the unrecognized items recognized to unassigned funds as part of the transition guidance (even if recognized subsequent to initial recognition under the deferral option) for the amount that will be amortized into periodic pension cost for the current period.~~

~~X. Unassigned Funds 18.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 18.70~~

~~Entry reflects the change in nonadmitted assets from entry "W."~~

~~Y. Net Periodic Pension Cost 218.70~~

~~Prepaid Benefit Cost 218.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the noted items. As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost.~~

~~Z. Change in Nonadmitted – Prepaid Benefit Cost 218.70~~

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~~Unassigned Funds 218.70~~

~~Entry reflects the change in nonadmitted assets from entry "Y." This example assumes no additional changes in the PBO or Fair Value of Plan Assets at year-end. In practice, there will always be changes in the year-end PBO due to changes in the discount rate used to calculate the PBO, actuarial demographics different than expected, etc. An additional variation is actual return on plan assets different from expected return on plan assets. All of these factors will impact the year-end funded status, and will also need to be recorded at year-end in an additional entry impacting the Overfunded Plan Asset. If the plan became underfunded due to these changes, then the amount of the underfunding would then be recorded as a Liability for Pension Benefits.~~

~~*Example: Assume the PBO increased by $100 at year-end due to discount rate changes, etc. This would cause the plan to be underfunded by $77.00.*~~

~~*1. Unassigned Funds 100.00*~~

~~*Overfunded Plan Asset 23.00*~~

~~*Liability for Pension Benefits 77.00*~~

~~*2. Change in Nonadmitted – Overfunded Plan Asset 23.00*~~

~~*Unassigned Funds 23.00*~~

~~Example 5 - Underfunded Plan with Prepaid Benefit Cost – Surplus Deferral, Funded ABO:~~

	~~Aggregate Write-In For Other-Than-Invested Assets~~		~~Change in Nonadmitted Assets~~	~~Net Periodic Cost~~	~~Unassigned Funds~~	~~Liability for Pension Benefits~~	~~Cash~~
	~~Overfunded Plan Asset~~	~~Prepaid Benefit Cost~~					
~~Existing Balance 12/31/2012~~ ~~(This reflects pre-2012 Entries)~~		~~496 DR~~	~~496 CR~~[13]	–	~~496 CR~~ ~~496 DR~~	–	

[13] ~~This reflects the change reported in prior years.~~

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~~Transition Entries – 1/1/2013~~ ~~A~~ ~~B~~ ~~C~~	~~496 CR~~		~~496 DR~~		~~496 DR~~ ~~496 CR~~ ~~25.20 DR~~	~~25.20 CR~~	
~~Jan 1, 2013~~	~~496 CR~~	~~496 DR~~	~~–~~	~~–~~	~~25.20 DR~~	~~25.20 CR~~	
~~Jan 1, 2013 - Net~~	~~–~~		~~–~~	~~–~~	~~25.20 DR~~	~~25.20 CR~~	
~~Dec. 31, 2013:~~ ~~D~~ ~~E~~ ~~F~~ ~~G~~ ~~H~~ ~~I~~	~~318.70 DR~~	~~318.70 CR~~	~~318.70 DR~~ ~~318.70 CR~~	~~318.70 DR~~[14]	~~18.70 CR~~ ~~318.70 CR~~ ~~318.70 CR~~ ~~318.70 DR~~ ~~318.70 DR~~	~~18.70 DR~~ ~~318.70 CR~~	
~~Dec. 31, 2013~~	~~177.30 CR~~	~~177.30 DR~~	~~–~~		~~325.20 DR~~	~~325.20 CR~~	
~~Dec. 31, 2013 - Net~~	~~–~~		~~–~~	~~–~~	~~325.20 DR~~	~~325.20 CR~~	
~~Dec. 31, 2014:~~ ~~J~~ ~~K~~ ~~L~~ ~~M~~ ~~N~~ ~~O~~ ~~P~~	~~143.70 DR~~	~~143.70 CR~~	~~143.70 DR~~ ~~143.70 CR~~	~~143.70 DR~~[14]	~~25.20 DR~~ ~~18.70 CR~~ ~~143.70 CR~~ ~~143.70 CR~~ ~~143.70 DR~~ ~~143.70 DR~~	~~25.20 CR~~ ~~18.70 DR~~ ~~143.70 CR~~	
~~Dec. 31, 2014~~	~~33.60 CR~~	~~33.60 DR~~	~~–~~		~~475.40 DR~~	~~475.40 CR~~	
~~Dec. 31, 2014 – Net~~	~~–~~		~~–~~	~~–~~	~~475.40 DR~~	~~475.40 CR~~	

[14] ~~Since Net Periodic Cost closes to unassigned funds at the end of each year, the balance does not carry forward.~~

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Jan. 1, 2015 – Contribution Q R S T U V	 475.40 CR 201.60 CR	900.00 DR	 900.00 CR 475.40 DR 201.60 DR		 900.00 DR 475.40 CR 201.60 DR 201.60 CR	475.40 DR	900.00 CR
Jan. 1, 2015 – After Contribution	710.60 CR	933.60 DR	223.00 CR		900 DR	–	900 CR
Jan 1, 2015 - Net	223.00 DR		223.00 CR	–	900 DR	–	900 CR
Dec. 31, 2015: W X Y Z	 18.70 DR	 218.70 CR	 18.70 CR 218.70 DR	 218.70 DR[14]	 18.70 CR 18.70 DR 218.70 CR		
Dec. 31, 2015	691.90 CR	714.90 DR	23.00 CR		900.00 DR		900.00 CR
Dec. 31, 2015 - Net	23.00 DR		23.00 CR		900.00 DR		900.00 CR

6. Underfunded Plan with Prepaid Benefit Cost – Surplus Deferral, Unfunded ABO

Consideration of contributions or tax effects are not reflected in this example.

Example 6	Dec. 31, 2012[15]	Jan. 1, 2013	Dec. 31, 2013	Dec. 31, 2014	Jan. 1, 2015	Dec. 31, 2015
Accumulated Benefit Obligation	$(1,632)	$(1,632)	$(1,932)	$(2,057)	$(2,457)	(2,457)
Plus: Non-Vested Liability	(100)	(100)	(100)	(100)	(100)	(100)
Total Accumulated	$(1,732)	$(1,732)	(2,032)	(2,157)	(2,557)	(2,557)

[15] The amount shown for December 31, 2012, reflects the non-vested liability, which must be considered at transition under SSAP No. 102. However, the non-vested liability is not a factor in the December 31, 2012, financial statements under SSAP No. 89.

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~~Benefit Obligation~~						
~~Projected Benefit Obligation~~	~~$(1,752)~~	~~$(1,752)~~	~~(2,052)~~	~~(2,177)~~	~~(2,177)~~	~~(2,377)~~
~~Plus: Non-Vested liability~~	~~(100)~~	~~(100)~~	~~(100)~~	~~(100)~~	~~(100)~~	~~100~~
~~Total PBO~~	~~$(1,852)~~	~~$(1,852)~~	~~(2,152)~~	~~(2,277)~~	~~(2,277)~~	~~(2,477)~~
~~Plan Assets at Fair Value~~	~~1,600~~	~~1,600~~	~~1,600~~	~~1,600~~	~~2,500~~	~~2,500~~
~~Funded Status~~	~~($252)~~	~~($252)~~	~~(552)~~	~~(677)~~	~~223~~	~~23~~
~~Transition Obligation / (Asset)~~	~~0~~	~~0~~	~~0~~	~~0~~	~~0~~	
~~Prior Service Cost~~	~~48~~	~~0~~	~~0~~	~~0~~	~~0~~	
~~Prior Service Cost (Non-Vested)~~	~~100~~	~~0~~	~~0~~	~~0~~	~~0~~	
~~Unrecognized Losses / (Gains)~~	~~600~~	~~0~~	~~0~~	~~0~~	~~0~~	
~~Total Unrecognized Items~~	~~748~~	~~0~~	~~0~~	~~0~~	~~0~~	
~~Net Overfunded Plan Asset / (Liability for Benefits)~~	~~496~~	~~(132)~~	~~(432)~~	~~(582.20)~~	~~223~~	~~23~~
~~Additional Minimum Liability (Unfunded ABO)~~	~~(32)~~	~~0~~	~~The concept of an additional minimum liability and related intangible asset for plans with an unfunded ABO is eliminated in SSAP No. 102.~~			
~~Intangible Asset~~	~~32~~	~~0~~				
~~Surplus Impact Deferred~~		~~(120)~~	~~(120)~~	~~(94.80)~~	~~–~~	~~–~~

~~Surplus Impact – The transition guidance in SSAP No. 92 and SSAP No. 102 requires a minimum of 10% of the surplus impact on the transition date. If a systematic 10-year allocation was applied to the total "unrecognized items" rather than the surplus impact, there would be a number of years in which a prepaid asset would still be reflected, without any impact to surplus, even though the plan is underfunded. This is because a reduced in overfunded plan assets alone has a corresponding change to nonadmitted assets, resulting in a net zero surplus impact.~~

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~~Determine the initial transition surplus impact under the deferral election:~~

~~In accordance with paragraph 93.b. of SSAP No. 102, the surplus impact initially recognized as of January 1, 2013 under the transition option, and subsequently over the transition period, shall be the greater of:~~

	~~Minimum Transition Liability~~	
~~93.b.i~~	~~10% of Calculated Surplus Impact at Transition~~	~~25.20~~
~~93.b.ii~~	~~Anticipated Annual Amortization of "Unrecognized Items" (Assume 40-year Uniform Amortization)~~	~~18.70~~
~~93.b.iii~~	~~Difference Between unfunded ABO and Accrued Benefit Cost.~~	~~132.00~~
	~~Transition Liability~~	~~132.00~~

~~*93.b.ii. Note: If the amortization cannot be determined at transition, at a minimum, the amount amortized for unrecognized items during the prior year shall be utilized for this calculation. If the amount recognized for transition (greater of all three components) is subsequently determined to be less than what was amortized for the year, the difference between what was recognized for transition and what is amortized must immediately be recognized as an adjustment to the transition impact to unassigned funds – surplus.*~~

~~January 1, 2013 – Transition Date~~

~~*Reversal of Additional Minimum Liabilities/Intangible Plan Assets*: As this plan has an unfunded ABO, following the guidance under SSAP No. 89, the entity had recognized an additional minimum liability and corresponding admitted intangible asset. As the concept of an additional minimum liability has been eliminated from SSAP No. 102, at transition these amounts are eliminated, with the determination of the overfunded/unfunded projected benefit obligation calculated subsequent to the elimination.~~

~~Unassigned Funds 32~~

~~Intangible Asset 32~~

~~Additional Minimum Liability 32~~

~~Unassigned Funds 32~~

~~*Application of SSAP No. 102 – Recognition of Unfunded Status with Surplus Deferral:*~~

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~~A. Unassigned Funds 496~~

~~Overfunded Plan Asset 496~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~B. Change in Nonadmitted – Overfunded Plan Asset 496~~

~~Unassigned Funds 496~~

~~C. Unassigned Funds – Transition Liability 132~~

~~Liability for Pension Benefits 132~~

~~Prepaid Benefit Cost and Overfunded Plan Assets are both reflected as Aggregate Write-Ins for Other-Than-Invested Assets. However, Prepaid Benefit Cost can only be reduced with a corresponding income statement impact. Entry A, which uses a contra-asset, effectively results with a net elimination of the assets reported for the plan. (Reporting entities will need to continue to track these categories separately.) Entries A & B have a ZERO surplus impact and the third entry recognizes a liability for the unfunded ABO per the requirements of paragraph 93.b.~~

~~December 31, 2013 – Recognition of Net Periodic Pension Cost~~

~~After transition, recognition of net periodic pension cost includes: 1) service cost, 2) interest cost, 3) expected return on plan assets, 4) amortization of prior service cost included in unassigned funds, 5) amortization of gains and losses, and 6) amortization of any transition asset or obligation remaining in unassigned funds.~~

~~As noted in paragraph 93.b., if surplus deferral is elected at the transition date, subsequently, starting with the 2014 year-end financial statement, the reporting entity shall annually recognize the remaining surplus impact. As such, unless the entity elects to recognize the remaining surplus impact early (which is permitted under SSAP No. 102), there is no additional surplus impact from transition recognized as of December 31, 2013.~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2013~~

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~~Service Cost~~	~~250~~
~~Interest Cost~~	~~100~~
~~Expected Return on Plan Assets~~	~~(50)~~
~~Total~~	~~300~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~
~~o Prior Service Cost (nonvested)~~	~~2.50~~
~~o Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~318.70~~

~~Note – This example assumes no changes in the amortization timeframe. As noted in footnote 5 of SSAP No. 102, unless otherwise impacted from SSAP No. 102, or in accordance with changes to the pension plan, the amortization of the unrecognized items into net periodic pension cost shall continue to follow the existing amortization schedules in effect on the transition date. Although the amortization of Prior Service Cost (assuming no additional changes) and non-vested Prior Service Cost will typically follow a straight-line amortization into Net Periodic Pension Cost, this is not the case for the Unrecognized Gains/Losses. The total amount of unrecognized gains/losses subject to amortization will continuously change due to changes in the discount rates, actuarial assumptions, differences between expected and actual return on assets, etc. In addition, unrecognized gains/losses are amortized into expense only to the extent that they exceed the 10% corridor (SSAP 102, paragraph 22). The 10% corridor is based on the greater of the PBO or the Fair Value of Plan assets, and these amounts are also continuously changing. Therefore, the amortization of the gain/loss will never occur on a straight-line basis using the corridor method described in paragraph 22. There is no "amortization schedule" in effect at transition date for the unrecognized gains/losses.~~

~~D. Liability for Pension Benefits 18.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Transition Liability 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the original transition entry for the amount that will be amortized into periodic pension cost for the current period.~~

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~~E. Net Periodic Pension Cost 318.70~~

~~Prepaid Benefit Cost 318.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the unrecognized items. (As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost.)~~

~~F. Overfunded Plan Asset 318.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds 318.70~~

~~Entry reflects a reduction in the contra-asset recognized at transition at an amount equal to the reduction of prepaid benefit cost.~~

~~G. Change in Nonadmitted – Prepaid Benefit Cost 318.70~~

~~Unassigned Funds 318.70~~

~~H. Unassigned Funds 318.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 318.70~~

~~Entries to reflect the change in nonadmitted assets for both entries "E" and "F." These entries offset.~~

~~I. Unassigned Funds 318.70~~

~~Liability for Pension Benefits 318.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Entry reflects the unfunded liability from the 2013 plan-related costs. This entry assumes no additional changes in the PBO or Fair Value of Plan Assets at year-end. In practice, there will always be changes in the year-end PBO due to changes in the discount rate used to calculate the PBO, actuarial demographics different than expected, etc. An additional variation is actual return on plan assets different from expected return on plan~~

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~~assets. All of these factors will impact the year-end funded status and will also need to be recorded as part of entry "I" at year-end.~~

~~December 31, 2014 – Recognition of Deferred Transition Impact~~

~~In accordance with paragraph 93 of SSAP No. 102, the minimum amount recognized each subsequent year shall be an amount that reflects the conditions of paragraph 93.b. As such, the surplus recognized shall be the greater of:~~

	~~Minimum Transition Liability~~	
~~93.b.i.~~	~~10% of Calculated Surplus Impact at Transition~~	~~25.20~~
~~93.b.ii.~~	~~Anticipated Annual Amortization of "Unrecognized Items" (Assume 40-year Uniform Amortization)~~	~~18.70~~
~~93.b.iii.~~	~~Difference Between unfunded ABO and Accrued Benefit Cost/Fair Value of Plan Assets.~~ ~~(Dec. 31, 2014 - Fair value of plan assets together with the Liability for Pension Benefits exceed the ABO.)~~	~~–~~
	~~Transition Liability~~	~~25.20~~

~~(Previous note on amortization continues to apply.)~~

~~J. Unassigned Funds – Transition Liability 25.20~~

~~Liability for Pension Benefits 25.20~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Entry represents the minimum transition liability to be recognized subsequent to transition. (10% of the transition surplus impact is the greatest component of paragraph 93.b. as of Dec. 31, 2014.)~~

~~December 31, 2014 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2014~~

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~~Service Cost~~	~~100~~
~~Interest Cost~~	~~75~~
~~Expected Return on Plan Assets~~	~~(50)~~
~~Total~~	~~125~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~
~~o Prior Service Cost (nonvested)~~	~~2.50~~
~~o Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~143.70~~

~~(Previous note on amortization continues to apply.)~~

~~K. Liability for Pension Benefits 18.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Unassigned Funds – Transition Liability 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the unrecognized items recognized to unassigned funds as part of the transition guidance (even if recognized subsequent to initial recognition under the deferral option) for the amount that will be amortized into periodic pension cost for the current period.~~

~~L. Net Periodic Pension Cost 143.70~~

~~Prepaid Benefit Cost 143.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the unrecognized items. (As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost.)~~

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~~M. Overfunded Plan Asset 143.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds 143.70~~

~~Entry reflects the change in overfunded plan assets as a reduction in the contra-asset to correspond with the change in net periodic pension cost. With this entry, the Prepaid Benefit Cost and Overfunded Plan Assets net to zero. This is appropriate as the plan is underfunded and a liability is reflected.~~

~~N. Change in Nonadmitted – Prepaid Benefit Cost 143.70~~

~~Unassigned Funds 143.70~~

~~O. Unassigned Funds 143.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 143.70~~

~~Entries to reflect the change in nonadmitted assets for both entries "L" and "M." These entries offset.~~

~~P. Unassigned Funds 143.70~~

~~Liability for Pension Benefits 143.70~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Entry reflects the full unfunded liability, including impact from the 2014 plan-related costs.~~

~~Note - This entry assumes no additional changes in the PBO or Fair Value of Plan Assets at year-end. In practice, there will always be changes in the year-end PBO due to changes in the discount rate used to calculate the PBO, actuarial demographics different than expected, etc. An additional variation is actual return on plan assets different from expected return on plan assets. All of these factors will impact the year-end funded status and will also need to be recorded as part of entry "P" at year-end.~~

~~January 1, 2015 – Recognition of Cash Contribution~~

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	~~Jan. 1, 2015~~
~~Contribution~~	~~$900~~

~~Q. Prepaid Benefit Costs 900.00~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Cash 900.00~~

~~R. Liability for Pension Benefits 582.20~~

~~*(Aggregate Write-In for Liabilities)*~~

~~Overfunded Plan Asset 582.20~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~S. Unassigned Funds 900.00~~

~~Change in Nonadmitted – Prepaid Benefit Cost 900.00~~

~~T. Change in Nonadmitted – Overfunded Plan Asset 582.20~~

~~Unassigned Funds 582.20~~

~~With the cash contribution, the plan becomes overfunded with a prepaid benefit cost. The contribution directly increases the Prepaid Benefit Cost. The liability for pension benefits is eliminated, with an offset to the Overfunded Plan asset. The plan now has a NET overfunded plan asset of $223.~~

~~U. Unassigned Funds 94.80~~

~~Overfunded Plan Assets 94.80~~

~~As the surplus deferral was elected, with the overfunded status, per paragraph 93.b. of SSAP No. 102, the entity is required to recognize the deferred surplus impact from initial transition to the extent that the plan is overfunded. As the plan is overfunded by more than the remaining transition surplus impact, this entry recognizes the full remaining surplus impact deferred at transition.~~

~~V. Change in Nonadmitted – Overfunded Plan Assets 94.80~~

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~~Unassigned Funds 94.80~~

~~Entry reflects the change in nonadmitted assets from entry U.~~

~~December 31, 2015 – Recognition of Net Periodic Pension Cost~~

~~Components of Net Periodic Cost~~	~~Dec. 31, 2015~~
~~Service Cost~~	~~100~~
~~Interest Cost~~	~~175~~
~~Expected Return on Plan Assets~~	~~(75)~~
~~Total~~	~~200~~
~~Amortization of:~~	
~~o Prior Service Cost~~	~~1.20~~
~~o Prior Service Cost (nonvested)~~	~~2.50~~
~~o Unrecognized Losses~~	~~15.00~~
~~Total~~	~~18.70~~
~~Total Net Periodic Pension Cost~~	~~218.70~~

~~(Prior amortization note continues to apply.)~~

~~W. Overfunded Plan Asset 18.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~Unassigned Funds 18.70~~

~~This entry occurs prior to amortization of the transition items. This entry reverses a portion of the original transition entry for the amount that will be amortized into periodic pension cost for the current period.~~

~~X. Unassigned Funds 18.70~~

~~Change in Nonadmitted – Overfunded Plan Asset 18.70~~

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~~Entry reflects the change in nonadmitted assets from entry "W."~~

~~Y. Net Periodic Pension Cost 218.70~~

~~Prepaid Benefit Cost 218.70~~

~~*(Aggregate Write-In for Other-Than-Invested Assets)*~~

~~This entry recognizes net periodic pension cost for the service cost, interest cost, expected return on plan assets and amortization of the unrecognized items. As the plan has a prepaid benefit cost, this will be reduced with the recognition of periodic cost.~~

~~Z. Change in Nonadmitted – Prepaid Benefit Cost 218.70~~

~~Unassigned Funds 218.70~~

~~Entry reflects the change in nonadmitted assets from entry "Y."~~

~~Example 6 - Underfunded Plan with Prepaid Benefit Cost – Surplus Deferral, Unfunded ABO:~~

	~~Aggregate Write-In For Other-Than-Invested Assets~~		~~Change in Nonadmitted Assets~~	~~Net Periodic Cost~~	~~Unassigned Funds~~	~~Liability for Pension Benefits~~	~~Cash~~
	~~Overfunded Plan Asset~~	~~Prepaid Benefit Cost~~					
~~Existing Balance 12/31/2012~~ ~~(This reflects pre-2012 Entries)~~		~~496 DR~~	~~496 CR~~[16]	~~–~~	~~496 CR~~ ~~496 DR~~	~~–~~	
~~Transition Entries – 1/1/2013~~ ~~A~~	~~496 CR~~				~~496 DR~~		

[16] ~~This reflects the change reported in prior years.~~

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B C			496 DR		496 CR 132 DR	132 CR	
Jan 1, 2013	496 CR	496 DR	–	–	132 DR	132 CR	
Jan. 1, 2013 – Net	–		–	–	132 DR	132 CR	–
Dec. 31, 2013: D E F G H I	318.70 DR	318.70 CR	318.70 DR 318.70 CR	318.70 DR[17]	18.70 CR 318.70 CR 318.70 CR 318.70 DR 318.70 DR	18.70 DR 318.70 CR	
Dec. 31, 2013	177.30 CR	177.30 DR	–		432.00 DR	432.00 CR	
Dec. 31, 2013 – Net	–		–	–	432.00 DR	432.00 CR	–
Dec. 31, 2014: J K L M N O P	143.70 DR	143.70 CR	143.70 DR 143.70 CR	143.70 DR[17]	25.20 DR 18.70 CR 143.70 CR 143.70 CR 143.70 DR 143.70 DR	25.20 CR 18.70 DR 143.70 CR	
Dec. 31, 2014	33.60 CR	33.60 DR	–		582.20 DR	582.20 CR	
Dec. 31, 2014 – Net	–		–	–	582.20	582.20 CR	–

[17] Since Net Periodic Cost closes to unassigned funds at the end of each year, the balance does not carry forward.

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				DR		
Jan. 1, 2015 – Contribution Q R S T U V	 582.20 CR 94.80 CR	900 DR	 900 CR 582.20 DR 94.80 DR		 900 DR 582.20 CR 94.80 DR 94.80 CR	 582.20 DR	900 CR
Jan. 1, 2015 – After Contribution	710.60 CR	933.60 DR	223.00 CR		900 DR	–	900 CR
Jan. 1, 2015 – Net	223.00 DR		223.00 CR	–	900 DR	–	900 CR
Dec. 31, 2015: W X Y Z	 18.70 DR	 218.70 CR	 18.70 CR 218.70 DR	 218.70 DR[17]	 18.70 CR 18.70 DR 218.70 CR		
Dec. 31, 2015	691.90 CR	714.90 DR	23 CR		900 DR		900 CR
Dec. 31, 2015 - Net	23 DR		23 CR	–	900 DR	–	900 CR

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EXHIBIT ~~B~~A - CHANGES IN THE MEASUREMENT DATE AND PLAN SETTLEMENT

Note: Footnote references in this section link numbers together for ease of reference.

The reporting entity adopted this SSAP as of the transition date (January 1, 2013.) In accordance with this SSAP, Company B is changing the measurement date for its defined benefit pension plan from September 30 to December 31 for its December 31, 2014, financial statements. In accordance with this SSAP, statutory accounting principles require that change to be implemented by remeasuring plan assets and obligations as of December 31, 2013. Company B has a plan settlement on November 30, 2013, and remeasures its plan assets and benefit obligations as of November 30, 2013, resulting in a settlement loss before taxes of $60,000[6], which is a portion of the net loss in unassigned funds (surplus). However, the effects of remeasuring plan assets and obligations as of November 30, 2013, on the funded status reported in Company B's statement of financial position are not recognized until the following fiscal year because the change in measurement date has not been adopted at November 30, 2013. In recognizing the effects of the plan settlement and change in measurement date:

a. Recognize the settlement loss in net income in the fourth quarter of 2013 and a corresponding decrease in the cumulative net loss in unassigned funds (surplus).

b. Recognize the net periodic pension cost incurred from October 1, 2013, to December 31, 2013, net of tax, as an adjustment to beginning unassigned funds (surplus) for 2014.

c. Recognize any gains or losses arising during the period from October 1, 2013, to December 31, 2013, net of tax, as an adjustment to unassigned funds (surplus) for 2014.

d. Recognize corresponding changes in pension liability and deferred tax amounts for the above items.

The funded status of Company B's Plan assets as of September 30, 2013, November 30, 2013, December 31, 2013 and December 31, 2014, and amounts included in unassigned funds (surplus) to be recognized as a component of net periodic pension cost are shown below. Company B has no remaining transition asset or obligation. Company B is not required to amortize the cumulative net loss because it is less than 10% of the greater of the fair value of plan assets or the projected benefit obligation for all years presented. The applicable tax rate for 2013 and 2014 is 40%.

	9/30/13	**11/30/13**	**12/31/13**	**12/31/14**
Projected Benefit Obligation	(3,660)	(3,200)	(3,210)	(3,700)
Plan Asset – Fair Value	2,600	2,200	2,225	2,200
Funded Status	**(1,060)**	**(1,000)**	**(985)**	**(1,500)**
Items not yet recognized as a component of net periodic cost:	380	360	350	230
Prior Service Cost	265[5]	220	315[4]	365
Net Loss	**645**	**580**	**665**	**595**

Based on actuarial valuations performed as of September 30, 2013, and November 30, 2013, the reporting entity determines its net periodic pension cost for the two-month period from October 1, 2013, to November 30, 2013, and for the one-month period from December 1, 2013, to December 31, 2013, as follows:

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Net Periodic Pension Cost	2 Months	1 Month	Total
Service Cost	25	15	40
Interest Cost	30	15	45
Expected Return on Plan Assets	(30)	(15)	(45)
Total service cost, interest cost, and expected return on plan assets	**25**	**15**	**40**[2]
Amortization of prior service cost	20	10	30[3]
Amortization of net loss	0	0	0
Total Amortization	20	10	30
Net Periodic Benefit Cost	**45**	**25**	**70**[1]

a. In the fourth quarter of 2013, the reporting entity makes the following journal entry to recognize the $60,000[6] settlement loss: (40% tax rate - $24,000)

Net Periodic Pension Cost (settlement loss)	60	
Deferred Tax Asset	24	
Unassigned Funds (Surplus)		84

b. In 2014, the reporting entity makes the following net journal entry to apply the measurement date provisions and adjust the beginning balances of unassigned funds (surplus), pension liability and deferred tax accounts for the amortization of prior service cost and the service cost, interest cost, and expected return on plan assets.

Unassigned Funds (Surplus)	24	
Deferred Tax Asset	16	
Accrued Benefit Cost		40

This journal entry reflects the following considerations:

- Debit to unassigned funds (surplus) for the $70[1] net periodic benefit cost
- Debit to deferred tax asset for $16 calculated as 40% of the $40[2] total service cost, interest cost, and expected return on plan assets
- Debit to unassigned funds (surplus) for $12 for the tax impact calculated as 40% of the $30[3] amortization of the prior service cost
- Credit to Unassigned funds (surplus) for $28 for the tax impact calculated as 40% of the $70[1] net periodic benefit cost
- Credit to Unassigned funds (surplus) for $30[3] for the amortization of the prior service cost.
- Credit to liability for pension benefits for the $40[2] total service cost, interest cost, and expected return on plan assets

c. The following entry adjusts the beginning balances of unassigned funds (surplus), pension liability and deferred tax accounts for the net loss arising during the period. (Net loss is calculated as follows: Net loss at December 31, 2013 of $315[4], less net loss at November 30, 2013 of $265[5], plus settlement loss of $60[6] to equal $110.)

Unassigned Funds (Surplus)	66	
Deferred Tax Asset	44	
Accrued Benefit Cost		110

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Statement of Statutory Accounting Principles No. 103 – Revised

Transfers and Servicing of Financial Assets and Extinguishments of Liabilities

STATUS

Type of Issue	Common Area
Issued	March 3, 2012; Substantively revised June 9, 2016
Effective Date	January 1, 2013; Substantive revisions detailed in Issue Paper No. 152 effective January 1, 2017
Affects	Supersedes SSAP No. 91R; Nullifies and incorporates INT 99-22 and INT 03-05
Affected by	No other pronouncements
Interpreted by	INT 01-31; INT 04-21; INT 20-06
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **2**

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SCOPE OF STATEMENT

1. Transfers of financial assets take many forms. Accounting for transfers in which the transferor has no continuing involvement with the transferred financial assets or with the transferee are generally straightforward. However, transfers of financial assets often occur in which the transferor has some continuing involvement either with the assets transferred or with the transferee. Examples of continuing involvement include, but are not limited to, servicing arrangements, recourse or guarantee arrangements, agreements to purchase or redeem transferred financial assets, options written or held, derivative financial instruments that are entered into contemporaneously with, or in contemplation of the transfer, arrangements to provide financial support, pledges of collateral, and the transferor's beneficial interests in the transferred financial assets. Transfers of financial assets with continuing involvement raise issues about the circumstances under which the transfers should be considered as sales of all or part of the assets or as secured borrowings. An objective in accounting for transfers of financial assets is for each reporting entity that is a party to the transaction to recognize only assets it controls and liabilities it has incurred, to derecognize assets only when control has been surrendered, and to derecognize liabilities only when they have been extinguished. Sales and other transfers may frequently result in a disaggregation of financial assets and liabilities into components, which become separate assets and liabilities. The guidance in this statement also applies to transactions in which servicing assets are transferred with loans retained by the transferor.

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2. This statement focuses on the issues of accounting for transfers and servicing of financial assets and extinguishments of liabilities. This statement establishes statutory accounting principles for transfers and servicing of financial assets, including asset securitizations and securitizations of policy acquisition costs, extinguishments of liabilities, repurchase agreements, repurchase financing and reverse repurchase agreements, including dollar repurchase and dollar reverse repurchase agreements that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts). This statement discusses generalized situations. Facts and circumstances and specific contracts need to be considered carefully in applying this statement. Securitizations of nonfinancial assets are outside the scope of this statement. Transfers of financial assets that are in substance real estate shall be accounted for in accordance with *SSAP No. 40R—Real Estate Investments*. Additionally, retained beneficial interests from the sale of loan-backed or structured securities are to be accounted for in accordance with *SSAP No. 43R—Loan-Backed and Structured Securities, Revised*.

3. *SSAP No. 25—Affiliates and Other Related Parties* shall be followed for accounting and disclosure requirements for all related party transactions.

4. *SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* has been superseded by this statement.

5. This statement does not address the securitization of mortality or morbidity risk. The National Association of Insurance Commissioners' (NAIC's) Insurance Securitization Working Group of the Financial Condition (E) Committee is charged with the development of model laws, model regulations and proposed accounting guidance for the securitization of mortality and morbidity risk. When such proposed accounting guidance is finalized the development of a statement will be considered.

SUMMARY CONCLUSION

Accounting for Transfers and Servicing of Financial Assets

6. The objective of paragraph 8 and related implementation guidance is to determine whether a transferor has surrendered control over transferred financial assets. This determination must consider the transferor's continuing involvement in the transferred financial assets and requires the use of judgment that must consider all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer, even if they were not entered into at the time of the transfer.

7. The requirements of paragraph 8 apply to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a participating interest in an entire financial asset (all of which are referred to collectively in this statement as transferred financial assets). A participating interest has all of the following characteristics:

a. From the date of the transfer, it represents a proportionate (pro rata) ownership interest in an entire financial asset. The percentage of ownership interests held by the transferor in the entire financial asset may vary over time, while the entire financial asset remains outstanding as long as the resulting portions held by the transferor (including any participating interest retained by the transferor or its agents) and the transferee(s) meet the other characteristics of a participating interest. For example, if the transferor's interest in an entire financial asset changes because it subsequently sells another interest in the entire financial asset, the interest held initially and subsequently by the transferor must meet the definition of a participating interest.

b. From the date of the transfer, all cash flows received from the entire financial asset are divided proportionately among the participating interest holders in an amount equal to their share of ownership. Cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided those cash flows are not subordinate

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to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace. In addition, any cash flows received by the transferor as proceeds of the transfer of the participating interest shall be excluded from the determination of proportionate cash flows provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows.

c. The rights of each participating interest holder (including the transferor in its role as a participating interest holder) have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any other participating interest holder. Participating interest holders have no recourse to the transferor, its agents or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder. For example, if a participating interest holder also is the servicer of the entire financial asset and receives cash in its role as servicer, that arrangement would not violate this requirement.

d. No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

If a transfer of a portion of an entire financial asset meets the definition of a participating interest, the transferor shall apply the guidance in paragraph 8. If a transfer of a portion of a financial asset does not meet the definition of a participating interest, the transferor and transferee shall account for the transfer in accordance with the guidance in paragraph 14 as a secured borrowing. However, if the transferor transfers an entire financial asset in portions that do not individually meet the participating interest definition, paragraph 8 shall be applied to the entire financial asset once all portions have been transferred.

8. A transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset in which the transferor surrenders control over those financial assets shall be accounted for as a sale if, and only if, all of the following conditions are met:

a. The transferred financial assets have been isolated from the transferor—put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership. Transferred financial assets are isolated in bankruptcy or other receivership only if the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor.

b. Each transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities and that entity is constrained from pledging or exchanging the assets it receives, each third-party holder of its beneficial interests) has the right to pledge or exchange the assets (or beneficial interests) it received, and no condition both constrains the transferee (or third-party holder of its beneficial interests) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor (paragraphs 43-46).

c. The transferor or its agents do not maintain effective control over the transferred financial assets or third-party beneficial interests related to those transferred assets (paragraph 50). Examples of a transferor's effective control over the transferred financial assets include, but are not limited to (1) an agreement that both entitles and obligates the transferor to

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repurchase or redeem them before their maturity (paragraphs 51-52), (2) an agreement that provides the transferor with both the unilateral ability to cause the holder to return specific financial assets and a more-than-trivial benefit attributable to that ability, other than through a cleanup call (paragraphs 53-57), or (3) an agreement that permits the transferee to require the transferor to repurchase the transferred financial assets at a price that is so favorable to the transferee that it is probable that the transferee will require the transferor to repurchase them (paragraph 58).

Accounting for Transfers of Participating Interests

9. Upon completion of a transfer of a participating interest that satisfies the conditions to be accounted for as a sale (paragraph 8), the transferor (seller) shall:

a. Allocate the previous carrying amount of the entire financial asset between the participating interests sold and the participating interest that continues to be held by the transferor on the basis of their relative fair values at the date of the transfer (paragraph 61).

b. Derecognize the participating interest(s) sold.

c. Recognize and initially measure at fair value servicing assets, servicing liabilities, and any other assets obtained and liabilities incurred in the sale (such as cash) (paragraphs 62-66).

d. Recognize in earnings any gain or loss on the sale.

e. Report any participating interest or interests that continue to be held by the transferor as the difference between the previous carrying amount of the entire financial asset and the amount derecognized.

The transferee shall recognize the participating interest(s) obtained, other assets obtained, and any liabilities incurred and initially measure them at fair value.

10. Upon completion of a transfer of participating interests that does not satisfy the conditions to be accounted for as a sale, the guidance in paragraph 14 shall be applied.

Accounting for Transfers of an Entire Financial Asset or Group of Entire Financial Assets

11. Upon completion of a transfer of an entire financial asset or a group of entire financial assets that satisfies the conditions to be accounted for as a sale (see paragraph 8), the transferor (seller) shall:

a. Derecognize the transferred financial assets;

b. Recognize and initially measure at fair value servicing assets, servicing liabilities, and any other assets obtained (including a transferor's beneficial interest in the transferred financial assets) and liabilities incurred[1] in the sale (paragraphs 60 and 62-66).

c. For reporting entities required to maintain an Interest Maintenance Reserve (IMR), the accounting for realized and unrealized capital gains and losses shall be determined per the guidance in the SSAP for the specific type of investment (e.g., SSAP No. 43R for loan-backed and structured securities), or if not specifically stated in the related SSAP, in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*.

[1] Some assets that might be obtained and liabilities that might be incurred include cash, put or call options that are held or written (for example, guarantee or recourse obligations), forward commitments (for example, commitments to deliver additional receivables during the revolving periods of some securitizations) and swaps (for example, provisions that convert interest rates from fixed to variable).

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For reporting entities not required to maintain an IMR, realized capital gains and losses shall be reported as net realized capital gains or losses in the statement of income, and unrealized capital gains and losses shall be reported as net unrealized gains and losses in unassigned funds (surplus).

The transferee shall recognize all assets obtained and any liabilities incurred, and initially measure them at fair value.

12. Repurchase agreements, reverse repurchase agreements, repurchase financing, collateral requirements and dollar repurchase agreements are described in paragraphs 102-118. When an asset is sold and the proceeds are reinvested within 30 days in the same or substantially the same security, such transfers shall be considered to be wash sales and shall be accounted for as sales as discussed in paragraphs 96-101 and disclosed as required by paragraph 28[2]. Unless there is a concurrent contract to repurchase or redeem the transferred financial assets from the transferee, the transferor does not maintain effective control over the transferred financial assets.

13. Upon completion of a transfer of an entire financial asset or a group of entire financial assets that does not satisfy the conditions to be accounted for as a sale in its entirety, the guidance in paragraph 14 shall be applied.

Secured Borrowing

14. If a transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset does not meet the conditions for a sale in paragraph 8, or if a transfer of a portion of an entire financial asset does not meet the definition of a participating interest (paragraph 7), the transferor and transferee shall account for the transfer as a secured borrowing with pledge of collateral (paragraph 19). The transferor shall continue to report the transferred financial assets in its statement of financial position with no change in their measurement (that is, basis of accounting).

Recognition and Measurement of Servicing Assets and Liabilities

15. An entity shall recognize and initially measure at fair value, a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in either of the following situations:

a. A servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset that meets the requirements for sale accounting; or

b. An acquisition or assumption of a servicing obligation that does not relate to financial assets of the servicer.

An entity that transfers its financial assets to an entity in a transfer that qualifies as a sale in which the transferor obtains the resulting securities and classifies them as debt securities shall separately recognize its servicing assets or servicing liabilities.

16. A servicer that transfers or securitizes financial assets in a transaction that does not meet the requirements for sale accounting and is accounted for as a secured borrowing with the underlying assets remaining on the transferor's balance sheet shall not be recognized as a servicing asset or servicing liability.

17. If distinct servicing rights exist in accordance with the above guidelines, the reporting entity shall recognize a servicing asset or liability. When the servicing fees to be received exceed the cost of servicing the transferred assets, a servicing asset is recognized and nonadmitted. When the cost of servicing the

[2] Paragraph 28.l. also details the items that are excluded from the wash sale disclosure.

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transferred assets is greater than the servicing fees to be received, a liability shall be recorded for the excess to recognize this obligation. A corresponding loss shall be recorded through the Summary of Operations in other income. Servicing assets or liabilities shall be measured subsequently at fair value at each reporting date with fluctuations in fair value reported as unrealized gains and losses. Declines in fair value which are determined to be other than temporary shall be recorded as realized losses.

Financial Assets Subject to Prepayment

18. Financial assets, except for instruments that are within the scope of *SSAP No. 86—Derivatives*, that can contractually be prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment shall be subsequently measured like investments in debt securities and loan-backed and structured securities in accordance with SSAP No. 43R. Examples of such financial assets include, but are not limited to, interest-only strips, other beneficial interests, loans, or other receivables.

Secured Borrowings and Collateral

19. A debtor may grant a security interest in certain assets to a lender (the secured party) to serve as collateral for its obligation under a borrowing, with or without recourse to other assets of the debtor. An obligor under other kinds of current or potential obligations, for example, interest rate swaps, also may grant a security interest in certain assets to a secured party. If collateral is transferred to the secured party, the custodial arrangement is commonly referred to as a pledge. Secured parties sometimes are permitted to sell or repledge (or otherwise transfer) collateral held under a pledge. The same relationships occur, under different names, in transfers documented as sales that are accounted for as secured borrowings (paragraph 14). The accounting for noncash[3] collateral by the debtor (or obligor) and the secured party depends on whether the secured party or its agent has the right to sell or repledge the collateral and on whether the debtor has defaulted. (Paragraphs 85-121 provide application guidance for securities lending, securities borrowing and repurchase agreements.)

a. If the secured party (transferee) or its agent has the right by contract or custom to sell or repledge the collateral, then the debtor (transferor) shall report that asset in its balance sheet.

b. If the secured party (transferee) sells collateral pledged to it, it shall recognize the proceeds from the sale and its obligation to return the collateral. The sale of the collateral is a transfer subject to the provisions of this statement.

c. If the debtor (transferor) defaults under the terms of the secured contract and is no longer entitled to redeem the pledged asset, it shall derecognize the pledged asset, and the secured party (transferee) shall recognize the collateral as its asset initially measured at fair value or, if it has already sold the collateral, derecognize its obligation to return the collateral.

d. Except as provided in paragraph 19.c., the debtor (transferor) shall continue to carry the collateral as its asset, and the secured party (transferee) shall not recognize the pledged asset.

20. Reporting entities may enter into certain transactions that require the granting of a security interest in certain assets to another party to serve as collateral for their performance under a contract. If the assets pledged are recorded as admitted assets under *SSAP No. 4—Assets and Nonadmitted Assets* and *INT 01-31: Assets Pledged as Collateral* and are not impaired under the provisions of *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*, the pledging entity records the collateral as an admitted asset

[3] Cash "collateral," sometimes used, for example, in securities lending transactions, shall be derecognized by the payer and recognized by the recipient, not as collateral, but rather as proceeds of either a sale or a borrowing.

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until committing a contract default that has not been cured in accordance with the contract provisions. At the time of an uncured default, the provisions of paragraph 19 shall be used to determine the appropriate accounting treatment for the collateral. If the secured party utilizes collateral to offset all or a portion of the liability owed by the pledging entity as a result of the default, then the collateral amount utilized to offset the liability shall be removed from the balance sheet. At the same time, the amount of the liability that was offset shall be removed from the balance sheet since that obligation has been satisfied through the secured party's utilization of that collateral. To the extent that an uncured default remains without the secured party utilizing the collateral to offset the obligation, the pledging insurer shall only record an admitted asset for the amount of collateral that it can redeem.

Extinguishments of Liabilities

21. A debtor shall derecognize a liability if and only if it has been extinguished (see *SSAP No. 15—Debt and* Holding *Company Obligations*). A liability has been extinguished if either of the following conditions is met:

a. The debtor pays the creditor and is relieved of its obligation for the liability. Paying the creditor includes delivery of cash, other financial assets, goods, or services or reacquisition by the debtor of its outstanding debt securities whether the securities are canceled or held as so-called treasury bonds; or

b. The debtor is legally released[4] from being the primary obligor under the liability, either judicially or by the creditor.

22. An exchange of debt instruments with substantially different terms is also considered a debt extinguishment and shall be accounted for in accordance with paragraph 21. A debtor's exchange of debt instruments (in a nontroubled debt situation) is accomplished with debt instruments that are substantially different if the present value of the cash flows under the terms of the new debt instrument is at least 10% ~~percent~~ different from the present value of the remaining cash flows under the terms of the original instrument. If the difference between the present value of the cash flows under the terms of the new debt instrument and the present value of the remaining cash flows under the terms of the original debt instrument is less than 10% ~~percent~~, a creditor should evaluate whether the modification is more than minor based on the specific facts and circumstances (and other relevant considerations) surrounding the modification.

Disclosures

23. The principal objectives of the disclosures required by this statement are to provide users of the financial statements with an understanding of all of the following:

a. A transferor's continuing involvement (as defined in the glossary of this statement), if any, with transferred financial assets.

b. The nature of any restrictions on assets reported by an entity in its statement of financial position that relate to a transferred financial asset, including the carrying amounts of those assets.

c. How servicing assets and servicing liabilities are reported under this statement.

d. For transfers accounted for as sales when a transferor has continuing involvement with the transferred financial assets and for transfers of financial assets accounted for as secured

[4] If nonrecourse debt (such as certain mortgage loans) is assumed by a third party in conjunction with the sale of an asset that serves as sole collateral for that debt, the sale and related assumption effectively accomplish a legal release of the seller-debtor for purposes of applying this statement.

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borrowings, how the transfer of financial assets affects a transferor's financial position, financial performance, and cash flows.

Those objectives apply regardless of whether this statement requires specific disclosures. The specific disclosures required by this statement are minimum requirements and an entity may need to supplement the required disclosures specified in paragraph 28 depending on the facts and circumstances of a transfer, the nature of an entity's continuing involvement with the transferred financial assets, and the effect of an entity's continuing involvement on the transferor's financial position, financial performance, and cash flows. Disclosures required by other statement of statutory accounting principles (SSAPs) for a particular form of continuing involvement shall be considered when determining whether the disclosure objectives of this statement have been met.

24. Disclosures required by this statement may be reported in the aggregate for similar transfers if separate reporting of each transfer would not provide more useful information to financial statement users. A transferor shall disclose how similar transfers are aggregated. A transferor shall distinguish transfers that are accounted for as sales from transfers that are accounted for as secured borrowings. If specific disclosures are required for a particular form of a transferor's continuing involvement by other SSAPs, the transferor shall provide the information required in (a) through (c) with a cross-reference to the separate notes to financial statements so a financial statement user can understand the risks retained in the transfer. In determining whether to aggregate the disclosures for multiple transfers, the reporting entity shall consider quantitative and qualitative information about the characteristics of the transferred financial assets. For example, consideration should be given, but not limited, to the following:

a. The nature of the transferor's continuing involvement.

b. The types of financial assets transferred.

c. Risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the change in the transferor's risk profile as a result of the transfer.

25. The disclosures shall be presented in a manner that clearly and fully explains to financial statement users the transferor's risk exposure related to the transferred financial assets and any restrictions on the assets of the entity. An entity shall determine, in light of the facts and circumstances, how much detail it must provide to satisfy the disclosure requirements of this statement and how it aggregates information for assets with different risk characteristics. The entity must strike a balance between obscuring important information as a result of too much aggregation and excessive detail that may not assist financial statement users to understand the entity's financial position. For example, an entity shall not obscure important information by including it with a large amount of insignificant detail. Similarly, an entity shall not disclose information that is so aggregated that it obscures important differences between the different types of involvement or associated risks.

26. The disclosures in paragraph 28.g. of this statement apply to transfers accounted for as sales when the transferor has continuing involvement with transferred financial assets as a result of a securitization, asset-backed financing arrangement, or a similar transfer. If specific disclosures are required for a particular form of the transferor's continuing involvement by other SSAPs, the transferor shall provide the information required in paragraphs 28.f.i.(a) and 28.f.ii.(a) of this statement with a cross-reference to the separate notes to financial statements so a financial statement user can understand the risks retained in the transfer. The entity need not provide each specific disclosure required in paragraphs 28.f.i.(b), 28.f.ii.(a)(1)–(4), and 28.f.ii.(b)–(e) if the disclosure is not required by other SSAPs and the objectives of paragraph 23 are met. For example, if the transferor's only form of continuing involvement is a derivative, the entity shall provide the disclosures required in paragraphs 28.f.i.(a) and 28.f.ii.(a) of this statement and the disclosures about derivatives required by applicable SSAPs. In addition, the entity would evaluate whether the other disclosures in paragraph 28.g. are necessary for the entity to meet the objectives in paragraph 23.

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27. To apply the disclosures in paragraph 28, an entity shall consider all involvements by the transferor or its agents to be involvements by the transferor.

28. A reporting entity shall disclose the following[5]:

a. For Repurchase and Reverse Repurchase Agreements:

i. If the entity has entered into repurchase or reverse repurchase agreements, information regarding the company policy or strategies for engaging in repo programs, policy for requiring collateral, as well as whether transactions have been accounted for as secured borrowings or as sale transactions. This disclosure shall include the terms of reverse repurchase agreements whose amounts are included in borrowing money. The following information shall be disclosed by type of agreement:

(a) Whether repo agreements are bilateral and/or tri-party trades;

(b) Maturity time frame divided by the following categories: open or continuous term contracts for which no maturity date is specified, overnight, 2 days to 1 week, from 1 week to 1 month, greater than 1 month to 3 months, greater than 3 months to 1 year, and greater than 1 year[6];

(c) Aggregate narrative disclosure of the fair value of securities sold and/or acquired that resulted in default. (This disclosure is not intended to capture "failed trades", which are defined as instances in which the trade did not occur as a result of an error and was timely corrected. Rather, this shall capture situations in which the non-defaulting party exercised their right to terminate after the defaulting party failed to execute.)

ii. For repurchase transactions accounted for as secured borrowings[7], the maximum amount and end balance as of each reporting period (quarterly and annual) for the following:

(a) Fair value of securities sold. (Book adjusted carrying value shall be provided as an end balance only.) This information is required in the aggregate, and by type of security categorized by NAIC designation, with identification of nonadmitted assets. Although legally sold as a secured borrowing, these assets are still reported by the insurer and shall be coded as restricted pursuant to the annual statement instructions, disclosed in accordance with *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*, reported in the general interrogatories, and

[5] All repurchase and reverse repurchase transactions (collectively referred to as "repos"), and securities borrowing and securities lending transactions shall be reported gross for disclosure purposes and when detailed on the respective investment schedules. However, repurchase and reverse repurchase transactions, and securities borrowing and securities lending transactions may be reported net in the financial statements (pages 2 and 3 of the statutory financial statements) in accordance with *SSAP No. 64—Offsetting and Netting of Assets and Liabilities* when a valid right to offset exists. When these transactions are offset in accordance with SSAP No. 64 and reported net in the financial statements, the disclosure requirements in SSAP No. 64, paragraph 6, shall be followed.

[6] Only short-term repo agreements (with a stated short-term maturity date) are allowed as admitted assets. Long-term repo agreements (agreements with maturity dates in excess of 365 days) are nonadmitted.

[7] For secured borrowing repurchase transactions, the insurance reporting entity is selling a security, and receiving collateral (generally cash) in an exchange that does not qualify as a sale.

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included in any other statutory schedules or disclosure requirements requesting information for restricted assets.

(b) Cash collateral and the fair value of security collateral (if any) received. This information is required in the aggregate and by type of security categorized by NAIC designation with identification of collateral securities received that do not qualify as admitted assets.

(1) For collateral received, aggregate allocation of the collateral by the remaining contractual maturity of the repurchase agreements (gross): overnight and continuous, up to 30 days, 30-90 days, greater than 90 days. This disclosure shall also include a discussion of the potential risks associated with the agreements and related collateral received, including the impact arising changes in the fair value of the collateral received and/or the provided security and how those risks are managed.

(2) For cash collateral received that has been reinvested, the total reinvested cash and the aggregate amortized cost and fair value of the invested asset acquired with the cash collateral. This disclosure shall be reported by the maturity date of the invested asset: under 30 days, 60 days, 90 days, 120 days, 180 days, less than 1 year, 1-2 years, 2-3 years and greater than 3 years. To the extent that the maturity dates of the liability (collateral to be returned) does not match the invested assets, the reporting entity shall explain the additional sources of liquidity to manage those mismatches.

(c) Liability recognized to return cash collateral, and the liability recognized to return securities received as collateral as required pursuant to the terms of the secured borrowing transaction.

iii. For reverse repurchase transactions accounted for as secured borrowings[8], the maximum amount and end balance as of each reporting period (quarterly and annual) for the following:

(a) Fair value of securities acquired. This information shall be reported in the aggregate, and by type of security categorized by NAIC designation, with identification of whether acquired assets would not qualify as admitted assets.

(b) Cash collateral and the fair value of security collateral (if any) provided. (If security collateral was provided, book adjusted carrying value shall be provided as an end balance only.) Disclosure shall identify the book adjusted carrying value of any nonadmitted securities provided as collateral. For collateral pledged, the aggregate allocation of the collateral by the remaining contractual maturity of the reverse-repurchase agreements (gross): overnight and continuous, up to 30 days, 30-90 days, greater than 90 days. This disclosure shall also include a discussion of the potential risks associated with the agreements and related collateral

[8] For secured borrowing reverse repurchase transactions, the insurance reporting entity is buying a security and providing collateral (generally cash) in an exchange that does not qualify as a sale.

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pledged, including obligations arising from a decline in the fair value of the collateral pledged and how those risks are managed.

(c) Recognized receivable for the return of collateral. (Generally cash collateral, but including securities provided as collateral as applicable under the terms of the secured borrowing transaction. Receivables are not recognized for securities provided as collateral if those securities are still reported as assets of the reporting entity.)

(d) Recognized liability to return securities acquired under the reverse-repurchase agreement as required pursuant to the secured borrowing transaction. (Generally, a liability is required if the acquired securities are sold.)

iv. For repurchase transactions accounted for as a sale[9], the maximum amount and end balance as of each reporting period (quarterly and annual) for the following:

(a) Fair value of securities sold (derecognized from the financial statements). (Book adjusted carrying value shall be provided as an end balance only, reflecting the amount derecognized from the sale transaction.) This information is required in the aggregate, and by type of security categorized by NAIC designation, with information on the book adjusted carrying value of nonadmitted assets sold.

(b) Cash and the fair value of securities (if any) received as proceeds and recognized in the financial statements. This information is required in the aggregate and by type of security categorized by NAIC designation, with identification of received assets nonadmitted in the financial statements. All securities received shall be coded as restricted pursuant to the annual statement instructions, disclosed in accordance with SSAP No. 1, reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for restricted assets.

(c) The forward repurchase commitment recognized to return the cash or securities received. Amount reported shall reflect the stated repurchase price under the repurchase transaction.

v. For reverse repurchase transactions accounted for as sale[10], the maximum amount and end balance as of each reporting period (quarterly and annual):

(a) Fair value of securities acquired and recognized on the financial statements. (Book adjusted carrying value shall be provided as an end balance only.) This information shall be reported in the aggregate, and by type of security categorized by NAIC designation. The disclosure also requires the book adjusted carrying value of nonadmitted assets acquired.

(b) Cash collateral and the fair value of security collateral (if any) provided. (If security collateral was provided, book adjusted carrying value shall be

[9] For sale repurchase transactions, the insurance reporting entity sold a security and received "proceeds" in exchange. With a sale transaction, the insurer removes the asset from their financial statements and recognizes the proceeds from the sale. This transaction requires recognition of a forward repurchase commitment.

[10] For sale reverse repurchase transactions, the insurance reporting entity has purchased a security and provided "proceeds" in exchange. With a sale transaction, the insurer reports the acquired asset in their financial statements and removes the proceeds provided. This transaction requires recognition of a forward resale commitment.

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provided as an end balance only.) Disclosure shall also identify whether any nonadmitted assets were provided as collateral (derecognized from the financial statements).

(c) The forward resale commitment recognized (stated repurchase price) to sell the acquired securities.

b. Collateral:

i. If the entity has entered into securities lending transactions, its policy for requiring collateral or other security and the fair value of the loaned security;

ii. If the entity has pledged any of its assets as collateral that are not reclassified and separately reported in the statement of financial position pursuant to paragraph 19.a., the carrying amounts and classifications of both those assets and associated liabilities as of the date of the latest statement of financial position presented, including qualitative information about the relationship(s) between those assets and associated liabilities. For example, if assets are restricted solely to satisfy a specific obligation, the carrying amounts of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets, shall be disclosed.

iii. If the entity or its agent has accepted collateral that it is permitted by contract or custom to sell or repledge, the fair value as of the date of each statement of financial position presented of that collateral and of the portion of that collateral that it has sold or repledged, and information about the sources and uses of that collateral. Additionally, the reporting entity shall disclose the aggregate amount of contractually obligated open collateral positions (aggregate amount of securities at current fair value or cash received for which the borrower may request the return of on demand) and the aggregate amount of contractually obligated collateral positions under 30-day, 60-day, 90-day, and greater than 90-day terms.

iv. If the entity has accepted collateral that it is not permitted by contract or custom to sell or repledge, provide detail on these transactions, including the terms of the contract, and the current fair value of the collateral.

v. For all securities lending transactions, disclose collateral for transactions that extend beyond one year from the reporting date; and

vi. For securities lending transactions administered by an affiliated agent in which "one-line" reporting (paragraph 89.a.) of the reinvested collateral per paragraph 89.c. is optional, at the discretion of the reporting entity, disclose the aggregate value of the reinvested collateral which is "one line" reported and the aggregate value of items which are reported in the investment schedules (paragraph 89.b.). Identify the rationale between the items which are one line reported and those that are investment schedule reported and if the treatment has changed from the prior period and

vii. For securities lending transactions, include separately, the amount of any loaned securities within the separate account and if the policy and procedures for the separate account differ from the general account.

c. The reporting entity shall provide the following information by type of program (securities lending or dollar repurchase agreement) with respect to the reinvestment of the cash

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collateral and any securities which it or its agent receives as collateral that can be sold or repledged.

i. The aggregate amount of the reinvested cash collateral (amortized cost and fair value). Reinvested cash collateral shall be broken down by the maturity date of the invested asset – under 30 days, 60 days, 90 days, 120 days, 180 days, less than 1 year, 1-2 years, 2-3 years and greater than 3 years.

ii. To the extent that the maturity dates of the liability (collateral to be returned) does not match the invested assets, the reporting entity shall explain the additional sources of liquidity to manage those mismatches.

d. For in-substance defeasance of debt

i. If debt was considered to be extinguished by in-substance defeasance, a general description of the transaction and the amount of debt that is considered extinguished at the end of each the period so long as that debt remains outstanding.

e. For all servicing assets and servicing liabilities:

i. A description of the risks inherent in servicing assets and servicing liabilities and, if applicable, the instruments used to mitigate the income statement effect of changes in fair value to the servicing assets and servicing liabilities. (Disclosure of quantitative information about the instruments used to manage the risks inherent in servicing assets and servicing liabilities is encouraged but not required.)

ii. The amount of contractually specified servicing fees, late fees and ancillary fees earned for each period for which results of operations are presented, including a description of where each amount is reported in the statement of income.

iii. Quantitative and qualitative information about the assumptions used to estimate the fair value (for example, discount rates, anticipated credit losses, and prepayment speeds). An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by paragraph 28.e.i., also is encouraged, but not required to disclose the quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.

f. When servicing assets and servicing liabilities are subsequently measured at fair value:

i. For each class of servicing assets and servicing liabilities, the activity in the balance of servicing assets and the activity in the balance of servicing liabilities (including a description of where changes in fair value are reported in the statement of income for each period for which results of operations are presented), including, but not limited to, the following:

(a) The beginning and ending balances

(b) Additions (through purchases of servicing assets, assumptions of servicing obligations, and recognition of servicing obligations that result from transfers of financial assets)

(c) Disposals

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(d) Changes in fair value during the period resulting from (i) changes in valuation inputs or assumptions used in the valuation model and (ii) other changes in fair value and a description of those changes

(e) Other changes that affect the balance and a description of those changes.

g. For securitizations, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary) with the transferred financial assets:

i. For each income statement presented:

(a) The characteristics of the transfer including a description of the transferor's continuing involvement with the transferred financial assets, the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer, and the gain or loss from sale of transferred financial assets. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

(1) The level within the fair value hierarchy in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3);

(2) The key inputs and assumptions[11] used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable[12] financial assets, and anticipated credit losses, including expected static pool losses[13, 14]).

(b) Cash flows between a transferor and transferee, including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets, servicing fees, and cash flows received from a transferor's beneficial interests.

ii. For each statement of financial position presented, regardless of when the transfer occurred:

[11] If an entity has aggregated multiple transfers during a period in accordance with paragraphs 24 and 25, it may disclose the range of assumptions.

[12] The weighted-average life of prepayable assets in periods (for example, months or years) can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

[13] Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets.

[14] The timing and amount of future cash flows for transferor's interests in transferred financial assets are commonly uncertain, especially if those interests are subordinate to more senior beneficial interests. Thus, estimates of future cash flows used for a fair value measurement depend heavily on assumptions about default and prepayment of all the financial assets transferred, because of the implicit credit or prepayment risk enhancement arising from the subordination.

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(a) Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk, and other risks), including:

(1) The total principal amount outstanding (BACV), the amount that has been derecognized, and the amount that continues to be recognized in the statement of financial position. The amount recognized (allocated fair value) by the reporting entity for the acquired participation in the transferred assets. The reporting schedules of both the transferred and reacquired assets. The percentage of beneficial interests from the reporting entity's transferred assets acquired by affiliated entities.

(2) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the transferee or its beneficial interest holders, including a description of any events or circumstances that could expose the transferor to loss and the amount of the maximum exposure to loss.

(3) Whether the transferor has provided financial or other support during the periods presented that it was not previously contractually required to provide to the transferee or its beneficial interest holders, including when the transferor assisted the transferee or its beneficial interest holders in obtaining support, including:

(i.) The type and amount of support

(ii.) The primary reasons for providing the support

(4) Information is encouraged about any liquidity arrangements, guarantees, and/or other commitments provided by third parties related to the transferred financial assets that may affect the transferor's exposure to loss or risk of the related transferor's interest.

(b) The entity's accounting policies for subsequently measuring assets and liabilities that relate to the continuing involvement with the transferred financial assets;

(c) The key inputs and assumptions used in measuring the fair value of assets or liabilities that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets, and anticipated credit losses, including expected static pool losses);

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(d) For the transferor's interests in the transferred financial assets, a sensitivity analysis or stress test showing the hypothetical effect on the fair value of those interests (including any servicing assets or servicing liabilities) of two or more unfavorable variations from the expected levels for each key assumption that is reported under paragraph 28.g.ii.(c) independently from any change in another key assumption, and a description of the objectives, methodology, and limitations of the sensitivity analysis or stress test;

(e) Information about the asset quality of transferred financial assets and any other assets that it manages together with them. This information shall be separated between assets that have been derecognized and assets that continue to be recognized in the statement of financial position. This information is intended to provide financial statement users with an understanding of the risks inherent in the transferred financial assets as well as in other assets and liabilities that it manages together with transferred financial assets. For example, information for receivables shall include, but is not limited to:

(i.) Delinquencies at the end of the period; and

(ii.) Credit losses, net of recoveries, during the period.

h. Disclosure requirements for transfers of financial assets accounted for as secured borrowing (excluding repurchase and reverse repurchase transactions disclosed under paragraph 28.a.):

i. The carrying amounts and classifications of both assets and associated liabilities recognized in the transferor's statement of financial position at the end of each period presented, including qualitative information about the relationship(s) between those assets and associated liabilities. For example, if assets are restricted solely to satisfy a specific obligation, the carrying amounts of those assets and associated liabilities, including a description of the nature of restrictions placed on the assets.

i. Description of any loaned securities, including the amount, a description of, and the policy for, requiring collateral, and whether or not the collateral is restricted;

j. A description of the securities underlying, dollar repurchase and dollar reverse repurchase agreements, including book values and fair values, and maturities for the following categories: (i) securities subject to dollar repurchase agreements; and (ii.) securities subject to dollar reverse repurchase agreements.

k. Disclose any transfers of receivables with recourse.

l. A reporting entity shall disclose the following information for wash sales, as defined in paragraph 12, for all affiliated investment transactions (including items originally classified as cash equivalents and short-term investments) and for non-affiliated investment transactions with an NAIC designation of 3 or below, or that do not have an NAIC designation. (For non-affiliated investments, all cash equivalents, derivative instruments and short-term investments with credit assessments equivalent to an NAIC 1-2 designation are excluded from this disclosure.) This disclosure shall be included in the financial statements for when the investment was initially sold and is only applicable for sales and purchases that cross quarter-end or year-end reporting periods. For example, if the investment was sold December 20, 2017, and reacquired on January 10, 2018, the

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transaction shall be captured in the wash sale disclosure included in the year-end 2017 financial statements, while an investment sold on May 1, 2019, and reacquired on May 20, 2019, would not be required to be disclosed:

i. A description of the reporting entity's objectives regarding these transactions;

ii. An aggregation of transactions by NAIC designation 3 or below, or that do not have an NAIC designation;

iii. The number of transactions involved during the reporting period;

iv. The book value of securities sold;

v. The cost of securities repurchased; and

vi. The realized gains/losses associated with the securities involved.

m. For reporting entities that have sold securities short within the reporting period, provide the following disclosures:

i. Unsettled Short Sale Transactions (outstanding at reporting date) – The amount of proceeds received and the fair value of the securities to deliver, with current unrealized gains and/or losses, and the expected settlement timeframe (number of days). This disclosure shall include the fair value of current transactions that were not settled within three days and the fair value of the short sales expected to be satisfied by a securities borrowing transaction. This disclosure shall be aggregated by security type. (For example, short sales of common stock shall be aggregated and reported together.)

ii. Settled Short Sale Transactions (settled during the reporting period) – The aggregate amount of proceeds received and the fair value of the security as of the settlement date with recognized gains and/or losses. This disclosure shall identify the aggregated fair value of settled transactions that were not settled within three days and the fair value of transactions that were settled through a securities borrowing transaction.

29. Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures required by paragraph 28 shall be made for the current quarter in the quarterly statement and for the year in the annual statement.

Application Guidance

30. This application guidance describes certain provisions of this statement in more detail and describes how they apply to certain types of transactions. It also discusses generalized situations. Facts and circumstances and specific contracts need to be considered carefully in applying this statement. This application guidance is an integral part of the standards provided in this statement.

31. Paragraph 6 of this statement states that the objective of paragraph 8 and related implementation guidance is to determine whether a transferor has surrendered control over transferred financial assets.

Unit of Account

32. Paragraph 7 establishes the unit of account to which the sale accounting conditions in paragraph 8 shall be applied. Paragraph 7 states that paragraph 8 shall be applied to transfers of an entire financial asset, transfers of a group of entire financial assets, and transfers of a participating interest in an entire financial

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asset. Inherent in that principle is that to be eligible for sale accounting an entire financial asset cannot be divided into components before a transfer unless all of the components meet the definition of a participating interest.

33. The legal form of the asset and what the asset conveys to its holders shall be considered in determining what constitutes an entire financial asset. The following examples illustrate the application of what constitutes an entire financial asset:

a. A loan to one borrower in accordance with a single contract that is transferred to a securitization entity before securitization shall be considered an entire financial asset. Similarly, a beneficial interest in securitized financial assets after the securitization process has been completed shall be considered an entire financial asset. In contrast, a transferred interest in an individual loan shall not be considered an entire financial asset; however, if the transferred interest meets the definition of a participating interest, the participating interest would be eligible for sale accounting.

b. In a transaction in which the transferor creates an interest-only strip from a loan and transfers the interest-only strip, the interest-only strip does not meet the definition of an entire financial asset (and an interest-only strip does not meet the definition of a participating interest; therefore, sale accounting would be precluded). In contrast, if an entire financial asset is transferred to a securitization entity and the transfer meets the conditions for sale accounting, the transferor may obtain an interest-only strip as proceeds from the sale. An interest-only strip received as proceeds of a sale is an entire financial asset for purposes of evaluating any future transfers that could then be eligible for sale accounting.

c. If multiple advances are made to one borrower in accordance with a single contract (such as a line of credit, credit card loan, or a construction loan), an advance on that contract would be a separate unit of account if the advance retains its identity, does not become part of a larger loan balance, and is transferred in its entirety. However, if the transferor transfers an advance in its entirety and the advance loses its identity and becomes part of a larger loan balance, the transfer would be eligible for sale accounting only if the transfer of the advance does not result in the transferor retaining any interest in the larger balance or if the transfer results in the transferor's interest in the larger balance meeting the definition of a participating interest. Similarly, if the transferor transfers an interest in an advance that has lost its identity, the interest must be a participating interest in the larger balance to be eligible for sale accounting.

Participating Interests in an Entire Financial Asset

34. Paragraph 7.b. requires that all cash flows received from the entire financial asset be divided among the participating interest holders (including any interest retained by the transferor or its agents) in proportion to their share of ownership. That is, the participating interest definition does not allow for the allocation of specified cash flows unless each cash flow is proportionately allocated to the participating interest holders. For example, in the case of an individual loan in which the borrower is required to make a contractual payment that consists of a principal amount and interest amount on the loan, the transferor and transferee shall share in the principal and interest payments on the basis of their proportionate ownership interest in the loan. In contrast, if the transferor is entitled to receive an amount that represents the principal payments and the transferee is entitled to receive an amount that represents the interest payments on the loan, that arrangement would not be consistent with the participating interest definition because the transferor and transferee do not share proportionately in the cash flows received from the loan. In other cases, a transferor may transfer a portion of an individual loan that represents either a senior interest or a junior interest in an individual loan. In both of those cases, the transferor would account for the transfer as a secured borrowing

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because the senior interest or junior interest in the loan does not meet the requirements to be participating interests (see paragraph 38).

35. Paragraph 7.b. states that cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided that those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, including any profit that would be demanded in the marketplace. Cash flows allocated as compensation for services performed that are significantly above an amount that would fairly compensate a substitute service provider would result in a disproportionate division of cash flows of the entire financial asset among the participating interest holders and, therefore, would preclude the portion of a transferred financial asset from meeting the definition of a participating interest. Examples of cash flows that are compensation for services performed include loan origination fees paid by the borrower to the transferor, fees necessary to arrange and complete the transfer paid by the transferee to the transferor, and fees for servicing the financial asset.

36. The transfer of a portion of an entire financial asset may result in a gain or loss on the transfer when the contractual interest rate on the entire financial asset differs from the market rate at the time of transfer. Paragraph 7.b. states that any cash flows received by the transferor as proceeds of a transfer of a participating interest shall be excluded from the determination of whether the cash flows of the participating interest are proportionate provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows. For example, if the transferor transfers an interest in an entire financial asset and the transferee agrees to incorporate the excess interest (between the contractual interest rate on the financial asset and the market interest rate at the date of transfer) into the contractually specified servicing fee, the excess interest would likely result in the conveyance of an interest-only strip to the transferor from the transferee. An interest-only strip would result in a disproportionate division of cash flows of the financial asset among the participating interest holders and would preclude the portion from meeting the definition of a participating interest.

37. Paragraph 7.c. requires that the rights of each participating interest holder (including the transferor in its role as participating interest holder) have the same priority and that no participating interest holder's interest is subordinated to the interest of another participating interest holder. In certain transfers, recourse is provided to the transferee that requires the transferor to reimburse any premium paid by the transferee if the underlying financial asset is prepaid within a defined timeframe of the transfer date. Such recourse would preclude the transferred portion from meeting the definition of a participating interest. However, once the recourse provision expires, the transferred portion shall be reevaluated to determine if it meets the participating interest definition.

38. Paragraph 7.c. also requires that participating interest holders have no recourse to the transferor (or its agents) or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits. Recourse in the form of an independent third-party guarantee shall be excluded from the evaluation of whether the participating interest definition is met. Similarly, cash flows allocated to a third-party guarantor for the guarantee fee shall be excluded from the determination of whether the cash flows are divided proportionately among the participating interest holders.

Isolation Beyond the Reach of the Transferor and Its Creditors

39. The nature and extent of supporting evidence required for an assertion in financial statements that an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset (which are referred to collectively in this statement as transferred financial assets) have been isolated—put presumptively beyond the reach of the transferor and its creditors, either by a single transaction or a series of transactions taken as a whole—depend on the facts and circumstances. All available evidence that either supports or questions an assertion shall be considered, including whether the contract or circumstances permit the transferor to revoke the transfer. It also may include consideration of

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the legal consequences of the transfer in the jurisdiction in which bankruptcy or other receivership would take place, whether a transfer of financial assets would likely be deemed a true sale at law (as described in paragraph 40.a.) or otherwise isolated (as described in paragraph 40.b.), whether the transferor is affiliated with the transferee, and other factors pertinent under applicable law. Derecognition of transferred financial assets is appropriate only if the available evidence provides reasonable assurance that the transferred financial assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor and its creditors (paragraph 74.c.). Transactions between related parties or affiliates are accounted for in accordance with SSAP No. 25.

40. In the context of U.S. bankruptcy laws, a true sale opinion from an attorney is often required to support a conclusion that transferred financial assets are isolated from the transferor, and its creditors. In addition, a nonconsolidation opinion is often required if the transfer is to an affiliated entity. In the context of U.S. bankruptcy laws:

a. A true sale opinion is an attorney's conclusion that the transferred financial assets have been sold and are beyond the reach of the transferor's creditors and that a court would conclude that the transferred financial assets would not be included in the transferor's bankruptcy estate.

b. A nonconsolidation opinion is an attorney's conclusion that a court would recognize that an entity holding the transferred financial assets exists separately from the transferor. Additionally, a nonconsolidation opinion is an attorney's conclusion that a court would not order the substantive consolidation of the assets and liabilities of the entity holding the transferred financial assets and the assets and liabilities of the transferor in the event of the transferor's bankruptcy or receivership.

A legal opinion may not be required if a transferor has a reasonable basis to conclude that the appropriate legal opinion(s) would be given if requested. For example, the transferor might reach a conclusion without consulting an attorney if (1) the transfer is a routine transfer of financial assets that does not result in any continuing involvement by the transferor or (2) the transferor had experience with other transfers with similar facts and circumstances under the same applicable laws and regulations.

41. For insurers that are subject to conservatorship, or other receivership procedures, judgments about whether transferred financial assets have been isolated need to be made in relation to the powers of conservators or receivers in those jurisdictions.

42. Whether securitizations isolate transferred financial assets may depend on such factors as whether the securitization is accomplished in one step or multiple step transfers (paragraphs 71-76). Some common financial transactions, for example, typical repurchase agreements and securities lending transactions, may isolate transferred financial assets from the transferor, although they may not meet the other conditions for surrender of control (paragraph 8).

Conditions That Constrain a Transferee

43. Sale accounting is allowed under paragraph 8.b. only if each transferee (or, if the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing arrangements and that entity is constrained from pledging or exchanging the assets it receives, each third-party holder of its beneficial interests) has the right to pledge or exchange the assets or beneficial interests it received, and no condition both constrains the transferee (or third-party holder of its beneficial interests) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor. Many transferor-imposed or other conditions on a transferee's right to pledge or exchange both constrain a transferee from pledging or exchanging and, through that constraint, provide more than a trivial benefit to the transferor. Judgment is required to assess whether a particular condition results in a constraint. Judgment also is required to assess whether a constraint provides a more-than-trivial benefit to the transferor. If the

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transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities, that entity may be constrained from pledging or exchanging the transferred financial assets to protect the rights of beneficial interest holders in the financial assets of the entity. Paragraph 8.b. requires that the transferor look through the constrained entity to determine whether each third-party holder of its beneficial interests has the right to pledge or exchange the beneficial interests that it holds. The considerations in paragraphs 47-49 apply to the transferee or the third-party holders of its beneficial interests in an entity that is constrained from pledging or exchanging the assets it receives and whose sole purpose is to engage in securitization or asset-backed financing activities

44. Some conditions may constrain a transferee from pledging or exchanging the financial asset and may provide the transferor with more than a trivial benefit. For example, a provision that prohibits selling or pledging a transferred loan receivable not only constrains the transferee but also provides the transferor with the more-than-trivial benefit of knowing who holds the financial asset (a prerequisite to repurchasing the financial asset) and of being able to block the financial asset from being transferred to a competitor for the loan customer's business. Transferor-imposed contractual constraints that narrowly limit timing or terms, for example, allowing a transferee to pledge only on the day assets are obtained or only on terms agreed to with the transferor, also constrain the transferee and presumptively provide the transferor with more-than-trivial benefits. In some circumstances in which the transferor has no continuing involvement with the transferred financial assets, some conditions may constrain a transferee from pledging or exchanging the financial assets. If the transferor and its agents have no continuing involvement with the transferred financial assets, the condition under paragraph 8.b. is met. For example, if a transferor receives only cash in return for the transferred financial assets and the transferor and its agents have no continuing involvement with the transferred financial assets, sale accounting is allowed under paragraph 8.b. even if the transferee entity is significantly limited in its ability to pledge or exchange the transferred assets.

45. However, some conditions may not constrain a transferee from pledging or exchanging the transferred financial asset. For example, a transferor's right of first refusal on the occurrence of a bona fide offer to the transferee from a third party presumptively would not constrain a transferee. This is because the right in itself does not enable the transferor to compel the transferee to sell the financial asset and the transferee would be in a position to receive the sum offered by exchanging the financial asset, albeit possibly from the transferor rather than the third party. Further examples of conditions that presumptively would not constrain a transferee for purposes of this statement include (a) a requirement to obtain the transferor's permission to sell or pledge that is not to be unreasonably withheld, (b) a prohibition on sale to the transferor's competitor if other potential willing buyers exist, (c) a regulatory limitation such as on the number or nature of eligible transferees (as in the case of securities issued under Securities Act Rule 144A or debt placed privately), and (d) illiquidity, for example, the absence of an active market. However, judgment is required to assess the significance of some conditions. For example, a prohibition on sale to the transferor's competitor would be a constraint if that competitor were the only potential willing buyer other than the transferor.

46. A condition imposed by a transferor that constrains the transferee presumptively provides more than a trivial benefit to the transferor. A condition not imposed by the transferor that constrains the transferee may or may not provide more than a trivial benefit to the transferor. For example, if the transferor refrains from imposing its usual contractual constraint on a specific transfer because it knows an equivalent constraint is already imposed on the transferee by a third party, it presumptively benefits more than trivially from that constraint. However, the transferor cannot benefit from a constraint if it is unaware at the time of the transfer that the transferee is constrained.

Transferor's Rights or Obligations to Reacquire Transferred Assets or Beneficial Interests

47. Some rights or obligations to reacquire transferred financial assets or beneficial interests both constrain the transferee and provide more than a trivial benefit to the transferor, thus precluding sale accounting under paragraph 8.b. A freestanding call option written by a transferee to the transferor may benefit the transferor and, if the transferred financial assets are not readily obtainable in the marketplace, is

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likely to constrain a transferee because the transferee might have to default if the call was exercised and the transferee had pledged or exchanged the financial assets. For example, if a transferor in a securitization transaction has a call option to repurchase third-party beneficial interests at the price paid plus a stated return, that arrangement conveys more than a trivial benefit to the transferor (paragraphs 53 and 54). If the third-party holders of its beneficial interests are constrained from pledging or exchanging their beneficial interests due to that call option, the transferor would be precluded from accounting for the transfer of financial assets to the securitization entity as a sale. Similarly, a freestanding forward purchase-sale contract between the transferor and the transferee on transferred financial assets not readily obtainable in the marketplace would benefit the transferor and is likely to constrain a transferee in much the same manner. Alternatively, freestanding rights to reacquire transferred assets that are readily obtainable presumptively do not constrain the transferee from pledging or exchanging them and thus do not preclude sale accounting under paragraph 8.b.

48. Other rights or obligations to reacquire transferred financial assets, regardless of whether they constrain the transferee, may result in the transferor's maintaining effective control over the transferred financial assets, as discussed in paragraphs 50-58, thus precluding sale accounting under paragraph 8.c. For example, an attached call in itself would not constrain a transferee who is able, by exchanging or pledging the asset subject to that call, to obtain substantially all of its economic benefits. However, an attached call could result in the transferor's maintaining effective control over the transferred asset(s) because the attached call gives the transferor the unilateral ability to cause whoever holds that specific asset to return it.

49. The concept of qualified special-purpose entities (QSPEs) was previously included within SSAP No. 91R. With the issuance of this statement, this concept is no longer included within statutory accounting guidance. Although this concept has been eliminated and is no longer a factor in determining whether a transfer of assets qualifies for sale accounting, reporting entities may continue to form, conduct transfers between, or have investments in trusts or other such legal vehicles that may have previously met the conditions to be considered a QSPE. Accounting for transfers of assets between the insurer and such trusts or other legal vehicles, including whether such transfers qualify for sale accounting, are subject to the provisions of this statement. As noted within paragraph 4, SSAP No. 25 shall be followed for accounting and disclosure requirements for all related party transactions.

Effective Control Over Transferred Financial Assets or Beneficial Interests

50. Judgment is required to assess whether the transferor maintains effective control over transferred financial assets or third-party beneficial interests. The transferor must evaluate whether a combination of multiple arrangements maintains effective control of transferred financial assets. When the transferee issues beneficial interests in the transferred financial assets, the evaluation of whether the transferor maintains effective control over the transferred financial assets also shall consider whether the transferor maintains effective control over the transferred financial assets through its control over the third-party beneficial interests. To assess whether the transferor maintains effective control over the transferred financial assets, all continuing involvement by the transferor or its agents shall be considered continuing involvement by the transferor. When assessing effective control, the transferor only considers the involvements of an agent when the agent acts for and on behalf of the transferor. In other words, if the transferor and transferee have the same agent, the agent's activities on behalf of the transferee would not be considered in the transferor's evaluation of whether it has effective control over a transferred financial asset. For example, an investment manager may act as a fiduciary (agent) for both the transferor and the transferee; therefore, the transferor need only consider the involvements of the investment manager when it is acting on its behalf.

Agreement to Repurchase or Redeem Transferred Financial Assets

51. An agreement that both entitles and obligates the transferor to repurchase or redeem transferred financial assets from the transferee maintains the transferor's effective control over those assets as described in paragraph 8.c.(1) when all of the following conditions are met:

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a. The financial assets to be repurchased or redeemed are the same or substantially the same as those transferred (paragraph 52).

b. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.

c. The agreement is entered into contemporaneously with, or in contemplation of, the transfer.

52. To be substantially the same, the financial asset that was transferred and the financial asset that is to be repurchased or redeemed need to have all of the following characteristics:

a. The same primary obligor (except for debt guaranteed by a sovereign government, central bank, government-sponsored enterprise or agency thereof, in which case the guarantor and the terms of the guarantee must be the same);

b. Identical form and type so as to provide the same risks and rights;

c. The same maturity (or in the case of mortgage-backed pass-through and pay-through securities similar remaining weighted-average maturities that result in approximately the same market yield);

d. Identical contractual interest rates;

e. Similar assets as collateral; and

f. The same aggregate unpaid principal amount or principal amounts within accepted “good delivery" standards for the type of security involved.

Unilateral Ability to Cause the Return of Specific Transferred Financial Assets

53. A transferor maintains effective control over transferred financial assets when the transferor has the unilateral ability to cause the holder to return specific financial assets and that ability provides more than a trivial benefit to the transferor. A cleanup call, however, is permitted as an exception to that general principle. A call on a transferred financial asset provides the transferor with effective control over that financial asset if, under its price and other terms, the call provides the transferor with the unilateral ability to reclaim the transferred financial asset and conveys more than a trivial benefit to the transferor. A call or other right conveys more than a trivial benefit if the price to be paid is fixed, determinable, or otherwise potentially advantageous, unless because that price is so far out of the money or for other reasons it is probable when the option is written that the transferor will not exercise it. A transferor’s unilateral ability to cause a securitization entity to return to the transferor or otherwise dispose of specific transferred financial assets, for example, in response to its decision to exit a market or a particular activity, would provide the transferor with effective control over the transferred financial assets if it provides more than a trivial benefit to the transferor. However, a call on readily obtainable assets at fair value may not provide the transferor with more than a trivial benefit. (Paragraph 56 provides an example in which, due to the combination of arrangements, the transferor would maintain effective control.)

54. Effective control over transferred financial assets can be present even if the right to reclaim is indirect. For example, if a call allows a transferor to buy back the beneficial interests at a fixed price, the transferor may maintain effective control of the financial assets underlying those beneficial interests. If the transferee is an entity whose sole purpose is to engage in securitization or asset-backed financing activities, that entity may be constrained from choosing to pledge or exchange the transferred financial assets. In that circumstance, any call held by the transferor on third-party beneficial interests is effectively an attached call on the transferred financial assets. Depending on the price and other terms of the call, the transferor may maintain effective control over the transferred financial assets.

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55. An embedded call would not result in the transferor's maintaining effective control because it is the issuer rather than the transferor who holds the call and the call does not provide more than a trivial benefit to the transferor. For example, a call embedded by the issuer of a callable bond or the borrower of a prepayable mortgage loan would not provide the transferor with effective control over the transferred financial asset.

56. A right to reclaim specific transferred financial assets by paying their fair value when reclaimed generally does not maintain effective control when it does not convey a more than trivial benefit to the transferor. However, a transferor has maintained effective control if it has such a right and also holds the residual interest in the transferred financial assets. For example, if a transferor holds the residual interest in securitized financial assets and can reclaim the transferred financial assets at termination of the securitization entity by purchasing them in an auction, and thus at what might appear to be fair value, then sale accounting for the transfer of those financial assets it can reclaim would be precluded. Such circumstances provide the transferor with a more than trivial benefit and effective control over the financial assets because it can pay any price it chooses in the auction and recover any excess paid over fair value through its residual interest in the transferred financial assets.

57. Removal-of-account provisions do not result in the transferor's maintaining effective control, and are thus precluded from being accounted for as sales under statutory accounting as discussed in paragraph 78.

Arrangements to Reacquire Transferred Financial Assets

58. A transferor maintains effective control over the transferred financial asset as described in paragraph 8.c.(3) through an agreement that permits the transferee to require the transferor to repurchase the transferred financial asset at a price that is so favorable to the transferee at the date of the transfer that it is probable that the transferee will require the transferor to repurchase the transferred financial asset. For example, a put option written to the transferee generally does not provide the transferor with effective control over the transferred financial asset. However, a put option that is sufficiently deep in the money when it is written would provide the transferor effective control over the transferred financial asset because it is probable that the transferee will exercise the option and the transferor will be required to repurchase the transferred financial asset. In contrast, a sufficiently out-of-the-money put option held by the transferee would not provide the transferor with effective control over the transferred financial asset if it is probable when the option is written that the option will not be exercised. Likewise, a put option held by the transferee at fair value would not provide the transferor with effective control over the transferred financial asset.

Changes That Result in the Transferor's Regaining Control of Financial Assets Sold

59. A change in law or other circumstance may result in a transferred portion of an entire financial asset no longer meeting the conditions of a participating interest (paragraph 7) or the transferor's regaining control of transferred financial assets after a transfer that was previously accounted for as a sale, because one or more of the conditions in paragraph 8 are no longer met. Such changes, unless they arise solely from the initial application of this statement or from a change in market prices (for example, an increase in price that moves into-the-money a freestanding call on a non-readily-obtainable transferred financial asset that was originally sufficiently out-of-the-money that it was judged not to constrain the transferee), are accounted for in the same manner as a purchase of the transferred financial assets from the former transferee(s) in exchange for liabilities assumed (paragraph 9 or 11). (This "re-purchase" premise is consistent with *INT 04-21: EITF 02-09: Accounting for Changes that Result in a Transferor Regaining Control of Financial Assets Sold*.) After that change, the transferor recognizes in its financial statements those transferred financial assets together with liabilities to the former transferee(s) or beneficial interest holders of the former transferee(s). The transferor initially measures those transferred financial assets and liabilities at fair value on the date of the change, as if the transferor purchased the transferred financial assets and assumed the liabilities on that date. The former transferee would derecognize the transferred

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financial assets on that date, as if it had sold the transferred financial assets in exchange for a receivable from the transferor.

Measurement of Interests Held after a Transfer of Financial Assets

Assets Obtained and Liabilities Incurred as Proceeds

60. The proceeds from a sale of financial assets consist of the cash and any other assets obtained, including beneficial interests and separately recognized servicing assets, in the transfer less any liabilities incurred, including separately recognized servicing liabilities. Any asset obtained is part of the proceeds from the sale. Any liability incurred, even if it is related to the transferred financial assets, is a reduction of the proceeds. Any derivative financial instrument entered into concurrently with a transfer of financial assets is either an asset obtained, or a liability incurred and part of the proceeds received in the transfer. All proceeds and reductions of proceeds from a sale shall be initially measured at fair value.

Participating Interests in Financial Assets That Continue to be Held by a Transferor

61. Participating interests in financial assets that continue to be held by a transferor are not part of the proceeds of the transfer, and the carrying amount of those participating interests shall be measured at the date of the transfer by allocating the previous carrying amount between the participating interests transferred and sold, and the participating interests that are not transferred and continue to be held by a transferor, based on their relative fair values.

Servicing Assets and Liabilities

62. Servicing of mortgage loans, credit card receivables, or other financial assets commonly includes, but is not limited to, collecting principal, interest, and escrow payments from borrowers; paying taxes and insurance from escrowed funds; monitoring delinquencies; executing foreclosure if necessary; temporarily investing funds pending distribution; remitting fees to guarantors, trustees, and others providing services; and accounting for and remitting principal and interest payments to the holders of beneficial interests or participating interests in the financial assets. Servicing is inherent in all financial assets; it becomes a distinct asset or liability for accounting purposes only in the circumstances described in paragraph 63. If a transferor sells a participating interest in an entire financial asset, it will recognize a servicing asset or a servicing liability only related to the participating interest sold.

63. An entity that undertakes a contract to service financial assets shall recognize either a servicing asset or a servicing liability, each time it undertakes an obligation to service a financial asset that (a) results from a servicer's transfer of an entire financial asset, a group of entire financial assets, or a participating interest in an entire financial asset that meets the requirements for sale accounting, or (b) is acquired or assumed and the servicing obligation does not relate to financial assets of the servicer. However, if the transferor transfers the assets to an entity in a transfer that qualifies as a sale in which the transferor obtains the resulting securities, and classifies them as debt securities, the servicing asset or servicing liability may be reported together with the asset being serviced and not recognized separately. A servicer of financial assets commonly receives the benefits of servicing—revenues from contractually specified servicing fees, a portion of the interest from the financial assets, late charges, and other ancillary sources, including "float," all of which it is entitled to receive only if it performs the servicing—and incurs the costs of servicing the financial assets. Typically, the benefits of servicing are expected to be more than adequate compensation to a servicer for performing the servicing, and the contract results in a servicing asset. However, if the benefits of servicing are not expected to adequately compensate a servicer for performing the servicing, the contract results in a servicing liability. (A servicing asset may become a servicing liability, or vice versa, if circumstances change, and the initial measure for servicing may be zero if the benefits of servicing are just adequate to compensate the servicer for its servicing responsibilities.) A servicer would account for its servicing contract that qualifies for separate recognition as a servicing asset or a servicing liability initially measured at its fair value regardless of whether explicit consideration was exchanged.

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64. A servicer that transfers or securitizes financial assets in a transaction that does not meet the requirements for sale accounting and is accounted for as a secured borrowing with the underlying financial assets remaining on the transferor's balance sheet shall not recognize a servicing asset or a servicing liability.

65. A servicer that recognizes a servicing asset or servicing liability shall account for the contract to service financial assets separately from those financial assets, as follows:

a. Report servicing assets separately from servicing liabilities as a nonadmitted asset in the statement of financial position.

b. Initially measure servicing assets and servicing liabilities at fair value, (paragraph 15).

c. Account separately for rights to future interest income from the serviced assets that exceed contractually specified servicing fees. Those rights are not servicing assets; they are financial assets, effectively interest-only strips to be accounted for in accordance with paragraph 18 of this statement. (Interest-only strips preclude a portion of a financial asset from meeting the definition of a participating interest; see paragraph 36.)

d. Identify classes of servicing assets and servicing liabilities based on (1) the availability of market inputs used in determining the fair value of servicing assets and servicing liabilities, (2) an entity's method for managing the risks of its servicing assets and servicing liabilities, or (3) both.

e. Subsequently measure each class of separately recognized servicing assets and servicing liabilities at fair value. Changes in fair value should be reported as unrealized gains and losses (paragraph 17). Declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses.

66. As indicated above, transferors sometimes agree to take on servicing responsibilities when the future benefits of servicing are not expected to adequately compensate them for performing that servicing. In that circumstance, the result is a servicing liability rather than a servicing asset. For example, if in the transaction illustrated in Exhibit B – Illustration 3 the transferor had agreed to service the loans without explicit compensation and it estimated the fair value of that servicing obligation at $50, net proceeds would be reduced to $980, gain on sale would become a loss on sale of $20, and the transferor would report a servicing liability of $50.

Securitizations

67. Financial assets, such as mortgage loans, are commonly transferred in securitizations. Securitizations of mortgage loans may include pools of single-family residential mortgages or other types of real estate mortgage loans, for example, multifamily residential mortgages and commercial property mortgages. Both financial and nonfinancial assets can be securitized; life insurance policy loans, patent and copyright royalties, and even taxi medallions also have been securitized. But securitizations of nonfinancial assets are outside the scope of this statement.

68. An originator of a typical securitization (the transferor) transfers a portfolio of financial assets to a securitization entity, commonly a trust. In "pass-through" and "pay-through" securitizations, receivables are transferred to the entity at the inception of the securitization, and no further transfers are made; all cash collections are paid to the holders of beneficial interests in the entity.

69. Beneficial interests in the securitization entity are sold to investors and the proceeds are used to pay the transferor for the assets transferred financial assets. Those beneficial interests may comprise either a single class having equity characteristics or multiple classes of interests, some having debt characteristics

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and others having equity characteristics. The cash collected from the portfolio is distributed to the investors and others as specified by the legal documents that established the entity.

70. Pass-through and pay-through securitizations that meet the conditions in paragraph 8 qualify for sale accounting under this statement. All financial assets obtained and liabilities incurred by the transferor of a securitization that qualifies as a sale shall be recognized and measured as provided in paragraphs 9 and 11; that includes the implicit forward contract to sell additional financial assets during a revolving period, which may become valuable or onerous to the transferor as interest rates and other market conditions change.

Isolation of Transferred Financial Assets in Securitizations

71. A securitization carried out in one transfer or a series of transfers may or may not isolate the transferred financial assets beyond the reach of the transferor and its creditors. Whether it does depends on the structure of the securitization transaction taken as a whole, considering such factors as the type and extent of further involvement in arrangements to protect investors from credit, and interest rate, and other risks, the availability of other financial assets, and the powers of bankruptcy courts or other receivers. The discussion in paragraphs 72-74 relates only to the isolation condition in paragraph 8.a. The conditions in paragraphs 8.b. and 8.c. also must be considered to determine whether a transferor has surrendered control over the transferred financial assets.

72. In certain securitizations, a corporation that, if it failed, would be subject to the U.S. Bankruptcy Code transfers financial assets to a securitization entity exchange for cash. The entity raises that cash by issuing to investors beneficial interests that pass through all cash received from the financial assets, and the transferor has no further involvement with the trust or the transferred financial assets. The Board understands that those securitizations generally would be judged as having isolated the assets, because, in the absence of any continuing involvement, there would be reasonable assurance that the transfer would be found to be a true sale at law that places the assets beyond the reach of the transferor, and its creditors, even in bankruptcy or other receivership.

73. In other securitizations, a similar corporation transfers financial assets to a securitization entity in exchange for cash and beneficial interests in the transferred financial assets. That entity raises the cash by issuing to investors commercial paper that gives them a senior beneficial interest in cash received from the financial assets. The beneficial interests obtained by the transferring corporation represent a junior interest to be reduced by any credit losses on the financial assets in the entity. The senior beneficial interests (commercial paper) are highly rated by credit rating agencies only if both (a) the credit enhancement from the junior interest is sufficient and (b) the transferor is highly rated. Depending on facts and circumstances, the Board understands that those "single-step" securitizations often would be judged in the United States as not having isolated the financial assets, because the nature of the continuing involvement may make it difficult to obtain reasonable assurance that the transfer would be found to be a true sale at law that places the financial assets beyond the reach of the transferor and its creditors in U.S. bankruptcy (paragraph 39). If the transferor fell into bankruptcy and the transfer was found not to be a true sale at law, investors in the transferred financial assets might be subjected to an automatic stay that would delay payments due them, and they might have to share in bankruptcy expenses and suffer further losses if the transfer was recharacterized as a secured loan.

74. Still other securitizations use multiple transfers intended to isolate transferred financial assets beyond the reach of the transferor and its creditors, even in bankruptcy. For example, in "two-step" structures:

a. First, the corporation transfers a group of financial assets to a special-purpose corporation that, although wholly owned, is so designed that the possibility is remote that the transferor or its creditors could reclaim the financial assets. This first transfer is designed to be judged to be a true sale at law, in part because the transferor does not provide "excessive" credit

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or yield protection to the special-purpose corporation, and the Board understands that transferred financial assets are likely to be judged beyond the reach of the transferor or the transferor's creditors even in bankruptcy or other receivership.

b. Second, the special-purpose corporation transfers a group of financial assets to a trust or other legal vehicle with a sufficient increase in the credit or yield protection on the second transfer (provided by a transferor's junior beneficial interest or other means) to merit the high credit rating sought by third-party investors who buy senior beneficial interests in the trust. Because of that aspect of its design, that second transfer might not be judged to be a true sale at law and, thus, the transferred financial assets could at least in theory be reached by a bankruptcy trustee for the special-purpose corporation.

c. However, the special-purpose corporation is designed to make remote the possibility that it would enter bankruptcy. For example, its charter forbids it from undertaking any other business or incurring any liabilities, so that there can be no creditors to petition to place it in bankruptcy. Furthermore, its dedication to a single purpose is intended to make it extremely unlikely, even if it somehow entered bankruptcy, that a receiver under the U.S. Bankruptcy Code could reclaim the transferred financial assets because it has no other assets to substitute for the transferred financial assets.

75. The Board understands that the "two-step" securitizations described above, taken as a whole, generally would be judged under present U.S. law as having isolated the financial assets beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership. However, each entity involved in a transfer must be evaluated under the applicable accounting guidance.

76. The powers of receivers vary considerably by state of domicile, and therefore some receivers may be able to reach financial assets transferred under a particular arrangement and others may not. A securitization may isolate transferred financial assets from a transferor subject to such a receiver and its creditors even though it is accomplished by only one transfer directly to a securitization entity that issues beneficial interests to investors and the transferor provides credit or yield protection.

Sales of Future Revenues

77. In addition to securitization of assets, some reporting entities have entered into transactions characterized as a sale of future revenues. These transactions are sometimes referred to as securitizations and are sometimes characterized as selling deferred acquisition costs. A sale of future revenues by a reporting entity shall not result in the immediate recognition of income or surplus. The proceeds of any such sale shall be established as a liability and shall be reduced as the proceeds are repaid.

Removal-of-Accounts Provisions

78. Many transfers of financial assets that involve transfers of a group of entire financial assets to an entity whose sole purpose is to engage in securitization or asset-backed financing activities empower the transferor to reclaim assets subject to certain restrictions. Such a power is sometimes called a removal-of-accounts provision (ROAP). Transfers of assets that include ROAP provisions are precluded from being accounted for as sales under statutory accounting and shall follow the guidance in paragraph 14 for secured borrowing.

Short Sales

79. A short sale, as defined for statutory accounting, is the sale of a security that a selling reporting entity (seller) does not own at the time of sale or a sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller. Short sales are normally settled by the delivery of a security borrowed by or on behalf of the seller. The seller later closes out the position by returning the borrowed

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security to the lender, typically by purchasing securities on the open market. If the price of the security rises, short sellers who buy it at the higher price will incur a loss.

80. In a “naked” short sale, the seller does not borrow or arrange to borrow the securities in time to make delivery to the buyer within the standard three-day settlement period (T+3). As a result, the seller fails to deliver securities to the buyer when delivery is due (known as a "failure to deliver" or "fail").

81. Consistent with U.S. GAAP guidance, short sales generally do not meet the definition of a derivative unless a forward purchase or forward sale is involved. Even if a forward purchase or forward sale element is included, if the contract meets the regular-way security trade exception, it would not be subject to the derivative guidance.

82. State statutes or state laws may have restrictions regarding whether a reporting entity is permitted to sell securities short. In situations in which state regulations do not prohibit, or otherwise provide specific guidance, short-sale transactions shall be accounted for in accordance with this statement.

83. Selling a security short is an action by a reporting entity, which results with the reporting entity recognizing proceeds from the sale and an obligation to deliver the sold security. For statutory accounting purposes, obligations to deliver securities resulting from short sales shall be reported as contra-assets (negative assets) in the respective investment schedule for the type of asset sold, with an investment code detailing the item as a short sale. The obligation (negative asset) shall be initially reflected at fair value, with changes in fair value recognized as unrealized gains and losses. These unrealized gains and losses shall be realized upon settlement of the short sale obligation. Interest on short sale positions shall be accrued periodically and reported as interest expense.

84. If short sales are supported by a securities borrowing transaction, the accounting and reporting guidelines in paragraphs 93-95 shall also be followed.

Securities Lending Transactions

85. Securities lending transactions are generally initiated by broker-dealers and other financial institutions that need specific securities to cover a short sale or a customer’s failure to deliver securities sold. Securities lending transactions typically extend less than one year. Transferees (borrowers) of securities generally are required to provide collateral to the transferor (lender) of securities, commonly cash but sometimes other securities or standby letters of credit, with a value slightly higher than that of the securities borrowed. If the collateral is cash, the transferor typically earns a return by investing that cash at rates higher than the rate paid or rebated to the transferee. If the collateral is other than cash, the transferor typically receives a fee. Securities custodians or other agents commonly carry out securities lending activities on behalf of clients. Because of the protection of collateral (typically valued daily and adjusted frequently for changes in the market price of the securities transferred) and the short terms of the transactions, most securities lending transactions in themselves do not impose significant credit risks on either party. Other risks arise from what the parties to the transaction do with the assets they receive. For example, investments made with cash collateral impose market and credit risks on the transferor.

86. If the criteria conditions in paragraph 8 (sales criteria) are met, securities lending transactions shall be accounted for:

a. By the transferor as a sale of the “loaned” securities for proceeds consisting of the cash collateral[15] and a forward repurchase commitment.

[15] If the “collateral” in a transaction that meets the criteria in paragraph 8 is a financial asset that the holder or its agent is permitted by contract or custom to sell or repledge, that financial asset is proceeds of the sale of the “loaned” securities. To the extent that the “collateral” consists of letters of credit or other financial instruments that the holder or its agent is not permitted by contract or custom to sell or repledge, a securities lending transaction does not satisfy the sale criteria and is accounted for as a loan of securities by the transferor to the transferee.

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b. By the transferee as a purchase of the "borrowed" securities in exchange for the collateral and a forward resale commitment. During the term of that agreement, the transferor has surrendered control over the securities transferred and the transferee has obtained control over those securities with the ability to sell or transfer them at will. In that case, creditors of the transferor have a claim only to the "collateral" and the forward repurchase commitment.

87. Many securities lending transactions are accompanied by an agreement that entitles and obligates the transferor to repurchase or redeem the transferred financial assets before their maturity under which the transferor maintains effective control over those financial assets (paragraphs 51-52). Those transactions shall be accounted for as secured borrowings, in which cash (or securities that the holder or its agent is permitted by contract or custom to sell or repledge) received as collateral is considered the amount borrowed, the securities loaned are considered pledged as collateral against the cash or securities borrowed and reclassified as set forth in paragraph 19.a., and any rebate paid to the transferee of securities is interest on the cash or securities the transferor is considered to have borrowed.

88. The transferor of securities being "loaned" accounts for cash received in the same way whether the transfer is accounted for as a sale or a secured borrowing. The cash received shall be recognized as the transferor's asset – as shall investments made with that cash, even if made by agents or in pools with other securities lenders – along with the obligation to return the cash. If securities that may be sold or repledged are received, the transferor of the securities being "loaned" accounts for those securities in the same way as it would account for cash received.

89. The transferor of securities being "loaned" accounts for collateral received in the same way whether the transfer is accounted for as a sale or a secured borrowing. The collateral received shall be recognized as the transferor's asset – as shall investments made with that collateral, even if made by agents or in pools with other securities lenders – along with the obligation to return the collateral. If securities that may be sold or repledged are received by the transferor or its agent, the transferor of the securities being "loaned" accounts for those securities in the same way as it would account for collateral received. Collateral which may be sold or repledged by the transferor or its agent is reflected on balance sheet, along with the obligation to return the asset[16]. Collateral received which may not be sold or repledged by the transferor or its agent is off balance sheet[17]. For collateral on the balance sheet, the reporting is determined by the administration of the program.

a. Securities lending programs where the collateral received by the reporting entity's unaffiliated agent that can be sold or repledged is reported on the balance sheet. The collateral received and reinvestment of that collateral by the reporting entity's unaffiliated agent shall be reflected as a one-line entry on the balance sheet (Securities Lending Collateral) and a detailed schedule will be required each quarter and at year-end to list the description of the collateral asset. This description shall include the NAIC designation, fair value; book adjusted carrying value and maturity date. A separate liability shall also be established to record the obligation to return the collateral (Collateral from Securities Lending Activities).

b. Securities lending programs where the collateral received by the reporting entity that can be sold or repledged is reported on the balance sheet. If the reporting entity is the administrator of the program, then, the collateral received and any reinvestment of that

[16] If cash is received by the transferor or its agent and reinvested or repledged it is reported on balance sheet. It is explicitly intended that when the lender bears reinvestment risk, that collateral is on balance sheet.

[17] An example of collateral which is off balance sheet is when securities are received by the transferor or its agent in which the collateral must be held and returned, without the ability to transfer or repledge the collateral. This would involve limited situations in which the transferor or agent is prohibited from reinvesting the collateral.

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collateral is reported with the invested assets of the reporting entity based on the type of investment (i.e. bond, common stock, etc.). A separate liability shall also be established to record the obligation to return the collateral (Collateral from Securities Lending Activities).

c. Securities lending programs where the collateral received by the reporting entity's affiliated agent can report using either one-line reporting (paragraph 89.a.) or investment schedule reporting (paragraph 89.b.).

90. Reinvestment of the collateral by the reporting entity or its agent shall follow the same impairment guidance as other similar invested assets reported on the balance sheet. Any fees received by the transferor for loaning the securities shall be recorded as miscellaneous investment income.

Securities Lending Transactions – Collateral Requirements[18]

91. The reporting entity shall receive collateral having a fair value as of the transaction date at least equal to 102% ~~percent~~ of the fair value of the loaned securities at that date. If at any time the fair value of the collateral received from the counterparty is less than 100% ~~percent~~ of the fair value of the loaned securities, the counterparty shall be obligated to deliver additional collateral by the end of the next business day, the fair value of which, together with the fair value of all collateral then held in connection with the transaction at least equals 102% ~~percent~~ of the fair value of the loaned securities. If the collateral received from the counterparty is less than 100% ~~percent~~ at the reporting date, the difference between the actual collateral and 100% ~~percent~~ will be nonadmitted. Collateral value is measured and compared to the loaned securities in aggregate by counterparty.

92. In the event that foreign securities are loaned and the denomination of the currency of the collateral is other than the denomination of the currency of the loaned foreign securities, the amount of collateral shall be at least equal to 105% ~~percent~~ of the fair value of the loaned securities at that date. If at any time the fair value of the collateral received from the counterparty is less than 102% ~~percent~~ of the fair value of the loaned securities, the reporting entity must obtain additional collateral by the end of the next business day, the fair value of which together with the fair value of all collateral then held in connection with the transaction at least equals 105% ~~percent~~ of the fair value of the loaned securities. If the collateral received from the counterparty is less than 100% ~~percent~~ at the reporting date, the difference between the actual collateral and 100% ~~percent~~ will be nonadmitted. Collateral value is measured and compared to the loaned securities in aggregate by counterparty.

Securities Borrowing Transactions – Sale Criteria is Not Met (Secured Borrowing)

93. In addition to being the transferor of securities being loaned and receiving collateral under a securities lending arrangement, reporting entities may be a transferee of borrowed securities, and provide collateral under a securities borrowing arrangement.

94. A transferee that sells borrowed securities shall recognize the proceeds from the sale of the securities and an obligation, at fair value, to return the borrowed securities to the transferor. If cash proceeds from the sale of borrowed securities are invested into other assets, or if non-cash proceeds are received from the sale, the assets acquired shall be shown as assets on the reporting entity's (transferee's) financial statements and accounted and reported in accordance with the SSAP for the type of assets acquired. For all instances in which the transferee sells borrowed securities, the reporting entity shall designate restricted assets equivalent to the fair value of the obligation to return the borrowed securities to the transferor.

95. A reporting entity transferee that borrows securities captured under this section (sale criteria is not met) and uses the borrowed securities to settle a short sale transaction shall eliminate the contra-asset recognized under the short sale (paragraph 83) and establish a liability to return the borrowed security. The

[18] The collateral requirements are required for determining admitted assets under statutory accounting, but the receipt of collateral is not a factor in determining whether the transferor has effective control over the loaned assets in accordance with paragraph 51.

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liability to return the borrowed security shall remain on the books until the reporting entity acquires the security to return to the transferor. The accounting/reporting for the short sale and the secured borrowing transaction shall be separately reflected within the financial statements. As such, use of the borrowed asset for the short sale would be similar to recognizing “proceeds” from selling a borrowed asset, as such, if the borrowed asset is used to settle a short sale, the reporting entity shall recognize the borrowed asset and the obligation to return the asset under the secured borrowing agreement until the asset has been returned under the secured borrowing transaction. and recognize an obligation, at fair value, to return the borrowed securities.

Repurchase Agreements and "Wash Sales"

96. Government securities dealers, banks, other financial institutions, and corporate investors commonly use repurchase agreements to obtain or use short-term funds. Under those agreements, the transferor ("repo party") transfers a security to a transferee ("repo counterparty" or "reverse party") in exchange for cash[19] and concurrently agrees to reacquire that security at a future date for an amount equal to the cash exchanged plus a stipulated "interest" factor. Repurchase agreements, reverse repurchase agreements and dollar repurchase agreements meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

97. Repurchase agreements can be affected in a variety of ways. Some repurchase agreements are similar to securities lending transactions in that the transferee or its agent has the right to sell or repledge the securities to a third party during the term of the repurchase agreement. In other repurchase agreements, the transferee does not have the right to sell or repledge the securities during the term of the repurchase agreement. For example, in a tri-party repurchase agreement, the transferor transfers securities to an independent third-party custodian that holds the securities during the term of the repurchase agreement. Also, many repurchase agreements are for short terms, often overnight, or have indefinite terms that allow either party to terminate the arrangement on short notice. However, other repurchase agreements are for longer terms, sometimes until the maturity of the transferred financial asset. Some repurchase agreements call for repurchase of securities that need not be identical to the securities transferred.

98. If the conditions in paragraph 8 are met, the transferor shall account for the repurchase agreement as a sale of financial assets and a forward repurchase commitment, and the transferee shall account for the agreement as a purchase of financial assets and a forward resale commitment. Other transfers that are accompanied by an agreement to repurchase the transferred financial assets that may be accounted for as sales include transfers with agreements to repurchase at maturity. (Repurchase financing is addressed in paragraphs 105-110.)

99. Furthermore, "wash sales" that previously were not recognized if the same financial asset was purchased within 30 days before or after the sale shall be accounted for as sales under this statement. Unless there is a concurrent contract to repurchase or redeem the transferred financial assets from the transferee, the transferor does not maintain effective control over the transferred financial assets.

100. As with securities lending transactions, under many agreements to repurchase transferred financial assets before their maturity the transferor maintains effective control over those financial assets. Repurchase agreements that do not meet all the conditions in paragraph 8 shall be treated as secured borrowings. Fixed-coupon and dollar-roll repurchase agreements, and other contracts under which the securities to be repurchased need not be the same as the securities sold, qualify as borrowings if the return of substantially the same (paragraph 52) securities as those concurrently transferred is assured. Therefore, those transactions shall be accounted for as secured borrowings by both parties to the transfer.

[19] Instead of cash, other securities or letters of credit sometimes are exchanged. Those transactions are accounted for in the same manner as securities lending transactions (paragraphs 85-92).

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101. If a transferor has transferred securities to an independent third-party custodian, or to a transferee, under conditions that preclude the transferee from selling or repledging the assets during the term of the repurchase agreement (as in most tri-party repurchase agreements), the transferor has not surrendered control over those assets.

Repurchase Agreements

102. Repurchase agreements are defined as agreements under which a reporting entity sells securities and simultaneously agrees to repurchase the same or substantially the same securities at a stated price on a specified date. For securities to be substantially the same, the criteria defined in paragraph 52 must be met, and for mortgage-backed securities excluding mortgage pass-through securities, the projected cash flows of the securities must be substantially the same under multiple scenario prepayment assumptions.

103. For repurchase agreements that are accounted for as collateralized borrowings in accordance with paragraph 100 of this statement, the underlying securities shall continue to be accounted for as an investment owned by the reporting entity. The proceeds from the sale of the securities shall be recorded as a liability, and the difference between the proceeds and the amount at which the securities will be subsequently reacquired shall be reported as interest expense, calculated on the straight-line method or the scientific interest (constant yield) method, over the term of the agreement.

104. Reporting entities generally take possession of the underlying collateral under repurchase agreements and in many cases may obtain additional collateral when the estimated fair value of such securities falls below their current contract value. However, to the extent that the current fair value of the collateral is less than the recorded amount, the shortfall shall reduce the admitted asset value of the repurchase agreement.

Repurchase Financing

105. Repurchase financing is a repurchase agreement that relates to a previously transferred financial asset between the same counterparties (or affiliates of either counterparty) that is entered into contemporaneously with, or in contemplation of, the initial transfer.

106. A repurchase financing involves the transfer of a previously transferred financial asset back to the initial transferor as collateral for a financing between the initial transferee (the borrower) and the initial transferor (the lender). A repurchase financing also typically involves the initial transferor returning the transferred financial asset (or substantially the same asset) to the initial transferee when the financing is repaid on a stated date. A repurchase financing is entered into in contemplation of the initial transfer if both transactions are considered together at the execution of the initial transfer.

107. When the transferor transfers a financial asset and also enters into a repurchase financing with the transferee, there are typically three transfers of the financial assets:

a. Initial transfer – An initial transferor transfers a financial asset to an initial transferee.

b. Repurchase financing – The initial transferee (the borrower) transfer the previously transferred financial asset back to the initial transferor (the lender) as collateral for a financing between the initial transferor and initial transferee.

c. Settlement – The initial transferor (the lender) returns the financial asset (or substantially the same asset) to the initial transferee (the borrower) upon receipt of payment from the initial transferee.

108. Repurchase financing that is entered into contemporaneously with, or in contemplation of, an initial transfer of financial asset between the same counterparties (or affiliates of either counterparty) shall not be separately accounted for as a transfer of a financial asset and a related repurchase financing unless (a) the

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two transactions have a valid and distinct business or economic purpose for being entered into separately and (b) the repurchase financing does not result in the initial transferor regaining control over the financial asset. Unless the provisions in paragraph 109 are met, the initial transfer and repurchase financing shall be evaluated as a linked transaction. The linked transaction shall be evaluated to determine whether it meets the requirements for sale accounting per paragraph 8. If the linked transaction does not meet the requirements for sale accounting, the linked transaction shall be accounted for based on the economies of the combined transactions, which generally represent a forward contract. SSAP No. 86 shall be used to evaluate whether the linked transaction shall be accounted for as a derivative.

109. An initial transfer of a financial asset and repurchase financing that are entered into contemporaneously with, or in contemplation of, one another shall be considered linked unless all of the following criteria are met at the inception of the transaction:

a. The initial transfer and the repurchase financing are not contractually contingent on one another. Even if no contractual relationship exists, the pricing and performance of either the initial transfer or the repurchase financing must not be dependent on the terms and execution of the other transaction.

b. The repurchase financing provides the initial transferor with recourse to the initial transferee upon default. That recourse must expose the initial transferor to the credit risk of the initial transferee, or its affiliates, and not solely to the market risk of the transferred financial asset. The initial transferee's agreement to repurchase the previously transferred financial asset (or substantially the same asset) for a fixed price and not fair value.

c. The financial asset subject to the initial transfer and repurchase financing is readily obtainable in the marketplace. In addition, the initial transfer of a financial asset and the repurchase financing are executed at market rates. This criterion may not be circumvented by embedding off-market terms in a separate transaction contemplated with the initial transfer or the repurchase financing.

d. The financial asset and repurchase agreement are not coterminous (the maturity of the repurchase financing must be before the maturity of the financial asset).

110. In accordance with paragraph 108, an initial transfer of assets and a repurchase financing shall not be considered separate transactions unless the provisions of paragraph 109 are met. If the provisions of paragraph 109 are met, the initial transfer shall be evaluated to determine whether it meets the requirements for sale accounting without taking into consideration the repurchase financing. In such situations, the repurchase financing shall then be separately analyzed as a repurchase agreement.

Reverse Repurchase Agreements

111. Reverse repurchase agreements are defined as agreements under which a reporting entity purchases securities and simultaneously agrees to resell the same or substantially the same securities at a stated price on a specified date. For securities to be substantially the same, the criteria defined in paragraph 52 must be met, and for mortgage-backed securities excluding mortgage pass-through securities, the projected cash flows of the securities must be substantially the same under multiple scenario prepayment assumptions.

112. For reverse repurchase agreements that are accounted for as collateralized lendings in accordance with paragraph 100 of this statement, the underlying securities shall not be accounted for as investments owned by the reporting entity. The amount paid for the securities shall be reported as a short-term investment, and the difference between the amount paid and the amount at which the securities will be subsequently resold shall be reported as interest income, calculated on the straight-line method or the scientific interest (constant yield) method, over the term of the agreement.

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Collateral Requirements – Repurchase and Reverse Repurchase Agreements[20]

113. The collateral requirements for repurchase and reverse repurchase agreements are as follows:

Repurchase Transaction

a. The reporting entity shall receive collateral having a fair value as of the transaction date at least equal to 95% ~~percent~~ of the fair value of the securities transferred by the reporting entity in the transaction as of that date. If at any time the fair value of the collateral received from the counterparty is less than 95% ~~percent~~ of the fair value of the securities so transferred, the counterparty shall be obligated to deliver additional collateral by the end of the next business day the fair value of which, together with the fair value of all collateral then held in connection with the transaction, at least equals 95% ~~percent~~ of the fair value of the transferred securities. If the collateral is less than 95% ~~percent~~ at the reporting date, the difference between the actual collateral and 95% ~~percent~~ will be nonadmitted.

Reverse Repurchase Transaction

b. The reporting entity shall receive as collateral transferred securities having a fair value at least equal to 102% ~~percent~~ of the purchase price paid by the reporting entity for the securities. If at any time the fair value of the collateral is less than 100% ~~percent~~ of the purchase price paid by the reporting entity, the counterparty shall be obligated to provide additional collateral, the fair value of which, together with fair value of all collateral then held in connection with the transaction, at least equals 102% ~~percent~~ of the purchase price.

Dollar Repurchase Agreements

114. Dollar repurchase and dollar reverse repurchase agreements are defined as repurchase and reverse repurchase agreements involving debt instruments that are pay-through securities collateralized with Government National Mortgage Association (GNMA), Federal Home Loan Mortgage Corporation (FHLMC) and Federal National Mortgage Association (FNMA) collateral, and pass-through certificates sponsored by GNMA, mortgage participation certificates issued by the FHLMC or similar securities issued by the FNMA. Dollar repurchase agreements are also commonly referred to as dollar roll transactions. To meet the definition of dollar repurchase and dollar reverse repurchase agreements, the securities underlying the agreements must meet the criteria defined in paragraph 52, and for mortgage-backed securities excluding mortgage pass-through securities, the projected cash flows of the securities must be substantially the same under multiple scenario prepayment assumptions.

115. For the seller in a dollar repurchase agreement accounted for as collateralized borrowing in accordance with paragraph 100 of this statement, a liability is recorded for the amount of proceeds of the sale and the sold mortgage-backed securities are not removed from the accounting records. During the period of the agreement, interest income is recorded as if the mortgage-backed security had been held during the term of the agreement. This is offset by an equal amount of interest expense related to the proceeds received from the sale. Additional interest expense is recorded representing the difference between the sales price and the repurchase price of the mortgage-backed securities sold.

116. When the mortgage-backed securities are repurchased under the agreement, the original mortgage-backed securities sold are removed from the accounting records and the purchased mortgage-backed securities are recorded. The principal amount of the mortgage-backed securities repurchased must be in good delivery form consistent with paragraph 52.

[20] The collateral requirements are required for determining admitted assets under statutory accounting, but the receipt of collateral is not a factor in determining whether the transferor has effective control over the loaned assets in accordance with paragraph 50.

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117. If the principal amount repurchased is greater than the amount sold, the cash paid is recorded as an additional investment in the newly acquired certificates. If the principal amount repurchased is less than the amount sold, a gain or loss relating to the original certificates held is recorded.

118. For the purchaser in a dollar reverse repurchase agreement accounted for as collateralized lending in accordance with paragraph 100 of this statement, an asset is recorded for the amount of the purchase. Upon completion of the reverse repurchase agreement, cash is received in exchange for a "substantially the same" security. The difference between the purchase and reselling price represents interest income for the lending of short-term funds.

Separate Transactions

119. Agreements to repurchase and resell securities that do not meet the definitions in paragraphs 85-101 of this statement shall be accounted for as two separate transactions, that is, as a sale and purchase or as a purchase and sale, in accordance with the relevant statutory accounting guidance. For example, sales of bonds would result in recognition of realized gains or losses.

Offsetting

120. Reporting entities may operate on both sides of the repurchase agreement market resulting in recording of liabilities and assets representing repurchase and reverse repurchase agreements, respectively.

121. Reporting entities shall offset such liabilities and assets only to the extent that a legal right to offset exists as defined in SSAP No. 64, paragraph 2. Otherwise, separate assets and liabilities shall be recognized.

Loan Syndications

122. Borrowers often borrow amounts greater than any one lender is willing to lend. Therefore, it is common for groups of lenders to jointly fund those loans. That may be accomplished by a syndication under which several lenders share in lending to a single borrower, but each lender loans a specific amount to the borrower and has the right to repayment from the borrower.

123. A loan syndication is not a transfer of financial assets. Each lender in the syndication shall account for the amounts it is owed by the borrower. Repayments by the borrower may be made to a lead lender who then distributes the collections to the other lenders of the syndicate. In those circumstances, the lead lender is also functioning as a servicer and, therefore, shall only recognize its portion of the loan as a financial asset.

Loan Participations

124. Groups of banks or other entities also may jointly fund large borrowings through loan participations in which a single lender makes a large loan to a borrower and subsequently transfers interests in the loan to other entities.

125. Transfers by the originating lender may take the legal form of either assignments or participations. The transfers are usually on a nonrecourse basis, and the transferor (originating lender) continues to service the loan. The transferee (participating entity) may or may not have the right to sell or transfer its participation during the term of the loan, depending upon the terms of the participation agreement.

126. If the loan participation agreement transfers a participating interest in an entire financial asset (as described in paragraph 7 of this statement) and the conditions in paragraph 8 are met, the transfer shall be accounted for by the transferor as a sale of a participating interest. A transferor's right of first refusal on a bona fide offer from a third party, a requirement to obtain the transferor's permission that shall not be unreasonably withheld, or a prohibition on sale to the transferor's competitor is a limitation on the transferee's rights but presumptively does not constrain a transferee from exercising its right to pledge or

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exchange. However, if the loan participation agreement constrains the transferees from pledging or exchanging its participating interest and that constraint provides a more-than-trivial benefit to the transferor, the transferor has not relinquished control and shall account for the transfer as a secured borrowing.

Factoring Arrangements

127. Factoring arrangements are a means of discounting accounts receivable on a nonrecourse, notification basis. Accounts receivable in their entireties are sold outright, usually to a transferee (the factor) that assumes the full risk of collection, without recourse to the transferor in the event of a loss. Debtors are directed to send payments to the transferee. Factoring arrangements that meet the conditions in paragraph 8 shall be accounted for as sales of financial assets because the transferor surrenders control over the receivables to the factor.

Transfers of Receivables with Recourse

128. In a transfer of an entire receivable, a group of entire receivables, or a portion of an entire receivable with recourse, the transferor provides the transferee with full or limited recourse. The transferor is obligated under the terms of the recourse provision to make payments to the transferee or to repurchase receivables sold under certain circumstances, typically for defaults up to a specified percentage. A transfer of receivables with recourse shall not be recognized as a sale, but rather as secured borrowing. (This provision is applied regardless if the transfer was comprised of the entire receivable, a group of the entire receivable, or a portion of the entire receivable.) A transfer of receivables without recourse shall only be recognized if the transferor receives cash for the receivables. The sale shall be recognized when cash is received. Sales of premium receivables are addressed in *SSAP No. 42—Sale of Premium Receivables*.

Extinguishments of Liabilities

129. If a creditor releases a debtor from primary obligation on the condition that a third party assumes the obligation and that the original debtor becomes secondarily liable, that release extinguishes the original debtor's liability. However, in those circumstances, whether or not explicit consideration was paid for that guarantee, the original debtor becomes a guarantor. As a guarantor, it shall recognize a guarantee obligation in the same manner as would a guarantor that had never been primarily liable to that creditor, with due regard for the likelihood that the third party will carry out its obligations. The guarantee obligation shall be initially measured at fair value, and that amount reduces the gain or increases the loss recognized on extinguishment.

130. Exchanges of debt instruments or debt instrument modifications are considered extinguishments if the exchange or modification results with substantially different terms or is considered more than minor. If the cash flows under the terms of the new debt instrument are at least 10% ~~percent~~ different from the present value of the remaining cash flows under the terms of the original instrument, then the exchange of, or modification to, debt instruments is consider substantially different and/or more than minor.

Relevant Literature

131. The accounting guidance in this statement adopts with modification *FAS 166, Accounting for the Transfers of Financial Assets, an Amendment to FAS 140* (FAS 166), *FAS 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (FAS 140), as amended by FAS 166, and FAS 156, *Accounting for Servicing of Financial Assets, an amendment of FASB Statement No. 140*, as amended by FAS 166. Statutory modifications from these adoptions include:

a. Rejects the GAAP consideration for "consolidated affiliates" as the concept of consolidation has not been adopted for statutory accounting.

b. Rejects reference to GAAP standards and GAAP methods not adopted for statutory as well as concepts that are not pertinent for insurers. For example, references to investments

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"held-to-maturity", "available for sale" or "trading" and reference to FASB standards are replaced with statutory terms and references to statutory standards.

c. Rejects GAAP reference and guidance regarding "Revolving-Period Securitizations" as this GAAP guidance is not applicable to statutory accounting. This concept was also deemed not applicable to statutory accounting under SSAP No. 91R.

d. Rejects GAAP guidance for "Sale-Type and Direct-Financing Lease Receivables" as leases shall be accounted for in accordance with *SSAP No. 22R—Leases*. This conclusion is consistent with SSAP No. 91R.

e. Rejects GAAP guidance for "Banker's Acceptances and Risk Participations in Them," as not applicable for statutory accounting. This GAAP guidance was also deemed not applicable to statutory accounting under SSAP No. 91R.

f. Rejects GAAP guidance for "Removal of Account Provisions" that allows recognition of sale accounting. For statutory, transfers that would empower the transferor to reclaim assets under certain conditions (considered "removal-of-accounts provisions") are precluded from being accounted for as sales. This conclusion is consistent with SSAP No. 91R.

g. Rejects GAAP guidance for "Transfers of Receivables with Recourse" that allows transfers of receivables in their entirety with recourse to be accounted for as sales. For statutory, a transfer of receivables with recourse shall be accounted for as a secured borrowing. This conclusion is consistent with SSAP No. 91R.

h. Rejects illustrations for transactions involving transfers of lease financing receivables with residual values and banker's acceptances with a risk participation as the GAAP guidance in FAS 166 related to these topics has been rejected for statutory accounting.

i. Rejects the optionality provided within FAS 156 for subsequent measurement of servicing assets and servicing liabilities using either fair value or an amortization method. This statement requires application of a fair value method for subsequent measurement.

j. Incorporates guidance previously included in SSAP No. 91R specific to insurance entities, and guidance that was adopted from GAAP guidance not revised through the issuance of FAS 166. Items incorporated include:

    i. Clarification that transfers of financial assets that are in substance real estate shall be accounted for in accordance with *SSAP No. 40R—Real Estate Investments* (paragraph 2).

    ii. Clarification that transactions between related parties or affiliates are accounted for in accordance with *SSAP No. 25—Affiliates and Other Related Parties* (paragraph 4).

    iii. Clarification that the guidance does not address the securitization of mortality or morbidity risk (paragraph 5).

    iv. Guidance on the accounting of sale transactions for entities required to maintain an interest maintenance reserve (IMR). This guidance requires such entities to account for realized and unrealized capital gains and losses per the guidance in the SSAP for the specific type of investment, or if not specifically stated in the related SSAP, in accordance with SSAP No. 7 (paragraph 11.c.).

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v. Clarification of when servicing assets and servicing liabilities shall be recognized as well as measurement of these items. Continues prior statutory decision that servicing rights assets shall be nonadmitted (paragraphs 15-17).

vi. Guidance on the accounting for transactions that require the granting of a security interest in certain assets to another party to serve as collateral for their performance under a contract (paragraph 20).

vii. Disclosures on security lending transactions, loaned securities; securities underlying repurchase and reverse repurchase agreements, dollar repurchase and dollar reverse repurchase agreements; receivables with recourse; and wash sales (paragraphs 28.a., 28.b., and 28.h.-28.l.).

viii. Guidance on the sales of future revenues (paragraph 77).

ix. Guidance on collateral requirements for securities lending transactions (paragraph 91).

x. Clarification that repurchase agreements, reverse repurchase agreements and dollar repurchase agreements meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this guidance (paragraph 96).

xi. Guidance on Repurchase Agreements (paragraphs 96-110).

xii. Guidance on Reverse Repurchase Agreements (paragraphs 111-112).

xiii. Guidance on Collateral for Reverse and Repurchase Agreements (paragraph 113).

xiv. Guidance on Dollar Repurchase Agreements (paragraph 114-118).

xv. Guidance for Separate Transactions (paragraph 119).

xvi. Guidance for Offsetting (paragraph 121). (This guidance was revised in November 2012 to only allow offsetting when a valid right to offset exists in accordance with SSAP No. 64. This is different from previous guidance reflected in SSAP No. 91R.)

xvii. Guidance for Transfers of Receivables with Recourse (paragraph 129).

132. This statement also adopts *FASB Staff Position 140-3, Accounting for Transfers of Financial Assets and Repurchase Financing Transactions* (FSP FAS 140-3), *ASU 2011-03, Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements* and *AICPA Statement of Position 90-3, Definition of the Term Substantially the Same for Holders of Debt Instruments, as used In Certain Audit Guides and a Statement of Position.* This statement adopts *FASB Emerging Issues Task Force (EITF) No. 87-34, Sale of Mortgage Servicing Rights with a Subservicing Agreement, FASB EITF No. 88-11, Allocation of Recorded Investment When a Loan as Part of a Loan is Sold, FASB EITF No. 88-18, Sales of Future Revenues, FASB EITF No. 88-22, Securitization of Credit Card and Other Receivable Portfolios, FASB EITF No. 90-21, Balance Sheet Treatment of a Sale of Mortgage Servicing Rights with a Subservicing Agreement, FASB EITF No. 95-5, Determination of What Risks and Rewards, If Any, Can Be Retained and Whether Any Unresolved Contingencies May Exist in a Sale of Mortgage Loan Servicing Rights, FASB EITF No. 96-19, Debtor's Accounting for a Modification or Exchange of Debt Instruments*, as amended by FAS 166, and *FASB EITF No. 01-7, Creditor's Accounting for a Modification or Exchange of Debt Instruments*. This statement adopts ASC guidance for short sales with modification to require the short sale obligation to be reflected as a contra-asset rather than a liability. Also, the recognition of unrealized gains

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and losses is consistent with statutory accounting recognition, rather than directly to net income under U.S. GAAP. (The adopted ASC guidance includes guidance reflected in 942-405-25-1 through 25-2, 942-405-35-1, and 942-405-45-1. Additionally, the guidance in ASC 815-10-55-57 through 59 and 815-10-15-15 through 17, which addresses whether short sales are within the scope of SSAP No. 86, and the definition of a regular-way security trade is also adopted.)

133. This statement rejects FASB *EITF No. 84-5, Sale of Marketable Securities with a Put Option*, and FASB *EITF No. 92-2, Measuring Loss Accruals by Transferors of Receivables with Recourse* and *FTB 01-1:* Effective *Date for Certain Financial Institutions of Certain Provisions of Statement 140 related to Isolation of Transferred Financial Assets*. This statement rejects *FIN 41, Offsetting Amounts Related to Certain Repurchase and Reverse Repurchase Agreements*. This rejection, as it is a reversal of the prior adoption of this guidance in SSAP No. 45, and the revisions to paragraphs 121-122 adopted November 2012, are effective January 1, 2013. This guidance has been rejected as it permits optionality as to whether offsetting and net reporting occurs for repurchase and reverse purchase agreements under master netting agreements. The provisions of SSAP No. 64 shall be used in determining whether assets and liabilities shall be offset and reported net.

134. Effective December 31, 2023, this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~134.~~135. This standard shall be effective for years beginning on and after January 1, 2013 (effective date) and shall be applied prospectively. This statement must be applied as of the beginning of the reporting entity's first annual reporting period after the effective date, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. This statement must be applied to transfers occurring on or after the effective date. On and after the effective date, the concept of a qualifying special purpose entity is no longer relevant for statutory accounting purposes. The disclosure provisions of this statement shall be applied to transfers that occurred both before and after the effective date of this statement. Guidance reflected in paragraph 22 added from *INT 03-05, EITF 01-7: Creditor's Accounting for a Modification or Exchange of Debt Instruments* has been in effect since June 22, 2003. Guidance in paragraphs 22 and 121 was originally contained in *INT 99-14: EITF No. 96-19, Debtor's Accounting for a Modification or Exchange of Debt Instruments, as amended by FAS 166* and was effective October 4, 1999. Revisions to incorporate guidance for short sales, detailed in *Issue Paper No. 152—Short Sales*, are effective on a prospective basis for transactions occurring on or after January 1, 2017, unless a reporting entity has previously been following an approach similar to the adopted guidance. Reporting entities that have previously been following a similar approach shall not deviate from that approach prior to the effective date of the adopted guidance. Revisions to paragraph 28.a. of this statement to incorporate enhanced disclosures on repurchase and reverse repurchase transactions are effective December 31, 2017.

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REFERENCES

Other

- *SSAP No. 18—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*
- *SSAP No. 33—Securitization*
- *SSAP No. 45—Repurchase Agreements, Reverse Repurchase Agreements and Dollar Repurchase Agreements*
- *SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*
- *Purposes and Procedures Manual of the NAIC Investment Analysis Office*

Relevant Issue Papers

- *Issue Paper No. 122—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*
- *Issue Paper No. 134—Servicing Assets/Liabilities, An Amendment of SSAP No. 91*
- *Issue Paper No. 141—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*
- *Issue Paper No. 144—Substantive Revisions to SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities – Revised*
- *Issue Paper No. 152—Short Sales*

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EXHIBIT A - GLOSSARY

Adequate Compensation

The amount of benefits of servicing that would fairly compensate a substitute servicer should one be required, which includes the profit that would be demanded in the marketplace.

Agent

A party that acts for and on behalf of another party. For example, a third-party intermediary is an agent of the transferor if it acts on behalf of the transferor.

Attached Call

A call option held by the transferor of a financial asset that becomes part of and is traded with the underlying instrument. Rather than being an obligation of the transferee, an attached call is traded with and diminishes the value of the underlying instrument transferred subject to that call.

Beneficial Interests

Rights to receive all or portions of specified cash inflows received by a trust or other entity, including, but not limited to, senior and subordinated shares of interest, principal, or other cash inflows to be "passed-through" or "paid-through," premiums due to guarantors, commercial paper obligations, and residual interests, whether in the form of debt or equity.

Benefits of Servicing

Revenues from contractually specified servicing fees, late charges, and other ancillary sources, including "float."

Cleanup Call

An option held by the servicer or its affiliate, which may be the transferor, to purchase the remaining transferred financial assets, or the remaining beneficial interests not held by the transferor, its affiliates, or its agents in an entity (or in a series of beneficial interests in transferred financial assets within an entity), if the amount of outstanding financial assets or beneficial interests falls to a level at which the cost of servicing those assets or beneficial interests becomes burdensome in relation to the benefits of servicing.

Collateral

Personal or real property in which a security interest has been given.

Continuing Involvement

Any involvement with the transferred financial assets that permits the transferor to receive cash flows or other benefits that arise from the transferred financial assets or that obligates the transferor to provide additional cash flows or other assets to any party related to the transfer. All available evidence shall be considered, including, but not limited to, explicit written arrangements, communications between the transferor and the transferee or its beneficial interest holders, and unwritten arrangements customary to similar transfers. Examples of continuing involvement with the transferred financial assets include, but are not limited to, servicing arrangements, recourse or guarantee arrangements, agreements to purchase or redeem transferred financial assets, options written or held, derivative financial instruments that are entered into contemporaneously with, or in contemplation of, the transfer, arrangements to provide financial support, pledges of collateral, and the transferor's beneficial interests in the transferred financial assets.

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Contractually Specified Servicing Fees

All amounts that, per contract, are due to the servicer in exchange for servicing the financial asset and would no longer be received by a servicer if the beneficial owners of the serviced assets (or their trustees or agents) were to exercise their actual or potential authority under the contract to shift the servicing to another servicer. Depending on the servicing contract, those fees may include some or all of the difference between the interest rate collectible on the financial asset being serviced and the rate to be paid to the beneficial owners of those financial assets.

Derecognize

Remove previously recognized assets or liabilities from the statement of financial position.

Derivative Financial Instrument

A derivative instrument (as defined in *SSAP No. 86—Derivatives*) that is a financial instrument (refer to *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures*, paragraph 2).

Embedded Call

A call option held by the issuer of a financial instrument that is part of and trades with the underlying instrument. For example, a bond may allow the issuer to call it by posting a public notice well before its stated maturity that asks the current holder to submit it for early redemption and provides that interest ceases to accrue on the bond after the early redemption date. Rather than being an obligation of the initial purchaser of the bond, an embedded call trades with and diminishes the value of the underlying bond.

Financial Asset

Cash, evidence of an ownership interest in an entity, or a contract that conveys to a one entity a right (a) to receive cash or another financial instrument from a second entity or (b) to exchange other financial instruments on potentially favorable terms with the second entity.

Financial Liability

A contract that imposes on one entity an obligation (a) to deliver cash or another financial instrument to a second entity or (b) to exchange other financial instruments on potentially unfavorable terms with the second entity.

Freestanding Call

A call that is neither embedded in nor attached to an asset subject to that call.

Interest-Only Strip

A contractual right to receive some or all of the interest due on a bond, mortgage loan, collateralized mortgage obligation, or other interest-bearing financial asset.

Naked Short Sale

A short sale in which the seller does not borrow or arrange to borrow the securities in time to make delivery to the buyer within the standard three-day settlement period (T+3). As a result, the seller fails to deliver securities to the buyer when delivery is due (known as a "failure to deliver" or "fail").

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Participating Interest

A participating interest has the following characteristics:

a. From the date of the transfer, it represents a proportionate (pro rata) ownership interest in an entire financial asset. The percentage of ownership interests held by the transferor in the entire financial asset may vary over time, while the entire financial asset remains outstanding as long as the resulting portions held by the transferor or its agents) and the transferee(s) meet the other characteristics of a participating interest. For example, if the transferor's interest in an entire financial asset changes because it subsequently sells another interest in the entire financial asset, the interest held initially and subsequently by the transferor must meet the definition of a participating interest.

b. From the date of the transfer, all cash flows received from the entire financial asset are divided proportionately among the participating interest holders in an amount equal to their share of ownership. Cash flows allocated as compensation for services performed, if any, shall not be included in that determination provided those cash flows are not subordinate to the proportionate cash flows of the participating interest and are not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace. In addition, any cash flows received by the transferor as proceeds of the transfer of the participating interest shall be excluded from the determination of proportionate cash flows provided that the transfer does not result in the transferor receiving an ownership interest in the financial asset that permits it to receive disproportionate cash flows.

c. The rights of each participating interest holder (including the transferor in its role as a participating interest holder) have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That priority does not change in the event of bankruptcy or other receivership of the transferor, the original debtor, or any other participating interest holder. Participating interest holders have no recourse to the transferor, its agents or to each other, other than standard representations and warranties, ongoing contractual obligations to service the entire financial asset and administer the transfer contract, and contractual obligations to share in any set-off benefits received by any participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder. For example, if a participating interest holder also is the servicer of the entire financial asset and receives cash in its role as servicer, that arrangement would not violate this requirement.

d. No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

Proceeds

Cash, beneficial interests, servicing assets, derivatives, or other assets that are obtained in a transfer of financial assets, less any liabilities incurred.

Recourse

The right of a transferee of receivables to receive payment from the transferor of those receivables for (a) failure of debtors to pay when due, (b) the effects of prepayments, or (c) adjustments resulting from defects in the eligibility of the transferred receivables.

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Regular-Way Security Trade

Contracts that provide for delivery of a security within a period of time after the trade date generally established by regulations or conventions in the marketplace or exchange in which it is being executed.

Securitization

The process by which financial assets are transformed into securities.

Security Interest

A form of interest in property that provides that upon default of the obligation for which the security interest is given, the property may be sold in order to satisfy that obligation.

Seller

A transferor that relinquishes control over financial assets by transferring them to a transferee in exchange for consideration.

Servicing Asset

A contract to service financial assets under which the estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues are expected to more than adequately compensate the servicer for performing the servicing. A servicing contract is either (a) undertaken in conjunction with selling or securitizing the financial assets being serviced or (b) purchased or assumed separately.

Short Sale

A short sale, as defined for statutory accounting, is the sale of a security that a selling reporting entity (seller) does not own at the time of sale or a sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller.

Servicing Liability

A contract to service financial assets under which the estimated future revenues from contractually specified servicing fees, late charges, and other ancillary revenues are not expected to adequately compensate the servicer for performing the servicing.

Standard Representations and Warranties

Representations and warranties that assert the financial asset being transferred is what it is purported to be at the transfer date. Examples include representations and warranties about (a) the characteristics, nature, and quality of the underlying financial asset, including characteristics of the underlying borrower and the type and nature of the collateral securing the underlying financial asset, (b) the quality, accuracy, and delivery of documentation relating to the transfer and the underlying financial asset, and (c) the accuracy of the transferor's representations in relation to the underlying financial asset.

Transfer

The conveyance of a noncash financial asset by and to someone other than the issuer of that financial asset. Thus, a transfer includes selling a receivable, putting it into a securitization trust, or posting it as collateral but excludes the origination of that receivable, the settlement of that receivable, or the restructuring of that receivable into a security in a troubled debt restructuring.

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Transferee

An entity that receives a financial asset, an interest in a financial asset, or a group of financial assets from a transferor.

Transferor

An entity that transfers a financial asset, an interest in a financial asset, or a group of financial assets that it controls to another entity.

Unilateral Ability (See paragraphs 53 and 54)

A capacity for action not dependent on the actions (or failure to act) of any other party.

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EXHIBIT B - ILLUSTRATIONS

Illustration—Recording Transfers with Proceeds of Cash, Derivatives, and Other Liabilities

1. Company A transfers entire loans with a carrying amount of $1,000 to a subsidiary and receives proceeds with a fair value of $1,030 and the transfer is accounted for as a sale. Company A undertakes no servicing responsibilities and assumes a limited recourse obligation to repurchase delinquent loans.

Company A agrees to provide the transferee a return at a floating rate of interest even though the contractual terms of the loan are fixed rate in nature (that provision is effectively an interest rate swap).

Fair Values		
Cash proceeds		$1,050
Interest rate swap asset		40
Recourse obligation		60
Net Proceeds		
Cash received		$1,050
Plus: Interest rate swap asset		40
Less: Recourse obligation		(60)
Net proceeds		$1,030
Gain on Sale		$1,030
Net proceeds		1,000
Carrying amount of loans sold		$30
Gain on sale		
Journal Entry		
Cash	1,050	
Interest rate swap asset	40	
Loans		1,000
Recourse obligation		60
Gain on sale		30
To record transfer		

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Illustration—Recording Transfers of Participating Interests

2. Company B transfers a nine-tenths participating interest in a loan with a fair value of $1,100 and a carrying amount of $1,000, and the transfer is accounted for as a sale. The servicing contract has a fair value of zero because Company B estimates that the benefits of servicing are just adequate to compensate it for its servicing responsibilities.

Fair Values	
Cash proceeds for nine-tenths sold ($1,100 x 9/10)	$990
One-tenth interest continued to be held by the transferor ($1,100 x 1/10)	110

Allocated Carrying Amount Based on Relative Fair Values

	Fair Value	**Percentage Of Total Fair Value**	**Allocated Carrying Amount**
Nine-tenths participating interest sold ($1,100 x 9/10)	$990	90	$900
One-tenth participating interest continued to be held by the transferor ($1,100 x 1/10)	110	10	100
Total	$ 1,100	100	$1,000

Gain on Sale	
Net proceeds	$ 990
Less: Carrying amount of loans sold	(900)
Gain on sale	$90

Journal Entry		
Cash	990	
Loans		900
Gain on sale		90
To record transfer		

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Illustration—Sale of Receivables with Servicing Obtained

3. Company C originates $1,000 of loans that yield 10% ~~percent~~ interest income for their estimated lives of 9 years. Company C transfers the entire loans to an entity and the transfer is accounted for as a sale. Company C receives as proceeds $1,000 cash, a beneficial interest to receive 1% ~~percent~~ on the contractual interest on the loans (an interest-only strip receivable), and an additional 1% ~~percent~~ of the contractual interest as compensation for servicing the loans. The fair values of the servicing asset and the interest-only strip receivable are $40 and $60, respectively.

Fair Values	
Cash proceeds	$1,000
Servicing asset	40
Interest-only strip receivable	60

Net Proceeds	
Cash proceeds	$1,000
Servicing Asset	40
Interest-only strip receivable	60
Net Proceeds	$1,100

Gain on Sale	
Net proceeds	$1,100
Less: Carrying amount of loans sold	(1,000)
Gain on sale	$ 100

Journal Entries		
Cash	1,000	
Interest-only strip receivable	60	
Servicing Asset	40	
Loans		1,000
Gain on sale		100
To record transfer and to recognize interest-only strip receivable and servicing asset		

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Illustration—Securities Lending Transaction Treated as a Secured Borrowing

4. The following example illustrates the accounting for a securities lending transaction treated as a secured borrowing, in which the securities borrower sells the securities upon receipt and later buys similar securities to return to the securities lender:

Facts	
Transferor's carrying amount and fair value of security loaned	$1,000
Cash "collateral"	1,020
Transferor's return from investing cash collateral at a 5% ~~percent~~ annual rate	5
Transferor's rebate to the securities borrower at a 4% ~~percent~~ annual rate	4

For simplicity, the fair value of the security is assumed not to change during the 35-day term of the transaction.

Journal Entries for the Transferor

At inception:		
Cash	1,020	
Payable under securities loan agreements		1,020
To record the receipt of cash collateral		
Securities pledged to creditors	1,000	
Securities		1,000
To reclassify loaned securities that the secured party has the right to sell or repledge		
Money market instrument	1,020	
Cash		1,020
To record investment of cash collateral		
At conclusion:		
Cash	1,025	
Interest		5
Money market instrument		1,020
To record results of investment		
Securities	1,000	
Securities pledged to creditors		1,000
To record return of security		
Payable under securities loan agreements	1,020	
Interest ("rebate")	4	
Cash		1,024
To record repayment of cash collateral plus interest		

Journal Entries for the Transferee

At inception:		
Receivable under securities loan agreements	1,020	
Cash		1,020
To record transfer of cash collateral		

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Cash	1,000	
Obligation to return borrowed securities		1,000

To record sale of borrowed securities to a third party and the resulting obligation to return securities that it no longer holds

At conclusion:

Obligation to return borrowed securities	1,000	
Cash		1,000

To record the repurchase of securities borrowed

Cash	1,024	
Receivable under securities loan agreements		1,020
Interest revenue (“rebate”)		4

To record the receipt of cash collateral and rebate interest

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Illustration—Short Sale Settled with Securities Borrowed Under a Secured Borrowing Agreement

5. The following example illustrates the accounting for a securities borrowing transaction treated as a secured borrowing, in which the insurer borrows securities and delivers the borrowed securities to a different counterparty to settle a short sale transaction.

Cash
    Contra-Asset – Securities Sold Short

To recognize the cash received and the obligation to delivery securities under a short sale.

Receivable Under Securities Loan Agreement (Borrow Securities)
    Cash

To recognize transfer of cash under the security borrowing agreement, with recognition of a receivable for the return. The actual securities borrowed under the agreement (as sale accounting criteria is not met) shall not be recognized on the financial statements.

Borrowed Asset ("Proceeds" of selling asset)
    Obligation to return Securities Borrowed

To recognize the use of the borrowed security to settle a short-sale transaction. This transaction would be similar to receiving "proceeds" from the sale of a borrowed security – but instead of "cash" recognition of the actual borrowed asset, with an obligation to return the borrowed securities.

Contra-Asset – Securities Sold Short
    Borrowed Asset

Close out the short sale by delivering the asset to the counterparty.

Obligation to Return Securities Borrowed
    Cash

Eliminate the liability to return the borrowed asset by purchasing the asset and re-establishing it as off-balance sheet collateral for the securities borrowing transaction.

Cash
    Receivable Under Securities Loan Agreement

To recognize the return of cash collateral from the transferor and the unwinding of the securities borrowing agreement.

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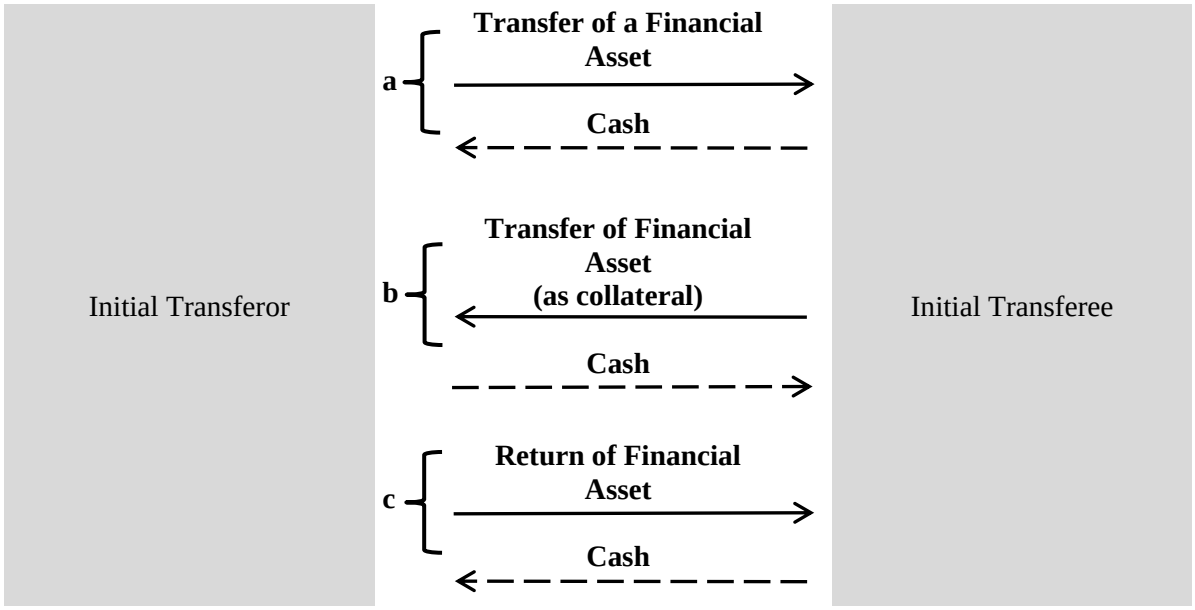
Illustration—Initial Transfer and Repurchase Financing

6. The following diagram is an example of an initial transfer of a financial asset and a subsequent repurchase financing, as described in paragraphs 105-110.



Statement of Statutory Accounting Principles No. 104 – Revised

Share-Based Payments

STATUS

Type of Issue	Common Area
Issued	August 11, 2012; Substantively revised December 15, 2013
Effective Date	January 1, 2013
Affects	Supersedes SSAP No. 13; Nullifies and incorporates INT 99-17, INT 00-06, INT 00-32 and INT 01-14
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. This statement provides statutory accounting principles for transactions in which an entity exchanges its equity instruments to employees and non-employees[1] in share-based payment transactions, including employee share purchase plans and deferred compensation obligations held in a rabbi trust. This

[1] Guidance referencing grantees is intended to be applicable to recipients of both employee and nonemployee awards, and guidance referencing employees or nonemployees is only applicable to those specific types of awards.

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statement does not provide statutory accounting principles for employee share ownership plans; those transactions are addressed in *SSAP No. 12—Employee Stock Ownership Plans*.

SUMMARY OF ISSUE

2. The objective of accounting for transactions under share-based payment arrangements is to recognize in the financial statements the goods or services received in exchange for equity instruments granted or liabilities incurred and the related cost to the entity as those goods or services are received. This statement uses the terms "compensation" and "payment" in their broadest senses to refer to the consideration paid for goods, ~~or~~ services, or the consideration paid to a customer.

3. This statement requires that the cost resulting from all share-based payment transactions be recognized in the financial statements. This statement establishes fair value as the measurement objective in accounting for share-based payment arrangements and requires all entities to apply a fair-value-based measurement method[2] in accounting for share-based payment transactions .

Scope and Scope Exceptions

4. This statement applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in the grantor's own operations, or provides consideration payable to a customer by issuing (or offering to issue) its shares, share options, or other equity instruments or by incurring liabilities to an employee or nonemployee that meet either of the following conditions:

a. The amounts are based, at least in part[3], on the price of the entity's shares or other equity instruments.

b. The awards require or may require settlement by issuing the entity's equity shares or other equity instruments.

5. Share-based payments awarded to a grantee by a related party or other holder of an economic interest in the entity as compensation for goods or services provided to the reporting entity are share-based payment transactions to be accounted for under this statement unless the transfer is clearly for a purpose other than compensation for goods or services to the reporting entity. The substance of such a transaction is that the economic interest holder makes a capital contribution to the reporting entity, and that entity makes a share-based payment to the grantee in exchange for services rendered or goods received. An example of a situation in which such a transfer is not compensation is a transfer to settle an obligation of the economic interest holder to the grantee that is unrelated to goods or services to be used or consumed in a grantor's own operations.

[2] Accounting pronouncements that require fair value measurements but that are excluded from *SSAP No. 100R—Fair Value* is limited to this statement addressing share-based payment transactions. The fair value measurement objective in this statement is generally consistent with the fair value measurement objective in SSAP No. 100R. However, for certain share-based payment transactions, the measurements at the grant date are fair-value-based measurements, not fair value measurements. Although some measurements in this statement are fair value measurements, for practical reasons this statement is excluded in its entirety from SSAP No. 100R. To be consistent with GAAP guidance on share-based payment transactions, the definition of fair value for use in this statement is: "the amount at which the asset (or liability) could be bought (or incurred) or sold (settled) in a current transaction between willing parties, that is, other than in a forced or liquidation sale." Observable market prices of identical or similar equity or liability instruments in active markets are the best estimate of fair value and, if available, should be used as the basis for the measurement of equity and liability instruments awarded in a share-based payment transaction with employees.

[3] The phrase "at least in part" is used because an award of share-based compensation may be indexed to both the price of an entity's shares and something else that is neither the price of the entity's shares nor a market, performance, or service condition.

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6. The guidance in this statement does not apply to:

a. Equity instruments held by an employee stock ownership plan. Such equity instruments shall follow the guidance in *SSAP No. 12—Employee Stock Ownership Plans*.

b. Transactions involving equity instruments granted to a lender or investor that provides financing to the issuer.

c. Transactions involving equity instruments granted in conjunction with selling goods or services to customers as part of a contract (for example, sales incentives). If consideration payable to a customer is payment for a distinct good or service from the customer, then the entity shall account for the purchase of the good or service in the same way it accounts for other purchases from suppliers. Therefore, share-based payment awards granted to a customer for a distinct good or service to be used or consumed in the grantor's own operations are accounted for under this statement.

7. Paragraphs 116-123 apply to all entities that use employee share purchase plans. This is a separate and distinct scope from share-based payment transactions captured in paragraph 4.

Recognition

8. An entity shall recognize the goods acquired or services received in a share-based payment transaction when it obtains the goods or as services are received, as further described in paragraphs 9-10. The entity shall recognize either a corresponding increase in equity or a liability, depending on whether the instruments granted satisfy the equity or liability classification criteria (see paragraphs 15-29).

9. Employee services themselves are not recognized before they are received. As the services are consumed, the entity shall recognize the related cost. For example, as services are consumed, the cost usually is recognized in determining net income of that period, for example, as expenses incurred for employee services. In some circumstances, the cost of services may be initially capitalized as part of the cost to acquire or construct another asset, such as inventory, and later recognized in the income statement when that asset is disposed of or consumed. This statement refers to recognizing compensation cost rather than compensation expense because any compensation cost that is capitalized as part of the cost to acquire or construct an asset would not be recognized as compensation expense in the income statement.

10. Transactions with nonemployees in which share-based payment awards are granted in exchange for the receipt of goods or services may involve a contemporaneous exchange of the share-based payment awards for goods or services or may involve an exchange that spans several financial reporting periods. Furthermore, by virtue of the terms of the exchange with the grantee, the quantity and terms of the share-based payment awards to be granted may be known or not known when the transaction arrangement is established because of specific conditions dictated by the agreement (for example, performance conditions). Judgment is required in determining the period over which to recognize cost, otherwise known as the nonemployee's vesting period.

11. This guidance does not address the period(s) or the manner (that is, capitalize versus expense) in which an entity granting the share-based payment award (the purchaser or grantor) to a nonemployee shall recognize the cost of the share-based payment award that will be issued, other than to require that a nonadmitted prepaid asset or expense be recognized (or previous recognition reversed) in the same period(s) and in the same manner as if the grantor had paid cash for the goods or services instead of paying with or using the share-based payment award.

12. The accounting for all share-based payment transactions shall reflect the rights conveyed to the holder of the instruments and the obligations imposed on the issuer of the instruments, regardless of how those transactions are structured. For example, the rights and obligations embodied in a transfer of equity shares for a note that provides no recourse to other assets of the grantee (that is, other than the shares) are

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substantially the same as those embodied in a grant of equity share options. Thus, that transaction shall be accounted for as a substantive grant of equity share options.

13. Assessment of both the rights and obligations in a share-based payment award and any related arrangement and how those rights and obligations affect the fair value of an award requires the exercise of judgment in considering the relevant facts and circumstances.

Determining the Grant Date

14. As a practical accommodation, in determining the grant date of an award subject to this statement, assuming all other criteria in the grant date definition have been met, a mutual understanding of the key terms and conditions of an award to an individual grantee shall be presumed to exist at the date the award is approved in accordance with the relevant corporate governance requirements (that is, by the Board or management with the relevant authority) if both of the following conditions are met:

a. The award is a unilateral grant and, therefore, the recipient does not have the ability to negotiate the key terms and conditions of the award with the grantee.

b. The key terms and conditions of the award are expected to be communicated to an individual recipient within a relatively short time period from the date of approval. A relatively short time period is that period in which an entity could reasonably complete all actions necessary to communicate the awards to the recipients in accordance with the entity's customary practices.

Determining Whether to Classify a Financial Instrument as a Liability or As Equity

15. Paragraphs 15-29 provide guidance for determining whether certain financial instruments awarded in share-based payment transactions are liabilities. In determining whether an instrument not specifically discussed in those paragraphs shall be classified as a liability or as equity, an entity shall apply statutory accounting principles applicable to financial instruments issued in transactions not involving share-based payment.

16. Unless paragraphs 17-29 require otherwise, an entity shall apply the classification criteria in Exhibit A in determining whether to classify as a liability a freestanding financial instrument given to a grantee in a share-based payment transaction. Paragraphs 78-83 provide criteria for determining when instruments subject to this statement subsequently become subject to other applicable statutory accounting principles.

17. In determining the classification of an instrument, an entity shall take into account the classification requirements as established by Exhibit A. In addition, a call option written on an instrument that is not classified as a liability under those classification requirements also shall be classified as equity so long as those equity classification requirements for the entity continue to be met, unless liability classification is required under the provisions of paragraphs 20-21.

18. Exhibit A does not apply to outstanding shares embodying a conditional obligation to transfer assets, for example, shares that give the grantee the right to require the grantor to repurchase them for cash equal to their fair value (puttable shares). A put right may be granted to the grantee in a transaction that is related to a share-based compensation arrangement. If exercise of such a put right would require the entity to repurchase shares issued under the share-based compensation arrangement, the shares shall be accounted for as puttable shares. A puttable (or callable) share awarded to an grantee as compensation shall be classified as a liability if either of the following conditions is met:

a. The repurchase feature permits the grantee to avoid bearing the risks and rewards normally associated with equity share ownership for a reasonable period of time from the date the good is delivered or the service is rendered, and the share is issued. A grantee begins to bear the risks and rewards normally associated with equity share ownership when all the

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goods are delivered, or all the service has been rendered and the share is issued. A repurchase feature that can be exercised only upon the occurrence of a contingent event that is outside the grantee's control (such as an initial public offering) would not meet this condition until it becomes probable that the event will occur within the reasonable period of time.

b. It is probable that the grantor would prevent the grantee from bearing those risks and rewards for a reasonable period of time from the date the share is issued.

For this purpose, a period of six months or more is a reasonable period of time.

19. A puttable (or callable) share that does not meet either of those conditions shall be classified as equity.

20. Options or similar instruments on shares shall be classified as liabilities if either of the following conditions is met:

a. The underlying shares are classified as liabilities.

b. The entity can be required under any circumstances to settle the option or similar instrument by transferring cash or other assets. A cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the grantee's control (such as an initial public offering) would not meet this condition until it becomes probable that event will occur.

21. For example, a reporting entity that is a Securities and Exchange Commission (SEC) registrant may grant an option to a grantee that, upon exercise, would be settled by issuing a mandatorily redeemable share. Because the mandatorily redeemable share would be classified as a liability under Exhibit A (as well as under *SSAP No. 72—Surplus and Quasi-Reorganizations*), the option also would be classified as a liability.

22. An award may be indexed to a factor in addition to the entity's share price. If that additional factor is not a market, performance, or service condition, the award shall be classified as a liability for purposes of this statement, and the additional factor shall be reflected in estimating the fair value of the award.

23. For this purpose, an award of equity share options granted to a grantee of an entity's foreign operation that provides for a fixed exercise price denominated either in the foreign operation's functional currency or in the currency in which the foreign operation's employee's pay is denominated shall not be considered to contain a condition that is not a market, performance, or service condition. Therefore, such an award is not required to be classified as a liability if it otherwise qualifies as equity. For example, equity share options with an exercise price denominated in euros granted to employees or nonemployees of a U.S. entity's foreign operation whose functional currency is the euro are not required to be classified as liabilities if those options otherwise qualify as equity. In addition, options granted to employees and nonemployees are not required to be classified as liabilities even if the functional currency of the foreign operation is the U.S. dollar, provided that the foreign operation's employees are paid in euros.

24. For purposes of applying paragraph 22, a share-based payment award with an exercise price denominated in the currency of a market in which a substantial portion of the entity's equity securities trades shall not be considered to contain a condition that is not a market, performance, or service condition. Therefore, in accordance with that paragraph, such an award shall not be classified as a liability if it otherwise qualifies for equity classification. For example, a parent entity whose functional currency is the Canadian dollar grants equity share options with an exercise price denominated in U.S. dollars to grantees of a Canadian entity with the functional and payroll currency of the Canadian dollar. If a substantial portion of the parent entity's equity securities trades on a U.S. dollar denominated exchange, the options are not precluded from equity classification.

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25. The accounting for an award of a share-based payment shall reflect the substantive terms of the award and any related arrangement. Generally, the written terms provide the best evidence of the substantive terms of an award. However, an entity's past practice may indicate that the substantive terms of an award differ from its written terms. For example, an entity that grants a tandem award under which a grantee receives either a stock option or a cash-settled stock appreciation right is obligated to pay cash on demand if the choice is the grantee's, and the entity thus incurs a liability to the grantee. In contrast, if the choice is the entities, it can avoid transferring its assets by choosing to settle in stock, and the award qualifies as an equity instrument. However, if an entity that nominally has the choice of settling awards by issuing stock predominately settles in cash or if the entity usually settles in cash whenever a grantee asks for cash settlement, the entity is settling a substantive liability rather than repurchasing an equity instrument. In determining whether an entity that has the choice of settling an award by issuing equity shares has a substantive liability, the entity also shall consider whether:

a. It has the ability to deliver the shares. Requirements to deliver registered shares do not, by themselves, imply that an entity does not have the ability to deliver shares and thus do not require an award that otherwise qualifies as equity to be classified as a liability.)

b. It is required to pay cash if a contingent event occurs (see paragraphs 20-21).

26. A provision that permits grantees to effect a broker-assisted cashless exercise of part or all of an award of share options through a broker does not result in liability classification for instruments that otherwise would be classified as equity if both of the following criteria are satisfied:

a. The cashless exercise requires a valid exercise of the share options.

b. The grantee is the legal owner of the shares subject to the option (even though the grantee has not paid the exercise price before the sale of the shares subject to the option).

27. A broker that is a related party of the entity must sell the shares in the open market within a normal settlement period, which generally is three days, for the award to qualify as equity.

28. Similarly, a provision for either direct or indirect (through a net-settlement feature) repurchase of shares issued upon exercise of options (or the vesting of nonvested shares), with any payment due employees withheld to meet the employer's statutory withholding requirements resulting from the exercise, does not, by itself, result in liability classification of instruments that otherwise would be classified as equity. However, if the amount that is withheld, or may be withheld at the employer's discretion, is in excess of the maximum statutory tax rates in the employee's applicable jurisdictions, the entire award shall be classified and accounted for as a liability. That is, to qualify for equity classification, the employer must have a statutory obligation to withhold taxes on the employee's behalf, and the amount withheld cannot exceed the maximum statutory tax rates in the employees' applicable jurisdictions. The maximum statutory tax rates are based on the applicable rates of the relevant tax authorities (for example, federal, state, and local), including the employee's share of payroll or similar taxes, as provided in tax law, regulations, or the authority's administrative practices, not to exceed the highest statutory rate in that jurisdiction, even if that rate exceeds the highest rate that may be applicable to the specific award grantee.

29. Cash paid to a tax authority by an grantor when withholding shares from a grantee's award for tax withholding purposes shall be considered cash flows from financing activities in the Statement of Cash Flows as it represents an outlay to reacquire the entity's equity instruments.

Market, Performance, and Service Conditions

30. Accruals of compensation cost for an award with a performance condition shall be based on the probable outcome of that performance condition—compensation cost shall be accrued if it is probable that the performance condition will be achieved and shall not be accrued if it is not probable that the performance condition will be achieved. If an award has multiple performance conditions (for example, if the number of

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options or shares a grantee earns varies depending on which, if any, of two or more performance conditions is satisfied), compensation cost shall be accrued if it is probable that a performance condition will be satisfied. In making that assessment, it may be necessary to take into account the interrelationship of those performance conditions.

31. If an award requires satisfaction of one or more market, performance, or service conditions (or any combination thereof), compensation cost shall be recognized if the good is delivered or the service is rendered, and no compensation cost shall be recognized if the good is not delivered or the service is not rendered.

Payroll Taxes

32. A liability for employee payroll taxes on employee stock compensation shall be recognized on the date of the event triggering the measurement and payment of the tax to the taxing authority (for a nonqualified option in the United States, generally the exercise date). Payroll taxes, even though directly related to the appreciation on stock options, are operating expenses and shall be reflected as such in the statement of operations.

Initial Measurement

33. While some of the material in paragraphs 33-63 was written in terms of awards classified as equity, it applies equally to awards classified as liabilities.

34. A share-based payment transaction shall be measured based on the fair value (or in certain situations specified in this statement, a calculated value or intrinsic value) of the equity instruments issued.

35. An entity shall account for the compensation cost from share-based payment transactions in accordance with the fair-value-based method set forth in this statement. That is, the cost of goods obtained or services received in exchange for awards of share-based compensation generally shall be measured based on the grant-date fair value of the equity instruments issued or on the fair value of the liabilities incurred. The cost of goods obtained or services received by an entity as consideration for equity instruments issued or liabilities incurred in share-based compensation transactions with employees shall be measured based on the fair value of the equity instruments issued or the liabilities settled. The portion of the fair value of an instrument attributed to goods obtained or services received is net of any amount that a grantee pays (or becomes obligated to pay) for that instrument when it is granted. For example, if a grantee pays $5 at the grant date for an option with a grant-date fair value of $50, the amount attributed to goods or services provided by the grantee is $45.

36. However, this statement provides certain exceptions (paragraph 56) to that measurement method if it is not possible to reasonably estimate the fair value of an award at the grant date. A reporting entity that is not able to reasonably estimate the fair value of its equity options and similar instruments may measure its liabilities under share-based payment arrangements at intrinsic value (see paragraphs 38.b. and 52*)*.

37. The terms of a share-based payment award and any related arrangement affect its value and, except for certain explicitly excluded features, such as a reload feature, shall be reflected in determining the fair value of the equity or liability instruments granted. For example, the fair value of a substantive option structured as the exchange of equity shares for a nonrecourse note will differ depending on whether the grantee is required to pay nonrefundable interest on the note.

Measurement Objective – Fair Value at Grant Date

38. The measurement objective for equity instruments awarded to grantees is to estimate the fair value at the grant date of the equity instruments that the entity is obligated to issue when grantees have delivered the good or rendered the service and satisfied any other conditions necessary to earn the right to benefit

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from the instruments (for example, to exercise share options). That estimate is based on the share price and other pertinent factors, such as expected volatility, at the grant date.

a. Measurement Objective and Measurement Date for Awards Classified as Liabilities: At the grant date, the measurement objective for liabilities incurred under share-based compensation arrangements is the same as the measurement objective for equity instruments awarded to grantees as described in paragraph 38. However, the measurement date for liability instruments is the date of settlement.

b. Intrinsic Value Option for Awards Classified as Liabilities: A reporting entity shall make a policy decision of whether to measure all of its liabilities incurred under share-based payment arrangements (for employee and nonemployee awards) issued in exchange for goods or services at fair value or ~~to measure all such liabilities~~ at intrinsic value. However, the reporting entity shall initially and subsequently measure awards determined to be consideration payable to a customer at fair value.

39. The fair value of an equity share option or similar instrument shall be measured based on the observable market price of an option with the same or similar terms and conditions, if one is available.

40. Such market prices for equity share options and similar instruments granted in share-based payment transactions are frequently not available; however, they may become so in the future. As such, the fair value of an equity share option or similar instrument shall be estimated using a valuation technique such as an option-pricing model. For this purpose, a similar instrument is one whose fair value differs from its intrinsic value, that is, an instrument that has time value. For example, a share appreciation right that requires net settlement in equity shares has time value; an equity share does not.

41. To satisfy the measurement objective in paragraph 38, the restrictions and conditions inherent in equity instruments awarded are treated differently depending on whether they continue in effect after the requisite service period or the nonemployee's vesting period. A restriction that continues in effect after an entity has issued awards, such as the inability to transfer vested equity share options to third parties or the inability to sell vested shares for a period of time, is considered in estimating the fair value of the instruments at the grant date. For equity share options and similar instruments, the effect of nontransferability (and nonhedgeability, which has a similar effect) is taken into account by reflecting the effects of grantees' expected exercise and postvesting termination behavior in estimating fair value (referred to as an option's expected term).

42. On an award-by-award basis, an entity may elect to use the contractual term as the expected term when estimating the fair value of a nonemployee award to satisfy the measurement objective in paragraph 38. Otherwise, an entity shall apply the guidance in this statement in estimating the expected term of a nonemployee award, which may result in a term less than the contractual term of the award.

43. When a reporting entity chooses to measure a nonemployee share-based payment award by estimating its expected term and applies the practical expedient in paragraph 53, it must apply the practical expedient to all nonemployee awards that meet the condition in paragraph 54. However, a reporting entity may still elect, on an award-by-award basis, to use the contractual term as the expected term as described in paragraph 42.

44. A restriction that stems from the forfeitability of instruments to which grantees have not yet earned the right, such as the inability either to exercise a nonvested equity share option or to sell nonvested shares, is not reflected in estimating the fair value of the related instruments at the grant date. Instead, those restrictions are taken into account by recognizing compensation cost only for awards for which grantees deliver the good or render the service.

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45. Awards of share-based compensation ordinarily specify a performance condition or a service condition (or both) that must be satisfied for a grantee to earn the right to benefit from the award. No compensation cost is recognized for instruments forfeited because a service condition or a performance condition is not satisfied (for example, instruments for which the good is not delivered or service is not rendered).

46. The fair-value-based method described in paragraphs 38 and 41-47 uses fair value measurement techniques, and the grant-date share price and other pertinent factors are used in applying those techniques. However, the effects on the grant-date fair value of service and performance conditions that apply only during the employee's requisite service period or a nonemployee's vesting period are reflected based on the outcomes of those conditions. This statement refers to the required measure as fair value.

47. Some awards contain a market condition. The effect of a market condition is reflected in the grant-date fair value of an award. (Valuation techniques have been developed to value path-dependent options as well as other options with complex terms. Awards with market conditions, as defined in this statement, are path-dependent options.) Compensation cost thus is recognized for an award with a market condition provided that the good is delivered or the service is rendered, regardless of when, if ever, the market condition is satisfied.

48. Market, performance, and service conditions (or any combination thereof) may affect an award's exercise price, contractual term, quantity, conversion ratio, or other factors that are considered in measuring an award's grant-date fair value. A grant-date fair value shall be estimated for each possible outcome of such a performance or service condition, and the final measure of compensation cost shall be based on the amount estimated at the grant date for the condition or outcome that is actually satisfied.

49. A nonvested equity share or nonvested equity share unit shall be measured at its fair value as if it were vested and issued on the grant date.

50. Nonvested shares granted in share-based payment transactions usually are referred to as restricted shares, but this statement reserves that term for fully vested and outstanding shares whose sale is contractually or governmentally prohibited for a specified period of time.

51. A restricted share awarded to a grantee, that is, a share that will be restricted after the grantee has a vested right to it, shall be measured at its fair value, which is the same amount for which a similarly restricted share would be issued to third parties.

52. A reporting entity may not be able to reasonably estimate the fair value of its equity share options, nonemployee awards and similar instruments because it is not practicable for the reporting entity to estimate the expected volatility of its share price. In that situation, the entity shall account for its equity share options, nonemployee awards and similar instruments based on a value calculated using the historical volatility of an appropriate industry sector index instead of the expected volatility of the entity's share price (~~the calculated~~permitted value). A reporting entity's use of ~~calculated~~permitted value shall be consistent between employee share-based payment transactions and nonemployee share-based payment transactions. Throughout the remainder of this statement, provisions that apply to accounting for share options, nonemployee awards and similar instruments at fair value also apply to calculated value.

53. For an award that meets the conditions in paragraph 54, a reporting entity may make an entity-wide accounting policy election to estimate the expected term using the following practical expedient:

a. If vesting is only dependent upon a service condition, a reporting entity shall estimate the expected term as the midpoint between the employee's requisite service period or the nonemployee's vesting period and the contractual term of the award.

b. If vesting is dependent upon satisfying a performance condition, an entity first would determine whether the performance condition is probable of being achieved.

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i. If the reporting entity concludes that the performance condition is probable of being achieved, the entity shall estimate the expected term as the midpoint between the employee's requisite service period or the nonemployee's vesting period and the contractual term.

ii. If the reporting entity concludes that the performance condition is not probable of being achieved, the reporting entity shall estimate the expected term as either:

(a) The contractual term if the service period is implied (that is, the requisite service period or the nonemployee's vesting period is not explicitly stated but inferred based on the achievement of the performance condition at some undetermined point in the future).

(b) The midpoint between the employee's requisite service period or the nonemployee's vesting period and the contractual term if the requisite service period is stated explicitly.

54. A reporting entity that elects to apply the practical expedient in paragraph 53 shall apply the practical expedient to a share option or similar award that has all of the following characteristics:

a. The share option or similar award is granted at the money.

b. The grantee has only a limited time to exercise the award (typically 30-90 days) if the grantee no longer provides goods ~~or~~, terminates service after vesting, or ceases to be a customer.

c. The grantee can only exercise the award. The grantee cannot sell or hedge the award.

d. The award does not include a market condition.

A reporting entity that elects to apply the practical expedient in paragraph 53 may always elect to use the contractual term as the expected term when estimating the fair value of a nonemployee award as described in paragraph 42. However, a reporting entity must apply the practical expedient in paragraph 53 for all nonemployee awards that have all the characteristics listed in this paragraph if that reporting entity does not elect to use the contractual term as the expected term and that reporting entity elects the accounting policy election to apply the practical expedient in paragraph 53.

55. If a reporting entity is not able to reasonably estimate the current share price (fair value) as a practical expedient, a reporting entity may use a value determined by the reasonable application of a reasonable valuation method as the current price of its underlying share for purposes of determining the fair value of an award that is classified as equity at grant date or upon a modification. The determination of whether a valuation method is reasonable, or whether an application of a valuation method is reasonable, shall be made on the facts and circumstances as of the measurement date. Factors to be considered under a reasonable valuation method include, as applicable:

a. The value of tangible and intangible assets.

b. The present value of anticipated future cash flows.

c. The market value of stock or equity interests in similar corporations and other entities engaged in trades or businesses substantially similar to those engaged by the entity for which the stock is to be valued, the value of which can be readily determined through nondiscretionary, objective means (such as through trading prices on an established securities market or an amount in an arm's length transaction).

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d. Recent arm's length transactions involving the sale or transfer of stock or equity interest.

e. Other relevant factors such as control premiums or discounts for lack of marketability and whether the valuation method is used for other purposes that have a material economic effect on the entity, its stockholders, or its creditors.

f. The entity's consistent use of a valuation method to determine the value of its stock or assets for other purposes, including purposes unrelated to compensation of service providers.

56. It should be possible to reasonably estimate the fair value of most equity share options and other equity instruments at the date they are granted. However, in rare circumstances, it may not be possible to reasonably estimate the fair value of an equity share option or other equity instrument at the grant date because of the complexity of its terms.

57. An equity instrument for which it is not possible to reasonably estimate fair value at the grant date shall be accounted for based on its intrinsic value (paragraph 85) for measurement after issue date.

58. The fair value of each award of equity instruments, including an award of options with a reload feature (reload options), shall be measured separately based on its terms and the share price and other pertinent factors at the grant date. The effect of a reload feature in the terms of an award shall not be included in estimating the grant-date fair value of the award. Rather, a subsequent grant of reload options pursuant to that provision shall be accounted for as a separate award when the reload options are granted.

59. A contingent feature of an award that might cause a grantee to return to the entity either equity instruments earned or realized gains from the sale of equity instruments earned for consideration that is less than fair value on the date of transfer (including no consideration), such as a clawback feature shall not be reflected in estimating the grant-date fair value of an equity instrument.

60. An entity shall make its initial best estimate of the requisite service period at the grant date (or at the service inception date, if that date precedes the grant date) and shall base accruals of compensation cost on that period.

61. The initial best estimate and any subsequent adjustment to that estimate of the requisite service period for an award with a combination of market, performance, or service conditions shall be based on an analysis of all of the following:

a. All vesting and exercisability conditions

b. All explicit, implicit, and derived service periods

c. The probability that performance or service conditions will be satisfied.

62. Performance or service conditions that affect vesting are not reflected in estimating the fair value of an award at the grant date because those conditions are restrictions that stem from the forfeitability of instruments to which grantees have not yet earned the right. However, the effect of a market condition is reflected in estimating the fair value of an award at the grant date (paragraph 47). For purposes of this statement, a market condition is not considered to be a vesting condition, and an award is not deemed to be forfeited solely because a market condition is not satisfied.

63. In some cases, the terms of an award may provide that a performance target that affects vesting could be achieved after an employee completes the requisite service period or a nonemployee satisfies a vesting period. That is, the grantee would be eligible to vest in the award regardless of whether the grantee is rendering service or delivering goods on the date the performance target is achieved. A performance target that affects vesting and that could be achieved after an employee's requisite service period or a

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nonemployee's vesting period shall be accounted for as a performance condition. As such, the performance target shall not be reflected in estimating the fair value of the award at the grant date. Compensation cost shall be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the service or goods already have been provided. If the performance target becomes probable of being achieved before the end of the employee's requisite service period or the nonemployee's vesting period, the remaining unrecognized compensation cost for which service or goods have not yet been provided shall be recognized prospectively over the remaining employee's requisite service period or the nonemployee's vesting period. The total amount of compensation cost recognized during and after the employee's requisite service period or the nonemployee's vesting period shall reflect the number of awards that are expected to vest based on the performance target and shall be adjusted to reflect those awards that ultimately vest. An entity that has an accounting policy to account for forfeitures when they occur in accordance with paragraph 68 or paragraph 72 shall reverse compensation cost previously recognized, in the period the award is forfeited, for an award that is forfeited before completion of the employee's requisite service period or the nonemployee's vesting period. The employee's requisite service period and the nonemployee's vesting period end when the grantee can cease rendering service or delivering goods and still be eligible to vest in the award if the performance target is achieved. The stated vesting period (which includes the period in which the performance target could be achieved) may differ from the employee's requisite service period or the nonemployee's vesting period.

Subsequent Measurement

64. Guidance that equally applies to both liabilities and equity is generally found in paragraphs 64-84. Paragraphs 85-95 provide additional subsequent measurement guidance for awards classified as equity and paragraphs 96-99 provide additional subsequent measurement guidance for awards classified as liabilities.

Recognition of Nonemployee Compensation Costs

65. A grantor shall recognize the goods acquired or services received in a share-based payment transaction with nonemployees when it obtains the goods or as services are received. A grantor may need to recognize a nonadmitted prepaid asset before it actually receives goods or services if it first exchanges a share-based payment for an enforceable right to receive those goods or services. Nonetheless, the goods or services shall not be recognized before they are received. (The nonadmitted asset recognized prior to the goods and services would be eliminated upon receipt of the goods and services that are recognized.)

66. If fully vested, nonforfeitable equity instruments are granted at the date the grantor and nonemployee enter into an agreement for goods or services (no specific performance is required by the nonemployee to retain those equity instruments), then, because of the elimination of any obligation on the part of the nonemployee to earn the equity instruments, a grantor shall recognize the equity instruments when they are granted (in most cases, when the agreement is entered into). Whether the corresponding cost is an immediate expense or a nonadmitted prepaid asset depends on the specific facts and circumstances. A grantor may conclude that an asset (other than a note or a receivable) has been received in return for fully-vested, nonforfeitable nonemployee share-based payment awards that are issued at the date the grantor and nonemployee enter into an agreement for goods or services (and no specific performance is required by the nonemployee in order to retain those equity instruments). Such an asset shall not be displayed as contra-equity by the grantor of the. The transferability (or lack thereof) of the awards shall not affect the balance sheet display of this nonadmitted prepaid asset. This guidance is limited to transactions in which awards are transferred to nonemployees in exchange for goods or services.

67. An entity may grant fully vested, nonforfeitable equity instruments that are exercisable by the nonemployee only after a specified period of time if the terms of the agreement provide for earlier exercisability if the nonemployee achieves specified performance conditions. Any measured cost of the transaction shall be recognized in the same period(s) and in the same manner as if the entity had paid cash for the goods or services instead of paying with, or using, the share-based payment awards.

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68. The total amount of compensation cost recognized for share-based payment awards to nonemployees shall be based on the number of instruments for which a good has been delivered or a service has been rendered. To determine the amount of compensation cost to be recognized in each period, an entity shall make an entity-wide accounting policy election for all nonemployee share-based payment awards, including share-based payment awards granted to customers, to do either of the following:

a. Estimate the number of forfeitures expected to occur. The entity shall base initial accruals of compensation cost on the estimated number of nonemployee share-based payment awards for which a good is expected to be delivered or service is expected to be rendered. The entity shall revise that estimate if subsequent information indicates that the actual number of instruments is likely to differ from previous estimates. The cumulative effect on current and prior periods of a change in the estimates shall be recognized in compensation cost in the period of the change.

b. Recognize the effect of forfeitures in compensation cost when they occur. Previously recognized compensation cost for a nonemployee share-based payment award shall be reversed in the period that the award is forfeited.

69. A recognized nonadmitted prepaid asset or expense shall not be reversed if a stock option that the nonemployee has the right to exercise expires unexercised.

70. A grantor shall recognize either a corresponding increase in equity or a liability, depending on whether the instruments granted satisfy the equity or liability classification criteria established in paragraphs 15-29. As the goods or services are disposed of or consumed, the grantor shall recognize the related cost, unless other statutory accounting principles require costs to be expensed when incurred. In these instances, when the goods or services are received, the grantor shall recognize the related cost.

Recognition of Employee Compensation Costs

71. The compensation cost for an award of share-based employee compensation classified as equity shall be recognized over the requisite service period, with a corresponding credit to equity (generally, paid-in capital). The requisite service period is the period during which an employee is required to provide service in exchange for an award, which often is the vesting period. The requisite service period is estimated based on an analysis of the terms of the share-based payment award.

72. The total amount of compensation cost recognized at the end of the requisite service period for an award of share-based compensation shall be based on the number of instruments for which the requisite service has been rendered (that is, for which the requisite service period has been completed). Previously recognized compensation cost shall not be reversed if an employee share option (or share unit) for which the requisite service has been rendered expires unexercised (or unconverted). To determine the amount of compensation cost to be recognized in each period, an entity shall make an entity-wide accounting policy election for all employee share-based payment awards to do either of the following:

a. Estimate the number of awards for which the requisite service will not be rendered (that is, estimate the number of forfeitures expected to occur). The entity shall base initial accruals of compensation cost on the estimated number of instruments for which the requisite service is expected to be rendered. The entity shall revise that estimate if subsequent information indicates that the actual number of instruments is likely to differ from previous estimates. The cumulative effect on current and prior periods of a change in the estimated number of instruments for which the requisite service is expected to be or has been rendered shall be recognized in compensation cost in the period of the change.

b. Recognize the effect of awards for which the requisite service is not rendered when the award is forfeited (that is, recognize the effect of forfeitures in compensation cost when

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they occur). Previously recognized compensation cost for an award shall be reversed in the period that the award is forfeited.

73. An entity shall reverse previously recognized compensation cost for an award with a market condition only if the requisite service is not rendered.

74. The requisite service period for employee awards may be explicit or it may be implicit, being inferred from an analysis of other terms in the award, including other explicit service or performance conditions. The requisite service period for an award that contains a market condition can be derived from certain valuation techniques that may be used to estimate grant-date fair value. An award may have one or more explicit, implicit, or derived service periods; however, an award may have only one requisite service period for accounting purposes unless it is accounted for as in-substance multiple awards. An award with a graded vesting schedule that is accounted for as in-substance multiple awards is an example of an award that has more than one requisite service period (paragraph 77).

75. The service inception date is the beginning of the requisite service period. If the service inception date precedes the grant date, accrual of compensation cost for periods before the grant date shall be based on the fair value of the award at the reporting date. In the period in which the grant date occurs, cumulative compensation cost shall be adjusted to reflect the cumulative effect of measuring compensation cost based on fair value at the grant date rather than the fair value previously used at the service inception date (or any subsequent reporting date).

76. An entity shall adjust that initial best estimate in light of changes in facts and circumstances. Whether and how the initial best estimate of the requisite service period is adjusted depends on both the nature of the conditions identified in paragraph 61 and the manner in which they are combined, for example, whether an award vests or becomes exercisable when either a market or a performance condition is satisfied or whether both conditions must be satisfied.

77. An entity shall make a policy decision about whether to recognize compensation cost for an employee award with only service conditions that has a graded vesting schedule in either of the following ways:

a. On a straight-line basis over the requisite service period for each separately vesting portion of the award as if the award was, in-substance, multiple awards.

b. On a straight-line basis over the requisite service period for the entire award (that is, over the requisite service period of the last separately vesting portion of the award).

However, the amount of compensation cost recognized at any date must at least equal the portion of the grant-date value of the award that is vested at that date.

Awards May Become Subject to Other Guidance

78. Paragraphs 80-83 are intended to apply to those instruments issued in share-based payment transactions with employees and nonemployees accounted for under this statement, and to instruments exchanged in a business combination for share-based payment awards of the acquired business that were originally granted to grantees of the acquired business and are outstanding as of the date of the business combination..

79. A convertible instrument award granted to a nonemployee in exchange for goods or services to be used or consumed in a grantor's own operations is subject to recognition and measurement guidance in this statement until the award is fully vested. Once vested, a convertible instrument award that is equity in form, or debt in form, that can be converted into equity instruments of the grantor, shall follow recognition and measurement through reference to other applicable statutory accounting guidance.

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80. A freestanding financial instrument issued to a grantee ~~in exchange for goods or services received (or to be received)~~ that is subject to initial recognition and measurement guidance within this statement shall continue to be subject to the recognition and measurement provisions of this statement throughout the life of the instrument, unless its terms are modified after a ~~nonemployee~~grantee vests in the award and is no longer providing goods or services, a grantee vests in the award and is no longer a customer, or a grantee is no longer an employee. Only for purposes of this paragraph, a modification does not include a change to the terms of an award if that change is made solely to reflect an equity restructuring provided that both of the following conditions are met:

a. There is no increase in fair value of the award (or the ratio of intrinsic value to the exercise price of the award is preserved, that is, the holder is made whole) or the antidilution provision is not added to the terms of the award in contemplation of an equity restructuring.

b. All holders of the same class of equity instruments (for example, stock options) are treated in the same manner.

81. Other modifications of that instrument that take place after a ~~nonemployee~~grantee vests in the award and is no longer providing goods or services, is no longer a customer, or ~~a grantee~~ is no longer an employee shall be subject to the modification guidance in paragraph 83. Following modification, recognition and measurement of the instrument shall be determined through reference to other applicable statutory accounting principles.

82. Once the classification of an instrument is determined, the recognition and measurement provisions of this statement shall be applied until the instrument ceases to be subject to the requirements discussed in paragraph 80. Other applicable statutory accounting principles apply to a freestanding financial instrument that was issued under a share-based payment arrangement but that is no longer subject to this statement. This guidance is not intended to suggest that all freestanding financial instruments shall be accounted for as liabilities, but rather that freestanding financial instruments issued in share-based payment transactions may become subject to other applicable statutory accounting principles depending on their substantive characteristics and when certain criteria are met.

83. An entity may modify (including cancel and replace) or settle a fully vested, freestanding financial instrument after it becomes subject to other applicable statutory accounting principles. Such a modification or settlement shall be accounted for under the provisions of this statement unless it applies equally to all financial instruments of the same class regardless of the holder of the financial instrument. Following the modification, the instrument continues to be accounted for under other applicable statutory accounting principles. A modification or settlement of a class of financial instrument that is designed exclusively for and held only by grantees (or their beneficiaries) may stem from the employment or vendor relationship depending on the terms of the modification or settlement. Thus, such a modification or settlement may be subject to the requirements of this statement. See paragraph 80 for a discussion of changes to awards made solely to reflect an equity restructuring.

84. An option or similar instrument that is classified as equity, but subsequently becomes a liability because the contingent cash settlement event is probable of occurring, shall be accounted for similar to a modification from an equity to liability award. That is, on the date the contingent event becomes probable of occurring (and therefore the award must be recognized as a liability), the entity recognizes a share-based liability equal to the portion of the award attributed to past performance (which reflects any provision for acceleration of vesting) multiplied by the award's fair value on that date. To the extent the liability equals or is less than the amount previously recognized in equity, the offsetting debit is a charge to equity. To the extent that the liability exceeds the amount previously recognized in equity, the excess is recognized as compensation cost. The total recognized compensation cost for an award with a contingent cash settlement feature shall at least equal the fair value of the award at the grant date. The guidance in this paragraph is applicable only for options or similar instruments issued as part of compensation arrangements. That is, the

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guidance included in this paragraph is not applicable, by analogy or otherwise, to instruments outside share-based payment arrangements.

Subsequent Measurement - Awards Classified as Equity

85. An equity instrument for which it is not possible to reasonably estimate fair value at the grant date shall be remeasured at each reporting date through the date of exercise or other settlement. The final measure of compensation cost shall be the intrinsic value of the instrument at the date it is settled. Compensation cost for each period until settlement shall be based on the change (or a portion of the change, depending on the percentage of the requisite service that has been rendered for an employee award or the percentage that would have been recognized had the grantor paid cash for the goods or services instead of paying with a nonemployee award at the reporting date) in the intrinsic value of the instrument in each reporting period. The entity shall continue to use the intrinsic value method for those instruments even if it subsequently concludes that it is possible to reasonably estimate their fair value.

86. A contingent feature of an award that might cause a grantee to return to the entity either equity instruments earned or realized gains from the sale of equity instruments earned for consideration that is less than fair value on the date of transfer (including no consideration), such as a clawback feature, shall be accounted for if and when the contingent event occurs.

Modification of An Award

87. An entity shall account for the effects of a modification as described in paragraphs 88-95, unless all of the following are met:

a. The fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the modified award is the same as the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the original award immediately before the original award is modified. If the modification does not affect any of the inputs to the valuation technique that the entity uses to value the award, the entity is not required to estimate the value immediately before and after the modification.

b. The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified.

c. The classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified.

The disclosure requirements in paragraph 114 apply regardless of whether an entity is required to apply modification accounting.

88. Except as described in paragraph 87, a modification of the terms or conditions of an equity award shall be treated as an exchange of the original award for a new award. In substance, the entity repurchases the original instrument by issuing a new instrument of equal or greater value, incurring additional compensation cost for any incremental value. The effects of a modification shall be measured as follows:

a. Incremental compensation cost shall be measured as the excess, if any, of the fair value of the modified award determined in accordance with the provisions of this statement over the fair value of the original award immediately before its terms are modified, measured based on the share price and other pertinent factors at that date. As indicated in paragraph 52, references to fair value throughout this statement shall be read also to encompass calculated value. The effect of the modification on the number of instruments expected to vest also shall be reflected in determining incremental compensation cost. The estimate at

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the modification date of the portion of the award expected to vest shall be subsequently adjusted, if necessary, in accordance with paragraph 68 or 72.

b. Total recognized compensation cost for an equity award shall at least equal the fair value of the award at the grant date unless at the date of the modification the performance or service conditions of the original award are not expected to be satisfied. Thus, the total compensation cost measured at the date of a modification shall be the sum of the following:

i. The portion of the grant-date fair value of the original award for which the promised good is expected to be delivered (or has already been delivered) or the service is expected to be rendered (or has already been rendered) at that date, and

ii. The incremental cost resulting from the modification.

Compensation cost shall be subsequently adjusted, if necessary, in accordance with paragraph 68 or 72.

c. A change in compensation cost for an equity award measured at intrinsic value in accordance with paragraph 85 shall be measured by comparing the intrinsic value of the modified award, if any, with the intrinsic value of the original award, if any, immediately before the modification.

89. An entity that has an accounting policy to account for forfeitures when they occur in accordance with paragraph 68 or 72 shall assess at the date of the modification whether the performance or service conditions of the original award are expected to be satisfied when measuring the effects of the modification in accordance with paragraph 87. However, the entity shall apply its accounting policy to account for forfeitures when they occur when subsequently accounting for the modified award.

90. Paragraphs 78-83 provide additional guidance on accounting for modifications of certain freestanding financial instruments that initially were subject to this statement but subsequently became subject to other applicable statutory accounting principles.

Short-Term Inducements

91. Except as described in paragraph 87, a short-term inducement shall be accounted for as a modification of the terms of only the awards of grantees who accept the inducement, and other inducements shall be accounted for as modifications of the terms of all awards subject to them.

Equity Restructuring or Business Combination

92. Exchanges of share options or other equity instruments or changes to their terms in conjunction with an equity restructuring or a business combination are modifications for purposes of this statement. An entity shall apply the guidance in paragraph 87 to those exchanges or changes to determine whether it shall account for the effects of those modifications. See paragraph 80 for an exception.

Repurchase or Cancellation

93. The amount of cash or other assets transferred (or liabilities incurred) to repurchase an equity award shall be charged to equity, to the extent that the amount paid does not exceed the fair value of the equity instruments repurchased at the repurchase date. Any excess of the repurchase price over the fair value of the instruments repurchased shall be recognized as additional compensation cost. An entity that repurchases an award for which the promised goods have not been delivered or the service has not been rendered has, in effect, modified the employee's requisite service period or nonemployee's vesting period to the period for which goods have already been delivered or service already has been rendered, and thus the amount of

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compensation cost measured at the grant date but not yet recognized shall be recognized at the repurchase date.

Cancellation and Replacement

94. Except as described in paragraph 87, cancellation of an award accompanied by the concurrent grant of (or offer to grant) a replacement award or other valuable consideration shall be accounted for as a modification of the terms of the cancelled award. (The phrase *offer to grant* is intended to cover situations in which the service inception date precedes the grant date.) Therefore, incremental compensation cost shall be measured as the excess of the fair value of the replacement award or other valuable consideration over the fair value of the cancelled award at the cancellation date in accordance with paragraph 88. Thus, the total compensation cost measured at the date of a cancellation and replacement shall be the portion of the grant-date fair value of the original award for which the promised good is expected to be delivered (or has already been delivered) or the service is expected to be rendered (or has already been rendered) at that date plus the incremental cost resulting from the cancellation and replacement.

95. A cancellation of an award that is not accompanied by the concurrent grant of (or offer to grant) a replacement award or other valuable consideration shall be accounted for as a repurchase for no consideration. Accordingly, any previously unrecognized compensation cost shall be recognized at the cancellation date.

Subsequent Measurement - Awards Classified as Liabilities

96. The fair value of liabilities incurred in share-based payment transactions shall be remeasured at the end of each reporting period through settlement.

97. Changes in the fair value (or intrinsic value for a reporting entity that elects that method) of a liability incurred under a share-based payment arrangement issued in exchange for goods or services that occur during the employee's requisite service period or the nonemployee's vesting period shall be recognized as compensation cost over that period. The percentage of the fair value (or intrinsic value) that is accrued as compensation cost at the end of each period shall equal the percentage of the requisite service that has been rendered for an employee award or the percentage that would have been recognized had the grantor paid cash for the goods or services instead of paying with a nonemployee award at that date. Changes in the fair value (or intrinsic value) of a liability issued in exchange for goods or services that occur after the end of the employee's requisite service period or the nonemployee's vesting period are compensation costs of the period in which the changes occur. Any difference between the amount for which a liability award issued in exchange for goods or services is settled and its fair value at the settlement date as estimated in accordance with the provisions of this statement is an adjustment of compensation cost in the period of settlement.

98. Reporting entities shall measure a liability award under a share-based payment arrangement based on the award's fair value (or permitted value in accordance with paragraph 52) remeasured at each reporting date until the date of settlement. Compensation costs for each period until settlement shall be based on the change (or a portion of the change, depending on the percentage of the requisite service that has been rendered for an employee award or the percentage that would have been recognized had the grantor paid cash for the goods and services instead of paying with a nonemployee award at the reporting date) in the fair value of the instrument for each reporting period. A reporting entity shall subsequently measure awards determined to be consideration payable to a customer at fair value.

99. A modification of a liability award is accounted for as the exchange of the original award for a new award. However, because liability awards are remeasured at their fair value (or calculated value for an entity subject to paragraph 52) at each reporting date, no special guidance is necessary in accounting for a modification of a liability award that remains a liability after the modification.

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Accounting for Tax Effects of Share-Based Arrangements

100. Income tax regulations specify allowable tax deductions for instruments issued under share-based payment arrangements in determining an entity's income tax liability. For example, under tax law, allowable tax deductions may be measured as the intrinsic value of an instrument on a specified date. The time value component, if any, of the fair value of an instrument generally may not be tax deductible. Therefore, tax deductions may arise in different amounts and in different periods from compensation costs recognized in financial statements. Similarly, the amount of expense reported for an employee stock ownership plan during a period may differ from the amount of the related income tax deduction prescribed by income tax rules and regulations.

101. This guidance addresses how temporary differences are recognized for share-based payment arrangement awards that are classified either as equity or as liabilities under the requirements of paragraphs 16-29. Incremental guidance is also provided for issues related to employee stock ownership plans.

Tax Effects for Instruments Classified as Equity

102. The cumulative amount of compensation cost recognized for instruments classified as equity that ordinarily would result in a future tax deduction under existing tax law shall be considered to be a deductible temporary difference in applying the requirements of *SSAP No. 101—Income Taxes*. The deductible temporary difference shall be based on the compensation cost recognized for financial reporting purposes. Compensation cost that is capitalized as part of the cost of an asset, such as inventory, shall be considered to be part of the tax basis of that asset for financial reporting purposes.

103. Recognition of compensation cost for instruments that ordinarily do not result in tax deductions under existing tax law shall not be considered to result in a deductible temporary difference. A future event can give rise to a tax deduction for instruments that ordinarily do not result in a tax deduction. The tax effects of such an event shall be recognized only when it occurs. An example of a future event that would be recognized only when it occurs is an employee's sale of shares obtained from an award before meeting a tax law's holding period requirement, sometimes referred to as a disqualifying disposition, which results in a tax deduction not ordinarily available for such an award.

Tax Effects for Instruments Classified as Liability

104. The cumulative amount of compensation cost recognized for instruments classified as liabilities that ordinarily would result in a future tax deduction under existing tax law also shall be considered to be a deductible temporary difference. The deductible temporary difference shall be based on the compensation costs recognized for financial reporting purposes.

Accounting for Tax Effects

105. The deferred tax benefit (expense) that results from increases (or decreases) in the recognized share-based payment temporary difference, for example, an increase that results as additional service is rendered and the related cost is recognized or a decrease that results from forfeiture of an award, shall be recognized in the income statement.

106. SSAP No. 101 requires a deferred tax asset to be evaluated for future realization and to be reduced by a statutory valuation allowance if, based on the weight of the available evidence, it is more likely than not that some portion or all of the deferred tax asset will not be realized. Differences between the deductible temporary difference computed pursuant to paragraphs 102-103 and the tax deduction that would result based on the current fair value of the entity's shares shall not be considered in measuring the gross deferred tax asset or determining the need for a valuation allowance for a deferred tax asset recognized under these requirements.

107. The tax effect of the difference, if any, between the cumulative compensation cost of an award recognized for financial reporting purposes and the deduction for an award for tax purposes shall be

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recognized as income tax expense or benefit in the income statement. The tax effect shall be recognized in the period in which the amount of the deduction is determined, which is typically when an award is exercised, or expired, in the case of share options, or vests in the case of nonvested stock awards. The appropriate period depends on the type of award and the guidance in SSAP No. 101.

Tax Benefits of Dividends on Share-Based Payment Awards

108. An income tax benefit from dividends or dividend equivalents that are charged to unassigned-funds (surplus) and are paid to employees for any of the following equity classified awards shall be recognized as an income tax expense or benefit in the income statement:

a. Nonvested equity shares

b. Nonvested equity share units

c. Outstanding equity share options.

Accounting for Rabbi Trusts

109. This section addresses the accounting for deferred compensation arrangements where amounts earned by an employee are invested in the stock of the employer and placed in a rabbi trust. Certain of these plans allow the employee to immediately diversify into nonemployer securities or to diversify after a holding period (for example, six months); other plans do not allow for diversification. The deferred compensation obligation of some plans may be settled in any of the following:

a. Cash, by having the trust sell the employer stock (or the diversified assets) in the open market

b. Shares of employer's stock

c. Diversified assets

In other plans, the deferred compensation obligation may be settled only by the delivery of the shares of the employer stock.

110. The guidance in this section addresses the accounting for deferred compensation that have characteristics in paragraphs 110.a. or 110.b. This section does not address the accounting for stock appreciation rights, even if they are funded through a rabbi trust.

a. If amounts earned by an employee are invested in the stock of the employer and placed in a rabbi trust.

b. Where the employee elects to diversify the assets held by the rabbi trust into nonemployer securities.

111. Rabbi trusts are grantor trusts generally set up to fund compensation for a select group of management or highly paid executives. To qualify as a rabbi trust for income tax purposes, the terms of the trust agreement must explicitly state that the assets of the trust are available to satisfy the claims of general creditors in the event of bankruptcy of the employer.

112. The following are the four types of deferred compensation arrangements involving rabbi trusts covered in this guidance:

Plan A: The plan does not permit diversification and must be settled by the delivery of a fixed number of shares of employer stock.

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Plan B: The plan does not permit diversification and may be settled by the delivery of cash or shares of employer stock.

Plan C: The plan permits diversification; however, the employee has not diversified (the plan may be settled in cash, shares of employer stock, or diversified assets).

Plan D: The plan permits diversification and the employee has diversified (the plan may be settled in cash, shares of employer stock, or diversified assets).

113. The accounts of the rabbi trust should be consolidated with the accounts of the employer in the financial statements of the employer.

a. For Plan A, employer stock held by the rabbi trust should be classified in equity in a manner similar to the manner in which treasury stock is accounted for. Subsequent changes in the fair value of the employer's stock should not be recognized. The deferred compensation obligation should be classified as an equity instrument and changes in the fair value of the amount owed to the employee should not be recognized.

b. For Plans B and C, employer stock held by the rabbi trust should be classified in equity in a manner similar to the manner in which treasury stock is accounted for. Subsequent changes in the fair value of the employer's stock should not be recognized. The deferred compensation obligation should be classified as a liability and adjusted with a corresponding charge (or credit) to compensation cost, to reflect the changes in the fair value of the amount owed to the employee.

c. For Plan D, assets held by the rabbi trust should be accounted for in accordance with statutory accounting principles for the particular asset (for example, if the diversified asset is an unaffiliated common stock security, that security would be accounted for in accordance with *SSAP No. 30R—Unaffiliated Common Stock*. The deferred compensation obligation should be classified as a liability and adjusted, with a corresponding charge (or credit) to compensation cost, to reflect changes in the fair value of the amount owed to the employee. Changes in the fair value of the deferred compensation obligation should not be recorded in unrealized gains or losses, even if changes in the fair value of the assets held by the rabbi trust are recorded in surplus pursuant to SSAP No. 30R.

Disclosures

114. An entity with one or more share-based payment arrangements shall disclose information that enables users of the financial statements to understand all of the following:

a. The nature and terms of such arrangements that existed during the period and the potential effects of those arrangements on shareholders;

b. The effect of compensation costs arising from share-based payment arrangements on the income statement;

c. The method of estimating the fair value of the goods or services received, or the fair value of the equity instruments granted (or offered to grant), during the period; and

d. The cash flow effects resulting from share-based payment arrangements.

115. The disclosures in paragraph 114 are for annual audited statutory financial statements only. This statement adopts FASB Codification 718-10-50-2 for the minimum disclosure information needed to

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achieve the objective in paragraph 114 of this statement, noting that a reporting entity may need to disclose additional information to achieve the objectives.

Employee Share Purchase Plans

Overview and Background

116. This section provides guidance to all entities that use employee share purchase plans. The entity must first determine whether the plan is compensatory or noncompensatory. This is determined by the terms of the plan (paragraphs 117-118). A plan with an option feature, for example a look-back feature, is considered compensatory. (This section on employee share purchase plans has its own discrete scope, which is separate and distinct from the pervasive scope.)

Recognition

117. An employee share purchase plan that satisfies all of the following criteria does not give rise to recognizable compensation costs (that is, the plan is noncompensatory):

a. The plan satisfies either of the following conditions:

i. The terms of the plan are no more favorable than those available to all holders of the same class of shares. Note that a transaction subject to an employee share purchase plan that involves a class of equity shares designed exclusively for and held only by current or former employees or their beneficiaries may be compensatory depending on the terms of the arrangement.

ii. Any purchase discount from the market price does not exceed the per-share amount of share issuance costs that would have been incurred to raise a significant amount of capital by a public offering. A purchase discount of 5% ~~percent~~ or less from the market price shall be considered to comply with this condition without further justification. A purchase discount greater than 5% ~~percent~~ that cannot be justified under this condition results in compensation cost for the entire amount of the discount. Note that an entity that justifies a purchase discount in excess of 5% ~~percent~~ shall reassess at least annually, and no later than the first share purchase offer during the fiscal year, whether it can continue to justify that discount pursuant to this paragraph.

b. Substantially all employees that meet limited employment qualifications may participate on an equitable basis.

c. The plan incorporates no option features, other than the following:

i. Employees are permitted a short period of time—not exceeding 31 days—after the purchase price has been fixed to enroll in the plan.

ii. The purchase price is based solely on the market price of the shares at the date of purchase, and employees are permitted to cancel participation before the purchase date and obtain a refund of amounts previously paid (such as those paid by payroll withholdings).

118. A plan provision that establishes the purchase price as an amount based on the lesser of the equity share's market price at date of grant or its market price at date of purchase, commonly called a look-back plan, is an example of an option feature that causes the plan to be compensatory. Similarly, a plan in which the purchase price is based on the share's market price at date of grant and that permits a participating

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employee to cancel participation before the purchase date and obtain a refund of amounts previously paid contains an option feature that causes the plan to be compensatory.

119. The requisite service period for any compensation cost resulting from an employee share purchase plan is the period over which the employee participates in the plan and pays for the shares.

Initial Measurement

120. Paragraph 38 states that the objective of the fair value measurement method is to estimate the fair value of the equity instruments, based on the share price and other measurement assumptions at the grant date, that are issued in exchange for providing goods or rendering services. Estimating the fair value of equity instruments at the grant date, which are issued in exchange for employee services also applies to the fair value measurements associated with grants under a compensatory employee share purchase plan.

Look-Back Plans

121. Many employee share purchase plans with a look-back option have differing features. For example, some plans contain multiple purchase periods, others contain reset mechanisms, and still others allow changes in the withholding amounts or percentages after the grant date. In some circumstances, applying the measurement approaches described in this section may not be practicable for certain types of employee share purchase plans. Paragraph 85 provides guidance on the measurement requirements if it is not possible to reasonably estimate fair value at the grant date.

Subsequent Measurement

122. Changes in total employee withholdings during a purchase period that occur solely as a result of salary increases, commissions, or bonus payments are not plan modifications if they do not represent changes to the terms of the award that was offered by the employer and initially agreed to by the employee at the grant (or measurement) date. Under those circumstances, the only incremental compensation cost is that which results from the additional shares that may be purchased with the additional amounts withheld (using the fair value calculated at the grant date). For example, an employee may elect to participate in the plan on the grant date by requesting that 5% ~~percent~~ of the employee's annual salary be withheld for future purchases of stock. If the employee receives an increase in salary during the term of the award, the base salary on which the 5% ~~percent~~ withholding amount is applied will increase, thus increasing the total amount withheld for future share purchases. That increase in withholdings as a result of the salary increase is not considered a plan modification and thus only increases the total compensation cost associated with the award by the grant date fair value associated with the incremental number of shares that may be purchased with the additional withholdings during the period. The incremental number of shares that may be purchased is calculated by dividing the incremental amount withheld by the exercise price as of the grant date (for example, 85% ~~percent~~ of the grant date stock price).

123. Any decreases in the withholding amounts (or percentages) shall be disregarded for purposes of recognizing compensation cost unless the employee services that were valued at the grant date will no longer be provided to the employer due to a termination. However, no compensation cost shall be recognized for awards that an employee forfeits because of failure to satisfy a service requirement for vesting. The accounting for decreases in withholdings is consistent with the requirement in paragraph 63 that the total amount of compensation cost that must be recognized for an award be based on the number of instruments for which the requisite service has been rendered (that is, for which the requisite service period has been completed).

Consolidated / Holding Company Plans

124. Except for the disclosure requirement in paragraph 125, the provisions of this statement do not apply to a reporting entity, as long as:

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a. The reporting entity is not directly liable for obligations under the share-based payment plan.

b. Compensation costs associated with share-based payments provided by a related party or holder of an economic interest in the reporting entity, equal to the required contribution to the plan for the period, are included in allocated expenses to the reporting entity. A liability shall be established for any such contributions due and unpaid.

125. The reporting entity shall disclose in the financial statements that its employees participate in a plan sponsored by the holding company for which the reporting entity has no legal obligation. The amount of the expense incurred and the allocation methodology utilized by the provider of such benefits shall also be disclosed.

126. If the reporting entity is directly liable for the share-based payment plan, then the other provisions of this statement apply.

Relevant Literature

127. This statement adopts with modification the U.S. GAAP guidance for share-based payment transactions reflected in FASB *Accounting Standards Codification (ASC) Topic 718, Compensation – Stock Compensation*, as modified by the ASUs listed in paragraphs 127.a. through 127.e., excluding the guidance in *ASC Subtopic 718-40, Employee Stock Ownership Plans* (ESOPs). Statutory accounting guidance for ESOPs is addressed in *SSAP No. 12—Employee Stock Ownership Plans*. This adoption with modification includes the related implementation guidance reflected within the FASB Codification Topic 718 not reflected within this standard. The U.S. GAAP guidance adopted with modification reflects the adoption with modification of the following ASUs:

a. *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer.*

~~a.~~b. *ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting.* The revisions from ASU 2018-07 expand the scope of ASC 718 to include share-based payment transactions for acquiring goods and services from nonemployees. With ASU 2018-17, *ASC 505-50, Equity – Equity Payments to Nonemployees* was superseded.

~~b.~~c. *ASU 2017-09, Scope of Modification Accounting*

~~c.~~d. *ASU 2016-09, Improvements to Employee Share-Based Payment Accounting*

~~d.~~e. *ASU 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*

~~e.~~f. *ASU 2010-13, Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Current of the Market in Which the Underlying Equity Security Trades*

128. The statutory accounting guidance for share-based payments is intended to be consistent with U.S. GAAP. Adopted modifications to U.S. GAAP guidance are as follows:

a. GAAP references to "public and nonpublic" guidance have been eliminated. However, entities that report share-payment transactions under U.S. GAAP as "public" entities shall not report different amounts between U.S. GAAP and SAP. (For example, if a reporting entity reports "fair value" under U.S. GAAP, that entity shall not utilize a "calculated or intrinsic" amount under statutory accounting.

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b. Prepaid assets are nonadmitted.

c. GAAP references are revised to reference applicable statutory accounting guidance.

d. GAAP reporting line items (either explicitly provided in the statement or adopted by reference – such as the GAAP implementation guidance) shall be replaced to reference applicable statutory annual statement line items. (For example, GAAP references to "other comprehensive income" shall be reflected within "Surplus - Unassigned Funds").

e. GAAP guidance to calculate earnings per share is not applicable to statutory accounting and has not been included within the statement.

f. GAAP effective date and transition, and transition disclosures have not been incorporated. Reporting entities shall follow the effective date and transition elements provided within this statement.

g. Inclusion of guidance specific to statutory for consolidated/holding company plans.

129. The adoption with modification of FASB Codification Topic 718 detailed in paragraph 127 of this statement reflects adoption with modification of the following pre-codification GAAP standards:

a. *FAS 123R, Share-Based Payment* (FAS 123R);

b. *FAS 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity* (FAS 150) – (Adopted only to the extent referenced in FAS 123R for classifying instruments as equity or liability for application in this statement. Adopted guidance is reflected in Exhibit A);

c. *FASB Staff Position FAS 123(R)-1: Classification and Measurement of Freestanding Financial Instruments Originally issued in Exchange for Employee Services under FASB Statement No. 123(R)* (FAS 123R-1);

d. *FASB Staff Position (FSP) FAS 123(R)-2: Practical Accommodation to the Application of Grant Date as Defined in FASB Statement No. 123(R)* (FSP FAS 123R-2);

e. *FASB Staff Position (FSP) FAS123(R)-4: Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event* (FSP FAS 123R-4);

f. *FASB Staff Position (FSP) FAS 123(R)-5: Amendment of FASB Staff Position FAS 123R-1* (FSP FAS 123R-5);

g. *FASB Staff Position (FSP) FAS 123(R)-6: Technical Corrections of FASB Statement No. 123(R)* (FSP FAS 123R-6);

h. *FASB Emerging Issues Task Force 97-14: Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested* (EITF 97-14);

i. *FASB Emerging Issues Task Force 00-16: Recognition and Measurement of Employer Payroll Taxes on Employee Stock-Based Compensation* (EITF 00-16);

j. *FASB Technical Bulletin 97-01, Accounting under Statement 123 for Certain Employee Stock Purchase Plans with a Look-Back Option* (TB 97-01)

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130. The adoption with modification of FASB Codification Topic 718 in this statement reflects rejection of the following pre-codification GAAP standards:

a. *FASB Staff Position (FSP) FAS 123(R)-3: Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards* (FSP FAS 123R-3); and

b. *FASB Staff Position (FSP) EITF 03-6-1; Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* (FSP EITF 03-6-1).

Effective Date and Transition

131. This statement was effective January 1, 2013, with interim and annual financial reporting thereafter. Early adoption was permitted for December 31, 2012, financial statements with interim and annual reporting thereafter. At the time of initial adoption of this statement, reporting entities with existing share-based payment instruments that applied the guidance in *SSAP No. 13—Stock Options and Stock Purchase Plans* were to apply the requirements of SSAP No. 104 prospectively to new awards and to awards modified, repurchased or cancelled after the required effective date. Those reporting entities were to continue to account for any portion of awards outstanding at the date of initial application using the statutory accounting principles originally applied to those awards (e.g., SSAP No. 13).

132. Since the initial adoption of SSAP No. 104, subsequent revisions were effective as follows:

a. *ASU 2021-07, Compensation – Stock Compensation, Determining the Current Price of an Underlying Share for Equity-Classified Share-Based Awards.* This SAP clarification effective August 10, 2022.

b. *ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting:* Nonsubstantive revisions effective January 1, 2020, with early application permitted.

c. *ASU 2017-09, Scope of Modification Accounting:* Nonsubstantive revisions effective January 1, 2018, applicable to modifications that occur on or after the effective date, with early application permitted.

d. *ASU 2016-09, Improvements to Employee Share-Based Payment Accounting:* Nonsubstantive revisions effective December 31, 2017, with early adoption permitted. The adoption included the transition provisions from ASU 2016-19, although not duplicated within this statement.

e. *ASU 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period:* Nonsubstantive revisions effective January 1, 2016, with early adoption permitted.

f. *ASU 2010-13, Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Current of the Market in Which the Underlying Equity Security Trades:* Captured in the original adoption of SSAP No. 104, effective January 1, 2013.

133. After initial adoption of SSAP No. 104, substantive revisions, detailed in Issue Paper No. 146, were adopted to incorporate guidance for share-based payment transaction with nonemployees. These substantive revisions adopted with modification U.S. GAAP guidance reflected in *ASC 505-50, Equity Payments to Nonemployees*. Pursuant to the adoption with modification of ASU 2018-07, statutory accounting guidance previously adopted from ASC 505-50 has been superseded. As such, the following pre-codification standards have also been superseded and are no longer considered adopted for statutory accounting:

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a. *FASB Emerging Issues Task Force 96-18: Accounting for Equity Instruments That are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling Goods or Services;*

b. *FASB Emerging Issues Task Force 00-08: Accounting by a Grantee for an Equity Instrument to Be Received in Conjunction with Providing Goods or Services*; and

c. *FASB Emerging Issues Task Force 00-18: Accounting Recognition for Certain Transactions Involving Equity Instruments Granted to Other Than Employees*.

REFERENCES

Other

- *SSAP No. 12—Employee Stock Ownership Plans*

Relevant Issue Papers

- *Issue Paper No. 129—Share-Based Payment, A Replacement of SSAP No. 13*

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EXHIBIT A – Classification Criteria: Liability or Equity

Classification Criteria

1. As detailed in paragraph 16 of this statement, unless paragraphs 17-29 require otherwise, an entity shall apply the classification criteria in this Exhibit in determining whether to classify a freestanding financial instrument given to a grantee as a liability

2. The guidance in this Exhibit shall be applied to a freestanding financial instrument in its entirety. Any nonsubstantive or minimal features shall be disregarded in applying the classification provisions of this Exhibit. Judgment, based on consideration of all the terms of an instrument and other relevant facts and circumstances, is necessary to distinguish substantive, nonminimal features from nonsubstantive or minimal features.

Mandatorily Redeemable Financial Instruments

3. A mandatorily redeemable financial instrument shall be classified as a liability unless the redemption is required to occur only upon the liquidation or termination of the reporting entity.

4. A financial instrument that embodies a conditional obligation to redeem the instrument by transferring assets upon an event not certain to occur becomes mandatorily redeemable if that event occurs, the condition is resolved, or the event becomes certain to occur.

5. In determining if an instrument is mandatorily redeemable, all terms within a redeemable instrument shall be considered. The following items do not affect the classification of a mandatorily redeemable financial instrument as a liability:

a. A term extension option

b. A provision that defers redemption until a specified liquidity level is reached

c. A similar provision that may delay or accelerate the timing of a mandatory redemption.

6. If a financial instrument will be redeemed only upon the occurrence of a conditional event, redemption of that instrument is conditional and, therefore, the instrument does not meet the definition of mandatorily redeemable financial instrument in this statement. However, that financial instrument would be assessed at each reporting period to determine whether circumstances have changed such that the instrument now meets the definition of a mandatorily redeemable instrument (that is, the event is no longer conditional). If the event has occurred, the condition is resolved, or the event has become certain to occur, the financial instrument is reclassified as a liability.

Obligations to Repurchase Issuer's Equity Shares by Transferring Assets

7. An entity shall classify as a liability (or an asset in some circumstances) any financial instrument, other than an outstanding share, that, at inception, has both of the following characteristics:

a. It embodies an obligation to repurchase the issuer's equity shares, or is indexed to such an obligation, and

b. It requires or may require the issuer to settle the obligation by transferring assets.

8. In this statement, "indexed to" is used interchangeably with "based on variations in the fair value of." The phrase "requires or may require" encompasses instruments that either conditionally or unconditionally obligate the issuer to transfer assets. If the obligation is conditional, the number of conditions leading up to the transfer of assets is irrelevant.

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9. Examples of financial instruments that meet the criteria in paragraph 7 of this Exhibit include forward purchase contracts or written put options on the issuer's equity shares that are to be physically settled or net cash settled.

10. All obligations that permit the holder to require the issuer to transfer assets result in liabilities, regardless of whether the settlement alternatives have the potential to differ.

11. Certain financial instruments that embody obligations that are liabilities within the scope of this statement also may contain characteristics of assets but be reported as single items. Some examples include the following:

a. Net-cash-settled or net-share-settled forward purchase contracts.

b. Certain combined options to repurchase the issuer's shares.

Those instruments are classified as assets or liabilities initially or subsequently depending on the instrument's fair value on the reporting date.

12. An instrument that requires the issuer to settle its obligation by issuing another instrument (for example, a note payable in cash) ultimately requires settlement by a transfer of assets, accordingly:

a. When applying paragraphs 7-11 of this Exhibit, this also would apply for an instrument settled with another instrument that ultimately may require settlement by a transfer of assets (warrants for puttable shares).

b. It is clear that a warrant for mandatorily redeemable shares would be a liability under this statement.

Certain Obligations to Issue a Variable Number of Shares

13. A financial instrument that embodies an unconditional obligation, or a financial instrument other than an outstanding share that embodies a conditional obligation, that the issuer must or may settle by issuing a variable number of its equity shares shall be classified as a liability (or an asset in some circumstances) if, at inception, the monetary value of the obligation is based solely or predominantly on any one of the following:

a. A fixed monetary amount known at inception (for example, a payable settleable with a variable number of the issuer's equity shares),

b. Variations in something other than the fair value of the issuer's equity shares (for example, a financial instrument indexed to the Standard and Poor's S&P 500 Index and settleable with a variable number of the issuer's equity shares), or

c. Variations inversely related to changes in the fair value of the issuer's equity shares (for example, a written put option that could be net share settled).

Prohibition on Combining Freestanding Financial Instruments

14. A freestanding financial instrument that is within the scope of this statement shall not be combined with another freestanding financial instrument in applying paragraphs 3-13 of this Exhibit. For example, a freestanding written put option that is classified as a liability under this statement shall not be combined with an outstanding equity share.

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Distinguishing Liability from Equity – Scope and Scope Exclusions

15. The guidance in paragraphs 15-29 of this statement applies to any freestanding financial instrument, including one that has any of the following attributes:

a. Comprises more than one option or forward contract, or

b. Has characteristics of both a liability and equity and, in some circumstances, also has characteristics of an asset (for example, a forward contract to purchase the issuer's equity shares that is to be net cash settled). Accordingly, this statement does not address an instrument that has only characteristics of an asset.

16. For example, an instrument that consists of a written put option for an issuer's equity shares and a purchased call option and nothing else is a freestanding financial instrument. That freestanding financial instrument embodies an obligation to repurchase the issuer's equity shares and is subject to the requirements of this statement.

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Statement of Statutory Accounting Principles No. 105 – Revised

Working Capital Finance Investments

STATUS

Type of Issue	Common Area
Issued	December 15, 2013; Substantively revised May 20, 2020
Effective Date	January 1, 2014; Substantive revisions detailed in Issue Paper No. 163 effective June 30, 2020.
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

SUMMARY CONCLUSION **1**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for working capital finance investments held by reporting entities. This statement amends *SSAP No. 20—Nonadmitted Assets* (SSAP No. 20) to allow working capital finance investments as admitted assets to the extent they conform to the requirements of this statement.

SUMMARY CONCLUSION

2. Working capital finance investments represent a confirmed short-term obligation[1] to pay a specified amount owed by one party (the obligor) to another (typically a supplier of goods), generated as a part of a working capital finance investment program currently designated by the NAIC Securities Valuation Office.

[1] All references to short-term obligations in this statement to refer to obligations not exceeding one year.

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Pursuant to the working capital finance investment program, this short-term obligation has been transferred by the entity entitled to payment (typically a supplier of goods) to a third party investor.

3. Working capital finance investments held by a reporting entity represent a right of the reporting entity to receive future payment. This statement provides accounting and reporting guidelines for the right to receive payment under working capital finance programs that meet particular criteria.

Working Capital Finance Program - Definitions and Conditions

4. A "working capital finance program" is an open account program under which an investor may purchase interests, or evidence thereof, in commercial non-insurance receivables. A working capital finance program is created for the benefit of a commercial investment-grade obligor and its suppliers of goods or services, and facilitated by a finance agent.

5. A working capital finance program transfers a right to payment to an investor from a short term obligation and arises from transactions among:

a. a buyer of goods or services that becomes an obligor to the supplier of goods or services,

b. the supplier(s) of those goods or services,

c. a finance agent, and

d. an investor.

6. A "working capital finance investment" is an interest in payment(s) from a confirmed supplier receivable issued pursuant to a working capital finance program. The payment (maturity) date must not exceed one year from the date of invoice from the supplier to the obligor. This investment is created when the investor purchases from a working capital finance program that is currently designated as NAIC "1" or "2" by the NAIC Securities Valuation Office, any of the following:

a. One or more confirmed supplier receivables;

b. in case of a participation, a participation interest in one or more confirmed supplier receivables issued by the finance agent or lead lender holding confirmed supplier receivables; or

c. a certificate, note or other interest manifestation, documented in a way that is verifiable, representing a legally enforceable interest in a right to payment either directly to the investor or from a trust, other special purpose entity or pool holding confirmed supplier receivables.

7. "Obligor" is the party that purchases the goods or services that generates the original supplier receivable (which is the payable for that Obligor). The obligor must have an NAIC designation of "1" or "2" or a Credit Rating Provider equivalent. The obligor must confirm the supplier receivable described in paragraph 11 as described in the confirmation process in paragraphs 12 and 13.

8. "Supplier" is the party that sells the goods or services to the obligor. The supplier sells the confirmed supplier receivable in accordance with the terms of the working capital finance program designated by the NAIC Securities Valuation Office at a price agreed to by the finance agent and/or investor.

9. "Investor" is the party purchasing a working capital finance investment in accordance with the terms of the working capital finance program designated by the NAIC Securities Valuation Office.

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10. The "finance agent" is a bank, financial institution, other financial intermediary, or service provider that facilitates the working capital finance program, arranges the sale, assignment or transfer of the confirmed supplier receivable to the investor for a fee and administers the payment mechanism. In the case of participation, the finance agent must inform the reporting entity investor of a default or event of default as soon as it becomes aware of such default or event of default. For the working capital finance program to qualify under this SSAP, the finance agent must meet the requirements of either paragraph 10.a. or 10.b.:

a. The finance agent is directly regulated by, or falls under the supervision of, a financial regulator of its domiciliary country provided that such country appears on the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* List of Jurisdictions Eligible for Netting; or

b. Payments from the obligor must be paid directly to the reporting entity (investor) or into an account maintained by a regulated financial institution for the benefit of investors in the working capital finance program and, in either case, the finance agent cannot be the beneficiary of such payment.

11. A "confirmed supplier receivable" is a first priority perfected security interest or right to payment of a monetary obligation from the obligor arising from the sale of goods or services from the supplier to the obligor the payment of which has been confirmed by the obligor committing and stating that the obligations under the agreement and any payment shall not be affected by the invalidity, unenforceability, existence, performance or non-performance of the underlying commercial trade transaction or any related contract or undertaking nor that it will not protest, delay, or deny, nor offer nor assert any defenses, personal or otherwise, against payment to the supplier or any party taking claims, interests, or rights to payments made by the supplier.

a. The confirmed supplier receivable must be sold, assigned or otherwise transferred in a manner that results in an absolute, irrevocable and legally enforceable obligation that has been confirmed by the Obligor.

b. In the case of a participation, the certificates or other evidence of participation provide an absolute, irrevocable, and legally enforceable obligation of the finance agent or holder of the confirmed supplier receivable to pay to the reporting entity investor all of the amounts due to it under the confirmed supplier receivable, without reduction or delay arising from any claims that the finance agent may have against the reporting entity investor. The reporting entity investor's ability to exercise its rights as creditor, or to direct the finance agent to exercise the rights of a creditor on its behalf, shall not be subject to, other than during a cure period not to exceed thirty days, the discretion of the finance agent or other lenders or investors.

Confirmation Process

12. In the case of a purchase, the investor shall verify, prior to the sale that the obligor has confirmed the respective amounts, payment dates and related invoice numbers' specified dates and has waived all defenses to payment. In the case of a participation, the finance agent must verify that the obligor has confirmed the respective amounts, payment dates and related invoice reference numbers' specified due dates, and has waived all defenses to payment in accordance with the confirmation process.

13. The obligor must commit and state that upon confirmation of a supplier receivable it is obligated to pay to the investor, the finance agent, or any third party acting as agent or trustee for the investor, a sum equal to the full amount of that confirmed supplier receivable(s) on a date certain stated in the confirmation and that it waives any right of setoff or other defenses to avoid or delay the full and timely payment of that Confirmed Supplier Receivable. The documents establishing the working capital finance program or the confirmation must state and confirm that the obligation to pay must be independent of any other contracts

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or claims that might be raised in defense arising from any transaction financed in connection with the WCFI program, the confirmed supplier receivable, or any other courses of performance or courses of dealing with the supplier.

Program Requirements

14. The working capital finance program investor must provide in its annual filing with the NAIC Securities Valuation Office one of the following:

a. An annual independent report according to Statement on Standards for Attestation Engagements (SSAE) No. 16 (or functional equivalent), reporting on controls at a service organization related to the administration of the investment; or

b. An annual audit of the financial statements and internal controls of the consolidated group of which the finance agent is part, which does not note any material weaknesses related to servicing working capital financial investments.

The NAIC Securities Valuation Office would review the materiality of the report findings in making their determination of the assignment of a designation.

15. If the credit rating of the working capital finance program or obligor falls to non-investment grade (below the equivalent of NAIC designation "1" or "2"), the reporting entity shall nonadmit, the working capital finance investments obtained under the related working capital finance program and/or the related obligor. Due to the short-term nature of these investments, once an investment is nonadmitted due to the credit rating of the working capital finance program or the obligor, those investments will continue to be nonadmitted.

16. Reporting entity investors must have the ability to monitor the working capital finance program and the credit-related activities of the obligor. Reporting entity investors must provide information as requested to the state of domicile indicating that they have the ability to monitor on an ongoing basis the activities of the working capital finance program.

17. All contracts or agreements that are a part of or that together constitute a working capital finance program must provide that if a dispute arises among any of the parties under any of the contracts or agreements that are a part of or that together constitute the working capital finance program, each party agrees that the dispute will be submitted to a court of competent jurisdiction in the United States or a constituent state thereof or of an alternative dispute resolution process recognized thereby. All contracts or agreements that are a part of or that together constitute a working capital finance program must provide that any dispute arising under any of the contracts or agreements that are a part of or that together constitute the working capital finance program must be resolved pursuant to the laws of the United States or a constituent state thereof that address the substance of the dispute but excluding those laws addressing conflicts of law.

Exclusions

18. A working capital finance investment excludes any receivables financed through:

a. Factoring: the purchase of receivables in bulk from a supplier where the receivables represent the payment obligations of potentially thousands of buyers to a single supplier, in which the buyers have no relationship with or contractual obligation to pay the factor and retain all legal defenses to payment they may have against the supplier;

b. Forfaiting: the purchase of one or a series of receivables from exporters by a forfaiter to enable the exporter (seller) to finance a commercial transaction with a buyer in which the Obligor has no relationship with or contractual obligation to pay the forfaiter and retains all legal defenses to pay it may have against the seller; or

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c. Invoice discounting: the advancement of funds by a finance company to a business entity with the funds advanced limited to a defined percentage of the business entity's eligible and outstanding receivables.

19. Eligible Confirmed Supplier Receivables must not:

a. Include insurance or insurance related assets;

b. Be impaired or in default at the time of purchase;

c. Have a payment (maturity) date longer than one year from the date of the invoice from the Supplier to the Obligor giving rise to the confirmed supplier receivable, and the maturity date must not be subject to change or rolling; nor

d. Include any receivable of any parent or affiliate of the reporting entity investor, and neither the Obligor nor any Supplier may be affiliated with the reporting entity investor. Working Capital Finance Investments that have obligors or vendors that are affiliated with the investor are ineligible, and therefore, nonadmitted assets.

Accounting and Reporting

20. The right to receive payment generated by a working capital finance investment issued under a working capital finance program is considered to meet the definition of an asset as defined in *SSAP No. 4—Assets and Nonadmitted Assets*, and is an admitted asset to the extent the investment conforms to the requirements set forth in this statement and the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. For programs that comply with all of these elements, working capital finance investments shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and the designation assigned in the NAIC Valuations of Securities product. Programs that do not comply with the elements set forth in this statement, or the provisions set forth in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* are nonadmitted. Working capital finance investments are reported as other invested assets in the financial statements.

21. A working capital finance investment shall be recorded on the trade date. At acquisition, the Working Capital Finance Investment shall be initially reported at cost, excluding brokerage and other related fees, and all other costs (internal costs, or costs paid for origination, purchase or commitment to purchase such investments), which shall be expensed as incurred.

22. After initial acquisition, the Working Capital Finance Investment shall be reported at amortized cost until the specified maturity date, unless the investment, or a portion thereof, is deemed uncollectible or when an other-than-temporary impairment has occurred. In the event that a working capital finance investment is purchased by a reporting entity investor at a premium (amount to be received by the entity under the confirmed supplier receivable is less than the price paid for the investment), the excess paid by the reporting entity investor in comparison to the amount receivable under the confirmed supplier receivable must be immediately expensed.

23. For reporting entities required to maintain an Interest Maintenance Reserve (IMR), the accounting for realized capital gains and losses from working capital finance investments shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities not required to maintain an IMR, realized gains and losses from working capital finance investments shall be reported as net realized capital gains or losses in the statement of income. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

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24. A Working Capital Finance Investment may provide for a prepayment penalty or acceleration fee in the event the working capital finance investment is liquidated prior to its scheduled termination date. Such fees shall be reported as investment income when received.

25. *SSAP No. 34—Investment Income Due and Accrued* shall be followed for determining and recording investment income earned on working capital finance investments acquired at a discount. In accordance with *SSAP No. 34—Investment Income Due and Accrued*, investment income shall be reduced for amounts that have been determined to be uncollectible, however amounts more than 15 days overdue are nonadmitted.

Default

26. A working capital finance investment payment that is uncollected by the reporting entity within 30 days after the due date shall be considered in default and nonadmitted. If the reporting entity has any other working capital finance investment assets from the same defaulting counterparty, all other working capital finance investments from that counterparty shall be nonadmitted. All working capital finance investments from a counterparty identified in default shall be evaluated for impairment.

Impairment

27. An other-than-temporary impairment(INT 06-07) shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of a confirmed supplier receivable including the payment on the established due date. Pursuant to this guidance, assessment of other-than-temporary impairment shall include an evaluation of the financial condition and short-term prospects of the obligor. If it is determined that a decline in the fair value of a working capital finance investment below book/adjusted carrying value is due to an other-than-temporary impairment, an impairment loss shall be recognized as a realized loss equal to the entire difference between the working capital finance investment's carrying value and fair value as of the reporting period for which the assessment is made. Fair value shall be determined in accordance with *SSAP No. 100R—Fair Value*, and reflect the price to sell the asset in an orderly market between market participants. As such, the fair value shall reflect the assumptions market participants will use in pricing the asset, including assumptions about risk.

28. For reporting entities required to maintain an AVR/IMR, the entire amount of the realized loss from the other-than-temporary impairment shall be recorded through the AVR, in accordance with SSAP No. 7.

29. Upon recognition of an other-than-temporary impairment, the fair value of the working capital finance investment on the measurement date shall become the new cost basis of the working capital finance investment and the new cost basis shall not be adjusted for subsequent recoveries in fair value. Once an investment is determined to be other-than-temporarily impaired, until all expected payments are received, the reporting entity must re-evaluate the investment quarterly and reassess fair value, with recognized realized losses for the difference between the book/adjusted carrying value and the current fair value. This process shall continue until either all expected payments are received, or the entity has recognized a realized loss for the entire uncollected carrying value.

Disclosures

30. The financial statements shall include the following disclosures:

a. Fair value in accordance with SSAP No. 100R.

b. Concentrations of credit risk in accordance with *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures* in the annual audited statutory financial reports only.

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c. Information regarding the aggregate book/adjusted carrying value of working capital finance investment by designation including gross assets with nonadmitted and net admitted amounts annually. (Note that programs designated 3-6 are nonadmitted.)

	Gross Asset CY	Non-Admitted Asset CY	Net Admitted Asset CY
WCFI Designation 1			
WCFI Designation 2			
WCFI Designation 3			
WCFI Designation 4			
WCFI Designation 5			
WCFI Designation 6			
Total			

d. Annual and quarterly information regarding the aggregate book/adjusted carrying value maturity distribution on the underlying working capital finance investments by the categories of maturities up to 180 days and 181 to 365 days.

e. Any events of default of working capital finance investments during the reporting period.

31. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

32. *ASU 2022-04, Disclosure of Supplier Finance Program Obligations* is rejected.

33. Effective December 31, 2023, this statement rejects *ASU 2016-13, Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments; ASU 2018-19, Codification Improvements to Topic 326, Financial Instruments—Credit Losses; ASU 2019-04, Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842); ASU 2019-11, Codification Improvements to Topic 326, Financial Instruments—Credit Losses;* and *ASU 2020-03, Codification Improvements to Financial Instruments.* Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Effective Date and Transition

~~32.~~34. This statement is effective for years on or after January 1, 2014. Substantive revisions documented in *Issue Paper No. 163—Working Capital Finance Investment Updates* are effective for financial reporting periods on or after June 30, 2020. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 147—Working Capital Finance Investments*
- *Issue Paper No. 163—Working Capital Finance Investment Updates*

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Statement of Statutory Accounting Principles No. 107

Risk-Sharing Provisions of the Affordable Care Act

STATUS

Type of Issue	Common Area
Issued	December 12, 2014
Effective Date	December 15, 2014
Affects	Nullifies INT 13-04
Affected by	No other pronouncements
Interpreted by	INT 15-01
Relevant Appendix A Guidance	A-791

STATUS **1**

SCOPE OF STATEMENT **1**

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SCOPE OF STATEMENT

1. The Affordable Care Act (ACA) imposes fees and premium stabilization provisions on health insurance issuers offering commercial health insurance. This statement provides accounting for three programs known as risk adjustment, reinsurance and risk corridors that take effect in 2014. Risk adjustment is a permanent risk-spreading program (ACA Section 1343). The temporary transitional reinsurance program (ACA Section 1341) and temporary risk corridors program (ACA Section 1342) are for years 2014 through 2016.

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SUMMARY CONCLUSION

2. Specific terms included in Exhibit A are unique to these programs and should not be applied to other aspects of statutory accounting. The required payments to the programs by reporting entities are described as "contributions" in the program literature but are referred to in this guidance as assessments for clarity. Amounts redistributed by the programs back to reporting entities are termed "payments" by the programs. These "payments" are recoverables / receivables for the reporting entity and are termed program distributions or receivables (to the reporting entity) in this guidance. The reporting of payable or receivable amounts in this guidance is from the perspective of the reporting entity. This statement nullifies *INT 13-04: Accounting for the Risk-Sharing Provisions of the Affordable Care Act.*

3. This statement establishes statutory accounting principles for the risk-sharing provisions of the ACA. The manner in which these provisions are applied in the determination of the medical loss ratios (MLR) and rebates may be different from these as the MLR calculations are based on the ACA Section 2718(b).

Risk Adjustment Program – Description and Overview

4. The risk adjustment program based on Section 1343 of the ACA is effective beginning in the 2014 benefit year and continues as a permanent program.

5. The risk adjustment program includes health plans (except certain exempt and grandfathered plans) in the individual or small group markets both on and off the exchange. All covered risk adjustment plans are required to participate in the risk adjustment program.

6. The purpose of the risk adjustment program is to transfer funds from lower risk plans to higher risk plans within similar plans in the same state in order to adjust premiums for adverse selection among carriers caused by membership shifts due to guarantee issue and community rating mandates. States may set up their own risk adjustment programs, or they may permit the U.S. Department of Health and Human Services (HHS) to develop and manage the program in the state. In addition to the risk adjustment amount, HHS determines the user fee. In states operating their own risk adjustment program, the state will determine the fee.

7. Risk adjustment assessments and distributions will be computed based on the reporting entity's risk score versus the overall market risk score after applying adjustments. Effective for 2018 benefit plan years, the risk adjustments and distributions are calculated including the high-cost risk pool aspect of this program (see high-cost risk pool in paragraphs 10-11, paragraph 15 and paragraph 16). Risk adjustment assessments will be made if the plan average actuarial risk of all of their enrollees in a market and state is lower than the plan average risk of all enrollees in fully insured plans in that market and state risk pool. Risk adjustment distributions will be made to health plan issuers whose plans have an average actuarial risk that is greater than the plan average actuarial risk scores in that market and state risk pool. The reinsurance program is not considered in the computation.

8. HHS will collect a user fee to support the administration of the HHS-operated risk adjustment program. This fee applies to issuers of risk adjustment covered plans in states in which HHS is operating the risk adjustment program. For example, HHS projects that the per capita risk adjustment user fee for 2014 is approximately $1 per enrollee per year. Similar terms will apply for the user fees of state operated programs.

9. All risk adjustment distributions made to issuers are completely funded through the amounts assessed to other issuers within the same market in the same state to ensure equality between program distributions and assessments. Consequently, risk adjustment assessments will be invoiced prior to processing program distributions to issuers. Once applicable risk adjustment assessments by issuers are received by HHS or the state, funds will be redistributed to the higher risk plans. Each issuer that offers a

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risk adjustment covered plan will be notified of risk adjustment distributions or assessments by June 30 of the year following the benefit year to align with the program distributions and assessment processing. Risk adjustment assessments owed by an issuer to HHS or the state are required to be remitted within 30 days of notification of the assessment. Once applicable assessments are received by HHS or the state, funds will be redistributed to the higher risk plans.

10. In December 2016, the HHS adopted a new regulation that changed how the ACA risk adjustment program would function, beginning with the 2018 benefit year. Specifically, the ACA risk adjustment methodology will incorporate a high-cost risk pool calculation. This adds a reinsurance-like element to the risk adjustment program, which is referred to as high-cost risk pooling. The operation of the high-cost risk pools will exclude a percentage of costs above a threshold level in the calculation of enrollee-level plan liability risk scores so that risk adjustment factors in the risk adjustment program described in paragraphs 4-9 would be calculated for risk excluding these extreme costs as determined by federal regulations. The program will operate two national high-cost risk pools, one for individuals and one for small groups. An overview of the new high-cost risk pool aspect of ACA risk adjustment is as follows:

a. HHS will establish two new high-cost risk pool parameters: a threshold and a coinsurance rate. For 2018, the threshold has been set at $1 million, and the coinsurance rate has been set at 60%. For 2018, the high-cost risk pools for high-cost enrollees would fund 60% of an issuer's costs for individual enrollees with claims above $1 million.

b. In the calculation of each issuer's annual risk adjustment transfer amount, the issuer will be reimbursed for a portion (specifically, the coinsurance rate) of actual enrollee-level claims above the threshold. Conforming changes will be made to how each issuer's enrollee-level plan liability risk scores are calculated. For example, in 2018, claims in excess of $1 million per enrollee will be reimbursed from the respective high-cost risk pool at a 60% coinsurance rate. This payment is referred to hereafter as the high-cost risk pool claims reimbursement.

c. In order to maintain the zero-sum nature of risk adjustment across each market in light of the new high-cost risk pool claims reimbursements detailed in paragraph 10.b., each issuer's risk adjustment transfer amount payable to HHS will include an assessment to all risk adjustment entities, which will be calculated as a percentage of the issuer's total premiums in the applicable market. The sum of the assessments across all issuers is intended to equal the sum of the high-cost risk pool claims reimbursements across all issuers.

d. HHS will report the high-cost risk pool amounts as part of the risk adjustment payment transfer formula including all components as a single amount, which should be reported on a net basis.

11. Conceptually, high-cost risk pool can be thought of as an involuntary reinsurance pool or as an aspect of the risk adjustment program. Combining the estimates of the various parts of the risk adjustment program reduces the potential impact of misestimating each element.

Risk Adjustment Program – Accounting Treatment

12. The accounting elements of the ACA permanent risk adjustment program, which are considered separately, include the user fee and the risk adjustment assessments and distributions.

13. The user fee is paid to HHS in states where the risk adjustment program is being operated by HHS and to the state program if operated by the state. Risk adjustment user fees shall be treated as government assessments. These fees are treated the same as other non-income-based governmental taxes

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and fees in that they are recognized as an expense and liability when the premium subject to the assessment is written.

14. Premium adjustments pursuant to the risk adjustment program will be based upon the risk scores (health status) of enrollees, participating in risk adjustment covered plans rather than the actual loss experience of the insured. This program bears some similarities to the Medicare Advantage risk adjustment program[1] under which the plan receives additional funding (or pays additional amounts) based on adjustments to risk scores of enrollees (see *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*).

15. The risk adjustment payables and receivables shall be accounted for as premium adjustments subject to redetermination as specified in this statement. Effective beginning with 2018 benefit plan years, the risk adjustment assessments and distributions are calculated including the high-cost risk pool aspect of this program and should be reported on a net basis.

a. Risk adjustment payables meet the definition of liabilities as set forth in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Risk adjustment receivables meet the definition of an asset and are admissible to the extent that they meet all of the criteria in this statement.

b. Risk adjustment payables and receivables shall be estimated based on experience to date. The method used to estimate the payables and receivables shall be reasonable and consistent between reporting periods. Reporting entities shall be aware of the significant uncertainties involved in preparing estimates and be both diligent and conservative in their estimations. In exercising the judgment required to prepare reasonable estimates for the financial reporting of risk adjustment program payables and receivables, the statutory accounting concept of conservatism shall be followed. In addition, reporting entities are required to have sufficient data to determine a reasonable estimate. Ensuring sufficient data requires that the reporting entity's estimate is based on demonstrated knowledge of the marketplace and annual information which includes patient encounter and diagnosis code data to determine the differences in the actuarial risk profile of the reporting entity's insureds versus the market participants in the particular market and state risk pool. Sufficient data shall incorporate patient default scores, if applicable, under the terms of the risk adjustment program. In addition, the estimates shall be consistent with other financial statement assertions and the pricing scenarios used by the reporting entity.

c. Premium revenue adjustments for the risk adjustment program are estimated for the portion of the policy period that has expired and shall be reported as an immediate adjustment to premium. Accrued risk adjustment receivables shall be recorded in premium and considerations receivable, with a corresponding entry to written premiums. Accrued risk adjustment payables shall be recorded as a liability[2] with a corresponding entry to written premiums. Reporting entities shall record additions or reductions to revenue resulting from the risk adjustment program in the period in which the changes in risk scores of enrollees result in reasonably estimable additions or reductions. The risk adjustment program receivables shall be reported gross of payables.

[1] The ACA program also has significant differences from the Medicare Advantage risk adjustment program, which is retrospective, administered as a single national program, with most enrollees administered by the federal government. By contrast, the ACA risk adjustment is not retrospective, and is administered by each entity by state and by plan.

[2] The annual statement liability lines will vary by the type of annual statement the reporting entity files. Managed care/accident and health reporting entities report as aggregate health policy reserves; life and accident and health reporting entities report as aggregate reserves for accident and health contracts; and property and casualty reporting entities report as aggregate write-ins for liabilities.

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d. The risk adjustment receivables are administered through a federal governmental program. Once amounts are collected by the governmental entity, there is an obligation to distribute the funds. Amounts over 90 days due shall not cause the receivable to be treated as a nonadmitted asset based solely on aging.

e. Provided that the risk adjustment receivables due the reporting entity are determined in a manner that is consistent with the requirements of this statement, the receivables are admitted assets until determination of impairment or payment denial is received from the governmental entity or government-sponsored entity administering the program. Upon notification that payments to be paid to the reporting entity will be less than the recorded receivables, any amount in excess of the confirmed amount shall be written off and charged to income, except for amounts that are under appeal. Any receivable for risk adjustment amounts under appeal shall be reflected as a nonadmitted asset.

f. Evaluation of the collectibility of all amounts receivable from the risk adjustment program shall be made for each reporting period. If, in accordance with SSAP No. 5R, it is probable that the risk adjustment receivables are uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. If it is reasonably possible that a portion of the balance determined in accordance with this paragraph is not anticipated to be collected and is therefore not written off, the disclosure requirements outlined in SSAP No. 5R shall be followed.

Risk Adjustment Program – High-Cost Risk Pool – Accounting Treatment

16. The individual and small group high-cost risk pools of the ACA risk adjustment program shall be accounted for consistent with the rest of the ACA risk adjustment program. Reporting entity issuers in the individual or small group markets need to account for the following risk adjustment payables and receivables including the impairment and aging guidance reflected in paragraph 15 and paragraph 16:

a. The high-cost risk pool assessment payable by the reporting entity, which is the percent-of-premium charge to the issuer in order to fund reimbursements across all issuers of claims above the high cost risk pool threshold, shall be accounted for as decreases to written premium subject to redetermination.

b. High-cost risk pool distributions, which represent proportionate reimbursement for the issuer's claims above the high cost risk pool threshold, would be accounted for as increases to written premium subject to redetermination.

c. As the risk adjustments and distributions described in paragraphs 4-9 are calculated after excluding the percentage of costs above the threshold specified in the high-cost risk pool aspect of this program, the payments described in paragraphs 4-9 will continue to be accounted for consistent with guidance in paragraph 15 and paragraph 16 (i.e., as a premium adjustment subject to redetermination).

Transitional Reinsurance Program – Description and Overview

17. The transitional reinsurance program based on Section 1341 of the ACA is effective for plan years 2014 through 2016. Reinsurance assessments will be collected and distributions will be issued during the three-year term.

18. All issuers of major medical commercial products and third party administrators (TPAs) on behalf of uninsured group health plans are required to contribute funding at the national contribution rate to HHS. States establishing reinsurance programs may collect additional funding. Non-grandfathered individual plans are eligible to receive benefit program distributions via an excess-of-loss reinsurance

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system. Grandfathered plans are ineligible. Group plans are required to contribute funding, but are not eligible to receive reinsurance program distributions.

19. In general, this transitional reinsurance program provides funding to issuers in the individual market that incur high claims costs for enrollees. The program requires assessments from all issuers and TPAs on behalf of group health plans based on a per member annual fee established by HHS. The reinsurance assessment will fund reinsurance program distributions plus disbursements to the U.S. Treasury, in addition to covering administrative expenses of the program.

20. Consequently, the term "reinsurance" does not represent actual reinsurance between licensed insurers as defined by *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*. This program is similar to an involuntary pool in *SSAP No. 63—Underwriting Pools* for the individual insured health products subject to the 2014 ACA market reforms. For the group plans, which are required to contribute funding but are not eligible to receive program distributions, the program is an assessment payable by the reporting entity and not a pool.

21. The national transitional reinsurance program assessment rate for all issuers and TPAs will be established by HHS and will be designed to collect more than $12 billion in 2014 to cover the required $10 billion for the reinsurance program, the $2 billion contribution to the U.S. Treasury, and additional amounts to cover the administrative costs of the federal government entity and applicable reinsurance entities. States electing to operate their own reinsurance program have the option to increase the reinsurance assessment rate to provide additional funding for the reinsurance program or to fund the administrative expenses of the applicable reinsurance entity. Assessments for the reinsurance program must fund the reinsurance program of $10 billion in 2014, $6 billion in 2015 and $4 billion in 2016, plus disbursements to the U.S. Treasury of $2 billion, $2 billion and $1 billion for years 2014 through 2016, in addition to covering administrative expenses of the applicable reinsurance entity or HHS.

22. Reinsurance program distributions will be processed either by the applicable reinsurance entity or by HHS and will be made to issuers of non-grandfathered individual market plans for high claim costs of enrollees. Distributions from the applicable reinsurance entity to insurers providing individual coverage will be calculated as a coinsurance rate multiplied by the eligible claims submitted for an individual enrollee's covered benefits between an attachment point and the reinsurance cap for each benefit year. The coinsurance rate, attachment point and reinsurance cap are initially determined by HHS, but may be modified by the state, if the state chooses to establish its own reinsurance program.

23. Each state is eligible to establish a reinsurance program, regardless of whether the state establishes a Marketplace Exchange. If a state establishes a reinsurance program, the state must enter into a contract with an applicable reinsurance entity or entities or establish a reinsurance entity to carry out the program. If a state does not elect to establish its own reinsurance program, HHS will administer the reinsurance program on behalf of that state. HHS establishes the annual administrative portion for the fee. (For example, the 2014 fee will be $0.11 per-member per-year resulting in $20.3 million of administrative expense funding).

24. Reinsurance assessments to fund the program are made on an annual basis with billing beginning December 15, 2014. An insurer may submit claims for reimbursement when an enrollee of the reinsurance-eligible plan has met the applicable criteria as determined by either the state or HHS. Claims may be submitted through April 30 of the year following the benefit year. HHS will distribute reinsurance program funds among issuers nationally based on submitted claims. Issuers will be notified of pending reinsurance distributions by June 30 following the benefit year. If the requests for distributions exceed the actual assessments collected, HHS will reduce reinsurance distributions on a pro-rata basis. If the requests for distributions are less than actual assessments collected, HHS will increase reinsurance distributions on a pro-rata basis.

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Transitional Reinsurance Program – Accounting Treatment

25. Due to the diverse elements of the transitional reinsurance program, which includes characteristics of traditional reinsurance, involuntary pools and governmental assessments, a hybrid accounting approach is required. The accounting treatment for the transitional reinsurance program outlined below is discussed in terms of the payables and receivables and the impact to the health insurance products subject to the program.

26. The following are the broad groupings of the health insurance products subject to the transitional reinsurance program:

a. Individual insured health products subject to the 2014 ACA market reforms. This excludes grandfathered and non-grandfathered 2013 products (referred to as subject individual insured products);

b. Other insured health products. This encompasses products which are not subject to the ACA market reforms including individual grandfathered and non-grandfathered (referred to as other insured health products);

c. Self-insured health products.

27. The guidance in this section will provide treatment for each of the assessments payable and program distribution receivable elements of the program listed below for the health insurance products listed in paragraph 26.

a. Assessments for reinsurance

b. Administrative costs assessments

c. Additional U.S. Treasury assessment

d. Reinsurance distributions

Subject Individual Insured Health Products

Subject Individual Insured Issuers - Assessments Payable for Reinsurance

28. Transitional reinsurance assessments attributable to enrollees in individual plans are treated as ceded reinsurance premium. This applies both to assessments made at the national assessment rate and to any state-elected additional assessments that will fund reinsurance program distributions. Ceded premiums would be reported as a reinsurance cession and follow reinsurance accounting in accordance with SSAP No. 61R, paragraph 17 and paragraphs 25-27.

29. For the individual coverage issuers, this is an involuntary pool and under the terms of the transitional reinsurance program, the transfer of risk and timely reimbursement requirements of SSAP No. 61R are deemed to be met.

30. With regard to individual coverage issuers, the transitional reinsurance program is more similar to traditional reinsurance than it is to an assessment, because program assessments are made to and program distributions are received from the government or government-sponsored entity. Accordingly, the program is accounted for as reinsurance for individual insured products subject to the transitional reinsurance program.

31. The provisions of SSAP No. 63, paragraph 3, define involuntary pools.

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32. The transitional reinsurance program differs from an involuntary pool, in that there is not a proportionate sharing of the entire results of a pool. However, the purpose is very similar: to address the additional costs associated with high-risk individuals. Furthermore, HHS has noted, *"the Affordable Care Act … requires that states eliminate or modify high-risk pools to the extent necessary to carry out the reinsurance program,"* which likewise highlights the similar purposes of the two mechanisms. Therefore, SSAP No. 63, paragraph 8, provides additional relevant guidance. As the transitional reinsurance program is a mechanism for sharing the additional costs associated with high-risk individuals, it is accounted for as traditional reinsurance.

Subject Individual Insured Issuers - Reinsurance Administrative Expense Assessments

33. The assessment payable by the reporting entity for administrative expenses attributable to individual coverage is reflected as ceded premium. This applies both to assessments made at the national assessment rate and to any state-required assessments that will provide additional funding for administrative expenses.

34. Normally reinsurance premiums are set at a level intended to cover anticipated claim costs and include an administrative charge component. Therefore, as a matter of consistency, it is appropriate to include the administrative charge component for the transitional reinsurance program in ceded premium for individual insured products.

Subject Individual Insured Issuers - U.S. Treasury Assessment

35. Because this portion of the assessment is earmarked for the U.S. Treasury and not for the reimbursement of claims or to cover the operating costs of the reinsurance program, it is a federal assessment not based on income. This portion of the assessment is not treated as ceded premium, but as an assessment under SSAP No. 35R and is reflected in the same expense category as taxes, licenses and fees. This is also consistent with annual statement expense reporting categories.

Subject Individual Insured Issuers - Reinsurance Program Distributions

36. Program distributions received from the ACA transitional reinsurance program for individual insurance is reflected as ceded claim benefit recoveries. This applies both to distributions received pursuant to the uniform federal reinsurance parameters and to any state distribution received.

37. In keeping with the rationale for reinsurance assessments above, distributions receivable from the transitional reinsurance program for individual insurance products is reflected the same as traditional reinsurance recoveries as described in SSAP No. 61R, paragraph 27.

38. Therefore, recoveries received are reported in the summary of operations and will reduce the ceding entity's reported benefits paid.

39. HHS and all applicable reinsurance entities shall be reported consistent with providers to an involuntary pool and will be treated as authorized reinsurers for the purposes of financial reporting for subject individual health products.

40. All receivables from the transitional reinsurance program are subject to the 90-day nonadmission rule beginning from when program receivables are due to be disbursed by the government or a government-sponsored entity. That is, the 90-day rule begins when governmental receivables are due, not from the date of initial accrual. The announced governmental or government-sponsored entity distribution date shall be the contractual due date similar to Appendix A-791, paragraph 2.h., which requires that payments due from the reinsurer are made in cash within ninety (90) days of the settlement date. The receivable is also subject to impairment analysis.

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Other Insured Health Products

Other Insured Health Products – Assessments Payable for Reinsurance

41. Transitional reinsurance program reinsurance assessments made for enrollees in fully insured plans other than individual plans are treated as an assessment payable by the reporting entity and charged to taxes, licenses and fees. This applies both to assessments made at the national assessment rate and to any state assessments that will fund reinsurance program distributions. In this case, for fully insured non-individual plans, the entity cannot, under the terms of the program, be deemed to be "participating," as funds for claim recoveries will not be re-distributed back to the issuer for the coverage that is being assessed. Therefore, issuers of other insured health products that are not for individuals are paying an involuntary fee but are not participating in an involuntary pool.

42. The treatment of the transitional reinsurance program reinsurance assessments for non-individual fully insured plans differs from the treatment for individual plans. Since the non-individual plans are not eligible for reimbursement, they are not participating in a reinsurance arrangement, and thus, the assessments are not treated as ceded premium. As an involuntary assessment, the transitional reinsurance program reinsurance assessments, consistent with SSAP No. 35R are treated as an assessment payable by the reporting entity and charged to taxes, licenses and fees expense. The expense is accrued in proportion to the other insured health enrollees base that will be used to determine the assessments payable as the premium subject to the assessment is written.

Other Insured Health Products - Reinsurance Administrative Expense Assessments

43. The reinsurance program administrative costs for other insured health products are an assessment payable by the reporting entity. This applies both to assessments made at the national assessment rate and to any state assessment that will fund administrative expenses and is reflected in the same expense category as taxes, licenses and fees.

Other Insured Health Products - U.S. Treasury Assessment

44. The additional U.S. Treasury assessment for other insured health products is a federal assessment payable by the reporting entity which is not based on income and is reflected in the same expense category as taxes, licenses and fees.

Other Insured Health Products - Reinsurance Program Distributions (not applicable)

45. Reinsurance recoveries will not occur for insured health products other than individual. Other insured health products will pay the transitional reinsurance program assessments payable but not receive program distributions for claims.

Self-Insured Health Products

Self-Insured Health Products - Assessments Payable for Reinsurance

46. Assessments made on behalf of self-insured plans which are administered by the reporting entity are uninsured plans and are excluded from the reporting entity's statement of operations, with respect to both monies received from the plans and assessments disbursed by the reporting entity. Any resulting liabilities or receivables shall be reported as liabilities and receivables held in connection with uninsured plans. This treatment is consistent with *SSAP No. 47—Uninsured Plans,* paragraphs 5 and 8-11.

47. The self-insured plan, not the reporting entity, is legally liable for assessments for the transitional reinsurance program. The funds are a bona fide pass-through by the reporting entity, which is merely

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providing a service for the self-insured (uninsured) plan. Therefore, the reporting entity will not report revenues or expenses for the assessments for the transitional reinsurance program.

48. The reporting entity may have received funds from the self-insured plans in advance of making disbursements. In that event, a liability is established for funds held in connection with self-insured plans.

49. The reporting entity, depending on its arrangement with the (uninsured) plan, may make a disbursement before receiving full funding from the plan. In that event, an asset is established for amounts receivable in connection with uninsured plans. The asset would be subject to the rules for admissibility and impairment as prescribed in SSAP No. 47, paragraphs 9-10.

Self-Insured Health Products - Reinsurance Administrative Expense Assessments Payable and U.S. Treasury Assessment

50. A reporting entity providing a service for a self-insured plan that is uninsured shall apply the pass-through treatment for the transitional reinsurance program's administrative cost assessments and additional U.S. Treasury contribution amounts. The uninsured plan, not the reporting entity, is legally liable. Therefore, the reporting entity will not report revenues or expenses with respect to the transitional reinsurance program's administrative cost assessments and additional U.S. Treasury contribution amounts.

Self-Insured Health Products - Reinsurance Payments (not applicable)

51. Reinsurance recoveries will not occur for self-insured health products, as these products will pay fees but not receive claims reimbursements.

Risk Corridors – Description and Overview

52. The risk corridors program based on Section 1342 of the ACA is effective for benefit years beginning in 2014 through 2016. The risk corridors program applies to Qualified Health Plans (QHPs) in the individual and small group markets whether sold on or outside of an exchange.

53. The purpose of the risk corridors program is to provide limitations on issuer losses and gains for QHPs through additional protection against initial pricing risk. The program creates a mechanism for sharing the risk for Allowable Costs between the federal government and the QHP issuers. The program is applied at the QHP level, not the issuer or market segment level. Although the risk corridors program provides protection against extreme bounds of experience, there is a substantial corridor in which all variance in experience directly affects the financial return of the reporting entity.

54. To determine whether an issuer pays into (contributes), or receives distributions from, the risk corridors program, HHS will compare Allowable Costs[3] and the Target Amount[4] based on a formula that compares Allowable Costs. Below is an example (before transition requirements) for a QHP.

a. When a QHP's Allowable Costs for any benefit year are more than 103% but not more than 108% of the Target Amount, HHS will pay the QHP issuer an amount equal to 50% of the Allowable Costs in excess of 103% of the Target Amount.

[3] With respect to a QHP, Allowable Costs is an amount equal to the sum of incurred claims of the QHP issuer, adjusted to include qualifying expenditures by the QHP for activities that improve health care quality, expenditures for health information technology and meaningful use requirements and other required adjustments.

[4] With respect to a QHP, the Target Amount is an amount equal to the total premiums earned with respect to a QHP, including any premium tax credit under any governmental program, reduced by the allowable administrative costs of the plan.

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b. When a QHP's Allowable Costs for any benefit year are more than 108% of the Target Amount, HHS will pay the QHP issuer an amount equal to 2.5% of the Target Amount plus 80% of the Allowable Costs in excess of 108% of the Target Amount.

c. If a QHP's Allowable Costs for any benefit year are less than 97% but not less than 92% of the Target Amount, the QHP issuer must remit assessments payable to HHS in an amount equal to 50% of the difference between 97% of the Target Amount and the Allowable Costs.

d. When a QHP's Allowable Costs for any benefit year are less than 92% of the Target Amount, the QHP issuer must remit assessments payable to HHS in an amount equal to the sum of 2.5% of the Target Amount plus 80% of the difference between 92% of the Target Amount and the Allowable Costs.

55. The risk corridors program creates a mechanism for sharing risk for Allowable Costs between the federal government and QHP issuers. The ACA establishes the risk corridors program as a federal program; consequently, HHS will operate the risk corridors program under federal rules without state variations. The risk corridors program is intended to protect against inaccurate rate setting in the early years of the exchanges by limiting the extent of issuer losses and gains. In the event that risk corridors program collections are not sufficient to cover all the required distributions, the ACA requires the use of other sources of federal funding for the required distributions, subject to the availability of appropriations.

56. The final risk corridors settlement calculation will be communicated by HHS after the end of the benefit year and after premium and loss adjustments related to the reinsurance and risk adjustment programs have been determined.

Risk Corridors – Accounting Treatment(INT 15-01)

57. This program is similar to the risk corridors program established for the Medicare Part D prescription drug coverage[5]. However, due to the asymmetrical nature of the risk corridors calculation, an overstatement of expense in one cell, which is theoretically offset by the understatement of expense in another cell, does not necessarily result in zero financial impact.

58. Payables and receivables pursuant to the temporary risk corridors program shall be accounted for as specified in this statement.

59. Risk corridors assessments meet the definition of liabilities as set forth in SSAP No. 5R. Risk corridors receivables due to the reporting entity meet the definition of an asset and are admissible to the extent that they meet all of the criteria in this statement.

a. Assumptions used in estimating retrospective premium adjustments shall be consistent with the assumptions made in recording other assets and liabilities necessary to reflect the underwriting results of the reporting entity such as claim and loss reserves (including IBNR) and contingent commissions. Contingent commissions and other related expenses shall be adjusted in the same period the additional or return retrospective premiums are recorded.

b. The additions or reductions to premium revenue resulting from the risk corridors program are recognized over the contractual period of coverage, to the extent that such additions or reductions are reasonably estimable. Reporting entities shall be aware of the significant uncertainties involved in preparing estimates and be both diligent and

[5] The ACA risk corridors program also has significant differences between the Medicare risk corridors program. The ACA risk corridors program is performed at a significantly more granular plan specific level with a pro-rata allocation of the issuer's overall claim costs for the plan's state/market cell.

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conservative in their estimations. Risk corridors payables and receivables shall be estimated based on experience to date. The method used to estimate the payables and receivables shall be reasonable and consistent between reporting periods. In exercising the judgment required to prepare reasonable estimates for the financial reporting of risk corridors program payables and receivables, the statutory accounting concept of conservatism shall be followed. In addition, reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity's estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. In addition, the estimates shall be consistent with other financial statement assertions and the pricing scenarios used by the reporting entity.

c. The risk corridors receivables are from a federal governmental program. Amounts over 90 days due shall not cause the receivable to be treated as a nonadmitted asset based solely on aging.

d. Provided that the risk corridors receivables due the reporting entity are determined in a manner that is consistent with the requirements of this statement, the receivables are admitted assets until determination of impairment or payment denial is received from the governmental entity or government-sponsored entity administering the program. Upon notification that payments to be paid to the reporting entity will be less than the recorded receivables, any amount in excess of the confirmed amount shall be written off and charged to income, except for amounts that are under appeal. Any receivable for risk corridors amounts under appeal shall be reflected as a nonadmitted asset.

e. Evaluation of the collectibility of all amounts receivable from the risk corridors program shall be made for each reporting period. If, in accordance with SSAP No. 5R, it is probable that the risk corridors receivables are uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. If it is reasonably possible, that a portion of the balance determined in accordance with this paragraph is not anticipated to be collected and is therefore not written off, the disclosure requirements outlined in SSAP No. 5R shall be followed.

f. Reporting shall be consistent with *SSAP No. 66—Retrospectively Rated Contracts*, paragraph 9 guidance on reporting for retrospective premium.

Disclosures

60. The financial statements shall disclose on an annual and quarterly basis beginning in the first quarter of 2014, the assets, liabilities and revenue elements by program regarding the risk-sharing provisions of the Affordable Care Act for the reporting periods which are impacted by the programs including the listing in paragraphs 60.a. through 60.c. Reporting entities shall also indicate if they wrote any accident and health insurance premium, which is subject to the Affordable Care Act risk-sharing provisions. In the event that the balances are zero, the reporting entity should provide context to explain the reasons for the zero balances, including insufficient data to make an estimate, no balances or premium was excluded from the program, etc. Asset balances shall reflect admitted asset balances. The disclosure shall include the following:

a. ACA Permanent Risk Adjustment Program

i. Premium adjustments receivable due to ACA Risk Adjustment (including high-cost risk pool payments)

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ii. Risk adjustment user fees payable for ACA Risk Adjustment

iii. Premium adjustments payable due to ACA Risk Adjustment (including high-cost risk pool ceded premium)

iv. Reported as revenue in premium for accident and health contracts (written/collected) due to ACA Risk Adjustment

v. Reported in expenses as ACA risk adjustment user fees (incurred/paid)

b. ACA Transitional Reinsurance Program

i. Amounts recoverable for claims paid due to ACA Reinsurance

ii. Amounts recoverable for claims unpaid due to ACA Reinsurance (contra-liability)

iii. Amounts receivable relating to uninsured plans for contributions for ACA Reinsurance

iv. Liabilities for contributions payable due to ACA Reinsurance - not reported as ceded premium

v. Ceded reinsurance premiums payable due to ACA Reinsurance

vi. Liability for amounts held under uninsured plans contributions for ACA Reinsurance

vii. Ceded reinsurance premiums due to ACA Reinsurance

viii. Reinsurance recoveries (income statement) due to ACA Reinsurance payments or expected payments

ix. ACA Reinsurance Contributions – not reported as ceded premium

c. ACA Temporary Risk Corridors Program

i. Accrued retrospective premium due from ACA Risk Corridors

ii. Reserve for rate credits or policy experience rating refunds due to ACA Risk Corridors

iii. Effect of ACA Risk Corridors on net premium income (paid/received)

iv. Effect of ACA Risk Corridors on change in reserves for rate credits

61. In addition, beginning in annual 2014 and both quarterly and annual thereafter, a roll forward of prior year ACA risk-sharing provisions specified asset and liability balances shall be disclosed in the annual statutory Notes to Financial Statements, as illustrated in Exhibit B. Note for the roll forward illustration, assets shall be reflected gross of any nonadmission. The reasons for adjustments to prior year balances (i.e. federal audits, revised participant counts, information which impacted risk score projections, etc.) shall also be disclosed. For year-end 2014, all columns and rows are expected to be zero since 2014 is the first year that a receivable or liability will be recorded. For reporting periods on or after March 31, 2016, the risk corridors roll forward is amended to require disclosure of the risk corridors asset

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and liability balances and subsequent adjustments by program benefit year. The beginning receivable or payable in the roll forward will reflect the prior year-end balance for the specified benefit.

62. For reporting periods ending on or after March 31, 2016, for both quarterly and annual reporting, the following information is required for risk corridors balances by program benefit year:

a. Estimated amount to be filed or final amounts filed with federal agency

b. Amounts impaired or amounts not accrued for other reasons (not withstanding collectability concerns)

c. Amounts received from federal agency

d. Asset balance gross of nonadmission

e. Nonadmitted amounts

f. Net admitted assets

Relevant Literature

Generally Accepted Accounting Principles

63. U.S. GAAP did not issue additional guidance to address the risk-sharing provisions of the ACA.

Effective Date and Transition

64. This statement is effective for years ending on or after December 15, 2014. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Risk-sharing provisions guidance was previously reflected within *INT 13-04: Accounting for the Risk-Sharing Provisions of the Affordable Care Act* and was effective January 1, 2014. Upon adoption of this statement, INT 13-04 was nullified. Disclosures in paragraphs 60 and 61 were adopted in *SSAP No. 35R—Guaranty Fund and Other Assessments,* but were incorporated into this statement prior to publication. Statement revisions in paragraphs 10-11 and paragraphs 15-16 for risk adjustment high-cost risk pools and related disclosure changes are effective for reporting periods beginning on or after January 1, 2018.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 150—Accounting for the Risk-Sharing Provisions of the Affordable Care Act*

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EXHIBIT A – GLOSSARY

The terms included in this exhibit are specific to the risk-sharing provisions of the ACA; accordingly, they are not intended to be applied to other topics.

Affordable Care Act (ACA) – The Patient Protection and Affordable Care Act (PPACA), commonly called the Affordable Care Act (ACA), is a United States federal statute signed into law on March 23, 2010.

Applicable Reinsurance Entity – A tax-exempt not-for-profit organization, the duties of which shall be to carry out the transitional reinsurance program by coordinating the funding and operation of the risk-spreading mechanisms designed to stabilize the individual markets during the implementation of health reform.

Cell – The risk corridor calculation is done at the QHP (Qualified Health Plan) level – the cell is state, market (individual or small group), QHP.

Assessment – Required payments into the applicable reinsurance entity by all issuers of major medical commercial products and third-party administrators to fund the transitional reinsurance program.

Exchange – Health insurance marketplaces, also called Health Exchanges, are organizations set up to facilitate the purchase of health insurance in every state of the United States in accordance with the Patient Protection and Affordable Care Act. The exchanges are regulated, online marketplaces, administered by either federal or state government, where individuals, families and small businesses can purchase qualified health insurance plans starting October 1, 2013, with coverage beginning January 1, 2014. Exchanges will also determine who qualifies for subsidies and make subsidy payments to insurers on behalf of individuals receiving them. They will also accept applications for other health coverage programs such as Medicaid and Children's Health Insurance Program (CHIP).

Exempt Plans – Certain health plans that are determined not to be a risk adjustment covered plan in the applicable federally certified risk adjustment methodology (45 C.F.R. § 153.20), grandfathered health plans, group health insurance coverage benefits that are not an integral part of a group health plan, are limited scope, or supplemental benefits (45 C.F.R. § 146.145(c)), and individual health insurance coverage excepted benefits (45 C.F.R. § 148.220).

Grandfathered Plans – A group health plan that was created or an individual health insurance policy that was purchased on or before March 23, 2010. Grandfathered plans are exempted from many changes required under the ACA. Plans or policies may lose their "grandfathered" status if they make certain significant changes that reduce benefits or increase costs to consumers. New employees and new family members may be added to grandfathered group plans after March 23, 2010.

Health and Human Services (HHS) – The Department of Health and Human Services (HHS) is the United States government's principal agency that oversees CMS, which administers programs for protecting the health of all Americans and providing essential human services.

Market Segment – Subset of consumers with its own set of demographic and other assumptions such as individual, state/federal, small group, group, Medicaid or Medicare.

Program Distribution– Amounts payable to or redistributed by the applicable reinsurance entity or the HHS to issuers of non-grandfathered individual market plans that incur high claims costs for enrollees and are eligible to receive benefit payments (recoveries).

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Qualified Health Plan (QHP) – Under the Affordable Care Act, starting in 2014, an insurance plan that is certified by the Health Insurance Marketplace, provides essential health benefits and follows established limits on cost-sharing (such as deductibles, copayments, and out-of-pocket maximum amounts).

Risk Score – Individual risk score means a relative measure of predicted health care costs for a particular enrollee that is the result of a risk adjustment model. Claims-based risk-assessment models use data, typically from a 12-month period, to identify underlying conditions and assign a risk score for each individual based on an algorithm.

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EXHIBIT B – ACA RISK-SHARING PROVISIONS ROLL-FORWARD ILLUSTRATION

Receivables are reflected gross of any nonadmission for this illustration.

	Accrued During the Prior Year on Business Written Before December 31 of the Prior Year		Received or Paid as of the Current Year on Business Written Before December 31 of the Prior Year		Differences		Adjustments			Unsettled Balances as of the Reporting Date	
					Prior Year Accrued Less Payments (Col 1 – 3)	Prior Year Accrued Less Payments (Col 2 – 4)	To Prior Year Balances	To Prior Year Balances		Cumulative Balance from Prior Years (Col 1 – 3 + 7)	Cumulative Balance from Prior Years (Col 2 – 4 + 8)
	1	2	3	4	5	6	7	8	9	10	11
	Receivable	(Payable)	Receivable	(Payable)	Receivable	(Payable)	Receivable	(Payable)	Ref	Receivable	(Payable)
a. Permanent ACA Risk Adjustment Program											
1. Premium adjustments receivable	4,000,000		3,000,000		1,000,000		-800,000		A	200,000	0
2. Premium adjustments (payable)		8,000,000		9,000,000		-1,000,000		1,000,000	B		0
3. Subtotal ACA Permanent Risk Adjustment Program	**4,000,000**	**8,000,000**	**3,000,000**	**9,000,000**	**1,000,000**	**-1,000,000**	**-800,000**	**1,000,000**		**200,000**	**0**
b. Transitional ACA Reinsurance Program											
1. Amounts recoverable for claims paid	22,000,000		15,000,000		7,000,000		-7,000,000		C	0	
2. Amounts recoverable for claims unpaid (contra liability)	8,000,000		9,000,000		-1,000,000		990,000		D	-10,000	
3. Amounts receivable relating to uninsured plans	3,000,000		2,800,000		200,000		-100,000		E	100,000	
4. Liabilities for contributions payable due to ACA Reinsurance – not reported as ceded premium		90,000		75,000		15,000		-14,000	F		1,000
5. Ceded reinsurance premiums payable		100		200		-100		100	G		0
6. Liability for amounts held under uninsured plans		125,000		15,000		110,000		90,000	H		200,000
7. Subtotal ACA Transitional Reinsurance Program	**33,000,000**	**215,100**	**26,800,000**	**90,200**	**6,200,000**	**124,900**	**-6,110,000**	**76,100**		**90,000**	**201,000**
c. Temporary ACA Risk Corridors Program											
1. Accrued retrospective premium	12,000,000		14,000,000		-2,000,000		1,750,000		I	-250,000	
2. Reserve for rate credits or policy experience rating refunds		150,000		250,000		-100,000		100,000	J		0
3. Subtotal ACA Risk Corridors Program	**12,000,000**	**150,000**	**14,000,000**	**250,000**	**-2,000,000**	**-100,000**	**1,750,000**	**100,000**		**-250,000**	**0**
d. Total for ACA Risk-Sharing Provisions	**49,000,000**	**8,365,100**	**43,800,000**	**9,340,200**	**5,200,000**	**-975,100**	**-5,160,000**	**1,176,100**		**40,000**	**201,000**

Explanation of adjustments:

A. Adjusted due to federal audit.

B. Adjusted because of revised participant count.

C. Adjusted due to poor experience of other participants in the reinsurance pool.

D. Revised risk score information in the state of substantially impacted risk scores.

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Statement of Statutory Accounting Principles No. 108

Derivatives Hedging Variable Annuity Guarantees

STATUS

Type of Issue	Common Area
Issued	November 15, 2018
Effective Date	January 1, 2020, with early adoption permitted January 1, 2019
Affects	None
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **1**

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EXHIBIT A – CALCULATION OF DEFERRED ASSET OR DEFERRED LIABILITY **12**

SCOPE OF STATEMENT

1. Current statutory accounting guidance for derivatives qualifying for hedging effectiveness is in *SSAP No. 86—Derivatives*. Pursuant to the direction from the Financial Condition (E) Committee, this statement allows special accounting treatment for limited derivatives hedging variable annuity guarantee benefits subject to fluctuations as a result of interest rate sensitivity. The provisions within this statement are separate and distinct from the guidance in SSAP No. 86, as the items subject to the scope of this guidance, and the provisions within, would not qualify for hedge effectiveness under SSAP No. 86. The provisions provided within this statement are only permitted if all of the components of the statement are met and shall not be inferred as an acceptable statutory accounting approach for derivative transactions that do not meet the stated qualifications or that are not specifically addressed within this guidance.

SUMMARY CONCLUSION

2. This statement establishes statutory accounting principles to address certain, limited derivative transactions hedging variable annuity guarantees subject to fluctuations as a result of interest rate sensitivity. Eligibility for the special accounting provision within this standard is strictly limited to variable annuity contracts and other contracts involving certain guaranteed benefits similar to those offered with

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variable annuities that are reserved for in accordance with Valuation Manual 21: Requirements for Principal-Based Reserves for Variable Annuities (VM-21)[1]. The statutory accounting guidance within this statement is considered a special accounting provision, only permitted if all the components in the standard are met, and shall not be inferred as an acceptable statutory accounting approach for situations that do not meet the stated qualifications or that are not specifically addressed within this guidance.

Terms/Concepts (for purposes of this statement)

3. The following terms reflect concepts specific to this statement. (This listing only details the key concepts. Specific guidelines are reflected throughout the guidance.)

a. Derivative Instrument: An agreement, option, instrument or series or combination thereof: (1) To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or (2) That has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests.

b. Dynamic Hedging Approach: A dynamic hedging strategy allows for the portfolio of derivatives comprising the hedging instrument to be rebalanced in accordance with changes to the hedged item in order to adhere to the specified, documented hedging strategy.

c. Hedged Item: The hedged item shall consist of declared guarantee benefits on a pool, or portion thereof, of variable annuity contracts exposed to interest rate risk. The hedged item may relate to an open or flexible portfolio (e.g., group of variable annuity contracts with different characteristics and liability durations) that allows for addition of newly issued contracts, subtraction of surrenders and fluctuations in balances. The portfolio of variable annuity contracts may consist of an entire book of business or declared components thereof.

d. Hedging Instrument: The hedging instrument shall reflect a specified derivative, or a portfolio of specified derivatives, that hedges the interest rate sensitivity of the designated hedged item. The hedging instrument may reflect a dynamic hedging strategy in which a portfolio of derivatives comprising the hedging instrument is rebalanced in accordance with changes to the hedged item.

Special Accounting Provision

4. The special accounting provision within this statement permits reporting entities to utilize a form of "macro-hedging" in which a portfolio of variable annuity policies, which could include the entire book of business or subsections thereof, are jointly designated as the host contracts containing the hedged item, in a fair value hedge[2], pursuant to a Clearly Defined Hedging Strategy (throughout this issue paper also referred to as "CDHS" or "hedging strategy"). This is considered a macro-hedge, as the designated hedged item (rate sensitive guarantee benefits) may be attached to a portfolio of variable annuity contracts with different characteristics and liability durations. Under this special accounting provision, the portfolio of contracts giving rise to the hedged item is not required to be static, but can be revised to remove policies and/or include new policies to allow for continuous risk management (hedging) of the variable annuity guarantees in accordance with the specific risks being hedged and the hedge objectives of the specified, documented hedging strategy. In designating the hedged item, reporting entities are permitted to exclude specific components of the variable annuity contracts, but such exclusions must apply collectively to all

[1] Actuarial Guideline XLIII, CARVM for Variable Annuities (AG 43) shall apply in states that have not adopted the Valuation Manual.

[2] As detailed in paragraph 10, these hedges are required to be highly effective in achieving offsetting changes in fair value attributed to the hedged risk between the derivative hedging instruments and the hedged item during the period that the hedge is designated.

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policies included within the portfolio. For example, reporting entities may elect to only hedge the interest rate risk of rider cash flows, and if making this election, would define the hedged item as the "fair value of rider claims net of rider fees" for the portfolio of policies designated as giving rise to the hedged item.

5. This special accounting provision permits reporting entities to utilize a specified derivative, or a portfolio of specified derivatives, as the hedging instrument within a fair value hedge to hedge the interest rate sensitivity, or a specific percentage[3] of the interest rate sensitivity, of the designated hedged item. The hedging instrument may reflect a dynamic hedging strategy in which a portfolio of derivatives comprising the hedging instrument is rebalanced in accordance with changes to the hedged item in order to adhere to the specified, documented hedging strategy. Although the hedging instruments must address interest rate risk, this guidance does not preclude use of derivative instruments that may offset risks other than interest rate risk from being designated as the hedging instruments. For derivative instruments that are affected by multiple risk factors, including interest rate risk, reporting entities shall apply this special accounting treatment to the change in fair value due to interest rate risk. Reporting entities shall bifurcate the change in fair value due to the various risk factors - e.g., fair value volatility due to interest rates (rho), and other risk factors, such as equity level (delta) or volatility (vega). Pursuant to paragraphs 10 and 13, fair value fluctuations not attributed to the hedged risk, including fair value changes from excluded open components, shall be recognized as unrealized gains or losses.

6. With the provisions in this standard to allow for flexibility in the hedged item (changes to variable annuity contracts within a portfolio) coupled with a dynamic hedging approach (rebalancing of derivative hedging instruments), there is a greater risk of misrepresentation of successful risk management and achievement of a highly effective hedging relationship. Although this risk cannot be eliminated, the following provisions intend to ensure governance of the program and provide sufficient tools to allow for regulator review:

a. Prior to implementing a hedging program for application within scope of this standard, the reporting entity must obtain explicit approval from the domiciliary state commissioner allowing use of this special accounting provision. The domiciliary state commissioner may subsequently disallow use of this special accounting provision at their discretion. Although this guidance does not restrict the state domiciliary commissioner on when to prohibit future use, disallowance should be considered upon finding that the reporting entity's documentation, controls, measurement, prior execution of strategy or historical results are not adequate to support future use.

b. Actuarial certifications of VM-21 reserves, consistent with Valuation Manual requirements, which explicitly include the following:

i. Certification as to whether the hedging strategy is incorporated within the establishment of VM-21 reserves, and the impact of the hedging strategy within the VM-21 Conditional Tail Expectation Amount.

ii. Certification by a financial officer of the company (CFO, treasurer, CIO, or designated person with authority over the actual trading of assets and derivatives) that the hedging strategy meets the definition of a Clearly Defined Hedging Strategy within VM-21 and that the Clearly Defined Hedging Strategy is the hedging strategy being used by the company in its actual day-to-day risk mitigation efforts. This provision does not require reporting entities to use a hedging strategy in determining VM-21 reserves, nor does it require entities to use the special accounting provision within this standard. However, it does require reporting entities that use the special accounting provisions within this standard to certify

[3] In identifying the hedged risk, reporting entities must identify whether they are hedging the full, or a portion of (e.g., 40%), the interest rate sensitivity.

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that the hedging strategy within scope of this standard is a Clearly Defined Hedging Strategy and is reflected in the establishment of VM-21 reserves.

7. As identified in paragraph 2, eligibility for the special accounting provision within this standard is strictly limited to variable annuity contracts and other contracts involving certain guaranteed benefits similar to those offered with variable annuities that are reserved for in accordance with VM-21. This special accounting provision requires the reporting entity to engage in highly effective fair value hedges that follow a Clearly Defined Hedging Strategy, as defined in VM-21, meeting all required provisions of VM-21 allowing the reporting entity to reduce the amount of the Conditional Tail Expectation (CTE) Amount. In order to qualify as a Clearly Defined Hedging Strategy (which may be dynamic, static, or a combination thereof), the strategy must meet the principles outlined in VM-21, be in place (implemented) for at least three months[4], and shall at a minimum, identify:

a. Specific risks being hedged[5],

b. Hedge objectives,

c. Risks not being hedged,

d. Financial instruments that will be used to hedge the risks,

e. Hedge trading rules, including permitted tolerances from hedging objectives,

f. Metric(s) used for measuring hedging effectiveness,

g. Criteria that will be used to measure effectiveness,

h. Frequency of measuring hedging effectiveness,

i. Conditions under which hedging will not take place, and

j. The individuals responsible for implementing the hedging strategy.

8. While an initially documented hedging strategy may subsequently change, any change in hedging strategy, which includes a change in hedge target, shall be documented, with notification to the domiciliary state commissioner, and include an effective date of the change in strategy. Reporting entities that elect to change a documented hedging strategy prior to the end of the three-month minimum implementation timeframe shall identify the hedging strategy, and all hedging instruments executed under the strategy, as ineffective. The three-month timeframe begins with the stated effective date of the hedging strategy regardless if any hedging instruments have been executed under the hedging strategy. Changes in a documented hedging strategy that occur after the three-month implementation timeframe do not necessitate an ineffective determination as long as hedged items and hedging instruments under the revised/new strategy continue to meet the requirements of a highly effective fair value hedge. Reporting entities are permitted to have more than one hedging strategy implemented, but all implemented strategies must qualify as a component of a Clearly Defined Hedging Strategy pursuant to paragraph 7.

[4] As detailed in VM-21, before a new or revised hedging strategy can be used to reduce the amount of the Conditional Tail Expectation (CTE) otherwise calculated, the hedging strategy should be in place (effectively implemented) for at least three months. As detailed in VM-21, the reporting entity may meet the time requirement by having evaluated the effective implementation of the hedging strategy for at least three months without actually having executed the trades indicated by the hedging strategy (e.g., mock testing or by having effectively implemented the strategy with similar annuity products for at least three months.)

[5] The specific risk being hedged shall include a measure of the hedge coverage (e.g., percentage of interest rate sensitivity being hedged).

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Assessing Hedge Effectiveness

9. The provisions within this standard require the entity to use a specific method, as detailed in paragraph 10, to assess hedge effectiveness at inception and on an ongoing basis. At a minimum, hedge effectiveness assessment is required whenever financial statements are reported, at least every three months. Documentation requires prospective and retrospective[6] hedge effectiveness assessments, with on-going assessment consistent with the originally documented risk management strategy.

10. Both at inception, and on an ongoing basis, the hedging relationship must be highly effective in achieving offsetting changes in fair value attributed to the hedged risk during the period that the hedge is designated. Reporting entities electing to use this special accounting provision must calculate the fair value of the hedged item at inception and on an ongoing basis, and compare the fair value change of the hedged item to the fair value change of the hedging instruments in assessing whether the relationship is highly effective on a cumulative basis. This comparison is specific to the designated hedged risks and exposures, therefore, if only a portion of the interest rate risk is hedged or if the designated hedge only include specific components of the variable annuity policies (e.g., riders), for determining hedge effectiveness, the fair value comparisons is limited to those designated items. If an entity's defined risk management strategy for a particular hedging relationship excludes specific components of the hedging derivative from the assessment of hedge effectiveness, the excluded open components shall be reported at fair value with gains or losses recognized as unrealized gains or losses.

11. The term "highly effective" describes a fair value hedging relationship where the change in fair value of the derivative instrument is within 80% to 125% ~~percent~~ of the opposite change in fair value of the hedged item attributed to the hedged risk. It shall also apply when an R-squared of .80 or higher is achieved when using a regression analysis technique.

Measurement/Recognition of Gains and Losses of Outstanding (Open) Instruments

12. All designated hedging instruments (all derivatives, including those reflected in portfolios) shall be reported in the financial statements at fair value.

13. Fair value fluctuations in the measurement of outstanding (non-expired) derivatives within a highly effective hedging strategy shall be reflected as follows:

a. Fair value fluctuations in the hedging instruments attributable to the hedged risk that offset the current period change in the designated portion of the VM-21 reserve liability[7] shall be recognized as a realized[8] gain or loss.

[6] For situations in which there has been a change in hedging strategy pursuant to paragraph 8, when conducting retrospective hedge effectiveness assessments, reporting entities shall assess effectiveness based on the hedge target that was actually in effect during the retrospective time periods.

[7] Hedge effectiveness is determined by comparing fair value fluctuations between the hedging instruments and the hedged item. However, in determining recognition in the financial statements, the fair value fluctuation of the hedging instruments is compared to the change in the reported value of the designated portion of the VM-21 liability. The designated portion of the VM-21 liability is not reported at fair value in the statutory financial statements, as such, the offset reported as realized gains and losses is the portion of the fair value change in hedging instruments offset by the change in the reported value of the designated portion of the VM-21 reserve. In accordance with the documented hedging strategy, reporting entities shall compare the fair value fluctuations to the change in the designated portion of the reserve liability, after considering recognized derivative returns (including recognized derivative income), when determining the recognition of fair value fluctuations.

[8] Recognizing the fair value change for open derivative positions that offset the VM-21 change as a realized gain/loss (instead of an unrealized gain or loss) directly offsets the VM-21 reserve change in the income statement.

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b. Fair value fluctuations in the hedging instruments attributable to the hedged risk[9] that do not offset the current period change in the designated portion of the VM-21 reserve liability shall be recognized as deferred assets (admitted) and deferred liabilities. The ability to recognize a deferred asset and deferred liability is limited to only the portion of the fair value fluctuation in the hedging instruments that is attributed to the hedged risk and does not immediately offset changes in the designated portion of the VM-21 reserve liability.

c. An amount equal to the net deferred asset and deferred liability (net amount from all hedging strategies/programs captured within this guidance) shall be allocated from unassigned funds to special surplus. Upon domestic regulator request, reporting entities shall provide estimations of RBC as if the special accounting provisions had not been applied. This estimation shall reflect the removal of deferred assets or deferred liabilities and reflect the impact to unassigned funds as if the derivative gains and losses had been recognized.

d. As detailed in paragraph 10, fair value fluctuations in the hedging instruments that are not attributable to the hedged risk, shall be recognized as unrealized gains or unrealized losses.

e. Reporting entities shall utilize the following calculation for establishing the deferred asset (also illustrated in Exhibit A) unless a different method has been approved by the domiciliary state commissioner:

i. Calculate the fair value gain or loss in the hedged item attributable to the hedged risk.

ii. Express the quantity calculated in paragraph 13.e.i. as a percentage of the change in the full-contract fair value (i.e., with all product cash flows) attributed to interest rate movements[10].

iii. Calculate the VM-21 liability change attributed to the hedged risk as the quantity calculated in paragraph 13.e.ii. multiplied by the VM-21 liability change attributable to interest rate.

iv. Establish the deferred asset or deferred liability in the amount of the fair value loss or (gain) of the designated hedging instruments attributed to the hedged risk less the VM-21 liability decrease or (increase) attributed to the hedged risk as calculated in paragraph 13.e.iii.

v. Allocate an amount equal to the net deferred asset and deferred liability (net amount from all hedging strategies/programs captured within this guidance) to special surplus.

[9] The change in fair value of the hedging instruments and hedged item is limited to changes driven by market factors. For example, periodic recognition of a cost owed to acquire the derivative from a counterparty (financing cost) shall not be captured as a change in the derivative instrument's fair value. The fair value of the instrument shall be determined based on the underlying derivative without inclusion of acquisition costs (or other such contractual elements that may exist with the counterparty) that do not change based on the underlying derivative interests or market factors.

[10] The result of this calculation (the coverage ratio) should not exceed 100% nor drop below zero.

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14. Deferred assets and deferred liabilities recognized under paragraph 13.b. shall be amortized using a straight-line method into realized gains or realized losses over a finite amortization period. The amortization timeframe shall equal the Macaulay duration of the guarantee benefit cash flows based on the VM-21 Standard Projection[11], but shall not exceed a period of 10 years.

a. Future recognition of deferred assets or liabilities (fair value fluctuations attributed to the hedged risk that are not offset by the reserve liability change) do not extend the amortization timeframe for previously recognized deferred assets or deferred liabilities. Reporting entities are required to separately track, with a schedule to show the initial deferred amount and amortization schedule, of the deferred assets and deferred liabilities recognized and outstanding at each reporting date.

b. The amount reported on the financial statement at each reporting date shall reflect the net amount (net as either a deferred asset or deferred liability) for each hedging strategy captured within scope of this guidance. (Reporting entities that have more than one hedging strategy could have both deferred assets and deferred liabilities in the financial statements based on the net position of the separate hedging strategies.)

c. Reporting entities are permitted to amortize a greater portion of the deferred assets and/or deferred liabilities into realized gains or realized losses at any time in advance of the scheduled amortization period.

i. If electing to accelerate amortization, reporting entities are required to accelerate amortization equally between deferred assets and deferred liabilities within a single hedging strategy. For example, a reporting entity is not permitted to accelerate amortization of the deferred liabilities (recognizing the gains from fair value changes) and not accelerate amortization of the deferred assets (continuing to defer losses from fair value changes). If a reporting entity only has a single hedging strategy which only reflects deferred assets or deferred liabilities, the reporting entity is permitted to accelerate amortization without restrictions.

ii. If a reporting entity has more than one hedging strategy, and the strategies have offsetting net positions (both deferred assets and deferred liabilities are recognized in the financial statements), a reporting entity's election to accelerate amortization must be applied equally to programs with offsetting net positions. (For example, a decision to accelerate amortization of a program with a net deferred liability must be applied equally to a program with a deferred asset that best corresponds to the deferred liability[12].) In these situations, the guidance in paragraph 14.c.i. is also applicable, whereas, the accelerated amortization must also apply equally to the deferred assets and deferred liabilities within each individual hedging program. If a reporting entity with more than one hedging strategy only has net deferred assets or net deferred liabilities recognized, the reporting entity is permitted to accelerate

[11] The VM-21 Standard Projection benefit cash flows shall be based on the prescribed assumptions run for the scenario that produces the scenario reserve closest to conditional tail expectation (CTE) 70 (adjusted). The VM-21 Standard Projection with prescribed assumptions run is determined using the method (company specific market path (CSMP) or conditional tail expectations with prescribed assumptions (CTEPA)) applied by the reporting entity to calculate the prescribed projections amount. For the CSMP method, the economic scenario is Path A, with the guarantee benefit cash flows from the run to calculate Prescribed Amount A. For the CTEPA method, the economic scenario is the scenario that produces the scenario reserve closest to the CTE70 (adjusted) from the stochastic reserve calculation, with the guarantee benefit cash flows from the VM-21 Standard Projection with prescribed assumptions run for this economic scenario. The discount rate for the Macaulay duration calculation shall be equal to the valuation interest rate specified by the Standard Valuation Law for annuities valued on an issue year basis, using Plan Type A and a Guarantee Duration greater than 10 years but not more than 20 years.

[12] The intent of this guidance is to ensure that the ability to accelerate amortization does not result with elections that simply result in favorable financial statement presentation.

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amortization to a single program in a manner consistent with the guidelines in paragraphs 14.c.i.

15. For outstanding (non-expired) derivative instruments that were removed from a highly effective hedging strategy (rebalanced), subsequent gains and losses from fair value fluctuations shall not impact the previously recognized deferred assets or deferred liabilities. The deferred assets and deferred liabilities for these derivative instruments shall be "locked" and amortized under the remaining schedule unless the reporting entity elects to terminate or accelerate amortization. Subsequent to the removal from a highly effective strategy, all fair value fluctuations from the outstanding derivative instruments would be subject to the guidance in SSAP No. 86, and recognized as unrealized gains and/or unrealized losses. If the derivative is re-designated as part of a highly effective hedging strategy qualifying under this standard, subsequent fair value fluctuations (after the re-designation) may be accounted for under the special accounting provision detailed in this statement.

16. For outstanding (non-expired) derivative instruments in a hedging strategy that no longer qualifies within scope of this standard (e.g., VM-21 requirements are not met) or is no longer a highly effective hedge, any non-amortized deferred assets or deferred liabilities shall be amortized to unrealized gains or unrealized losses over the remaining amortization timeframe, not to exceed five-years. If the deferred assets/deferred liabilities have a remaining amortization period that is less than the shortened timeframe, amortization shall continue over the remaining period. If the remaining amortization period is greater than 5-years at the time of the program no longer qualifies, or is no longer highly effective, the amortization schedule shall be revised to require full amortization within the shortened 5-year timeframe. If elected by the reporting entity, deferred assets and deferred liabilities may be immediately recognized as unrealized gains and/or unrealized losses or have accelerated amortization (less than 5-years) as unrealized gains and/or unrealized losses. (An election to immediate eliminate or accelerate amortization must follow the provisions in paragraph 14.c.) All future fair value fluctuations for these derivative instruments would be subject to the guidance in SSAP No. 86, and shall be recognized as unrealized gains or unrealized losses unless the instrument is subsequently designated as part of a highly effective hedging strategy within scope of this statement. If the derivative is re-designated as part of a highly effective hedging strategy qualifying under this standard, subsequent fair value fluctuations (after the re-designation) may be accounted for under the special accounting provision detailed in this statement.

17. Reporting entities may elect to terminate use of this special accounting provision at any time. In those instances, if the derivative instruments are outstanding, all deferred assets and deferred liabilities shall be amortized to unrealized gains or unrealized losses over the remaining amortization timeframe, not to exceed five-years. If the deferred assets/deferred liabilities have an amortization period that is less than the shortened 5-year timeframe, amortization shall continue over the established period. If the remaining amortization period is greater than 5-years at the time of termination, the amortization schedule shall be revised to require full amortization within the shortened 5-year timeframe. If elected by the reporting entity, deferred assets and deferred liabilities may be immediately eliminated or have accelerated amortization (less than 5-years) with recognition as unrealized gains and/or unrealized losses. (An election to immediate eliminate or accelerate amortization must follow the provisions in paragraph 14.c.) Once the special accounting provision is terminated, unless re-designated by the reporting entity, subsequent accounting of the derivatives in a hedging strategy that would be captured within this statement shall follow the fair value accounting approach in SSAP No. 86[13].

Measurement/Recognition of Realized Gains or Losses of Expired Derivatives

18. With the ability to rebalance the hedging instrument, this guidance allows for individual derivative instruments to expire and/or be removed from the portfolio of the hedging instrument, and not immediately

[13] Macro-hedges and the ability to rebalance hedging instruments are not provisions permitted within "effective" hedges in scope of SSAP No. 86. As such, hedging strategies with these components accounted for under SSAP No. 86 shall follow the fair value accounting approach detailed in that standard.

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trigger an assessment that the overall hedging strategy is no longer highly effective. Furthermore, special allowances are included to consider the tenure differences between a hedging instrument and VM-21 liability duration. These allowances permit expired[14] derivative instruments that were part of a highly effective hedging strategy at the time of expiration to continue amortizing the deferred gains and deferred losses over the previously established amortization timeframe even if the overall hedging strategy is subsequently terminated or subsequently identified as no longer qualifying as a highly effective hedge.

19. Pursuant to the provisions in paragraph 14.c., reporting entities are permitted to amortize a greater portion of the deferred assets and/or deferred liabilities from expired derivatives into realized gains or realized losses in advance of the scheduled amortization period.

20. Consistent with the guidance in paragraph 17, reporting entities may elect to terminate use of this special accounting provision at any time. In those instances, if the derivative instruments have expired, all deferred assets and deferred liabilities shall be amortized to realized gains or realized losses over the remaining amortization timeframe, not to exceed 5-years. If the deferred assets/deferred liabilities had an amortization period that was less than the shortened timeframe, amortization shall continue over the established period. If the amortization period was greater than 5-years at the time of termination, the amortization schedule would be revised to require full amortization within the shortened timeframe. If elected by the reporting entity, the deferred assets and deferred liabilities may be immediately eliminated, or have accelerated amortization, with recognition as realized gains and/or realized losses. An election to immediate eliminate or accelerate amortization (less than 5 years) must follow the provisions in paragraph 14.c.)

Derivative Income

21. Derivative income shall be recognized when earned.

22. Pursuant to the documented hedging strategy as a fair value hedge, derivative income shall be considered as part of the overall hedging strategy and included in the assessments on whether the strategy is highly effective.

Disclosures

23. A reporting entity that has any outstanding derivatives accounted for under this special accounting provision, or that has unamortized deferred assets and/or deferred liabilities (representing previously unrecognized qualifying fair value fluctuations) from expired derivatives under the special accounting provision shall disclose the following within the financial statements:

a. Discussion of hedged item, including information on the guarantees sensitive to interest rate risk, along with information on the designated hedging instruments being used to hedge the risk. Discussion of the hedging instruments shall identify whether a hedging instrument is a single instrument or portfolio, as well as information on the hedging strategy (including whether there have been changes in strategy from the prior reporting period, along with detailed information on the changes), and assessment of hedging effectiveness and compliance with the "Clearly Defined Hedging Strategy" of VM-21. Identification shall occur on whether the hedged item is intended to be fully hedged under the hedging strategy, or if the strategy is only focused on a portion of the liability characteristics or a portion of the interest rate sensitivity. Hedging strategies shall be identified as highly effective or not highly effective. If the strategy for a particular hedging relationship excludes a specific component of the gain or loss, or related cash flows, from the assessment of hedge effectiveness, details on the excluded components shall be disclosed.

[14] Throughout this standard the use of the word "expire" is intended to capture all instances in which the derivative is no longer outstanding. It includes maturities, terminations, sales, and/or other closing transactions of a derivative.

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b. Aggregate disclosure of the original cost and fair value of hedging instruments (including all instruments within a portfolio), including any net investment income, realized and unrealized gains and losses during the reporting period. Additionally, disclose the fair value of the hedged item, the change in fair value from the prior reporting period, and the portion of the fair value change attributed to the hedged risk.

c. Schedule showing the aggregate fair value change from the prior reporting period for the designated components for all hedging instruments, with identification of the fair value change reflected in realized gains, realized losses, deferred assets, and deferred liabilities. This schedule shall also show the current period amortization, including any accelerated amortization elected by the reporting entity, and the future scheduled amortization of the deferred assets and deferred liabilities. This schedule shall identify the fair value of the excluded components of the hedging instruments, and the fair value change for those components reflected in unrealized gain and unrealized loss.

d. For hedging strategies no longer identified as highly effective previously captured within scope of this standard, information on the determination of ineffectiveness, including variations from prior assessments resulting in the change from classification as a highly effective hedge. This disclosure shall also include:

i. Identification of outstanding hedging instruments previously captured within scope of this standard and subsequently identified as no longer part of a highly effective hedging strategy. This disclosure shall identify the date in which the domiciliary state was notified that the hedging strategy had been identified by the reporting entity as no longer highly effective.

ii. Deferred assets and deferred liabilities previously recognized when the program was highly effective, with a schedule that shows the amortization that would have occurred if the program had remained highly effective, the amount of original amortization as well as a schedule that details the amortization that will occur as the program is no longer highly effective (maximum five-year timeframe).

iii. Disclosure on whether the reporting entity is electing to accelerate amortization (in advance of the remaining scheduled amortization or the maximum five-year timeframe), along with amounts immediately recognized to unrealized gains/losses, and how the election impacts the scheduled amortization.

e. For situations in which the reporting entity has elected to terminate the hedging strategy and/or discontinue the special accounting provisions permitted within this SSAP, the reporting entity shall disclose the key elements in the reporting's entity' decision to terminate, identifying changes in the reporting entity's objectives or perspectives from initial application. This disclosure shall also include:

i. Identification of outstanding hedging instruments previously captured within scope of this standard and the accounting impact as a result of the termination/discontinuation. (Open derivative transactions no longer captured within the special accounting provision would be subject to the accounting and reporting guidance within SSAP No. 86.) This disclosure shall identify the date in which the domiciliary state was notified that the hedging strategy or the election to use the special accounting provision in this SSAP had been terminated.

ii. Deferred assets and deferred liabilities previously recognized under the hedging strategy and/or program, with a schedule that shows the amortization that would have occurred if the strategy and/or program had remained highly effective, as well

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as a schedule that details the amortization that will occur with the termination of the strategy and/or program (maximum five-year timeframe).

iii. Disclosure on whether the reporting entity is electing to accelerate amortization (in advance of the remaining scheduled amortization or the maximum five-year timeframe), along with amounts immediately recognized to unrealized gains/losses, and the resulting impact to the scheduled amortization.

Effective Date and Transition

24. This statement is effective January 1, 2020, with early adoption permitted January 1, 2019. The guidance in this SSAP is required to be applied on a prospective basis for qualifying hedge programs in place on or after the effective date. This prospective application prohibits deferred asset and deferred liability recognition from fair value fluctuations previously recognized as unrealized gains or losses that occurred prior to the effective date of the guidance.

25. Reporting entities that have previously received permitted or prescribed practices for qualifying hedge programs, resulting with the recognition of deferred assets/deferred liabilities from unrecognized fair value fluctuations, shall work with their domiciliary state regulator to determine the appropriate method in transitioning from previously approved permitted practices. The reporting entity shall include disclosure of the transition approach approved by the domiciliary state in their financial statements in the first year of application. The approved transition approach is not considered a permitted practice as long as the reporting entity is fully compliant with the provisions of this statement after implementation. After the effective date of this statement, domiciliary state provisions that differ from this statement must be disclosed as a permitted or prescribed practice pursuant to *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures*.

REFERENCES

RELEVANT ISSUE PAPERS

- *Issue Paper No. 159—Special Accounting Treatment for Limited Derivatives*

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EXHIBIT A – CALCULATION OF DEFERRED ASSET OR DEFERRED LIABILITY

Under the special accounting provisions within this issue paper, as detailed in paragraph 13.e., fair value fluctuations in the hedging instruments attributable to the hedged risk that do not offset the current period change in the hedged item (the change in the VM-21 reserve liability) can be recognized as deferred assets (admitted) and deferred liabilities.

The ability to recognize a deferred asset and deferred liability is limited to only the portion of the fair value fluctuation in the hedging instruments that is attributed to the hedged risk and does not immediately offset changes in the hedged item. As detailed in the standard, the hedged risk may be designated as a specific component of the hedged item. For example, if the variable annuity reserve benefits are matched to bonds, the hedged risk could only be the portion of interest rate risk remaining after the natural hedge based on the asset-liability matching.

Unless a different method has been approved by the domiciliary state commissioner, reporting entities shall utilize the following calculation (detailed in paragraph 13) for establishing the deferred asset:

13.e.i. Calculate the fair value gain or loss in the hedged item attributable to the hedged risk (Step 1);

13.e.ii. Express the fair value gain or loss calculated (Step 1) as a percentage of the change in the full-contract fair value (i.e., with all product cash flows) attributed to interest rate movements (Step 2)[15].

13.e.iii. Calculate the VM-21 liability change attributed to the hedged risk as the quantity calculated in Step 2 multiplied by the VM-21 liability change attributable to interest rate (Step 3).

13.e.iv. Establish the deferred asset or deferred liability in the amount of the fair value loss or (gain) of the designated hedging instruments attributed to the hedged risk less the VM-21 liability decrease or (increase) attributed to the hedged risk as calculated in Step 3.

13.e.v. Allocate an amount equal to the net deferred asset and deferred liability (net amount from all hedging strategies/programs captured within this guidance) to special surplus.

To illustrate the above calculation:

Clearly Defined Hedging Strategy (CDHS) characteristics

Hedged item	Rider claims less rider fees
Hedged risk	50% of the rho (first-order IR level sensitivity)

Calculation of the deferred asset or liability

Note: positive values = increase in liability

Fair value gain (loss) in hedged item attributable to interest rate movement	(500)
13.e.i. – Fair value gain (loss) in hedged item attributable to hedged risk	(250)

[15] The result of this calculation (the coverage ratio) should not exceed 100% nor drop below zero.

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Hence, if the insurer were hedging per the CDHS perfectly, then the insurer should see a 250 fair value loss in the designated IR hedge instruments. To determine how much of that loss should be deferred:

Fair value gain (loss) in full-contract cash flows attributable to IR movement	(700)
13.e.ii. – Quantity calculated in 13.b.i. as a % of the (700) above	36%

VM-21 liability increase (decrease) from beginning of period to end of period	400
VM-21 liability increase (decrease) attributable to interest rate movements	(100)
13.e.iii. – VM-21 liability increase (decrease) attributable to the hedged risk	(36)

In this example, even though the VM-21 liability increased by 400 during the reporting period, interest rate movements actually contributed to a 100 *decrease*. The hedged risk (50% of the interest rate sensitivity of rider cash flows) accounts for 36% of this, or $36 of the liability decrease. As such, $36 of the fair value loss on the interest rate hedge instruments should be reflected immediately and the remainder deferred via a deferred asset equal in amount to 250 – 36 = 214.

13.e.iv. – Deferred asset (13.b.i less 13.b.iii) attributable to hedged risk	**(214)**

(This is shown as a negative – to be consistent with the decrease in VM-21 liability – but represents a deferred asset. Deferred assets reflect fair value losses.)

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GLOSSARY to the Statements of Statutory Accounting Principles

The terms in this Glossary are common in most SSAPs. Some SSAPs may have terminology that is topic-specific and not intended to be applied to other topics.

Adjusted Carrying Value – Carrying value amount adjusted to remove any accrued interest and to add back any of the following amounts: individual nonadmitted amounts, individual valuation allowances (if applicable), and aggregate valuation allowance (if applicable). In effect, this is equivalent to the SAP Book Value. (Not to be confused with the old "book value" reported in the annual statement blanks for data years 2000 and prior.)

Amortized Cost – See SAP Book Value.

Call Provision – Option to buy an asset at a specified price within a specified period. (Also applicable to Call and Call Option.)

Capitation Arrangement – A compensation plan used in connection with some managed care contracts in which a physician or other medical provider is paid a flat amount, usually on a monthly basis, for each subscriber who has elected to use that physician or medical provider.

Credit Rating Provider – CRP stands for Credit Rating Provider and refers to the nationally recognized statistical rating organizations (NRSROs) on the NAIC Credit Rating Provider List discussed in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*.

Deferred Tax Asset – The deferred tax consequences attributable to deductible temporary differences and carryforwards. A deferred tax asset is measured using the applicable enacted tax rate and provisions of the enacted tax law. Deferred tax assets are subject to the admissibility criteria as outlined in *SSAP No. 101—Income Taxes*, paragraph 11.

Deferred Tax Liability – The deferred tax consequences attributable to taxable temporary differences. A deferred tax liability is measured using the applicable enacted tax rate and provisions of the enacted tax law.

Equity Method – Accounting valuation approach used in which the initial investment is adjusted in accordance with the ownership of another entity. Guidance for using the equity method, and for determining adjustments to the investment under the equity method is detailed in *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* (SSAP No. 48) and *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* (SSAP No. 97).

Fair Value – Fair value is defined in *SSAP No. 100R—Fair Value.*

Guaranteed Investment Contract or Guaranteed Interest Contract (GIC) – An insurer-issued funding vehicle, typically issued to retirement plans, under which the insurer accepts a deposit (or, less frequently, a series of deposits) from the purchaser and guarantees to pay a specified interest rate of return on the funds deposited during a specified period of time.

Morbidity Risk – The potential for a person to experience illness, injury, or other physical or psychological impairment, whether temporary or permanent. Morbidity risk excludes the potential for an individual's death, but includes the potential for an illness or injury that results in death.

Mortality Risk – The potential for loss of life, with respect to a specified person or group of people. For reverse mortgages (SSAP No. 39), mortality risk is defined as the risk of loan payments extending beyond the borrower's original projected life expectancy.

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Nonforfeiture – The principle that some types of insurance contract have an economic value to which the contract owner is entitled even upon lapsation or surrender of the contract. A *nonforfeiture value* is the economic value that must be provided to the contract owner upon lapsation or surrender; it can take various forms, such as a lump-sum cash payment, an amount of paid-up insurance, an amount of term insurance, etc.

Nonoperating System Software – Application systems software such as language processors, library routines and debugging aides and other computer software are not considered operating system software.

Operating System Software – The operating system is a program or a series of programs controlling the data job and task management operations of a computer or a computer network through executive scheduling and monitoring. It increases the productivity of a computer installation by managing the allocation of all available computer resources including the control processing unit, main storage and input/output devices.

Original Cost – See SAP Book Value.

Par Value – The nominal (or face value) of a stock or bond.

Recorded Investment – The SAP Book Value (Adjusted Carrying Value) plus Accrued Interest.

SAP Book Value – Original cost, including capitalized acquisition costs and accumulated depreciation, unamortized premium and discount, deferred origination and commitment fees, direct write-downs, and increase/decrease by adjustment.

SAP Carrying Value (Amount) – The SAP book value plus accrued interest and reduced by any valuation allowance (if applicable) and any nonadmitted adjustment applied to the individual investment. Carrying value is used in the determination of impairment.

Statement Value – The SAP book value reduced by any valuation allowance and nonadmitted adjustment applied to an individual investment or a similar group of investments, e.g., bonds, mortgage loans, common stock.

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Appendix A
Excerpts of NAIC Model Laws

Introduction

The following appendices are an integral part of the NAIC *Accounting Practices and Procedures Manual*. The guidance herein is referred to by specific statements of statutory accounting principles (SSAPs).

Some appendices define certain terms. Such definitions are not intended to change the meaning of any terms used elsewhere in the NAIC *Accounting Practices and Procedures Manual* and should only be used in the context of the appendix in which it appears and the SSAP that refers to that appendix.

Certain appendices contain requirements regarding reserves, which are effective with new business written after the effective date of the related SSAP. Transition guidance is provided in the related SSAPs.

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Appendix A-001

Investments of Reporting Entities

Relevant SSAPs:
SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures
SSAP No. 21R—Other Admitted Assets
SSAP No. 83—Mezzanine Real Estate Loans

Introduction

Section 1. Reporting Requirements
Section 2. Investment Risk Interrogatories
Section 3. Summary Investment Schedule

Introduction

A reporting entity may acquire, hold or invest in investments or engage in investment practices as set forth in the laws and regulations of its domiciliary state. The disclosure required by this appendix is not intended to preempt such state authority. The financial information disclosed herein is intended solely for the use of state regulators for solvency analysis and should not be used for any other purpose.

Section 1. Reporting Requirements

The following reporting requirements apply to the provisions of this appendix:

1. Annual Statement – Section 3
2. Supplement to Annual Statement filed by April 1 – Section 2
3. Audited Statutory Financial Statements – Sections 2 and 3

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Section 2. Investment Risks Interrogatories

Of The..... Insurance Company
Address (City, State, Zip Code) .....
NAIC Group Code..... NAIC Company Code..... Employer's ID Number.....

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements.

Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement: $_____

2. Ten largest exposures to a single issuer/borrower/investment:

	1 Issuer	2 Description of Exposure	3 Amount	4 Percentage of Total Admitted Assets
2.01	.....	a.	$.....	.....%
2.02	.....	b.	$.....	.....%
2.03	.....	c.	$.....	.....%
2.04	.....	d.	$.....	.....%
2.05	.....	e.	$.....	.....%
2.06	.....	f.	$.....	.....%
2.07	.....	g.	$.....	.....%
2.08	.....	h.	$.....	.....%
2.09	.....	i.	$.....	.....%
2.10	.....	j.	$.....	.....%

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC designation:

	Bonds	1	2		**Preferred Stocks**	3	4
3.01	NAIC – 1	$.....	.....%	3.07	NAIC – 1	$.....	.....%
3.02	NAIC – 2	$.....	.....%	3.08	NAIC – 2	$.....	.....%
3.03	NAIC – 3	$.....	.....%	3.09	NAIC – 3	$.....	.....%
3.04	NAIC – 4	$.....	.....%	3.10	NAIC – 4	$.....	.....%
3.05	NAIC – 5	$.....	.....%	3.11	NAIC – 5	$.....	.....%
3.06	NAIC – 6	$.....	.....%	3.12	NAIC – 6	$.....	.....%

4. Assets held in foreign investments:

4.01	Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets?	Yes [ ] No [ ]	
	If response, to 4.01 above is yes, responses are not required for interrogatories 5 – 10.		
4.02	Total admitted assets held in foreign investments	$	..... %
4.03	Foreign-currency-denominated investments	$	..... %
4.04	Insurance liabilities denominated in that same foreign currency	$	..... %

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5. Aggregate foreign investment exposure categorized by NAIC sovereign designation:

		1	2
5.01	Countries designated NAIC – 1	$	..... %
5.02	Countries designated NAIC – 2	$	..... %
5.03	Countries designated NAIC – 3 or below	$	..... %

6. Two largest foreign investment exposures to a single country, categorized by the country's NAIC sovereign designation:

		1	2
	Countries designated NAIC – 1:		
6.01	Country:	$	..... %
6.02	Country:	$	..... %
	Countries designated NAIC – 2:		
6.03	Country:	$	..... %
6.04	Country:	$	..... %
	Countries designated NAIC – 3 or below:		
6.05	Country:	$	..... %
6.06	Country:	$	..... %

7. Aggregate unhedged foreign currency exposure: $..... ..... %

8. Aggregate unhedged foreign currency exposure categorized by NAIC sovereign designation:

		1	2
8.01	Countries designated NAIC – 1	$	..... %
8.02	Countries designated NAIC – 2	$	..... %
8.03	Countries designated NAIC – 3 or below	$	..... %

9. Two largest unhedged foreign currency exposures to a single country, categorized by the country's NAIC sovereign designation:

		1	2
	Countries designated NAIC – 1:		
9.01	Country:	$	..... %
9.02	Country:	$	..... %
	Countries designated NAIC – 2:		
9.03	Country:	$	..... %
9.04	Country:	$	..... %
	Countries designated NAIC – 3 or below:		
9.05	Country:	$	..... %
9.06	Country:	$	..... %

10. Ten largest non-sovereign (i.e., non-governmental) foreign issues:

	1 Issuer	2 NAIC Designation	3	4
10.01	.....	.....	$	..... %
10.02	.....	.....	$	..... %
10.03	.....	.....	$	..... %
10.04	.....	.....	$	..... %
10.05	.....	.....	$	..... %
10.06	.....	.....	$	..... %
10.07	.....	.....	$	..... %
10.08	.....	.....	$	..... %
10.09	.....	.....	$	..... %
10.10	.....	.....	$	..... %

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11. Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure:

11.01 Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11.

		1	2
11.02	Total admitted assets held in Canadian Investments	$.....	.....%
11.03	Canadian-currency-denominated investments	$.....	.....%
11.04	Canadian-denominated insurance liabilities	$.....	.....%
11.05	Unhedged Canadian currency exposure	$.....	.....%

12. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions:

12.01 Are assets held in investments with contractual sales restrictions less than 2.5% of the Reporting entity's total admitted assets. Yes [ ] No [ ]

If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12.

		1	2	3
12.02	Aggregate statement value of investments with contractual sales restrictions:		$	..... %
	Largest 3 investments with contractual sales restrictions:			
12.03	.....		$	..... %
12.04	.....		$	..... %
12.05	.....		$	..... %

13. Amounts and percentages of admitted assets held in the ten largest equity interests:

13.01 Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 13.01 is yes, responses are not required for the remainder of Interrogatory 13.

	1 Issuer	2	3
13.02	.....	$	..... %
13.03	.....	$	..... %
13.04	.....	$	..... %
13.05	.....	$	..... %
13.06	.....	$	..... %
13.07	.....	$	..... %
13.08	.....	$	..... %
13.09	.....	$.....	..... %
13.10	.....	$.....	..... %
13.11	.....	$	..... %

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14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:

14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14.

	1	2	3
14.02	Aggregate statement value of investments held in nonaffiliated, privately placed equities:	$	..... %
	Largest 3 investments held in nonaffiliated, privately placed equities:		
14.03	.....	$	..... %
14.04	.....	$	..... %
14.05	.....	$	..... %

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

	1	2	3
15.02	Aggregate statement value of investments held in general partnership interests:	$	..... %
	Largest 3 investments in general partnership interests:		
15.03	.....	$	..... %
15.04	.....	$	..... %
15.05	.....	$	..... %

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

	1 (Type (Residential, Commercial, Agricultural)	2	3
16.02	.....	$	..... %
16.03	.....	$	..... %
16.04	.....	$	..... %
16.05	.....	$	..... %
16.06	.....	$	..... %
16.07	.....	$	..... %
16.08	.....	$	..... %
16.09	.....	$	..... %
16.10	.....	$	..... %
16.11	.....	$	..... %

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Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

		Loans	
16.12	Construction loans	$	..... %
16.13	Mortgage loans over 90 days past due	$	..... %
16.14	Mortgage loans in the process of foreclosure	$	..... %
16.15	Mortgage loans foreclosed	$	..... %
16.16	Restructured mortgage loans	$	..... %

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

Loan-to-Value		Residential		Commercial		Agricultural	
		1	2	3	4	5	6
17.01	above 95%	$.....	..... %	$	..... %	$	..... %
17.02	91% to 95%	$.....	..... %	$	..... %	$	..... %
17.03	81% to 90%	$.....	..... %	$	..... %	$	..... %
17.04	71% to 80%	$.....	..... %	$	..... %	$	..... %
17.05	below 70%	$.....	..... %	$	..... %	$	..... %

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate:

18.01 Are assets held in real estate reported in less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate:

	Description		
	1	2	3
18.02	.....	$	..... %
18.03	.....	$	..... %
18.04	.....	$	..... %
18.05	.....	$	..... %
18.06	.....	$	..... %

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments held in mezzanine real estate loans:

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the Reporting entity's total admitted assets. Yes [ ] No [ ]

If response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

		1	2	3
19.02	Aggregate statement value of investments held in mezzanine real estate loans:	$	..... %	
	Largest 3 investments held in mezzanine real estate loans:			
19.03	.....	$	..... %	
19.04	.....	$	..... %	
19.05	.....	$	..... %	

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20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

		At Year-end		At End of Each Quarter		
				1st Qtr	2nd Qtr	3rd Qtr
		1	2	3	4	5
20.01	Securities lending agreements (do not include assets held as collateral for such transactions)	$	..... %	$	$	$ .....
20.02	Repurchase agreements	$	..... %	$	$	$ .....
20.03	Reverse repurchase agreements	$	..... %	$	$	$ .....
20.04	Dollar repurchase agreements	$	..... %	$	$	$ .....
20.05	Dollar reverse repurchase agreements	$	..... %	$	$	$ .....

21. Amounts and percentages of the reporting entity's total admitted assets for warrants not attached to other financial instruments, options, caps, and floors:

		Owned		Written	
		1	2	3	4
21.01	Hedging	$	..... %	$	..... %
21.02	Income generation	$	..... %	$	..... %
21.03	Other	$	..... %	$	..... %

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

		At Year-end		At End of Each Quarter		
				1st Qtr	2nd Qtr	3rd Qtr
		1	2	3	4	5
22.01	Hedging	$	..... %	$	$	$ .....
22.02	Income generation	$	..... %	$	$	$ .....
22.03	Replications	$	..... %	$	$	$ .....
22.04	Other	$	..... %	$	$	$ .....

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

		At Year-end		At End of Each Quarter		
				1st Qtr	2nd Qtr	3rd Qtr
		1	2	3	4	5
23.01	Hedging	$	..... %	$	$	$ .....
23.02	Income generation	$	..... %	$	$	$ .....
23.03	Replications	$	..... %	$	$	$ .....
23.04	Other	$	..... %	$	$	$ .....

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Section 3. Summary Investment Schedule (Revised for reporting periods effective January 1, 2019)

	Gross Investment Holdings		Admitted Assets as Reported in the Annual Statement			
	1	2	3	4	5	6
Investment Categories	Amount	Percentage	Amount	Securities Lending Reinvested Collateral Amount	Total (Col. 3+4) Amount	Percentage
1. Bonds (Schedule D, Part 1)						
1.1 U.S. Governments	.....	.....	.....	.....	.....	.....
1.2 All Other Government	.....	.....	.....	.....	.....	.....
1.3 U.S. States, Territories and Possessions, etc., Guaranteed	.....	.....	.....	.....	.....	.....
1.4 U.S. Political Subdivisions of States, Territories and Possessions, Guaranteed	.....	.....	.....	.....	.....	.....
1.5 U.S. Special Revenue & Special Assessment Obligations, etc., Non-Guaranteed	.....	.....	.....	.....	.....	.....
1.6 Industrial and Miscellaneous	.....	.....	.....	.....	.....	.....
1.7 Hybrid Securities	.....	.....	.....	.....	.....	.....
1.8 Parent, Subsidiaries and Affiliates	.....	.....	.....	.....	.....	.....
1.9 SVO Identified Funds	.....	.....	.....	.....	.....	.....
1.10 Bank Loans	.....	.....	.....	.....	.....	.....
1.11 Total Long-Term Bonds	.....	.....	.....	.....	.....	.....
2. Preferred Stock (Schedule D, part 2, Section 1)						
2.1 Industrial and Miscellaneous (Unaffiliated)	.....	.....	.....	.....	.....	.....
2.2 Parent Subsidiaries and Affiliates	.....	.....	.....	.....	.....	.....
3. Common Stocks (Schedule D, Part 2, Section 2)						
3.1 Industrial and Miscellaneous (Unaffiliated) Publicly Traded	.....	.....	.....	.....	.....	.....
3.2 Industrial and Miscellaneous (Unaffiliated) Other	.....	.....	.....	.....	.....	.....
3.3 Parent, Subsidiaries and Affiliates Publicly Traded	.....	.....	.....	.....	.....	.....
3.4 Parent, Subsidiaries and Affiliates Other	.....	.....	.....	.....	.....	.....
3.5 Mutual Funds	.....	.....	.....	.....	.....	.....
3.6 Total Common Stocks	.....	.....	.....	.....	.....	.....
4. Mortgage Loans (Schedule B)						
4.1 Farm Mortgages	.....	.....	.....	.....	.....	.....
4.2 Residential Mortgages	.....	.....	.....	.....	.....	.....
4.3 Commercial Loans	.....	.....	.....	.....	.....	.....
4.4 Mezzanine Real Estate Loans	.....	.....	.....	.....	.....	.....
4.5 Total Valuation Allowance	.....	.....	.....	.....	.....	.....
4.6 Total Mortgages	.....	.....	.....	.....	.....	.....
5. Real Estate Investments (Schedule A)						
5.1 Property occupied by company	.....	.....	.....	.....	.....	.....
5.2 Property held for production of income	.....	.....	.....	.....	.....	.....
5.3 Property held for sale	.....	.....	.....	.....	.....	.....

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Investment Categories	Gross Investment Holdings 1 Amount	Gross Investment Holdings 2 Percentage	Admitted Assets as Reported in the Annual Statement 3 Amount	Admitted Assets as Reported in the Annual Statement 4 Securities Lending Reinvested Collateral Amount	Admitted Assets as Reported in the Annual Statement 5 Total (Col. 3+4) Amount	Admitted Assets as Reported in the Annual Statement 6 Percentage
6. Cash, Cash Equivalents and Short-Term Investments						
6.1 Cash (Schedule E, Part 1)	.....	.....	.....	.....	.....	.....
6.2 Cash Equivalents (Schedule E, Part 2)	.....	.....	.....	.....	.....	.....
6.3 Short-Term Investments (Schedule DA)	.....	.....	.....	.....	.....	.....
6.4 Total Cash, Cash Equivalents and Short-Term Investments	.....	.....	.....	.....	.....	.....
7. Contract Loans	.....	.....	.....	.....	.....	.....
8. Derivatives (Schedule DB)	.....	.....	.....	.....	.....	.....
9. Other Invested Assets (Schedule BA)	.....	.....	.....	.....	.....	.....
10. Receivables for Securities	.....	.....	.....	.....	.....	.....
11. Securities Lending (Schedule DL, Part1)	.....	.....	.....	.....	.....	.....
12. Aggregate Write-Ins for Invested Assets	.....	.....	.....	.....	.....	.....
13. **Total Invested Assets**	.....	.....	.....	.....	.....	.....

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Appendix A-010

Minimum Reserve Standards for Individual and Group Health Insurance Contracts

Relevant SSAPs:
SSAP No. 35R—Guaranty Fund and Other Assessments
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Annual claim cost" is the net annual cost per unit of benefit before the addition of expenses, including claim settlement expenses, and a margin for profit or contingencies. For example, the annual claim cost for a $100 monthly disability benefit, for a maximum disability benefit period of one year, with an elimination period of one week, with respect to a male at age 35, in a certain occupation might be $12, while the gross premium for this benefit might be $18. The additional $6 would cover expenses and profit or contingencies.

2. "Claims accrued" is that portion of claims incurred on or prior to the valuation date that result in liability of the insurer for the payment of benefits for medical services that have been rendered on or prior to the valuation date, and for the payment of benefits for days of hospitalization and days of disability that have occurred on or prior to the valuation date, that the insurer has not paid as of the valuation date, but for which it is liable and will have to pay after the valuation date. This liability is sometimes referred to as a liability for "accrued" benefits. A claim reserve, which represents an estimate of this accrued claim liability, must be established. *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses defines this as a Claim Liability and not a Claim Reserve.*

3. "Claims reported" are considered as a reported claim for annual statement purposes when an insurer has been informed that a claim has been incurred, if the date reported is on or prior to the valuation date.

4. "Claims unaccrued" represent that portion of claims incurred on or prior to the valuation date which result in liability of the insurer for the payment of benefits for medical services expected to be rendered after the valuation date, and for benefits expected to be payable for days of hospitalization and days of disability occurring after the valuation date. This liability is sometimes referred to as a liability for unaccrued benefits. A claim reserve, which represents an estimate of the unaccrued claim payments expected to be made (which may or may not be discounted with interest), must be established. *SSAP No. 54R—Individual and Group Accident and Health Contracts defines this as a Claim Reserve differentiated from the Claim Liability in paragraph 2 above.*

5. When an insurer has not been informed, on or before the valuation date, concerning a claim that has been incurred on or prior to the valuation date, the claim is considered an "unreported claim" for annual statement purposes.

6. "Date of disablement" is the earliest date the insured is considered as being disabled under the definition of disability in the contract, based on a doctor's evaluation or other evidence. Normally this date will coincide with the start of any elimination period.

7. "Elimination period" is a specified number of days, weeks, or months starting at the beginning of each period of loss, during which no benefits are payable.

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8. "Gross premium" is the amount of premium charged by the insurer. It includes the net premium (based on claim-cost) for the risk, together with any loading for expenses, profit or contingencies.

9. The term "group long-term disability income" includes group contracts providing group disability income coverage with a maximum benefit duration longer than two years. Group long-term disability income contracts are based on a group pricing structure. The term "group long-term disability" does not include group short-term disability (coverage with benefit periods of two years or less in maximum duration). It also does not include voluntary group disability income coverage that is priced on an individual risk structure and generally sold in the workplace.

10. The term "group insurance" includes blanket insurance and franchise insurance and any other forms of group insurance.

11. "Level premium" is a premium calculated to remain unchanged throughout either the lifetime of the policy or for some shorter projected period of years. The premium need not be guaranteed; in which case, although it is calculated to remain level, it may be changed if any of the assumptions on which it was based are revised at a later time. Generally, the annual claim costs are expected to increase each year and the insurer, instead of charging premiums that correspondingly increase each year, charges a premium calculated to remain level for a period of years or for the lifetime of the contract. In this case the benefit portion of the premium is more than needed to provide for the cost of benefits during the earlier years of the policy and less than the actual cost in the later years. The building of a prospective contract reserve is a natural result of level premiums.

12. "Long-term care insurance" is any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than twelve (12) consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis; for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital. Such term also includes a policy or rider which provides for payment of benefits based upon cognitive impairment or the loss of functional capacity. Long-term care insurance may be issued by insurers; fraternal benefit societies; nonprofit health, hospital, and medical service corporations; prepaid health plans; health maintenance organizations or any similar organization to the extent they are otherwise authorized to issue life or health insurance. Long-term care insurance shall not include any insurance policy which is offered primarily to provide basic Medicare supplement coverage, basic hospital expense coverage, basic medical-surgical expense coverage, hospital confinement indemnity coverage, major medical expense coverage, disability income or related asset-protection coverage, accident only coverage, specified disease or specified accident coverage, or limited benefit health coverage.

13. "Modal Premium" refers to the premium paid on a contract based on a premium term which could be annual, semi-annual, quarterly, monthly, or weekly. Thus if the annual premium is $100 and if, instead, monthly premiums of $9 are paid then the modal premium is $9.

14. Normally the terminal reserve is a positive value. However, if the values of the benefits are decreasing with advancing age or duration it could be a negative value, called a "negative reserve."

15. "Preliminary Term Reserve Method" is a method of valuation whereby the valuation net premium for each year falling within the preliminary term period is exactly sufficient to cover the expected incurred claims of that year, so that the terminal reserves will be zero at the end of the year. As of the end of the preliminary term period, a new constant valuation net premium (or stream of changing valuation premiums) becomes applicable such that the present value of all such premiums is equal to the present value of all claims expected to be incurred following the end of the preliminary term period.

16. "Present value of amounts not yet due on claims" represents the reserve for "claims unaccrued" (see definition), which may be discounted at interest.

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17. "Rating block" means a grouping of contracts determined by the valuation actuary based on common characteristics, such as a policy form or forms having similar benefit designs.

18. The term "reserve" is used to include all items of benefit liability, whether in the nature of incurred claim liability or in the nature of contract liability relating to future periods of coverage, and whether the liability is accrued or unaccrued. An insurer under its contracts promises benefits which result in:

a. Claims that have been incurred, that is, for which the insurer has become obligated to make payment, on or prior to the valuation date. On these claims, payments expected to be made after the valuation date for accrued and unaccrued benefits are liabilities of the insurer which shall be provided for by establishing claim reserves; or

b. Claims that are expected to be incurred after the valuation date. Any present liability of the insurer for these future claims shall be provided for by the establishment of contract reserves and unearned premium reserves.

19. "Terminal reserve" is the reserve at the end of a contract year and is defined as the present value of benefits expected to be incurred after that contract year minus the present value of future valuation net premiums.

20. "Unearned premium reserve" values that portion of the premium paid or due to the insurer which is applicable to the period of coverage extending beyond the valuation date. Thus if an annual premium of $120 was paid on November 1, $20 would be earned as of December 31 and the remaining $100 would be unearned. The unearned premium reserve could be on a gross basis as in this example or on a valuation net premium basis.

21. "Valuation net modal premium" is the modal fraction of the valuation net annual premium that corresponds to the gross modal premium in effect on any contract to which contract reserves apply. Thus if the mode of payment in effect is quarterly, the valuation net modal premium is the quarterly equivalent of the valuation net annual premium.

22. "Worksite Disability Policies" refers to individual short-term disability policies that are sold at the worksite through employer-sponsored enrollment, cover normal pregnancy, and that have benefit periods up to 24 months. Worksite disability policies do not include personal disability policies sold to an individual and not associated with employer-sponsored enrollment. They also do not include business overhead expense, disability buyout or key person policies, in whatever manner those policies are sold.

Scope

23. These standards apply to all individual and group health and accident and sickness insurance coverages, including single premium credit disability insurance. All other credit insurance is not subject to Appendix A-010.

24. When an insurer determines that adequacy of its health insurance reserves requires reserves in excess of the minimum standards specified herein, such increased reserves shall be held and shall be considered the minimum reserves for that insurer.

25. With respect to any block of contracts, or with respect to an insurer's health business as a whole, a prospective gross premium valuation is the ultimate test of reserve adequacy as of a given valuation date. Such a gross premium valuation will take into account, for contracts in force, in a claims status, or in a continuation of benefits status on the valuation date, the present value as of the valuation date of: all expected benefits unpaid, all expected expenses unpaid, and all unearned or expected premiums, adjusted for future premium increases reasonably expected to be put into effect.

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26. Such a gross premium valuation is to be performed whenever a significant doubt exists as to reserve adequacy with respect to any major block of contracts, or with respect to the insurer's health business as a whole. In the event inadequacy is found to exist, immediate loss recognition shall be made and the reserves restored to adequacy. Adequate reserves (inclusive of claim, premium and contract reserves, if any) shall be held with respect to all contracts, regardless of whether contract reserves are required for such contracts under these standards.

27. Whenever minimum reserves, as defined in this Appendix, exceed reserve requirements as determined by a prospective gross premium valuation, such minimum reserves remain the minimum requirement under these standards.

28. The following paragraphs set forth minimum standards for three categories of health insurance reserves:

a. Claim Reserves;

b. Premium Reserves;

c. Contract Reserves.

29. Adequacy of an insurer's health insurance reserves is to be determined on the basis of all three categories combined. However, these standards emphasize the importance of determining appropriate reserves for each of the three categories separately.

Claim Reserves

30. General:

a. Claim reserves are required for all incurred but unpaid claims on all health insurance policies. For contracts with an elimination period, the duration of disablement shall be measured as dating from the time that benefits would have begun to accrue had there been no elimination period.

b. Appropriate claim expense reserves are required with respect to the estimated expense of settlement of all incurred but unpaid claims.

c. All such reserves for prior valuation years are to be tested for adequacy and reasonableness along the lines of claim runoff schedules in accordance with the statutory financial statement including consideration of any residual unpaid liability.

d. For claim reserves on policies that require contract reserves, the claim incurral date is to be considered the "issue date" for determining the table and interest rate to be used for claim reserves.

e. The maximum interest rate for claim reserves is specified in Exhibit 1.

f. With respect to claim reserves for policies issued before the operative date[1] of the Valuation Manual, the requirements for claim reserves on claims incurred after that date shall be as described in this Appendix A-010 based on the incurred date of the claim.

[1] The historical application of new requirements for claim reserves has been the incurred date of the claim. The 2009 changes to the Standard Valuation Law apply new requirements provided through the *Valuation Manual* only to policies issued after the effective date of the changes and the *Valuation Manual*. This addition makes new requirements for claim reserves applicable based on the incurred date irrespective of the policy issue date – i.e. consistent with historical practice.

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Minimum Morbidity Standards for Individual Disability Income Claim Reserves:

31. For individual disability income claims incurred January 1, 2001, to January 1, 2007, each insurer may elect which of the following to use as the minimum morbidity standard for claim reserves:

a. The minimum morbidity standard in effect for claim reserves as of the date the claim was incurred, or

b. The standards as defined in paragraph 32, which applies on or after January 1, 2017, shall be applied to all open claims unless the company chooses on or after January 1, 2017, to apply the standards in paragraph 31.c. Once an insurer elects to calculate reserves for all open claims on the newer standards defined in paragraph 32 or paragraph 31.c., all future valuations must be on that basis.

c. The standards as defined in paragraph 33 through paragraph 36, which apply on or after January 1, 2017, shall be applied to all open claims. Once an insurer elects to calculate reserves for all open claims on the standards defined in paragraph 33 through paragraph 36, all future valuations must be on that basis.

32. For individual disability income claims incurred on or after January 1, 2007, and prior to the effective date for the company as determined in paragraph 35, the minimum standards with respect to morbidity are those specified in Exhibit 1, except that, at the option of the insurer, assumptions regarding claim termination rates for the period less than two (2) years from the date of disablement may be based on the insurer's experience, if such experience is considered credible, or upon other assumptions designed to place a sound value on the liabilities.

33. For claims incurred on or after January 1, 2020, the minimum standards are those specified in Exhibit 1, including (as derived in accordance with *Actuarial Guideline L—2013 Individual Disability Income Valuation Table Actuarial Guideline*):

a. The use of the insurer's own experience;

b. An adjustment to include an own experience measurement margin; and

c. The application of a credibility factor.

34. In determining the minimum reserves in accordance with paragraph 33, the provisions in paragraph 33.a., 33.b. and 33.c. are not required if:

a. The insurer meets the Own Experience Measurement Exemption provided in Actuarial Guideline L; or

b. For worksite disability policies with benefit periods of up to two years, at the option of the insurer, disabled life reserves may be based on the insurer's experience, if such experience is considered credible, or upon other assumptions and methods designed to place a sound value on the liabilities.

35. An insurer may begin to use the minimum reserve standards in paragraph 33 at a date earlier than January 1, 2020, but not prior to January 1, 2017.

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36. An insurer may, within three years[2] of January 1, 2020 (or such earlier date it elects under paragraph 35), apply the new standards in paragraph 33 to all open claims incurred prior to the effective date of paragraph 33 for the insurer. Once an insurer elects to calculate reserves for all open claims based on paragraph 33, all future valuations must be on that basis.

Minimum Morbidity Standards for Group Disability Income Claim Reserves

37. For group disability income claims incurred from January 1, 2001, through December 31, 2006, with a duration from date of disablement of more than two (2) years but less than five (5) years, reserves may be based on the insurer's experience if such experience is considered credible and for which the insurer maintains underwriting and claim administration control.

38. For group disability income claims incurred prior to January 1, 2007, each insurer may elect to use as the minimum morbidity standard for claim reserves:

a. The group disability income claims minimum morbidity standard in effect for claim reserves as of the date the claim was incurred; or

b. After the effective date selected by the company in paragraphs 41 and 42, the standards as defined in paragraphs 41 and 42 applied to all open group long-term disability income claims, or

c. The standards as defined in paragraphs 41 and 42 applied to all open group disability income claims.

Once an insurer elects to calculate reserves for all open claims on a more recent standard, then all future valuations must be on that basis.

39. For group long-term disability income claims incurred on or after January 1, 2007, but before the effective date selected by the company in paragraph 42, and group disability income claims incurred on or after January 1, 2007, that are not group long-term disability income, the minimum standards with respect to morbidity are those specified in Exhibit 1, except that, at the option of the insurer:

a. Assumptions regarding claim termination rates for the period less than two (2) years from the date of disablement may be based on the insurer's experience, if the experience is considered credible, or upon other assumptions designed to place a sound value on the liabilities.

b. Assumptions regarding claim termination rates for the period two (2) or more years but less than five (5) years from the date of disablement may, with the approval of the commissioner, be based on the insurer's experience if such experience is considered credible and for which the insurer maintains underwriting and claim administration control.

c. With respect to claims termination standards in paragraphs 37 and 39.b., for experience to be considered credible for purposes of this appendix, the company should be able to provide claim termination patterns over no more than six (6) years reflecting at least

[2] The 2013 Table requires additional information that was not required to determine claim reserves under prior tables. The three year period is a period after the date a company starts using the 2013 Table for new claims to allow the company to update its claims data to use the 2013 Table for claims incurred prior to that date. For example, if a company begins to use the 2013 Table on January 1, 2020, for claims incurred after that date, it does not need to immediately convert all existing claims. This provision allows for the run-off of existing claims until December 31, 2022. As of that date (or an earlier date), the company must either continue use of the existing tables applicable to these claims or may convert all still open claims to the 2013 Table (adding the necessary data only for the remaining open claims).

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5,000 claims terminations during the third through fifth claims durations on reasonably similar applicable policy forms. The request for such approval of a plan of modification to the reserve basis must be in writing and must include:

i. An analysis of the credibility of the experience;

ii. A description of how all of the insurer's experience is proposed to be used in setting reserves;

iii. A description and quantification of the margins to be included;

iv. A summary of the financial impact that the proposed plan of modification would have had on the insurer's last filed annual statement;

v. A copy of the approval of the proposed plan of modification by the commissioner of the state of domicile; and

vi. Any other information deemed necessary by the commissioner.

d. For claim reserves to reflect "sound values" and/or reasonable margins, reserve tables based on credible experience should be adjusted regularly to maintain reasonable margins.

40. On or after October 1, 2014, with respect to incurred claims subject to paragraph 39, each insurer may elect which of the following to use as the minimum morbidity standard for group long-term disability income claim reserves:

a. The minimum morbidity standard in effect for claim reserves as of the date the claim was incurred, or

b. The standards as defined in paragraph 41, applied to all open claims.

Once an insurer elects to calculate reserves for all open claims on a more recent standard, then all future valuations must be on that basis.

41. For group long-term disability income claims incurred on or after January 1, 2017, or the earlier date that is chosen for optional early adoption, but not before October 1, 2014, the minimum standards with respect to morbidity shall be based on the 2012 GLTD termination table with considerations of:

a. The insurer's own experience computed in accordance with Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*,

b. An adjustment to include an own experience measurement margin derived in accordance with Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*, and

c. A credibility factor derived in accordance with Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*.

42. An insurer may begin to use the minimum reserve standards in paragraph 41 at a date earlier than January 1, 2017, but not prior to October 1, 2014. An insurer may apply the standards in paragraph 41 to all open claims incurred prior to the effective date of paragraph 41 for the insurer. Once an insurer elects to calculate reserves for all open claims based on paragraph 41, all future valuations must be on that basis. This option with respect to Exhibit 1, paragraph 1.a.iii.(a) and paragraph 1.a.iii.(b) may be selected only if

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the insurer maintains adequate claim records for claims incurred to use the 2013 Individual Disability Income (IDI) Valuation Table appropriately.

Minimum Morbidity Standards for Other Health Insurance Claim Reserves

43. The reserve shall be based on the insurer's experience, if such experience is considered credible, or upon other assumptions designed to place a sound value on the liabilities.

44. Claim Reserve Methods Generally – A generally accepted actuarial reserving method or other reasonable method, or a combination of methods may be used to estimate all claim liabilities. The methods used for estimating liabilities generally may be aggregate methods, or various reserve items may be separately valued. Approximations based on groupings and averages may also be employed. Adequacy of the claim reserves, however, shall be determined in the aggregate.

Premium Reserves

45. General:

a. Except as noted in paragraph 46.b., unearned premium reserves are required for all contracts with respect to the period of coverage for which premiums, other than premiums paid in advance, have been paid beyond the date of valuation.

b. Single premium credit disability insurance individual policies and group certificates are excluded from unearned premium reserve requirements of paragraphs 45-47.

c. If premiums due and unpaid are carried as an asset, such premiums must be treated as premiums in force, subject to unearned premium reserve determination. The value of unpaid commissions, premium taxes, and the cost of collection associated with due and unpaid premiums must be carried as an offsetting liability.

d. The gross premiums paid in advance for a period of coverage commencing after the next premium due date which follows the date of valuation may be appropriately discounted to the valuation date and shall be held as a separate liability.

46. Minimum Standards for Unearned Premium Reserves:

a. The minimum unearned premium reserve with respect to any contract is the pro rata unearned modal premium that applies to the premium period beyond the valuation date, with such premium determined on the basis of:

i. The valuation net modal premium on the contract reserve basis applying to the contract; or;

ii. The gross modal premium for the contract if no contract reserve applies.

b. However, in no event may the sum of the unearned premium and contract reserves for all contracts of the insurer subject to contract reserve requirements be less than the gross modal unearned premium reserve on all such contracts, as of the date of valuation. Such reserve shall never be less than the expected claims for the period beyond the valuation date represented by such unearned premium reserve, to the extent not provided for elsewhere.

47. Premium Reserve Methods Generally – The insurer may employ suitable approximations and estimates; including, but not limited to groupings, averages and aggregate estimation; in computing premium reserves. Such approximations or estimates shall be tested periodically to determine their continuing adequacy and reliability.

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Contract Reserves

48. General:

a. Contract reserves are required, unless otherwise specified in paragraph 48.b. for:

i. All individual and group contracts with which level premiums are used; or

ii. All individual and group contracts with respect to which, due to the gross premium pricing structure at issue, the value of the future benefits at any time exceeds the value of any appropriate future valuation net premiums at that time. This evaluation may be applied on a rating block basis if the total premiums for the block were developed to support the total risk assumed and expected expenses for the block each year, and a qualified actuary certifies the premium development. The actuary should state in the certification that premiums for the rating block were developed such that each year's premium was intended to cover that year's costs without any prefunding. If the premium is also intended to recover costs for any prior years, the actuary should also disclose the reasons for and magnitude of such recovery. The values specified in this paragraph shall be determined on the basis specified in paragraph 49.

iii. If rates are determined such that each year's premium is intended to cover that year's cost, the rating block approach results in no contract reserves unless required by paragraph 51. If rates are designed to prefund future years' costs, contract reserves will be required.

b. Contracts not requiring a contract reserve are contracts which cannot be continued after one year from issue and contracts already in force on January 1, 2001, for which no contract reserve was required under SSAP No. 54R, paragraph 42.

c. The contract reserve is in addition to claim reserves and premium reserves.

d. The methods and procedures for contract reserves shall be consistent with those for claim reserves for any contract, or else appropriate adjustment must be made when necessary to assure provision for the aggregate liability. The definition of the date of incurral must be the same in both determinations.

e. The total contract reserve established shall incorporate provisions for moderately adverse deviations.

49. Minimum Standards for Contract Reserves:

a. Basis:

i. Morbidity or other Contingency. Minimum standards with respect to morbidity are those set forth in Exhibit 1.

(a) Valuation net premiums used under each contract must have a structure consistent with the gross premium structure at issue of the contract as this relates to advancing age of insured, contract duration and period for which gross premiums have been calculated.

(b) Except as provided in paragraph 48.a.ii., if for a policy form there is no gross premium variation by age, the valuation net premiums will nonetheless vary based on age at issue for each contract since at issue the

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present value of valuation net premiums for a contract must equal the present value of tabular claim costs.

(c) Contracts for which tabular morbidity standards are not specified in Exhibit 1 shall be valued using tables established for reserve purposes by a qualified actuary. The morbidity tables shall contain a pattern of incurred claims cost that reflects the underlying morbidity and shall not be constructed for the primary purpose of minimizing reserves.

(d) Effective January 1, 2007, when determining the morbidity assumptions, the actuary shall use assumptions that represent the best estimate of anticipated future experience, but shall not incorporate any expectation of future morbidity improvement. Morbidity improvement is a change, in the combined effect of claim frequency and the present value of future expected claim payments given that a claim has occurred, from the current morbidity tables or experience that will result in a reduction to reserves. It is not the intent of this provision to restrict the ability of the actuary to reflect the morbidity impact for a specific known event that has occurred and that is able to be evaluated and quantified.

(e) Business in force prior to January 1, 2007, may be permitted to retain the original reserve basis, which may not meet the provisions of (d) above.

ii. Interest. The maximum interest rate is specified in Exhibit 1.

iii. Termination rates. Termination rates used in the computation of reserves shall be on the basis of a mortality table as specified in Exhibit 1 except as noted in the following paragraphs.

(a) Under contracts for which premium rates are not guaranteed, and where the effects of insurer underwriting are specifically used by policy duration in the valuation morbidity standard or for return of premium or other deferred cash benefits, total termination rates may be used at ages and durations where these exceed specified mortality table rates, but not in excess of the lesser of:

(1) Eighty percent of the total termination rate used in the calculation of the gross premiums, or

(2) Eight percent.

(b) For long-term care individual policies or group certificates, issued within the period January 1, 2001, to December 31, 2006, the contract reserve may be established on a basis of separate:

(1) Mortality (as specified in Exhibit 1) and

(2) Terminations other than mortality, where the terminations are not to exceed:

(i) For policy years one through four (4), the lesser of eighty percent (80%) of the voluntary lapse rate used in the calculation of gross premiums and eight percent (8%);

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(ii) For policy years five (5) and later, the lesser of one hundred percent (100%) of the voluntary lapse rate used in the calculation of gross premiums and four percent (4%).

(c) For long-term care individual policies or group certificates issued on or after January 1, 2007, the contract reserve shall be established on the basis of:

(1) Mortality (as specified in Exhibit 1); and

(2) Terminations other than mortality, where the terminations are not to exceed:

(i) For policy year one, the lesser of eighty percent (80%) of the voluntary lapse rate used in the calculation of gross premiums and six percent (6%).

(ii) For policy years two (2) through four (4), the lesser of eighty percent (80%) of the voluntary lapse rate used in the calculation of gross premiums and four percent (4%).

(iii) For policy years five (5) and later, the lesser of one hundred percent (100%) of the voluntary lapse rate used in the calculation of gross premiums and two percent (2%), except certificates under policies issued to one or more employers or labor organizations, or to a trust or to the trustees of a fund established by one or more employers or labor organizations, or a combination thereof, for employees or former employees or a combination thereof, or for members or former members or a combination thereof, of a labor organization where the 2% shall be three percent (3%).

(d) Where a morbidity standard specified in Exhibit 1 is on an aggregate basis, such morbidity standard may be adjusted to reflect the effect of insurer underwriting by policy duration. The adjustments must be appropriate to the underwriting.

b. Reserve Method:

i. For insurance except long-term care and return of premium or other deferred cash benefits, the minimum reserve is the reserve calculated on the two-year full preliminary term method; that is, under which the terminal reserve is zero at the first and also the second contract anniversary.

ii. For long-term care insurance, the minimum reserve is the reserve calculated on the one-year full preliminary term method.

iii. (a) For return of premium or other deferred cash benefits, the minimum reserve is the reserve calculated as follows:

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(1) On the one-year preliminary term method if the benefits are provided at any time before the twentieth anniversary;

(2) On the two-year preliminary term method if the benefits are only provided on or after the twentieth anniversary.

(b) The preliminary term method may be applied only in relation to the date of issue of a contract. Reserve adjustments introduced later, as a result of rate increases, revisions in assumptions (e.g., projected inflation rates) or for other reasons, are to be applied immediately as of the effective date of adoption of the adjusted basis.

c. Negative Reserves. Negative reserves on any benefit may be offset against positive reserves for other benefits in the same contract, but the total contract reserve with respect to all benefits combined may not be less than zero.

d. Nonforfeiture Benefits for Long-Term Care Insurance. The contract reserve on a policy basis shall not be less than the net single premium for the nonforfeiture benefits at the appropriate policy duration, where the net single premium is computed according to the above specifications.

50. Alternative Valuation Methods and Assumptions Generally – Provided the contract reserve on all contracts to which an alternative method or basis is applied is not less in the aggregate than the amount determined according to the applicable standards specified above; an insurer may use any reasonable assumptions as to interest rates, termination and/or mortality rates, and rates of morbidity or other contingency. Also, subject to the preceding condition, the insurer may employ methods other than the methods stated above in determining a sound value of its liabilities under such contracts, including but not limited to the following: the net level premium method; the one-year full preliminary term method; prospective valuation on the basis of actual gross premiums with reasonable allowance for future expenses; the use of approximations such as those involving age groupings, groupings of several years of issue, average amounts of indemnity, grouping of similar contract forms; the computation of the reserve for one contract benefit as a percentage of, or by other relation to, the aggregate contract reserves exclusive of the benefit or benefits so valued; and the use of a composite annual claim cost for all or any combination of the benefits included in the contracts valued.

51. Tests For Adequacy and Reasonableness of Contract Reserves:

a. Annually, an appropriate review shall be made of the insurer's prospective contract liabilities on contracts valued by tabular reserves, to determine the continuing adequacy and reasonableness of the tabular reserves giving consideration to future gross premiums. The insurer shall make appropriate increments to such tabular reserves if such tests indicate that the basis of such reserves is no longer adequate subject, however, to the minimum standards in paragraph 49.

b. In the event a company has a contract or a group of related similar contracts, for which future gross premiums will be restricted by contract, insurance department regulations, or for other reasons, such that the future gross premiums reduced by expenses for administration, commissions, and taxes will be insufficient to cover future claims, the company shall establish contract reserves for such shortfall in the aggregate.

Reinsurance

52. Increases to, or credits against reserves carried, arising because of reinsurance assumed or reinsurance ceded, must be determined in a manner consistent with these minimum reserve standards and with all applicable provisions of the reinsurance contracts which affect the insurer's liabilities.

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Exhibit 1 Specific Standards For Morbidity, Interest And Mortality

Morbidity

1. Minimum morbidity standards for valuation of specified individual contract health insurance benefits are as follows:

a. Disability Income Benefits Due to Accident or Sickness

i. Contract Reserves for Contracts issued before January 1, 2020:

(a) The 1985 Commissioners Individual Disability Tables A (85CIDA); or

(b) The 1985 Commissioners Individual Disability Tables B (85CIDB).

(c) Each insurer shall elect, with respect to all individual contracts issued in any one statement year, whether it will use Tables A or Tables B as the minimum standard.

ii. Contract Reserves for Contracts issued on or after January 1, 2020:

The 2013 IDI Valuation Table with modifiers as described in Actuarial Guideline L. An insurer may begin to use the 2013 IDI Valuation Table with modifiers at a date earlier than January 1, 2020, but not prior to January 1, 2017.

Within three years of 2020, or the earlier date that an insurer begins to use the 2013 IDI Valuation Table, the insurer may elect to apply that morbidity standard for all policies issued subject to other valuation tables. This may be done if the following conditions are met:

(a) The insurer must apply the morbidity standard to all inforce policies and incurred claims;

(b) The insurer elects or has elected to apply the 2013 IDI Valuation Table to all claims incurred, regardless of incurred date;

(c) The insurer maintains adequate policy records on policies issued prior to 2020 that allow the insurer to apply the 2013 IDI Valuation Table appropriately; and

(d) Once an insurer elects to calculate reserves for all inforce policies based on the 2013 IDI Valuation Table morbidity standard, all future valuations must be on that basis

iii. Claim Reserves:

(a) For claims incurred from January 1, 2001, through December 31, 2001:

Each insurer may elect which of the following to use as the minimum standard for claims incurred prior to January 1, 2002:

(1) The minimum morbidity standard in effect for contract reserves on currently issued contracts, as of the date the claim is incurred, or

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(2) The standard as defined in Exhibit 1, paragraph 1.a.iii.(b) on or after January 1, 2002, applied to all open claims, or

(3) The standard as defined in Exhibit 1, paragraph 1.a.iii.(c) on or after January 1, 2017, applied to all open non-worksite claims, provided the insurer maintains adequate claim records to allow the insurer to apply the standard defined in Exhibit 1, paragraph 1.a.iii.(c). This option is available whether claims incurred prior to January 1, 2002, were determined under Exhibit 1, paragraph 1.a.iii.(a) or paragraph 1.a.iii.(b).

(4) Once an insurer elects to calculate reserves for all open claims on the standard defined in Exhibit 1, in either paragraph 1.a.iii.(b) or paragraph 1.a.iii.(c), all future valuations must be on that basis.

(b) For claims incurred on or after January 1, 2002, and prior to January 1, 2020:

The 1985 Commissioners Individual Disability Table A (85CIDA) with claim termination rates multiplied by the following adjustment factors:

Duration	Adjustment Factor	Adjusted Termination Rates*
Week 1	0.366	0.04831
2	0.366	0.04172
3	0.366	0.04063
4	0.366	0.04355
5	0.365	0.04088
6	0.365	0.04271
7	0.365	0.04380
8	0.365	0.04344
9	0.370	0.04292
10	0.370	0.04107
11	0.370	0.03848
12	0.370	0.03478
13	0.370	0.03034
Month 4	0.391	0.08758
5	0.371	0.07346
6	0.435	0.07531
7	0.500	0.07245
8	0.564	0.06655
9	0.613	0.05520
10	0.663	0.04705
11	0.712	0.04486
12	0.756	0.04309
13	0.800	0.04080
14	0.844	0.03882
15	0.888	0.03730

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Duration	Adjustment Factor	Adjusted Termination Rates*
16	0.932	0.03448
17	0.976	0.03026
18	1.020	0.02856
19	1.049	0.02518
20	1.078	0.02264
21	1.107	0.02104
22	1.136	0.01932
23	1.165	0.01865
24	1.195	0.01792
Year 3	1.369	0.16839
4	1.204	0.10114
5	1.199	0.07434
6 and later	1.000	**

* The adjusted termination rates derived from the application of the adjustment factors to the DTS Valuation Table termination rates shown in exhibits 3a, 3b, 3c, 4, and 5 (*Transactions of the Society of Actuaries* (TSA) XXXVII, pp. 457-463) is displayed. The adjustment factors for age, elimination period, class, sex, and cause displayed in exhibits 3a, 3b, 3c, and 4 should be applied to the adjusted termination rates shown in this table.

** Applicable DTS Valuation Table duration rate from exhibits 3c and 4 (TSA XXXVII, pp. 462-463).

The 85CIDA table so adjusted for the computation of claim reserves shall be known as 85CIDC (The 1985 Commissioners Individual Disability Table C).

(c) For claims incurred on or after 2020, the 2013 IDI Valuation Table with modifiers and adjustments for company experience as prescribed in Actuarial Guideline L, except for worksite disability policies with benefit periods of 24 months or less.

(d) For worksite disability policies, claim reserves may be calculated using claim run-out analysis or claim triangles, or other methods that place a sound value on the reserves that are appropriate for the business and risks involved.

b. Hospital Benefits, Surgical Benefits and Maternity Benefits (Scheduled benefits or fixed time period benefits only)

i. Contract Reserves:

The 1974 Medical Expense Tables, Table A, Transactions of the Society of Actuaries, Volume XXX, pg. 63. Refer to the paper (in the same volume, pg. 9) to which this table is appended, including its discussions, for methods of adjustment for benefits not directly valued in Table A: "Development of the 1974 Medical Expense Benefits," Houghton and Wolf.

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ii. Claim Reserves:

No specific standard. See paragraph 1.f. of this Exhibit.

c. Cancer Expense Benefits

i. Contract Reserves:

(a) Contracts issued on or after January 1, 1986, and before January 1, 2019: The 1985 NAIC Cancer Claim Cost Tables (1985 CCCT).

(b) Contracts issued on or after January 1, 2019:

(i) For first occurrence and hospitalization benefits: The 2016 Cancer Claim Cost Valuation Tables (2016 CCCVT): *https://content.naic.org/sites/default/files/actuary-01-naic-2017-cancer-claim-cost-valuation-table.xlsx*.

(ii) For all other benefits: Assumptions based on company experience, relevant industry experience and actuarial judgement. Such assumptions should be appropriate for valuation which considers margin for adverse experience.

(iii) For contracts issued on or after January 1, 2018, and before January 1, 2019, a company may elect to use morbidity basis described in paragraphs (i.) and (ii). Once a company begins use of the 2016 CCCVT for new issues, it may not revert to the 1985 CCCT.

ii. Claim Reserves:

No specific standard. See paragraph 1.f. of this Exhibit.

d. Accidental Death Benefits

i. Contract Reserves:

The 1959 Accidental Death Benefits Table.

ii. Claim Reserves:

Actual amount incurred.

e. Single Premium Credit Disability

i. Contract Reserves:

(a) For contracts issued on or after January 1, 2002:

(i) For plans having less than a thirty-day elimination period, the 1985 Commissioners Individual Disability Table A (85CIDA) with claim incidence rates increased by twelve percent (12%).

(ii) For plans having a thirty-day and greater elimination period, the 85CIDA for a fourteen-day elimination period with the adjustment in Item (i).

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(b) For contracts issued prior to January 1, 2002, each insurer may elect either Item (i) or (ii) to use as the minimum standard. Once an insurer elects to calculate reserves for all contracts on the standard defined in Item (a), all future valuations must be on that basis.

(i) The minimum morbidity standard in effect for contract reserves on currently issued contracts, as of the date the contract was issued, or

(ii) The standard as defined in Item (a), applied to all contracts.

ii. Claim Reserves:

Claim reserves are to be determined as provided in paragraph 44.

f. Other Individual Contract Benefits

i. Contract Reserves:

For all other individual contract benefits, morbidity assumptions are to be determined as provided in the reserve standards.

ii. Claim Reserves:

For all benefits other than disability, claim reserves are to be determined as provided in the standards.

2. Minimum morbidity standards for valuation of specified group contract health insurance benefits are as follows:

a. Disability Income Benefits Due to Accident or Sickness where this Appendix references this Exhibit; otherwise, Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*.

i. Contract Reserves:

The 1987 Commissioners Group Disability Income Table (87CGDT).

ii. Claim Reserves:

The 1987 Commissioners Group Disability Income Table (87CGDT);

b. Single Premium Credit Disability

i. Contract Reserves:

(a) For contracts issued on or after January 1, 2002:

(i) For plans having less than a thirty-day elimination period, the 1985 Commissioners Individual Disability Table A (85CIDA) with claim incidence rates increased by twelve percent (12%).

(ii) For plans having a thirty-day and greater elimination period, the 85CIDA for a fourteen-day elimination period with the adjustment in item (i).

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ii. For contracts issued prior to January 1, 2002, each insurer may elect either Item (a) or (b) to use as the minimum standard. Once an insurer elects to calculate reserves for all contracts on the standard defined in Item (a), all future valuations must be on that basis.

(a) The minimum morbidity standard in effect for contract reserves on currently issued contracts, as of the date the contract was issued, or

(b) The standard as defined in Item (a), applied to all contracts.

iii. Claim Reserves:

Claim reserves are to be determined as provided in paragraph 44.

c. Other Group Contract Benefits

i. Contract Reserves:

For all other group contract benefits, morbidity assumptions are to be determined as provided in the reserve standards.

ii. Claim Reserves:

For all benefits other than disability, claim reserves are to be determined as provided in the standards.

Interest

3. For contract reserves the maximum interest rate is the maximum rate allowed by Appendix A-820 in the valuation of whole life insurance issued on the same date as the health insurance contract.

4. For claim reserves on policies that require contract reserves, the maximum interest rate is the maximum rate allowed by Appendix A-820 in the valuation of whole life insurance issued on the same date as the claim incurral date.

5. For claim reserves on policies not requiring contract reserves, the maximum interest rate is the maximum rate allowed by Appendix A-820 in the valuation of single premium immediate annuities issued on the same date as the claim incurral date, reduced by 100 basis points.

Mortality

6. a. Unless paragraph 7 or paragraph 8 of this Exhibit 1 applies, the mortality basis used for all policies except long-term care individual policies and group certificates issued before January 1, 2001, shall be according to a table (but without use of selection factors) permitted by law for the valuation of whole life insurance issued on the same date as the health insurance contract.

b. For long-term care insurance individual policies or group certificates issued from January 1, 2001, through December 31, 2006, the mortality basis used shall be the 1983 Group Annuity Mortality Table without projection. For long-term care insurance individual policies or group certificates issued on or after January 1, 2007, the mortality basis used shall be the 1994 Group Annuity Mortality Static Table.

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7. Other mortality tables adopted by the NAIC and promulgated by the commissioner may be used in the calculation of the minimum reserves if appropriate for the type of benefits and if approved by the commissioner. The request for approval shall include the proposed mortality table and the reason that the standard specified in paragraph 6.a. of this Exhibit 1 is inappropriate.

8. For single premium credit insurance using the 85CIDA table, no separate mortality shall be assumed.

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Exhibit 2 Reserves for Waiver of Premium (Supplementary explanatory material)

1. Waiver of premium reserves involve several special considerations. First, the disability valuation tables promulgated by the NAIC are based on exposures that include contracts on premium waiver as in-force contracts. Hence, contract reserves based on these tables are NOT reserves on "active lives" but rather reserves on contracts "in force." This is true for the 1964 CDT and for both the 1985 CIDA and CIDB tables.

2. Accordingly, tabular reserves using any of these tables should value reserves on the following basis:

a. Claim reserves should include reserves for premiums expected to be waived, valuing as a minimum the valuation net premium being waived.

b. Premium reserves should include contracts on premium waiver as in-force contracts, valuing as a minimum the unearned modal valuation net premium being waived.

c. Contract reserves should include recognition of the waiver of premium benefit in addition to other contract benefits provided for, valuing as a minimum the valuation net premium to be waived.

If an insurer is, instead, valuing reserves on what is truly an active life table, or if a specific valuation table is not being used but the insurer's gross premiums are calculated on a basis that includes in the projected exposure only those contracts for which premiums are being paid, then it may not be necessary to provide specifically for waiver of premium reserves. Any insurer using such a true "active life" basis should carefully consider, however, whether or not additional liability should be recognized on account of premiums waived during periods of disability or during claim continuation.

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Appendix A-200

Separate Accounts Funding Guaranteed Minimum Benefits Under Group Contracts

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Actuarial Opinion and Memorandum Regulation (#822)

Scope

1. This appendix applies to a group life insurance contract providing survivor income benefits, a group annuity contract, or a funding agreement if the contract is a group contract that utilizes a separate account and provides guaranteed minimum benefits. This appendix shall not apply to modified guaranteed annuities or modified guaranteed life insurance or variable annuity or variable life insurance subject to appendices A-255, A-588, A-250, and A-270 or equity index products but this appendix shall apply to index contracts as defined in paragraph 18.

Definitions

2. "Account assets" means separate account assets plus any assets held in the general account or a supplemental account to meet the asset maintenance requirements.

3. "Account contracts" means the contracts providing guaranteed minimum benefits or other benefits and funded by a separate account and, if applicable, funded in part by the general account or a supplemental account to meet the asset maintenance requirements.

4. "Actuarial opinion" means the valuation actuary's opinion covering reserves for contract liabilities under account contracts that is required to be submitted to the commissioner.

5. "Actuarial memorandum" means the memorandum of the valuation actuary that supports the actuarial opinion covering reserves for contract liabilities under account contracts.

6. "Appointed actuary" means the qualified actuary appointed or retained either directly by or by the authority of the board of directors through an executive officer of the company to prepare the annual statement of actuarial opinion for the company as a whole.

7. "Asset maintenance requirements" means the requirement to maintain assets to fund contract benefits in accordance with paragraphs 30-45.

8. "Book value contract" means a fixed accumulation contract (GIC), purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, that does not participate in the investment experience of a separate account, with a fixed interest rate guarantee, including a guarantee based on an external index, and that is supported by a separate account, the plan of operations of which provides that the separate account's assets are valued as if the assets were held in the insurance company's general account.

9. "Class of contracts" means the set of all contracts to which a given plan of operations pertains.

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10. “Contract” means a group life insurance policy, group annuity contract, or funding agreement that is within the scope of this appendix as set forth in paragraph 1.

11. “Contract benefits” means the amounts obligated to be paid by the insurance company under an account contract.

12. “Contract liabilities” means the liabilities of the insurance company under account contracts, including liabilities with respect to which guarantees as to amount are provided by the insurance company and liabilities with respect to which guarantees as to amount are not provided by the insurance company.

13. a. “Derivative instrument” means an agreement, option, instrument or a series or combination of them:

i. To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or

ii. That has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests.

b. Derivative instruments include options, warrants used in a hedging transaction and not attached to another financial instrument, caps, floors, collars, swaps, forwards, futures and any other agreements, options or substantially similar instruments or any series or combination of them.

14. “Duration” means, with respect to separate account or supplemental account assets or guaranteed contract liabilities, a measure of the price sensitivity of a stream of cash flows to interest rate movements, including, but not limited to, modified duration or option adjusted duration.

15. “General account” means the assets of the insurance company other than separate account and supplemental account assets, and associated reserves.

16. “Guaranteed minimum benefits” means benefits payable under the terms of the contract that are based on either (1) the greater of paragraph 16.a. or 16.b., or (2) paragraph 16.c. where:

a. Is that part of the market value of account assets that determines the contractholder’s benefits, i.e., to the extent the assets are beneficially “client” assets; provided, that if asset performance does not determine the contractholder’s benefit, this subparagraph equals zero;

b. Is a fixed minimum guarantee related to all or part of the considerations received under the contract; and

c. Is an amount based upon a publicly available interest rates series or an index of the aggregate market value of a group of publicly traded financial instruments, either of which is specified in the contract.

17. “Hedging transaction” means a derivative transaction, involving use of one or more derivative instruments, that is entered into and maintained to reduce:

a. The risk of a change in the value, yield, price, cash flow or quantity of assets or liabilities that the insurer has acquired or incurred or anticipates acquiring or incurring; or

b. The currency exchange risk or the degree of exposure as to assets or liabilities that an insurer has acquired or incurred or anticipates acquiring or incurring.

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18. "Index contract" means a contract under which contract benefits shall be based upon a publicly available interest rate series or an index of the aggregate market value of a group of publicly traded financial instruments, either of which is specified in the contract, and that does not provide a guarantee of some or all of the consideration received plus earnings at a fixed rate specified in advance and that does not provide any secondary guarantees on elective benefits or maturity values.

19. "Market value separate account" means a separate account in which the separate account assets are valued at their market value.

20. "Nationally Recognized Statistical Rating Organization (NRSRO)" means a rating organization so designated by the Securities and Exchange Commission of the United States of America (SEC) which has applied to, and whose NRSRO status has been confirmed by, the NAIC Securities Valuation Office.

21. "Plan of operations" means a written plan meeting the requirements of paragraph 29.

22. "Prudent estimate" assumption means an assumption developed by applying a margin to the best estimate assumption for that risk.

23. "Qualified actuary" means an individual who is qualified to sign statements of actuarial opinion in accordance with the qualification standards set forth in Appendix A-820.

24. "Spot rate"

a. "Treasury-based spot rate corresponding to a given time of benefit payment means the yield on a zero-coupon non-callable and non-prepayable United States government obligation maturing at that time, or the zero-coupon yield implied by the price of a representative sampling of coupon-bearing, non-callable and non-prepayable United States government obligations in accordance with a formula set forth in the plan of operation.

b. "Index spot rate" corresponding to a given time of benefit payment means the zero-coupon yield implied by (x) the Barclays Short Term Corporate Index (for a given time of benefit payment under one year) or (y) the zero-coupon yield implied by the Barclays U.S. Corporate Investment Grade Bond Index (for a given time of benefit payment greater than or equal to one year).

c. "Blended spot rate" corresponding to a given time of benefit payment means a blend of 50% of each of (i) the Treasury-based spot rate, and (ii) the index spot rate. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country rates, in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the commissioner and which are supported by investments denominated in the currency of the foreign country, the Treasury-based spot rate component of the blended spot rate may be determined by reference to substantially similar obligations of the government of the foreign country. For liabilities other than those described above, the blended spot rate shall be determined on a basis mutually agreed upon by the insurer and the commissioner.

25. "Supplemental account" means a separate account to which assets may be contributed by the insurance company for the purpose of complying, in whole or in part, with the asset maintenance requirement and with respect to which neither the account contracts nor applicable law shall provide that the assets of the supplemental account are not chargeable with liabilities arising out of any other business of the insurance company.

26. "United States government obligation" means a direct obligation issued, assumed, guaranteed or insured by the United States of America or by an agency or instrumentality of the United States.

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27. "Valuation actuary" means the appointed actuary or, alternatively, a qualified actuary designated by the appointed actuary to render the actuarial opinion. Written documentation of any such designation shall be on file at the company and available for review upon request.

Plan of Operations

28. The plan of operations for a class of contracts shall describe the financial implications for the insurer of the issuance of contracts in the class, and shall include at least the following:

a. A description of the class of contracts to which the plan of operations pertains. This should include a description of the products, the markets to which the products will be sold, the benefits that are being offered (including whether those benefits will be paid on a market or book value basis);

b. A statement of the investment policy for the separate account and any supplemental account, including requirements for diversification, maturity, type and quality of assets, and as applicable, target duration for matching guaranteed contract liabilities or the degree to which the investment policy is likely to match the performance of an interest rate series or index on which contract benefits are based;

c. A description of how the value of the separate account assets and any supplemental account is to be determined, including but not limited to, a statement of procedures and rules for valuing securities and other assets that are not publicly traded;

d. A description of how the guaranteed contract liabilities are to be valued, including, if applicable, with respect to guaranteed minimum benefits or other benefits, a description of the methodology for calculating spot rates and the rates proposed to be used to discount guaranteed contract liabilities if higher than the applicable spot rates, but the rate or rates used shall not exceed the blended spot rate, except that if the expected time of payment of a contract benefit is more than thirty (30) years, it shall be discounted from the expected time of payment to year thirty (30) at a rate of no more than eighty percent (80%) of the thirty-year blended spot rate and from year thirty (30) to the date of valuation at a rate not greater than the thirty-year blended spot rate, and shall conservatively reflect expected investment returns (taking into account foreign exchange risks);

e. A statement of how the separate account's operations are designed to provide for payment of contract benefits as they become due, including but not limited to:

i. A description of the method for estimating the amount and timing of benefit payments;

ii. The arrangements necessary to provide liquidity to cover contingencies;

iii. The method to be used to comply with the asset maintenance requirement;

iv. The manner in which account assets will be allocated between the separate account, any supplemental account, and the general account;

v. If applicable, the deductions to be used in determining the market value of an asset when determining the asset maintenance requirement when the investment policy of the separate account and any supplemental accounts is not likely to match the performance of an interest rate series or index on which contract benefits are based; and

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vi. For index contracts, the deductions to be used for replicated (synthetic) asset transactions in determining the market value of the separate account.

vii. For market value separate accounts supporting contracts other than index contracts:

(a) A description of the criteria used by the insurer in approving for contract issuance a pooled fund representing multiple employer-sponsored plans;

(b) A description of risk-mitigation techniques used by the insurer in connection with contracts issued to pooled funds representing multiple employer-sponsored plans

f. If hedging transactions are to be utilized in managing separate account or any supplemental account assets, a description of the instruments and techniques and an explanation of how they are intended to reduce risk of loss;

g. If the amount of the asset maintenance requirement depends on the separate account, any supplemental account or a subportfolio of either being duration matched, a description of the method used to determine the durations of separate account and any supplemental account assets and guaranteed contract liabilities;

h. If a part of the asset maintenance requirement is to be met by maintaining a reserve liability in the general account, a description of:

i. The circumstances under which increases and decreases in the general account portion of the reserve liability will be made;

ii. The circumstances under which transfers will be made between the separate account and the general account; and

iii. Any arrangements needed to provide sufficient liquidity in the general account to enable the insurance company to make transfers to the separate account when due.

i. A statement as to the extent to which the contracts in the class will provide or applicable law does provide that the separate account assets shall not be chargeable with liabilities arising out of any other business of the insurance company; and

j. If any person other than the insurance company may authorize, approve or review the acquisition and disposition of investments for the separate account or any supplemental account, a statement of the safeguards adopted by the insurance company to assure that the actions to be taken by these persons are appropriate, including a description of the criteria used by the insurance company in selecting the person.

29. Notwithstanding the descriptions in the plan of operations, the insurance company may change the rate used pursuant to paragraph 35 to discount guaranteed contract liabilities and other items applicable to the separate account or any supplemental accounts, such as if the investment portfolio is different from that anticipated by the plan of operations, provided that the rates used shall not exceed the blended spot rates as prescribed in paragraph 28.d.

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Asset Maintenance Requirements for Market Value Separate Accounts Supporting Contracts other than Index Contracts

30. At all times an insurer shall hold sufficient assets as a reserve in the general account, the separate account or supplemental accounts, as appropriate, such that the:

a. Market value of the assets held in the separate account, plus

b. The market value of any supplemental account, plus

c. Any assets held in the general account as a reserve for guaranteed contract liabilities, less

d. The deductions provided for in paragraph 31, equals or exceeds the value of guaranteed contract liabilities determined in accordance with paragraphs 35 and 36.

31. In determining compliance with the asset maintenance requirement and the reserve for guaranteed contract liabilities in accordance with paragraph 30, the insurance company shall deduct a percentage of the market value of the separate account or supplemental account asset or an amount attributable to a replicated (synthetic) asset transaction as follows:

a. For debt instruments, the percentage shall be the NAIC asset valuation reserve "reserve objective factor," but the factor shall be increased fifty percent (50%) for the purpose of this calculation if the difference in durations of the assets and liabilities is more than one-half year;

b. For assets that are not debt instruments, the percentage shall be the NAIC asset valuation reserve "maximum reserve factor"; and

c. For replicated (synthetic) asset transactions, the market value of the separate account or supplemental account assets shall be decreased by an amount equal to the asset valuation reserve for the transaction as if the transaction were occurring in the general account, determined in accordance with SSAP No. 7; but to the extent that the NAIC asset valuation reserve maximum reserve factor was not used in determining the amount of the deduction, the amount of the deduction shall be increased fifty percent (50%) for purposes of this calculation.

32. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by separate account or supplemental account assets denominated in the currency of the foreign country, the percentage deduction for these assets under paragraph 31 shall be that for a substantially similar investment denominated in the currency of the United States.

33. To the extent that guaranteed contract liabilities are denominated in the currency of the United States and are supported by separate account or supplemental account assets denominated in the currency of a foreign country, and to the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by separate account or supplemental account assets denominated in the currency of the United States, the deduction for debt instruments and replicated (synthetic) assets transactions under paragraph 31 shall be increased by fifteen percent (15%) of its market value unless the currency exchange risk has been adequately hedged, in which case the percentage deduction under paragraph 31 shall be increased by one-half percent (0.5%). No guaranteed contract liabilities denominated in the currency of a foreign country shall be supported by separate account or supplemental account assets denominated in the currency of another foreign country. For purposes of this paragraph, the currency exchange rate on an asset is deemed to be adequately hedged if:

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a. It is an obligation of a jurisdiction that is rated in one of two (2) highest rating categories by an NRSRO or a political subdivision or other governmental unit of the jurisdiction, or is organized under the laws of the jurisdiction; and

b. At all times the principal amount and scheduled interest payments on the principal are hedged against the United States dollar pursuant to contracts or agreements that are:

i. Issued by or traded on a securities exchange or board of trade regulated under the laws of the United States or Canada or a province of Canada;

ii. Entered into with a United States banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations, that are rated in one of the two (2) highest rating categories by an NRSRO, or with a broker-dealer registered with the Securities and Exchange Commission that has net capital in excess of $250 million; or

iii. Entered into with any other banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an NRSRO and that is organized under the laws of a jurisdiction that is rated in one of the two (2) highest rating categories by an NRSRO.

34. All or a portion of the amount needed to comply with the asset maintenance requirement may be allocated to one or more supplemental accounts. If the account contract or applicable law provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurance company, the insurance company shall maintain in a supplemental account or the general account the amount of any account assets in excess of the sum of (i) the amounts contributed (net of withdrawals) by the contractholder, and (ii) the earnings attributable to the amounts contributed (net of withdrawals) by the contractholder.

35. For purposes of paragraphs 30-36, the minimum value of guaranteed contract liabilities is defined to be the sum of the expected guaranteed contract benefits, each discounted at a rate corresponding to the expected time of payment of the contract benefit that is not greater than the rate supportable by the expected return from the separate account and any supplemental account assets provided that the rate used shall not exceed the blended spot rates as prescribed in paragraph 28.d. or as described in the actuarial opinion. In calculating the minimum value of contract benefits, all guaranteed contract benefits potentially available to the contractholder shall be considered in the valuation process and analysis, and the reserve held shall be sufficient to fund the greatest present value of each independent guaranteed benefit stream, including guaranteed annuitization options available.

36. To the extent that future cash flows are dependent upon the benefit responsiveness features of an employer-sponsored plan, a best estimate or an estimate based on the insurance company's experience shall be used in the projections of the future cash flows. In addition, the valuation actuary shall periodically review the actual experience under the contract to validate the assumptions used. In projecting cash flows for contingent benefits involving mortality, the mortality tables for these benefits prescribed in Appendix A-820 shall be used.

37. The minimum value of guaranteed contract benefits under a contract issued to a pooled fund representing multiple employer-sponsored plans shall be determined so as to reflect projected plan sponsor contract value withdrawals available to the member plans in the pooled fund. Projections of such future cash flows shall take into account (i) known plan sponsor withdrawals, and (ii) a prudent estimate of future plan sponsor withdrawals. The prudent estimate shall be based on company experience and other relevant criteria.

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38. A single valuation rate shall be determined equal to the lesser of:

a. The expected return from the separate account, or

b. The blended spot rate based on the duration of the separate account.

39. This single valuation rate shall be used to model future market values of the separate account. Future credited interest rates shall be modeled according to the contractually defined crediting rate formula. Modeled future contract values shall reflect modeled future market values, modeled future credited interest rates, known future plan sponsor withdrawals, the prudent estimate of future plan sponsor withdrawals, future withdrawals consistent with paragraph 37, and any remaining final payment at the modeled contract termination date.

40. All such modeled withdrawals and termination payments shall be discounted using the single valuation rate and the modeled times of those withdrawals and payments. The sum of these present values shall be deemed the minimum value of the guaranteed contract liabilities for a pooled fund contract.

Asset Maintenance Requirements for Market Value Separate Accounts Supporting Index Contracts

41. At all times an insurance company shall hold sufficient assets as a reserve in the general account, the separate account or supplemental accounts, as appropriate, such that the:

a. Market value of the assets held in the separate account, plus

b. The market value of any supplemental account, plus

c. Any assets held in the general account as a reserve for guaranteed contract liabilities, less

d. Any deduction provided for in paragraph 42, equals or exceeds the value of guaranteed contract liabilities determined in the manner set forth in the plan of operations.

42. In determining compliance with the asset maintenance requirement and the reserves for guaranteed contract liabilities in accordance with paragraph 41, the insurance company shall deduct a percentage of the market value of a separate account or supplemental account asset as set forth in the plan of operations, and for replication (synthetic asset) transactions, the value of the separate account or supplemental account assets shall be decreased in the manner set forth in the plan of operations.

43. All or a portion of the amount needed to comply with the asset maintenance requirement may be allocated to one or more supplemental accounts. If the account contract or applicable law provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurance company, the insurance company shall maintain in a supplemental account or the general account the amount of any account assets in excess of the sum of (i) the amounts contributed (net of withdrawals) by the contractholder, and (ii) the earnings attributable to the amounts contributed (net of withdrawals) by the contractholder.

Asset Maintenance Requirements for Separate Accounts Supporting Book Value Contracts

44. At all times an insurance company shall hold sufficient assets in the general account, the separate account or supplemental accounts, as appropriate, such that the value of the account assets, valued as if the assets were held in the insurance company's general account, equals or exceeds the reserve required for contracts supported by the separate account, determined as if the contracts were held in the general account.

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45. All or any portion of the amount needed to comply with the asset maintenance requirement may be allocated to one or more supplemental accounts. If the account contract or applicable law provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurance company, the insurance company shall maintain in a supplemental account or the general account the amount of any account assets in excess of the sum of (i) the amounts contributed (net of withdrawals) by the contractholder, and (ii) the earnings attributable to the amounts contributed (net of withdrawals) by the contractholder.

Asset Valuation Reserve

46. When the insurance company values separate account or supplemental account assets at market and complies with the asset maintenance requirements of the section entitled Asset Maintenance Requirements for Market Value Separate Accounts Supporting Contracts other than Index Contracts or the section entitled Asset Maintenance Requirements for Market Value Separate Accounts Supporting Index Contracts, it need not maintain an asset valuation reserve with respect to these assets.

Reserve Valuation and Documentation

47. Reserves for contracts funded by a market value separate account supporting contracts other than index contracts shall be an amount equal to the following:

a. The total reserve required to be maintained on the valuation date under paragraphs 30-36;

b. Plus the excess, if any, of the market value of separate account assets (to the extent that the market value of the assets determines the contractholder's benefits, i.e., to the extent the assets are beneficially "client" assets) over the amount determined in accordance with paragraph 47.a.;

c. Plus any additional amount determined by the valuation actuary as necessary to make adequate provision for all of the contract liabilities.

48. Reserves for index contracts funded by a market value separate account shall be an amount equal to the following:

a. The total reserve required to be maintained on the valuation date under paragraphs 41-43;

b. Plus the excess, if any, of the market value of separate account assets (to the extent that the market value of the assets determines the contractholder's benefits, i.e., to the extent the assets are beneficially "client" assets) over the amount determined in accordance with paragraph 48.a.;

c. Plus any additional amounts determined by the valuation actuary as necessary to make adequate provision for all of the contract liabilities.

49. Reserves for book value contracts shall be determined as if the contracts were held in the general account.

50. The amount of any reserves required by paragraph 47.c. or paragraph 48.c. may be established by either:

a. Allocating sufficient assets to the separate account or a supplemental account to satisfy the requirement; or

b. Setting up the additional reserves in the general account.

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51. Account assets shall make adequate provision for contract liabilities, taking into account any risk charge payable from the separate account assets and the amount of any reserve liability of the general account and amounts held in any supplemental account with respect to the asset maintenance requirement.

52. The level of risk charges, if any, payable to the general account shall be appropriate in view of such factors as the nature of the guaranteed contract liabilities and losses experienced in connection with account contracts and other pricing factors.

53. The fixed-income asset portfolio shall conform to and justify the rates used to discount contract liabilities for valuation pursuant to paragraph 35 if applicable.

54. The company shall document whether any rates used pursuant to paragraph 35 to discount guaranteed contract liabilities and other items applicable to the separate account or any supplemental account were modified from the rate or rates described in the plan of operations.

55. The company shall substantially conform with Appendix A-822 and maintain internal documentation to either:

a. Demonstrate the adequacy of account assets based upon cash flow analysis; or

b. Explain why cash flow analysis is not appropriate, describe the alternative methodology of asset adequacy testing used, and demonstrate the adequacy of account assets under such methodology.

56. The company's internal documentation pertaining to reserves for contract liabilities under account contracts shall also:

a. Clearly describe the assumptions used in projecting cash flows under each class of assets, and any dynamic portfolio hedging techniques utilized and the tests performed on the utilization of the techniques;

b. Clearly describe how the company reflected the risk of default on obligations and mortgage loans, including obligations and mortgage loans that are not investment grade;

c. Clearly describe how the company has reflected withdrawal risks, if applicable, including a discussion of the positioning of the contracts within the benefit withdrawal priority order pertaining to the contracts, the impact of any dynamic lapse assumption and the results of sensitivity testing the prudent estimate of future plan sponsor withdrawals pursuant to paragraphs 37-40;

d. If the plan of operations provides for investments in separate account or supplemental account assets other than United States government obligations, demonstrate that the rates used to discount contract liabilities pursuant to paragraph 35 conservatively reflect expected investment returns (taking into account any foreign exchange risks);

e. If the contracts provide that in certain circumstances they would cease to be funded by a separate account and, instead, would become contracts funded by the general account, clearly describe how any increased reserves would be provided for if and to the extent these circumstances occurred;

f. Document the amount of separate account assets that are not chargeable with liabilities arising out of any other business of the insurance company;

g. Document the amount of reserves and supporting assets as of December 31 and where the reserves and assets are shown in the annual statement;

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h. Document the amount of any contingency reserve carried as part of surplus;

i. For book value contracts, document the market value of supporting assets; and

j. Where separate account assets are not chargeable with liabilities arising out of any other business of the insurance company, describe how the level of risk charges payable to the general account provider are appropriate compensation for the risk taken by the general account.

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Appendix A-205

Illustrative Disclosure of Differences Between NAIC Statutory Accounting Practices and Procedures and Accounting Practices Prescribed or Permitted by the State of Domicile

Relevant SSAPs:
SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures

XYZ Insurance Company
Footnotes to Financial Statements
December 31, 2002, and 2001

Note 1–Organization

The XYZ Company is a mutual life insurance company domiciled in the state of ABC and licensed to do business in all 50 states. The company markets traditional whole life, term and disability income insurance policies to individuals through its career agency force.

Notes 2–Basis of Presentation

The financial statements of XYZ Company are presented on the basis of accounting practices prescribed or permitted by the ABC Insurance Department.

The ABC Insurance Department recognizes only statutory accounting practices prescribed or permitted by the state of ABC for determining and reporting the financial condition and results of operations of an insurance company, for determining its solvency under the ABC Insurance Law. The National Association of Insurance Commissioners' (the "NAIC") *Accounting Practices and Procedures Manual* version effective January 1, 2001 ("NAIC SAP") has been adopted as a component of prescribed or permitted practices by the state of ABC. The state has adopted certain prescribed accounting practices which differ from those found in NAIC SAP. Specifically, 1) goodwill arising from the purchase of a subsidiary, controlled or affiliated entity is written off directly to surplus in the year it originates by ABC domiciled companies; in NAIC SAP, goodwill in amounts not to exceed 10% of an insurer's capital and surplus may be capitalized and all amounts of goodwill are amortized to unrealized gains and losses on investments over periods not to exceed 10 years, and 2) 100% of all fixed assets may be admitted by ABC domiciled companies; in NAIC SAP, fixed assets are not admitted. The Commissioner of Insurance has the right to permit other specific practices which deviate from prescribed practices.

The Company, with the explicit permission of the Commissioner of Insurance of the state of ABC, records the value of its home office building at fair market value instead of at the depreciated cost method required by NAIC SAP. If the home office building were carried at depreciated cost, home office property and statutory surplus would be decreased by $2,500,000 and $2,300,000 as of December 31, 2002 and 2001, respectively. Additionally, net income would be increased by $120,000 and $103,000 respectively, for the years then ended.

Illustration to use if prescribed or permitted statutory accounting practices (individually or in the aggregate), which differ from the NAIC basis of accounting, prevent the triggering of a regulatory event:

> If the reporting entity had not used the above prescribed and permitted practices that differ from the NAIC basis of accounting a risk based capital regulatory event would have been triggered. The company would have moved to a risk based capital company action level and the total adjusted capital would have been decreased by $300,000.

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Illustration to use if prescribed or permitted practices statutory accounting practices, which differ from the NAIC basis of accounting, have no impact on regulatory events:

> If the reporting entity has not used the above prescribed and permitted practices that differ from the NAIC basis of accounting a risk based capital regulatory event would not have been triggered. The impact on net income and capital is shown in the following paragraphs.

A reconciliation of the Company's net income and capital and surplus between NAIC SAP and practices prescribed and permitted by the state of ABC is shown below.

	2002	2001
Net Income, ABC state basis	$3,200,000	$2,900,000
State Prescribed Practices:		
Depreciation of fixed assets	100,000	110,000
State Permitted Practices:		
Depreciation, home office property	120,000	103,000
Net Income, NAIC SAP	$3,420,000	$3,113,000
Statutory Surplus, ABC state basis	$30,000,000	$27,900,000
State Prescribed Practices:		
Goodwill, net	3,000,000	2,700,000
Fixed Assets, net	(850,000)	(950,000)
State Permitted Practices:		
Home Office Property	(2,500,000)	(2,300,000)
Statutory Surplus, NAIC SAP	$29,650,000	$27,350,000

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Appendix A-225

Managing General Agents

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 53—Property and Casualty Contracts–Premiums
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Definitions

1. "Managing General Agent" (MGA) means any person, firm, association or corporation who:

    a. Manages all or part of the insurance business of an insurer (including the management of a separate division, department or underwriting office); and

    b. Acts as an agent for such insurer whether known as a Managing General Agent, manager or other similar term, who, with or without the authority, either separately or together with affiliates, produces, directly or indirectly, and underwrites an amount of gross direct written premium equal to or more than five percent (5%) of the policyholder surplus as reported in the last annual statement of the insurer in any one quarter or year together with one or more of the following activities related to the business produced:

        i. Adjusts or pays claims in a material amount;

        ii. Negotiates reinsurance on behalf of the insurer.

    c. Notwithstanding the above, the following persons shall not be considered MGAs for the purposes of this Appendix:

        i. An employee of the insurer;

        ii. A U.S. Manager of the United States branch of an alien insurer;

        iii. An underwriting manager which, pursuant to contract, manages all or part of the insurance operations of the insurer, is under common control with the insurer, subject to a regulatory holding company act, if any, and whose compensation is not based on the volume of premiums written;

        iv. The attorney-in-fact authorized by and acting for the subscribers of a reciprocal insurer or inter-insurance exchange under powers of attorney.

2. "Underwrite" means the authority to accept or reject risk on behalf of the insurer.

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Appendix A-235

Interest-Indexed Annuity Contracts

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definition

1. "Interest-indexed annuity contract" means any annuity contract where the interest credits are linked to an external reference.

Valuation Requirements

2. In developing life insurance reserves for interest-indexed annuity contracts, the insurer must be in compliance with the minimum requirements of Appendix A-820.

3. In the calculation of reserves for interest-indexed annuity contracts, future guarantees will be determined by assuming that future interest crediting rates will be equal to the statutory valuation interest rate for such contracts as defined in Appendix A-820.

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Appendix A-250

Variable Annuities

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Variable annuity" means a policy or contract, individual or group, that provides for annuity benefits that vary according to the investment experience of a separate account or accounts maintained by the insurer as to the policy or contract.

2. The company shall maintain in each such separate account assets with a value at least equal to the reserves and other contract liabilities with respect to the account.

3. The reserve liability for variable annuities shall be established pursuant to the requirements of Appendix A-820 in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees.

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Appendix A-255

Modified Guaranteed Annuities

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. A "Modified Guaranteed Annuity" is a deferred annuity contract, individual or group, the underlying assets of which are held in a separate account, and the values of which are guaranteed if held for specified periods. The contract contains nonforfeiture values that are based upon a market-value adjustment formula if held for shorter periods. This formula may or may not reflect the value of assets held in the separate account. The assets underlying the contract must be in a separate account during the period or periods when the contract holder can surrender the contract.

2. "Interest credits" means all interest that is credited to the contract.

3. "Separate account" means a separate account established pursuant to the insurance laws pertaining to the insurer.

Valuation Requirements

4. Reserve liabilities for modified guaranteed annuities shall be established as provided in Appendix A-820 in accordance with actuarial procedures that recognize:

   a. That assets of the separate account are based on market values;

   b. The variable nature of benefits provided; and

   c. Any mortality guarantees.

5. As a minimum, the separate account liability will equal the surrender value based upon the market-value adjustment formula contained in the contract. If that liability is greater than the market value of the assets, a transfer of assets will be made into the separate account so that the market value of the assets at least equals that of the liabilities. Any additional reserve that is needed to cover future guaranteed benefits shall be established.

6. The market-value adjustment formula, the interest guarantees, and the degree to which projected cash flow of assets and liabilities are matched must also be considered. The company shall determine whether the assets in the separate account are adequate to provide all future benefits that are guaranteed.

Separate Accounts

7. The insurer shall maintain in each separate account assets with a value at least equal to the valuation reserves and other contract liabilities respecting such account.

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Appendix A-270

Variable Life Insurance

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Variable life insurance policy" means an individual or group policy that provides for life insurance the amount or duration of which varies according to the investment experience of any separate account or accounts established and maintained by the insurer as to the policy.

2. "Affiliate" of an insurer means a person, directly or indirectly, controlling, controlled by, or under common control with the insurer; a person who regularly furnishes investment advice to the insurer with respect to its separate accounts for which a specific fee or commission is charged; or any director, officer, partner or employee of the insurer, controlling or controlled person, or person providing investment advice or any member of the immediate family of such person.

3. "Assumed investment rate" means the rate of investment return that would be required to be credited to a variable life insurance policy, after deduction of charges for taxes, investment expenses and mortality and expense guarantees to maintain the variable death benefit equal at all times to the amount of death benefit, other than incidental insurance benefits, which would be payable under the plan of insurance if the death benefit did not vary according to the investment experience of the separate account.

4. "Benefit base" means the amount to which the net investment return is applied.

5. "Control" (including the terms "controlling," "controlled by" and "under common control with") means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or non-management services, or otherwise, unless the power is the result of an official position with or corporate office held by the person. Control shall be presumed to exist if a person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing more than ten percent (10%) of the voting securities of any other person. This presumption can be overcome by predominant evidence to the contrary, however, it shall stand until overcome by such predominant contradictory evidence.

6. "Flexible premium policy" means any variable life insurance policy other than a "scheduled premium policy" as defined in paragraph 13.

7. "General account" means all assets of the insurer other than assets in separate accounts.

8. "Incidental insurance benefit" means all insurance benefits in a variable life insurance policy, other than the variable death benefit and the minimum death benefit, including but not limited to, accidental death and dismemberment benefits, disability benefits, guaranteed insurability options, family income or term riders.

9. "Minimum death benefit" means the amount of the guaranteed death benefit, other than incidental insurance benefits, payable under a variable life insurance policy regardless of the investment performance of the separate account.

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10. "Net investment return" means the rate of investment return in a separate account to be applied to the benefit base.

11. "Person" means an individual, corporation, partnership, association, trust or fund.

12. "Policy processing day" means the day on which charges authorized in the policy are deducted from the policy's cash value.

13. "Scheduled premium policy" means a variable life insurance policy under which both the amount and timing of premium payments are fixed by the insurer.

14. "Variable death benefit" means the amount of the death benefit, other than incidental insurance benefits, payable under a variable life insurance policy dependent on the investment performance of the separate account, which the insurer would have to pay in the absence of any minimum death benefit.

Valuation Requirements

15. Reserve liabilities for variable life insurance policies shall be established as provided in Appendix A-820 in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees.

16. Reserve liabilities for the guaranteed minimum death benefit shall be the reserve needed to provide for the contingency of death occurring when the guaranteed minimum death benefit exceeds the death benefit that would be paid in the absence of the guarantee, and shall be maintained in the general account of the insurer and shall not be less than the greater of the following minimum reserves:

a. The aggregate total of the term costs, if any, covering a period of one full year from the valuation date or, if less, covering the period provided for in the guarantee not otherwise provided for by the reserves held in the separate account, on each variable life insurance contract, assuming an immediate one-third depreciation in the current value of the assets in the separate account followed by a net investment return equal to the assumed investment rate; or

b. The aggregate total of the "attained age level" reserves on each variable life insurance contract. The "attained age level" reserve on each variable life insurance contract shall not be less than zero and shall equal the "residue," as described in paragraph 16.b.i. below, of the prior year's "attained age level" reserve on the contract, with any such "residue," increased or decreased by a payment computed on an attained age basis as described in paragraph 16.b.ii. below.

i. The "residue" of the prior year's "attained age level" reserve on each variable life insurance contract shall not be less than zero and shall be determined by adding interest at the valuation interest rate to the prior year's reserve, deducting the tabular claims based on the "excess," if any, of the guaranteed minimum death benefit over the death benefit that would be payable in the absence of a guarantee, and dividing the net result by the tabular probability of survival. The "excess" referred to in the preceding sentence shall be based on the actual level of death benefits that would have been in effect during the preceding year in the absence of the guarantee, taking appropriate account of the reserve assumptions regarding the distribution of death claim payments over the year.

ii. The payment referred to in this paragraph shall be computed so that the present value of a level payment of that amount each year over the future period for which charges for this risk will be collected under the contract, is equal to (A) minus (B) minus (C), where (A) is the present value of the future guaranteed

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minimum death benefits, (B) is the present value of the future death benefits that would be payable in the absence of such guarantee, and (C) is any "residue," as described in paragraph 16.b.i. of the prior year's "attained age level" reserve on such variable life insurance contract. This result shall be divided by the present value, at the valuation date, of a temporary life annuity of one per annum at the current attained age payable over the period in which future charges for this risk will be collected under the contract. If no future charges for this risk will be collected under the contract, the payment shall equal (A) minus (B) minus (C). The amounts of the future death benefits referred to in (B) shall be computed assuming a net investment return of the separate account which may differ from the assumed investment rate or the valuation interest but in no event may exceed the maximum interest rate permitted for the valuation of life contracts.

c. The valuation interest rate and mortality table used in computing the two minimum reserves described in 16 a. and 16 b. above shall conform to acceptable standards for the valuation of life insurance contracts. In determining the minimum reserves, the company may employ suitable approximations and estimates, including but not limited to groupings and averages.

17. Incidental Insurance Benefit. Reserve liabilities for all fixed incidental insurance benefits and any guarantees associated with variable accidental insurance benefits shall be maintained in the general account and reserve liabilities for all variable aspects of the variable incidental insurance benefits shall be maintained in a separate account, in amounts determined in accordance with the actuarial procedures appropriate to the benefit.

Separate Accounts

18. The assets of separate accounts shall be valued at least as often as variable benefits are determined but, in any event, at least monthly.

19. The insurer shall maintain in each separate account assets with a value at least equal to the valuation reserves and other contract liabilities respecting such account.

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Appendix A-440

Insurance Holding Companies

Relevant SSAPs:
SSAP No. 25—Affiliates and Other Related Parties
SSAP No. 62R—Property and Casualty Reinsurance

Definitions

1. "Affiliate." An "affiliate" of, or person "affiliated" with, a specific person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.

2. "Control." The term "control" (including the terms "controlling," "controlled by" and "under common control with") means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position with or corporate office held by the person. Control shall be presumed to exist if any person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent (10%) or more of the voting securities of any other person. This presumption can be overcome by predominant evidence to the contrary, however, it shall stand until overcome by such predominant contradictory evidence.

3. "Insurance Holding Company System." An "insurance holding company system" consists of two (2) or more affiliated persons, one or more of which is an insurer.

4. "Person." A "person" is an individual, a corporation, a limited liability company, a partnership, an association, a joint stock company, a trust, an unincorporated organization, any similar entity or any combination of the foregoing acting in concert, but shall not include any joint venture partnership exclusively engaged in owning, managing, leasing or developing real or tangible personal property.

5. "Securityholder." A "securityholder" of a specified person is one who owns any security of such person, including common stock, preferred stock, debt obligations and any other security convertible into or evidencing the right to acquire any of the foregoing.

6. "Subsidiary." A "subsidiary" of a specified person is an affiliate controlled by such person directly or indirectly through one or more intermediaries.

7. "Voting Security." The term "voting security" shall include any security convertible into or evidencing a right to acquire a voting security.

Standards and Management of an Insurer Within a Holding Company System

8. Transactions Within a Holding Company System

9. Transactions within a holding company system to which an insurer subject to registration is a party shall be subject to the following standards:

   a. The terms shall be fair and reasonable;

   b. Charges or fees for services performed shall be reasonable;

   c. Expenses incurred and payment received shall be allocated to the insurer in conformity with statutory accounting practices consistently applied;

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d. The books, accounts and records of each party to all such transactions shall be so maintained as to clearly and accurately disclose the nature and details of the transactions including such accounting information as is necessary to support the reasonableness of the charges or fees to the respective parties; and

e. The insurer's surplus as regards policyholders following any dividends or distributions to shareholder affiliates shall be reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs. In determining whether an insurer's surplus as regards policyholders is reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs, the following factors, among others, shall be considered:

i. The size of the insurer as measured by its assets, capital and surplus, reserves, premium writings, insurance in force and other appropriate criteria;

ii. The extent to which the insurer's business is diversified among several lines of insurance;

iii. The number and size of risks insured in each line of business;

iv. The extent of the geographical dispersion of the insurer's insured risks;

v. The nature and extent of the insurer's reinsurance program;

vi. The quality, diversification and liquidity of the insurer's investment portfolio;

vii. The recent past and projected future trend in the size of the insurer's investment portfolio;

viii. The surplus as regards policyholders maintained by other comparable insurers;

ix. The adequacy of the insurer's reserves; and

x. The quality and liquidity of investments in affiliates.

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Appendix A-585

Universal Life Insurance

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Cash surrender value" means the net cash surrender value plus any amounts outstanding as policy loans.

2. "Fixed premium universal life insurance policy" means a universal life insurance policy other than a flexible premium universal life insurance policy.

3. "Flexible premium universal life insurance policy" means a universal life insurance policy which permits the policyowner to vary, independently of each other, the amount or timing of one or more premium payments or the amount of insurance.

4. "Interest-indexed universal life insurance policy" means any universal life insurance policy where the interest credits are linked to an external referent.

5. "Net cash surrender value" means the maximum amount payable to the policyowner upon surrender.

6. "Policy value" means the amount to which separately identified interest credits and mortality, expense, or other charges are made under a universal life insurance policy.

7. "Universal life insurance policy" means a life insurance policy where separately identified interest credits (other than in connection with dividend accumulations, premium deposit funds, or other supplementary accounts) and mortality and expense charges are made to the policy. A universal life insurance policy may provide for other credits and charges, such as charges for the cost of benefits provided by rider.

Valuation Requirements

8. The minimum valuation standard for universal life insurance policies shall be the Commissioners Reserve Valuation Method, as described below for such policies, and the tables and interest rates specified below. The terminal reserve for the basic policy and any benefits and/or riders for which premiums are not paid separately as of any policy anniversary shall be equal to the net level premium reserves less (C) and less (D), where:

   a. Reserves by the net level premium method shall be equal to ((A)-(B))r where (A), (B) and "r" are as defined below:

      i. (A) is the present value of all future guaranteed benefits at the date of valuation.

      ii. (B) is the quantity $\frac{PVFB}{\ddot{a}_x} \ddot{a}_{x+t}$ where PVFB is the present value of all benefits

guaranteed at issue assuming future guaranteed maturity premiums are paid by the policyowner and taking into account all guarantees contained in the policy or declared by the insurer.

b. äx and äx+t are present values of an annuity of one per year payable on policy anniversaries beginning at ages x and x+t, respectively, and continuing until the highest attained age at which a premium may be paid under the policy. The letter "x" is defined as the issue age and the letter "t" is defined as the duration of the policy.

c. The guaranteed maturity premium for flexible premium universal life insurance policies shall be that level gross premium, paid at issue and periodically thereafter over the period during which premiums are allowed to be paid, which will mature the policy on the latest maturity date, if any, permitted under the policy (otherwise at the highest age in the valuation mortality table), for an amount which is in accordance with the policy structure.[1] The guaranteed maturity premium is calculated at issue based on all policy guarantees at issue (excluding guarantees linked to an external referent). The guaranteed maturity premium for fixed premium universal life insurance policies shall be the premium defined in the policy which at issue provides the minimum policy guarantees.[2]

d. The letter "r" is equal to one, unless the policy is a flexible premium policy and the policy value is less than the guaranteed maturity fund, in which case "r" is the ratio of the policy value to the guaranteed maturity fund.

e. The guaranteed maturity fund at any duration is that amount which, together with future guaranteed maturity premiums, will mature the policy based on all policy guarantees at issue.

f. (C) is the quantity $((a)-(b))\frac{ä_{x+t}}{ä_x} r$ where (a)-(b) is as described in paragraph 9 of Appendix A-820 for the plan of insurance defined at issue by the guaranteed maturity premiums and all guarantees contained in the policy or declared by the insurer.

g. (D) is the sum of any additional quantities analogous to (C) which arise because of structural changes[3] in the policy, with each such quantity being determined on a basis consistent with that of (C) using the maturity date in effect at the time of the change.

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[1] The maturity amount shall be the initial death benefit where the death benefit is level over the lifetime of the policy except for the existence of a minimum-death-benefit corridor, or shall be the specified amount where the death benefit equals a specified amount plus the policy value or cash surrender value except for the existence of a minimum-death-benefit corridor.

[2] The Guaranteed Maturity Premium for both flexible and fixed premium policies shall be adjusted for death benefit corridors provided by the policy. The Guaranteed Maturity Premium may be less than the premium necessary to pay all charges. This can especially happen in the first year for policies with large first year expense charges.

[3] Structural changes are those changes which are separate from the automatic workings of the policy. Such changes usually would be initiated by the policyholder and include changes in the guaranteed benefits, changes in latest maturity date, or changes in allowable premium payment period. For fixed premium universal life policies with redetermination of all credits and charges no more frequently than annually, on policy anniversaries, structural changes also include changes in guaranteed benefits, or in fixed premiums, unanticipated by the guaranteed maturity premium for such policies at the date of issue, even if such changes arise from automatic workings of the policy. The recomputation of (B) in paragraph 8.a.ii. above, for fixed premium universal life structural changes, shall exclude from PVFB, the present value of future guaranteed benefits, those guaranteed benefits which are funded by the excess of the insurer's declared guarantees of interest, mortality and expenses, over the guarantees contained in the policy at the date of issue.

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h. The guaranteed maturity premium, the guaranteed maturity fund and (B) above shall be recalculated to reflect any structural changes in the policy. This recalculation shall be done in a manner consistent with the descriptions above.

i. Future guaranteed benefits are determined by (1) projecting the greater of the guaranteed maturity fund and the policy value, taking into account future guaranteed maturity premiums, if any, and using all guarantees of interest, mortality, expense deductions, etc., contained in the policy or declared by the insurer; and (2) taking into account any benefits guaranteed in the policy or by declaration which do not depend on the policy value.

j. All present values shall be determined using (i) an interest rate (or rates) specified by Appendix A-820 for policies issued in the same year; (ii) the mortality rates specified by Appendix A-820 for policies issued in the same year; and (iii) any other tables needed to value supplementary benefits provided by a rider which is being valued together with the policy.

9. To the extent that the insurer declares guarantees more favorable than those in the policy (contractual guarantees), such declared guarantees shall be applicable to the determination of future guaranteed benefits.

10. The mortality and interest bases for calculating present values are the minimum standards in Appendix A-820.

11. In effecting structural changes, consistent methods are prescribed when calculating reserves. Several such methods are possible, but perhaps the simplest such method would be that of maintaining proportionality between the Guaranteed Maturity Fund and Guaranteed Maturity Premium values and the current face amount. In applying this method, Guaranteed Maturity Fund and Guaranteed Maturity Premium values could be calculated per dollar of face amount and simply multiplied by the new face amount. This would eliminate much of the complexity involved in other methods.

Alternative Minimum Reserves

12. If, in any policy year, the guaranteed maturity premium on any universal life insurance policy is less than the valuation net premium for such policy, calculated by the valuation method actually used in calculating the reserve thereon but using the minimum valuation standards of mortality and rate of interest, the minimum reserve required for such contract shall be the greater of a. or b.

a. The reserve calculated according to the method, the mortality table, and the rate of interest actually used.

b. The reserve calculated according to the method actually used but using the minimum valuation standards of mortality and rate of interest and replacing the valuation net premium by the Guaranteed Maturity Premium in each policy year for which the valuation net premium exceeds the Guaranteed Maturity Premium.

13. For universal life insurance reserves on a net level premium basis, the valuation net premium is:

$$\frac{PVFB}{\ddot{a}x}$$

and for reserves on a Commissioners Reserve Valuation Method, the valuation net premium is:

$$\frac{PVFB}{\ddot{a}x} + \frac{(a)-(b)}{\ddot{a}x}$$

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Appendix A-588

Modified Guaranteed Life Insurance

The NAIC no longer maintains Model Law 588 as an NAIC sponsored model law; however, as this appendix is referenced in *SSAP No. 56—Separate Accounts,* the Statutory Accounting Principles (E) Working Group has chosen to retain this appendix as a valid NAIC standard.

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Interest Credits" means all interest that is credited to the policy.

2. "Modified Guaranteed Life Insurance Policy" means an individual or group policy of life insurance, the underlying assets which are held in a separate account, and the values of which are guaranteed if held for specified periods. It contains cash-surrender values that are based upon a market value adjustment formula if held for shorter periods. The formula may, or may not, reflect the value of assets held in the separate account. The assets underlying the policy must be in a separate account during the period or periods when the policyholder can surrender the policy.

3. "Policy processing day" means the day on which charges authorized in the policy are deducted from the policy's cash value.

4. "Separate account" means a separate account established pursuant to the insurance laws pertaining to the insurer.

Valuation Requirements

5. Reserve liabilities for modified guaranteed life insurance policies shall be established pursuant to the requirements of Appendix A-820 in accordance with actuarial procedures that recognize:

   a. That assets of the separate account are based on market value;

   b. The variable nature of the benefits provided; and

   c. Any mortality guarantees.

6. As a minimum, the separate account liability will equal the surrender value based upon the market value adjustment formula contained in the policy. If that liability is greater than the market value of the assets, a transfer of assets will be made into the separate account so that the market value of the assets at least equals that of the liabilities. Any additional reserve that is needed to cover future guaranteed benefits shall be established.

7. The market value adjustment formula, the interest guarantees and the degree to which projected cash flow of assets and liabilities are matched must also be considered. The company shall determine whether the assets in the separate account are adequate to provide all future guaranteed benefits.

8. Reserve liabilities for all fixed incidental insurance benefits and any guarantees associated with variable incidental insurance benefits shall be maintained in the general account.

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Separate Accounts

9. The insurer shall maintain in each separate account assets with a value at least equal to the valuation reserves and other contract liabilities respecting such account.

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Appendix A-620

Accelerated Benefits

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Purpose

The purpose of this Appendix is to provide guidance with respect to accelerated benefit related to individual and group life insurance policies. This Appendix shall apply to all accelerated benefits provisions of individual and group life insurance policies except those subject to Appendix A-641.

Definitions

1. "Accelerated benefits" covered under this Appendix are benefits payable under a life insurance contract:

    a. To a policyowner or certificateholder, during the lifetime of the insured, in anticipation of death or upon the occurrence of specified life-threatening or catastrophic conditions as defined by the policy or rider; and

    b. Which reduce the death benefit otherwise payable under the life insurance contract; and

    c. Which are payable upon the occurrence of a single qualifying event which results in the payment of a benefit amount fixed at the time of acceleration.

2. "Qualifying event" shall mean one or more of the following:

    a. A medical condition which would result in a drastically limited life span as specified in the contract, for example, twenty-four (24) months or less; or

    b. A medical condition which has required or requires extraordinary medical intervention, such as, but not limited to, major organ transplant or continuous artificial life support, without which the insured would die; or

    c. Any condition which usually requires continuous confinement in an eligible institution as defined in the contract if the insured is expected to remain there for the rest of his or her life; or

    d. A medical condition which would, in the absence of extensive or extraordinary medical treatment, result in a drastically limited life span. Such conditions may include, but are not limited to, one or more of the following:

        i. Coronary artery disease resulting in an acute infarction or requiring surgery;

        ii. Permanent neurological deficit resulting from cerebral vascular accident;

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iii. End stage renal failure; or

iv. Acquired Immune Deficiency Syndrome.

Valuation Requirements

3. When benefits are provided through the acceleration of benefits under group or individual life policies or riders to such policies, policy reserves shall be determined in accordance with Appendix A-820. Mortality tables and interest for life insurance reserves as specified in Appendix A-820 shall be used as well as appropriate assumptions for the other provisions incorporated in the policy form. Reserves in the aggregate should be sufficient to cover:

a. Policies upon which no claim has yet arisen.

b. Policies upon which an accelerated claim has arisen.

4. For policies and certificates which provide actuarially equivalent benefits, no additional reserves need to be established.

5. Policy liens and policy loans, including accrued interest, represent assets of the company for statutory reporting purposes. For any policy on which the policy lien exceeds the policy's statutory reserve liability such excess must be held as a nonadmitted asset.

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Appendix A-628

Title Insurance

Relevant SSAPs:
SSAP No. 57—Title Insurance

Definitions

1. "Abstract of title" or "abstract" means a written history, synopsis or summary of the recorded instruments affecting the title to real property.

2. "Affiliate" means a specific person that directly, or indirectly through one or more intermediaries, controls, or is controlled by or is under common control with the person specified.

3. "Bona fide employee" of the title insurer or title insurance agent means an individual who devotes substantially all of his or her time to performing services on behalf of a title insurer or title insurance agent and whose compensation for those services is in the form of salary or its equivalent paid by the title insurer or title insurance agent.

4. "Control" (including the terms "controlling," "controlled by" and "under common control with") means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position or corporate office held by the person. Control shall be presumed to exist if a person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent (10%) or more of the voting securities of another person. This presumption can be overcome by predominant evidence to the contrary; however, it shall stand until overcome by such predominant contradictory evidence.

5. "Escrow" means written instruments, money or other items deposited by one party with a depository, escrow agent or escrowee for delivery to another party upon the performance of a specified condition or the happening of a certain event.

6. "Escrow, settlement or closing fee" means the consideration for supervising or handling the actual execution, delivery or recording of transfer and lien documents and for disbursing funds.

7. "Net retained liability" means the total liability retained by a title insurer for a single risk, after taking into account any ceded liability and collateral, acceptable to the commissioner, maintained by the insurer.

8. "Person" means any natural person, partnership, association, cooperative, corporation, trust or other legal entity.

9. "Security" or "security deposit" means funds or other property received by the title insurer as collateral to secure an indemnitor's obligation under an indemnity agreement pursuant to which the insurer is granted a perfected security interest in the collateral in exchange for agreeing to provide coverage in a title insurance policy for a specific title exception to coverage.

10. "Title insurance agent" or "agent" means an authorized person, other than a bona fide employee of the title insurer who, on behalf of the title insurer, performs the following acts, in conjunction with the issuance of a title insurance report or policy:

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a. Determines insurability and issues title insurance reports or policies, or both, based upon the performance or review of a search or abstract of title; and

b. Performs one or more of the following functions:

i. Collects or disburses premiums, escrow or security deposits or other funds;

ii. Handles escrows, settlements or closings;

iii. Solicits or negotiates title insurance business; or

iv. Records closing documents.

11. "Title insurance business" or "business of title insurance" means:

a. Issuing as insurer or offering to issue as insurer a title insurance policy;

b. Transacting or proposing to transact by a title insurer any of the following activities when conducted or performed in contemplation of or in conjunction with the issuance of a title insurance policy:

i. Soliciting or negotiating the issuance of a title insurance policy;

ii. Guaranteeing, warranting or otherwise insuring the correctness of title searches for all instruments affecting titles to real property, any interest in real property, cooperative units and proprietary leases and for all liens or charges affecting the same;

iii. Handling of escrows, settlements or closings;

iv. Executing title insurance policies;

v. Effecting contracts of reinsurance; or

vi. Abstracting, searching or examining titles;

c. Guaranteeing, warranting or insuring searches or examinations of title to real property or any interest in real property; or

d. Guaranteeing or warranting the status of title as to ownership of or liens on real property and personal property by any person other than the principals to the transaction; or

e. Doing or proposing to do any business substantially equivalent to any of the activities listed in this paragraph in a manner designed to evade the provisions of this Appendix.

12. "Title insurance policy" or "policy" means a contract insuring or indemnifying owners of, or other persons lawfully interested in, real or personal property or any interest in real property, against loss or damage arising from any or all of the following conditions existing on or before the policy date and not excepted or excluded:

a. Defects in or liens or encumbrances on the insured title;

b. Unmarketability of the insured title;

c. Invalidity, lack of priority or unenforceability of liens or encumbrances on the stated property;

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d. Lack of legal right of access to the land; or

e. Unenforceability of rights in title to the land.

13. "Title insurance report" or "report" means a preliminary report, commitment or binder issued prior to the issuance of a title insurance policy containing the terms, conditions, exceptions and any other matters incorporated by reference under which the title insurer is willing to issue its title insurance policy.

14. "Title insurer" or "insurer" means a company organized for the purpose of transacting the business of title insurance.

15. "Title plant" means a set of records consisting of documents, maps, surveys or entries affecting title to real property or any interest in or encumbrance on the property, which have been filed or recorded in the jurisdiction for which the title plant is established or maintained.

Admitted Asset Standards

16. An investment in a title plant or plants in an amount equal to the actual cost shall be allowed as an admitted asset for title insurers. The aggregate amount of the investment shall not exceed the lesser of twenty percent (20%) of admitted assets or forty percent (40%) of surplus to policyholders, both as required to be shown on the statutory balance sheet of the insurer for its most recently filed statement with the domiciliary state commissioner; if the amount of the investment exceeds the above limits, the excess amount shall be recorded as a nonadmitted asset.

Reserves

17. A title insurer shall establish and maintain:

a. A known claim reserve in an amount estimated to be sufficient to cover all unpaid losses, claims and allocated loss adjustment expenses arising under title insurance policies, guaranteed certificates of title, guaranteed searches and guaranteed abstracts of title, and all unpaid losses, claims and allocated loss adjustment expenses for which the title insurer may be liable, and for which the insurer has received notice by or on behalf of the insured, holder of a guarantee or escrow or security depositor.

b. A Statutory or Unearned Premium Reserve consisting of:

i. The amount of the statutory or unearned premium or reinsurance reserve legally held at December 31, 2000. The balance of this reserve shall be released in accordance with the state laws in effect prior to January 1, 2001; and

ii. For those title insurance policies and guarantees written after January 1, 2001, reserves shall be established that are equal to the sum of the following items, as set forth in the title insurer's most recent annual statement:

(a) For each title insurance policy on a single risk written or assumed, an amount, as determined by the insurer's state of domicile, per $1,000 of net retained liability for policies under $500,000 and for policies of $500,000 or greater, or any other reasonable method as required by the insurer's state of domicile; and

(b) An amount as determined by the insurer's state of domicile for the escrow, settlement and closing fees collected in contemplation of the issuance of title insurance policies or guarantees.

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iii. The aggregate of the amounts set aside in this reserve in any calendar year pursuant to paragraph 17.b.ii. shall be released from the reserve and restored to net profits over a period of twenty (20) years pursuant to the following formula: thirty-five percent (35%) of the aggregate sum on July 1 of the year next succeeding the year of addition; fifteen percent (15%) of the aggregate sum on July 1 of each of the succeeding two (2) years; ten percent (10%) of the aggregate sum on July 1 of the next succeeding year; three percent (3%) of the aggregate sum on July 1 of each of the next three (3) succeeding years; two percent (2%) of the aggregate sum on July 1 of each of the next three (3) succeeding years; and one percent (1%) of the aggregate sum on July 1 of each of the next succeeding ten (10) years.

iv. The insurer shall calculate a retroactive adjusted statutory or unearned premium reserve on an aggregate basis at January 1, 2001. The adjusted aggregate reserve shall be calculated as if Subsection b. ii. had been in effect for all years beginning twenty (20) years prior to January 1, 2001. If the adjusted aggregate reserve exceeds the aggregate amount set aside for statutory or unearned premiums in the insurer's December 31, 2000 annual statement, the insurer shall–increase its statutory or unearned premium reserve by an amount equal to one-sixth of that excess in each of the succeeding six years, commencing with the 2001 calendar year.

v. The aggregate of the amounts set aside in this reserve in any calendar year as adjustments to the insurer's statutory or unearned premium reserve pursuant to Subsection b. iv. shall be released from the reserve and restored to net profits, or equity if the additions required by paragraph 17.b.iv. of this section reduced equity directly, over a period not exceeding ten (10) years pursuant to the following table:

Year of Addition	Release
2001	Equally over 10 years
2002	Equally over 9 years
2003	Equally over 8 years
2004	Equally over 7 years
2005	Equally over 6 years
2006	Equally over 5 years

c. A supplemental reserve shall be established consisting of any other reserves necessary, when taken in combination with the reserves required by paragraphs 17.a. and 17.b. to cover the company's liabilities with respect to all losses, claims and loss adjustment expenses.

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Appendix A-630

Mortgage Guaranty Insurance

Relevant SSAPs:
SSAP No. 58—Mortgage Guaranty Insurance

Definitions

1. "Mortgage guaranty insurance" is:

    a. Insurance against financial loss by reason of nonpayment of principal, interest or other sums agreed to be paid under the terms of any note or bond or other evidence of indebtedness secured by a mortgage, deed of trust, or other instrument constituting a lien or charge on real estate, provided the improvement on such real estate is a residential building or a condominium unit or buildings designed for occupancy by not more than four families.

    b. Insurance against financial loss by reason of nonpayment of principal, interest or other sums agreed to be paid under the terms of any note or bond or other evidence of indebtedness secured by a mortgage, deed of trust, or other instrument constituting a lien or charge on real estate, providing the improvement on such real estate is a building or buildings designed for occupancy by five (5) or more families or designed to be occupied for industrial or commercial purposes.

    c. Insurance against financial loss by reason of nonpayment of rent or other sums agreed to be paid under the terms of a written lease for the possession, use or occupancy of real estate, provided the improvement on such real estate is a building or buildings designed to be occupied for industrial or commercial purposes.

2. "Authorized real estate security" for the purpose of this Appendix means an amortized note, bond or other evidence of indebtedness, not exceeding ninety-five percent (95%) of the fair market value of the real estate, secured by a mortgage, deed of trust, or other instrument which constitutes, or is equivalent to, a first lien or charge on real estate; provided:

    a. The real estate loan secured in such manner is one of a type which a bank, savings and loan association, or an insurance company, which is supervised and regulated by a state department or the federal government, is authorized to make, or would be authorized to make, disregarding any requirement applicable to such an institution that the amount of the loan not exceed a certain percentage of the value of the real estate.

    b. The improvement on such real estate is a building or buildings designed for occupancy as specified by paragraphs 1.a. and 1.b. of this Appendix.

    c. The lien on such real estate may be subject to and subordinate to the following:

        i. The lien of any public bond, assessment or tax, when no installment, call or payment of or under such bond, assessment or tax is delinquent.

        ii. Outstanding mineral, oil, water or timber rights, rights-of-way, easements or rights-of-way of support, sewer rights, building restrictions or other restrictions or covenants, conditions or regulations of use, or outstanding leases upon such real property under which rents or profits are reserved to the owner thereof.

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3. "Contingency reserve" means an additional premium reserve established to protect policyholders against the effect of adverse economic cycles.

Investment Limitation

4. A mortgage guaranty insurance company shall not report as an admitted asset notes or other evidences of indebtedness secured by mortgage or other lien upon real property. This provision shall not apply to obligations secured by real property, or contracts for the sale of real property, which obligations or contracts of sale are acquired in the course of the good faith settlement of claims under policies of insurance issued by the mortgage guaranty insurance company, or in the good faith disposition of real property so acquired.

Reserves

5. Unearned Premium Reserves – A mortgage guaranty insurance company shall compute and maintain an unearned premium reserve.

6. Loss Reserve – A mortgage guaranty insurance company shall compute and maintain adequate case basis and other loss reserves which accurately reflect loss frequency and loss severity and shall include components for claims reported and for claims incurred but not reported, including estimated losses on:

a. Insured loans which have resulted in the conveyance of property which remains unsold;

b. Insured loans in the process of foreclosure;

c. Insured loans in default for four (4) months or for any lesser period which is defined as default for such purposes in the policy provisions; and

d. Insured leases in default for four (4) months or for any lesser period which is defined as default for such purposes in policy provisions.

7. Contingency Reserve – Each mortgage guaranty insurance company shall compute and maintain a contingency reserve.

8. Reinsurance – Whenever a mortgage guaranty insurance company obtains reinsurance from an insurance company which is properly licensed to provide such reinsurance or from an appropriate governmental agency, the mortgage guaranty insurer and the reinsurer shall establish and maintain the reserves required in this Appendix in appropriate proportions in relation to the risk retained by the original insurer and ceded to the assuming reinsurer so that the total reserves established shall not be less than the reserves required by this Appendix.

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Appendix A-641

Long-Term Care Insurance

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 54R—Individual and Group Accident and Health Contracts

Relevant NAIC Model Laws/Regulations:
Health Insurance Reserves Model Regulation (#010)
Standard Valuation Law (#820)

Definitions

1. "Long-term care insurance" means any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than twelve (12) consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis; for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital. Such term includes group and individual annuities and life insurance policies or riders which provide directly or which supplement long-term care insurance. Such term also includes a policy or rider which provides for payment of benefits based upon cognitive impairment or the loss of functional capacity. The term shall also include qualified long-term care insurance contracts. Long-term care insurance may be issued by insurers; fraternal benefit societies; nonprofit health, hospital, and medical service corporations; prepaid health plans; health maintenance organizations or any similar organization to the extent they are otherwise authorized to issue life or health insurance. Long-term care insurance shall not include any insurance policy which is offered primarily to provide basic Medicare supplement coverage, basic hospital expense coverage, basic medical-surgical expense coverage, hospital confinement indemnity coverage, major medical expense coverage, disability income or related asset-protection coverage, accident only coverage, specified disease or specified accident coverage, or limited benefit health coverage. With regard to life insurance, this term does not include life insurance policies which accelerate the death benefit specifically for one or more of the qualifying events of terminal illness, medical conditions requiring extraordinary medical intervention, or permanent institutional confinement, and which provide the option of a lump-sum payment for those benefits and in which neither the benefits nor the eligibility for the benefits is conditioned upon the receipt of long-term care. Notwithstanding any other provision contained herein, any product advertised, marketed or offered as long-term care insurance shall be subject to the provisions of this Appendix.

2. "Applicant" means:

   a. In the case of an individual long-term care insurance policy, the person who seeks to contract for benefits, and

   b. In the case of a group long-term care insurance policy, the proposed certificate holder.

3. "Certificate" means, for the purposes of this Appendix, any certificate issued under a group long-term care insurance policy, which policy has been delivered or issued for delivery.

4. "Group long-term care insurance" means a long-term care insurance policy which is delivered or issued for delivery to:

   a. One or more employers or labor organizations, or to a trust or to the trustees of a fund established by one or more employers or labor organizations, or a combination thereof, for employees or former employees or a combination thereof or for members or former members or a combination thereof, of the labor organizations; or

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b. Any professional, trade or occupational association for its members or former or retired members, or combination thereof, if such association:

i. Is composed of individuals all of whom are or were actively engaged in the same profession, trade or occupation; and

ii. Has been maintained in good faith for purposes other than obtaining insurance; or

c. An association or a trust or the trustee(s) of a fund established, created or maintained for the benefit of members of one or more associations. Prior to advertising, marketing or offering such policy, the association or associations, or the insurer of the association or associations, shall evidence that the association or associations have at the outset a minimum of 100 persons and have been organized and maintained in good faith for purposes other than that of obtaining insurance; have been in active existence for at least one year; and have a constitution and bylaws which provide that:

i. The association or associations hold regular meetings not less than annually to further purposes of the members;

ii. Except for credit unions, the association or associations collect dues or solicit contributions from members; and

iii. The members have voting privileges and representation on the governing board and committees.

5. "Policy" means, for the purposes of this Appendix, any policy, contract, subscriber agreement, rider or endorsement delivered or issued for delivery by an insurer; fraternal benefit society; nonprofit health, hospital, or medical service corporation; prepaid health plan; health maintenance organization or any similar organization.

6. a. "Qualified long-term care insurance contract" or "federally tax-qualified long-term care insurance contract" means an individual or group insurance contract that meets the requirements of Section 7702B(b) of the Internal Revenue Code of 1986, as amended, as follows:

i. The only insurance protection provided under the contract is coverage of qualified long-term care services. A contract shall not fail to satisfy the requirements of this subparagraph by reason of payments being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate;

ii. The contract does not pay or reimburse expenses incurred for services or items to the extent that the expenses are reimbursable under Title XVIII of the Social Security Act, as amended, or would be so reimbursable but for the application of a deductible or coinsurance amount. The requirements of this subparagraph do not apply to expenses that are reimbursable under Title XVIII of the Social Security Act only as a secondary payor. A contract shall not fail to satisfy the requirements of this subparagraph by reason of payments being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate;

iii. The contract is guaranteed renewable, within the meaning of section 7702B(b)(1)(C) of the Internal Revenue Code of 1986, as amended;

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iv. The contract does not provide for a cash surrender value or other money that can be paid, assigned, pledged as collateral for a loan, or borrowed except as provided in subparagraph 6.a.v. below;

v. All refunds of premiums, and all policyholder dividends or similar amounts, under the contract are to be applied as a reduction in future premiums or to increase future benefits, except that a refund on the event of death of the insured or a complete surrender or cancellation of the contract cannot exceed the aggregate premiums paid under the contract; and

vi. The contract meets the consumer protection provisions set forth in Section 7702B(g) of the Internal Revenue Code of 1986, as amended.

b. "Qualified long-term care insurance contract" or "federally tax-qualified long term care insurance contract" also means the portion of a life insurance contract that provides long-term care insurance coverage by rider or as part of the contract and that satisfies the requirements of Sections 7702B(b) and (e) of the Internal Revenue Code of 1986, as amended.

Valuation Requirements

7. When long-term care benefits are provided through the acceleration of benefits under group or individual life policies or riders to such policies, policy reserves for the benefits shall be determined in accordance with Appendix A-820. Claim reserves shall also be established in the case when the policy or rider is in claim status.

8. Reserves for policies and riders subject to this Appendix should be based on the multiple decrement model utilizing all relevant decrements except for voluntary termination rates. Single decrement approximations are acceptable if the calculation produces essentially similar reserves, if the reserve is clearly more conservative, or if the reserve is immaterial. The calculations may consider the reduction in life insurance benefits due to the payment of long-term care benefits. However, in no event shall the reserves for the long-term care benefit and the life insurance benefit be less than the reserves for the life insurance benefit assuming no long-term care benefit.

9. In the development and calculation of reserves for policies and riders subject to this Appendix, due regard shall be given to the applicable policy provisions, marketing methods, administrative procedures and all other considerations which have an impact on projected claim costs, including, but not limited to, the following:

a. Definition of insured events;

b. Covered long-term care facilities;

c. Existence of home convalescence care coverage;

d. Definition of facilities;

e. Existence or absence of barriers to eligibility;

f. Premium waiver provision;

g. Renewability;

h. Ability to raise premiums;

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i. Marketing method;

j. Underwriting procedures;

k. Claims adjustment procedures;

l. Waiting period;

m. Maximum benefit;

n. Availability of eligible facilities;

o. Margins in claim costs;

p. Optional nature of benefit;

q. Delay in eligibility for benefit;

r. Inflation protection provisions; and

s. Guaranteed insurability option.

10. When long-term care benefits are provided other than as in the above, reserves shall be determined in accordance with Appendix A-010.

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Appendix A-695

Synthetic Guaranteed Investment Contracts

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Actuarial Opinion and Memorandum Regulation (#822)

Scope and Application

1. This appendix applies to that portion of a group annuity contract or other agreement described in paragraph 25 and issued by a life insurer:

   a. That functions as an accounting record for an accumulation fund; and

   b. That has benefit guarantees relating to a principal amount and levels of interest at a fixed rate of return specified in advance.

2. The fixed rates of return:

   a. Shall be constant over the applicable rate periods;

   b. May reflect prior and current market conditions with respect to the segregated portfolio; and

   c. Shall not reference future changes in market conditions.

3. The updates to the appendix related to interest rates, including revisions to the method for determining the discount rate applied to the calculation of the minimum value of guaranteed contract liabilities, as primarily reflected in paragraph 29, and the definition of the blended spot rate are effective on or after January 1, 2016, for all[1] contracts inforce and contracts issued on or after the effective date.

Definitions

4. "Account assets" means the assets in the segregated portfolio plus any assets held in the general account or a separate account to meet the asset maintenance requirements.

5. "Actuarial opinion and memorandum" means the valuation actuary's opinion and memorandum covering synthetic guaranteed investment contract liabilities that is required to be submitted to the commissioner.

[1] This appendix is not intended to apply to contingent deferred annuities (CDAs), defined in the Contingent Deferred Annuity (A) Working Group recommendation on CDAs adopted by the Life Insurance and Annuities (A) Committee on April 7, 2013, (NAIC Proceedings, Spring 2013, Volume 1, pdf page 416) as "an annuity contract that establishes a life insurer's obligation to make periodic payments for the annuitant's lifetime at the time designated investments, which are not owned or held by the insurer, are depleted to a contractually defined amount due to contractually permitted withdrawals, market performance, fees and/or other charges."

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6. “Appointed actuary” means the qualified actuary appointed or retained either directly by or by the authority of the board of directors through an executive officer of the company to prepare the annual statement of actuarial opinion for the company as a whole.

7. “Asset maintenance requirement” means the requirement to maintain assets to fund contract benefits in accordance with paragraph 29 of this appendix.

8. “Class of contracts” means the set of all contracts to which a given plan of operation pertains.

9. “Contract value record” means an accounting record, provided by the contract in relation to a segregated portfolio of assets, that is credited with a fixed rate of return over regular periods, and that is used to measure the extent of the insurer’s obligation to the contractholder. The fixed rate of return credited to the contract value record is determined by means of a crediting rate formula or declared at the inception of the contract and valid for the entire term of the contract.

10. “Crediting rate formula” means a mathematical formula used to calculate the fixed rate of return credited to the contract value record during any rate period and based in part upon the difference between the contract value record and the market value record amortized over an appropriate period. The fixed rate of return calculated by means of this formula may reflect prior and current market conditions with respect to the segregated portfolio, but may not reference future changes in market conditions.

11. “Duration” means, with respect to the segregated portfolio assets or guaranteed contract liabilities, a measure of price sensitivity to changes in interest rates, such as the Macaulay duration or option-adjusted duration.

12. “Fair market value” means a reasonable estimate of the amount that a knowledgeable buyer of an asset would be willing to pay, and a knowledgeable seller of an asset would be willing to accept, for the asset without duress in an arm's length transaction. In the case of a publicly traded security, the fair market value is the price at which the security is traded or, if no price is available, a price that appropriately reflects the latest bid and asked prices for the security. In the case of a debt instrument that is not publicly traded, the fair market value is the discounted present value of the asset calculated at a reasonable discount rate. For all other non-publicly traded assets, fair market value will be determined in accordance with valuation practices customarily used within the financial industry.

13. “Guaranteed minimum benefits” means contract benefits on a specified date that may be either:

a. A principal guarantee, with or without a fixed minimum interest rate guarantee, related to the segregated portfolio;

b. An assurance as to the future investment return or performance of the segregated portfolio; or

c. The fair market value of the segregated portfolio, to the extent that the fair market value of the assets determines the contractholder’s benefits.

14. a. “Hedging instrument” means:

i. An interest rate futures agreement or foreign currency futures agreement, an option to purchase or sell an interest rate futures agreement or foreign currency futures agreement, or any option to purchase or sell a security or foreign currency, used in a bona fide hedging transaction; or

ii. A financial agreement or arrangement entered into with a broker, dealer or bank, qualified under applicable federal and state securities or banking law and regulation, in connection with investment in one or more securities in order to

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reduce the risk of changes in market valuation or to create a synthetic investment that, when added to the portfolio, reduces the risk of changes in market valuation.

b. An instrument shall not be considered a hedging instrument or a part of a bona fide hedging transaction if it is purchased in conjunction with another instrument where the effect of the combined transaction is an increase in the portfolio's exposure to market risk.

15. "Investment guidelines" means a set of written guidelines, established in advance by the person with investment authority over the segregated portfolio, to be followed by the investment manager. The guidelines shall include a description of:

a. The segregated portfolio's investment objectives and limitations;

b. The investment manager's degree of discretion;

c. The duration, asset class, quality, diversification, and other requirements of the segregated portfolio; and

d. The manner in which derivative instruments may be used, if at all, in the segregated portfolio.

16. "Investment manager" means the person (including the contractholder) responsible for managing the assets in the segregated portfolio in accordance with the investment guidelines in a fiduciary capacity to the owner of the assets.

17. "Market value record" means an accounting record provided by the contract to reflect the fair market value of the segregated portfolio.

18. "Nationally Recognized Statistical Rating Organization (NRSRO)" means a rating organization so designated by the Securities and Exchange Commission of the United States of America (SEC) which has applied to, and whose NRSRO status has been confirmed by, the NAIC Securities Valuation Office.

19. "Permitted custodial institution" means a bank, trust company or other licensed fiduciary services provider.

20. "Plan of operation" means a written plan meeting the requirements of paragraph 28 of this appendix.

21. "Qualified actuary" means an individual who meets the qualification standards set forth in Appendix A-820.

22. "Rate period" means the period of time during which the fixed rate of return credited to the contract value record is applicable between crediting rate formula adjustments.

23. "Segregated portfolio" means:

a. A portfolio or sub-portfolio of assets to which the contract pertains that is held in a custody or trust account by the permitted custodial institution and identified on the records of the permitted custodial institution as special custody assets held for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract; and

b. Any related cash or currency received by the permitted custodial institution for the account of the contractholder and held in a deposit account for the exclusive benefit of

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the retirement plans or other entities on whose behalf the contractholder holds the contract.

24. "Spot rate"

a. "Treasury-based spot rate" corresponding to a given time of benefit payment means the yield on a zero-coupon non-callable and non-prepayable United States government obligation maturing at that time, or the zero-coupon yield implied by the price of a representative sampling of coupon-bearing, non-callable and non-prepayable United States government obligations in accordance with a formula set forth in the plan of operation.

b. "Index spot rate" corresponding to a given time of benefit payment means the zero-coupon yield implied by (x) the Barclays Short-Term Corporate Index (for a given time of benefit payment under one year) or (y) the zero-coupon yield implied by the Barclays U.S. Corporate Investment Grade Bond Index (for a given time of benefit payment greater than or equal to one year).

c. "Blended spot rate" corresponding to a given time of benefit payment means a blend of 50% each of (i) the treasury-based spot rate, and (ii) the index spot rate. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country rated in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the NAIC Securities Valuation Office and are supported by investments denominated in the currency of the foreign country, the treasury-based spot rate component of the blended spot rate may be determined by reference to substantially similar obligations of the government of the foreign country.

25. "Synthetic guaranteed investment contract" or "contract" means a group annuity contract or other agreement that establishes the insurer's obligations by reference to a segregated portfolio of assets that is not owned by the insurer. The contract functions as an accounting record for an accumulation fund and the fixed rate of return credited to the fund reflects an amortization of the segregated portfolio's market gains and losses based on the period specified in the crediting formula, subject to any minimum interest rate guarantee.

26. "United States government obligation" means a direct obligation issued, assumed, guaranteed or insured by the United States of America or by an agency or instrumentality of the United States government.

27. "Valuation actuary" means the appointed actuary or, alternatively, a qualified actuary designated by the appointed actuary to render the actuarial opinion. Written documentation of any such designation shall be on file at the company and available for review upon request.

Plan of Operation

28. The plan of operation for a class of contracts shall describe the financial implications for the insurer of the issuance of contracts in the class, and shall include at least the following:

a. A statement describing the methods and procedures used to value statutory liabilities for purposes of paragraph 29;

b. A description of the allowable investment parameters (such as objectives, derivative strategies, asset classes, quality, duration and diversification requirements applied to the assets held within the segregated portfolio) to be reflected in the investment guidelines applicable to each contract issued in the class to which the submitted plan of operation applies; and a description of the procedures that will be followed by the insurer in

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evaluating the appropriateness of any specific investment guidelines submitted by the contractholder;

c. A description of the criteria used by the insurer in approving for contract issuance a pooled fund representing multiple employer-sponsored plans and in approving the investment manager for the segregated portfolio of assets associated with such pooled fund contract;

d. A description of risk-mitigation techniques used by the insurer in connection with contracts issued to pooled funds representing multiple employer-sponsored plans.

Reserves and Documentation

29. Asset maintenance requirements for segregated portfolios covered by this appendix.

a. At all times an insurer shall hold minimum reserves in the general account or one or more separate accounts, as appropriate, equal to the excess, if any, of the value of the guaranteed contract liabilities, determined in accordance with paragraphs 29.f. and 29.g., over the market value of the assets in the segregated portfolio less the deductions provided for in paragraph 29.b. These reserve requirements shall be applied on a contract-by-contract basis.

b. In determining compliance with the asset maintenance requirement and the reserve for guaranteed contract liabilities specified in paragraph 29.a., the insurer shall deduct a percentage of the market value of an asset as follows:

i. For debt instruments, the percentage shall be the NAIC asset valuation reserve "reserve objective factor," but the factor shall be increased by fifty percent (50%) for the purpose of this calculation if the difference in durations of the assets and liabilities is more than one-half year. The above notwithstanding, in the event that under the terms of the synthetic guaranteed investment contract, the asset default risk for debt instruments is borne solely by the contractholder, there shall be no asset valuation reserve percentage deduction from the market value of an asset, for purposes of complying with the asset maintenance requirement and the reserve for guaranteed contract liabilities specified in paragraph 29.a.

ii. For assets that are not debt instruments, the percentage shall be the NAIC asset valuation reserve “maximum reserve factor.”

c. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by segregated portfolio assets denominated in the currency of the foreign country, the percentage deduction for these assets under paragraph 29.b. shall be that for a substantially similar investment denominated in the currency of the United States.

d. To the extent that guaranteed contract liabilities are denominated in the currency of the United States and are supported by segregated portfolio assets denominated in the currency of a foreign country, and to the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by segregated portfolio assets denominated in the currency of the United States, the deduction for debt instruments under paragraph 29.b. shall be increased by fifteen percent (15%) of the market value of the assets unless the currency exchange risk on the assets has been adequately hedged, in which case the percentage deduction under paragraph 29.b. shall be increased by one-half percent (.5%). No guaranteed contract liabilities denominated in

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the currency of a foreign country shall be supported by segregated portfolio assets denominated in the currency of another foreign country. For purposes of this paragraph, the currency exchange risk on an asset is deemed to be adequately hedged if:

i. It is an obligation of

(a) A jurisdiction that is rated in one of the two (2) highest rating categories by an NRSRO;

(b) Any political subdivision or other governmental unit of such a jurisdiction, or any agency or instrumentality of jurisdiction, political subdivision or other governmental unit; or

(c) An institution that is organized under the laws of any such jurisdiction; and

ii. At all times the principal amount of the obligation and scheduled interest payments on the obligation are hedged against the United States dollar pursuant to contracts or agreements that are:

(a) Issued by or traded on a securities exchange or board of trade regulated under the laws of the United States or Canada or a province of Canada;

(b) Entered into with a United States banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an NRSRO, or with a broker-dealer registered with the Securities and Exchange Commission that has net capital in excess of $250 million; or

(c) Entered into with any other banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an NRSRO and that is organized under the laws of a jurisdiction that is rated in one of the two (2) highest rating categories by an NRSRO.

e. These contracts may provide for the allocation to one or more separate accounts of all or any portion of the amount needed to meet the asset maintenance requirement. If the contract provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurer, the insurer shall maintain in a distinct separate account that is so chargeable:

i. That portion of the amount needed to meet the asset maintenance requirement that has been allocated to separate accounts; less

ii. The amounts contributed to separate accounts by the contractholder in accordance with the contract and the earnings on the contract.

f. For purposes of this paragraph, the minimum value of guaranteed contract liabilities is defined to be the sum of the expected guaranteed contract benefits, each discounted at a rate corresponding to the expected time of payment of the contract benefit that is not greater than the spot rate supportable by the expected return from the segregated portfolio assets, and in no event greater than the blended spot rate as described in the plan of operation or the actuary's opinion and memorandum, except that if the expected time of

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payment of a contract benefit is more than thirty (30) years, it shall be discounted from the expected date of payment to year thirty (30) at a rate of no more than eighty percent (80%) of the thirty-year spot rate and from year thirty (30) to the date of valuation at a rate not greater than the thirty-year blended spot rate.

g. In calculating the minimum value of guaranteed contract benefits:

i. All guaranteed benefits potentially available to the contractholder on an ongoing basis shall be considered in the valuation process and analysis, and the reserve held must be sufficient to fund the greatest present value of each independent guaranteed contract benefit. For purposes of this subparagraph, the right granted to the contractholder to exit the contract by discharging the insurer of its guarantee obligation under the contract and taking control of the assets in the segregated portfolio shall not be considered a guaranteed benefit.

ii. To the extent that future guaranteed cash flows are dependent upon the benefit responsiveness of an employer-sponsored plan, a best estimate based on company experience, or other reasonable criteria if company experience is not available, shall be used in the projections of future cash flows.

iii. The minimum value of guaranteed contract benefits under a contract issued to a pooled fund representing multiple employer-sponsored plans shall be determined so as to reflect projected plan sponsor contract value withdrawals available to the member plans in the pooled fund.

Projections of such future cash flows shall take into account (i) known plan sponsor withdrawals, and (ii) a prudent estimate of future plan sponsor withdrawals. The prudent estimate shall be based on company experience and other relevant criteria.

A single valuation rate shall be determined, consistent with paragraph 29.f., equal to the lesser of:

(a) The expected return from the segregated portfolio of assets, or

(b) The blended spot rate based on the duration of the segregated portfolio of assets.

This single valuation rate shall be used to model future market values of the segregated portfolio of assets. Future credited interest rates shall be modeled according to the contractually defined crediting rate formula. Modeled future contract values shall reflect modeled future market values, modeled future credited interest rates, known future plan sponsor withdrawals, the prudent estimate of future plan sponsor withdrawals, future withdrawals consistent with paragraph 29.g.ii. of this subsection and any remaining final payment at the modeled contract termination date.

All such modeled withdrawals and termination payments shall be discounted using the single valuation rate and the modeled times of those withdrawals and payments. The sum of these present values shall be deemed the minimum value of the guaranteed contract liabilities for a pooled fund contract.

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30. Account assets shall make adequate provision for contract liabilities, taking into account any risk charge payable, the segregated portfolio assets, and the amount of any reserve liability with respect to the asset maintenance requirement.

31. The fixed-income segregated portfolio shall conform to and justify the rates used to discount contract liabilities for valuation pursuant to paragraph 29.f.

32. The company shall document whether any rates used pursuant to paragraph 29.f. to discount guaranteed contract liabilities and other items applicable to the segregated portfolio were modified from the rate or rates described in the plan of operation.

33. The level of risk charges, if any, retained in the general account shall be appropriate in view of such factors as the nature of the guaranteed contract liabilities and losses experienced in connection with account contracts and other pricing factors.

34. The company shall substantially conform with Appendix A-822 and maintain internal documentation to either:

a. Demonstrate the adequacy of account assets based upon cash flow analysis, or

b. Explain why cash flow testing analysis is not appropriate, describe the alternative methodology of asset adequacy testing used, and demonstrate the adequacy of account assets under that methodology;

35. The company's internal documentation pertaining to reserves for synthetic guaranteed investment contract liabilities shall also:

a. Clearly describe the assumptions used in projecting cash flows under each class of assets, and any dynamic portfolio hedging techniques utilized and the tests performed on the utilization of the techniques;

b. Clearly describe how the company has reflected the cost of capital;

c. Clearly describe how the company has reflected the risk of default on obligations and mortgage loans, including obligations and mortgage loans that are not investment grade;

d. Clearly describe how the company has reflected withdrawal risks, if applicable, including a discussion of the positioning of the contracts within the benefit withdrawal priority order pertaining to the contracts, the impact of any dynamic lapse assumption and the results of sensitivity testing the prudent estimate of future plan sponsor withdrawals pursuant to paragraph 29.g.iii.;

e. If the plan of operation provides for investments in segregated portfolio assets other than United States government obligations, demonstrate that the rates used to discount contract liabilities pursuant to paragraph 29.f. conservatively reflect expected investment returns, taking into account any foreign exchange risks;

f. If the contracts provide that in certain circumstances they would cease to be funded by a segregated portfolio and, instead would become contracts funded by the general account, clearly describe how any increased reserves would be provided for if and to the extent these circumstances occurred;

g. Document the amount of account assets maintained in a separate account that are not chargeable with liabilities arising out of any other business of the insurance company;

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h. Document the amount of reserves and supporting assets as of December 31 and where the reserves are shown in the annual statement;

i. Document the amount of any contingency reserve carried as part of surplus;

j. Document the market value of the segregated asset portfolio; and

k. Where separate account assets are not chargeable with liabilities arising out of any other business of the insurance company, describe how the level of risk charges payable to the general account provides an appropriate compensation for the risk taken by the general account.

36. When the insurer issues a synthetic guaranteed investment contract and complies with the asset maintenance requirements of paragraph 29, it need not maintain an asset valuation reserve with respect to those account assets.

37. This paragraph describes the reserve valuation requirements for contracts subject to this appendix.

a. Reserves for synthetic investment contracts subject to this appendix shall be an amount equal to the sum of the following:

i. The amounts determined as the minimum reserve as required under paragraph 29; and

ii. Any additional amount determined by the insurer's valuation actuary as necessary to make adequate provision for all contract liabilities.

b. The amount of any reserves required by paragraph 37.a. may be established by either:

i. Allocating sufficient assets to one or more separate accounts; or

ii. Setting up the additional reserves in the general account.

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Appendix A-785

Credit for Reinsurance

Relevant SSAPs:
SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance
SSAP No. 62R—Property and Casualty Reinsurance
SSAP No. 66—Retrospectively Rated Contracts

Definitions

1. "Commissioner" refers to the commissioner of insurance in the state where credit or a reduction from liability is taken.

2. "Jurisdiction" refers to any state, district or territory of the United States and also to territories, provinces or jurisdictions other than the United States.

3. "Liabilities" shall mean the assuming insurer's gross liabilities attributable to reinsurance ceded by U. S. domiciled insurers that are not otherwise secured by acceptable means.

4. "Beneficiary" means the entity for whose sole benefit the trust has been established and any successor of the beneficiary by operation of law. If a court of law appoints a successor in interest to the named beneficiary, then the named beneficiary includes and is limited to the court appointed domiciliary receiver (including conservator, rehabilitator or liquidator).

5. "Grantor" means the entity that has established a trust for the sole benefit of the beneficiary. When established in conjunction with a reinsurance agreement, the grantor is the unlicensed, unaccredited assuming insurer.

6. "Obligations," as used in paragraph 30 of this appendix means:

   a. Reinsured losses and allocated loss expenses paid by the ceding company, but not recovered from the assuming insurer;

   b. Reserves for reinsured losses reported and outstanding;

   c. Reserves for reinsured losses incurred but not reported; and

   d. Reserves for allocated reinsured loss expenses and unearned premiums.

Credit Allowed a Domestic Ceding Insurer

7. Credit for reinsurance shall be allowed a domestic ceding insurer as either an asset or a reduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of paragraphs 8, 9, 10, 11, 12, 13 or 14 of this appendix. Credit shall be allowed under paragraphs 8, 9, or 10 of this appendix only as respects cessions of those kinds or classes of business which the assuming insurer is licensed or otherwise allowed to write or assume in its state of domicile or, in the case of a U.S. branch of an alien assuming insurer, in the state through which it is entered and licensed to transact insurance or reinsurance. Credit shall be allowed under paragraphs 10 or 11 of this appendix only if the applicable requirements of paragraph 15 have been satisfied.

8. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is licensed to transact insurance or reinsurance in the domiciliary state of the ceding insurer.

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9. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is accredited as a reinsurer by the domiciliary state of the ceding insurer. In order to be eligible for accreditation, a reinsurer must:

a. File with the commissioner evidence of its submission to the domiciliary state's jurisdiction;

b. Submit to the domiciliary state's authority to examine its books and records;

c. Be licensed to transact insurance or reinsurance in at least one state, or in the case of a U.S. branch of an alien assuming insurer, is entered through and licensed to transact insurance or reinsurance in at least one state;

d. File annually with the commissioner a copy of its annual statement filed with the insurance department of its state of domicile and a copy of its most recent audited financial statement; and

e. Demonstrate to the satisfaction of the commissioner that it has adequate financial capacity to meet its reinsurance obligations and is otherwise qualified to assume reinsurance from domestic insurers. An assuming insurer is deemed to meet this requirement as of the time of its application if it maintains a surplus as regards policyholders in an amount not less than $20,000,000 and its accreditation has not been denied by the commissioner within ninety (90) days after submission of its application.

10. a. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is domiciled in, or in the case of a U.S. branch of an alien assuming insurer is entered through, a state that employs standards regarding credit for reinsurance substantially similar to those of the domiciliary state of the ceding insurer and the assuming insurer or U.S. branch of an alien assuming insurer:

i. Maintains a surplus as regards policyholders in an amount not less than $20,000,000; and

ii. Submits to the authority of the domiciliary state to examine its books and records.

b. The requirement of paragraph 10.a.i. does not apply to reinsurance ceded and assumed pursuant to pooling arrangements among insurers in the same holding company system.

11. a. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that maintains a trust fund in a qualified U.S. financial institution, as defined in paragraph 54, for the payment of the valid claims of its U.S. ceding insurers, their assigns and successors in interest. The assuming insurer shall report annually information substantially the same as that required to be reported on the NAIC Annual Statement form by licensed insurers. The assuming insurer shall submit to examination of its books and records by the commissioner and bear the expense of examination.

b. i. Credit for reinsurance shall not be granted under this paragraph 11 unless the form of the trust and any amendments to the trust have been approved by:

(a) The commissioner of the state where the trust is domiciled; or

(b) The commissioner of another state who, pursuant to the terms of the trust instrument, has accepted principal regulatory oversight of the trust.

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ii. The trust instrument shall provide that:

(a) Contested claims shall be valid and enforceable out of funds in trust to the extent remaining unsatisfied thirty (30) days after entry of the final order of any court of competent jurisdiction in the United States;

(b) Legal title to the assets of the trust shall be vested in the trustee for the benefit of the grantor's U.S. ceding insurers, their assigns and successors in interest;

(c) The trust shall be subject to examination as determined by the commissioner;

(d) The trust shall remain in effect for as long as the assuming insurer, or any member or former member of a group of insurers, shall have outstanding obligations under reinsurance agreements subject to the trust; and

(e) No later than February 28 of each year the trustee of the trust shall report to the commissioner in writing setting forth the balance in the trust and listing the trust's investments at the preceding year-end, and shall certify the date of termination of the trust, if so planned, or certify that the trust shall not expire prior to the following December 31.

c. The following requirements apply to the following categories of assuming insurer:

i. The trust fund for a single assuming insurer shall consist of funds in trust in an amount not less than the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers, and, in addition, the assuming insurer shall maintain a trusteed surplus of not less than $20,000,000, except as provided in paragraph 11.c.ii. of this appendix.

ii. At any time after the assuming insurer has permanently discontinued underwriting new business secured by the trust for at least three full years, the commissioner with principal regulatory oversight of the trust may authorize a reduction in the required trusteed surplus, but only after a finding, based on an assessment of the risk, that the new required surplus level is adequate for the protection of U.S. ceding insurers, policyholders and claimants in light of reasonably foreseeable adverse loss development. The risk assessment may involve an actuarial review, including an independent analysis of reserves and cash flows, and shall consider all material risk factors, including when applicable the lines of business involved, the stability of the incurred loss estimates and the effect of the surplus requirements on the assuming insurer's liquidity or solvency. The minimum required trusteed surplus may not be reduced to an amount less than thirty percent (30%) of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers covered by the trust.

iii. (a) In the case of a group including incorporated and individual unincorporated underwriters:

(1) For reinsurance ceded under reinsurance agreements with an inception, amendment or renewal date on or after January 1, 1993, the trust shall consist of a trusteed account in an amount not less than the respective underwriters' several liabilities

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attributable to business ceded by U.S. domiciled ceding insurers to any underwriter of the group;

(2) For reinsurance ceded under reinsurance agreements with an inception date on or before December 31, 1992, and not amended or renewed after that date, not-withstanding the other provisions contained herein, the trust shall consist of a trusteed account in an amount not less than the respective underwriters' several insurance and reinsurance liabilities attributable to business written in the United States; and

(3) In addition to these trusts, the group shall maintain in trust a trusteed surplus of which $100,000,000 shall be held jointly for the benefit of the U.S. domiciled ceding insurers of any member of the group for all years of account; and

(b) The incorporated members of the group shall not be engaged in any business other than underwriting as a member of the group and shall be subject to the same level of regulation and solvency control by the group's domiciliary regulator as are the unincorporated members.

(c) Within ninety (90) days after its financial statements are due to be filed with the group's domiciliary regulator, the group shall provide to the commissioner an annual certification by the group's domiciliary regulator of the solvency of each underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the group.

iv. In the case of a group of incorporated underwriters under common administration, the group shall:

(a) Have continuously transacted an insurance business outside the United States for at least three (3) years immediately prior to making application for accreditation;

(b) Maintain aggregate policyholders' surplus of at least $10,000,000,000;

(c) Maintain a trust fund in an amount not less than the group's several liabilities attributable to business ceded by U.S. domiciled ceding insurers to any member of the group pursuant to reinsurance contracts issued in the name of the group;

(d) In addition, maintain a joint trusteed surplus of which $100,000,000 shall be held jointly for the benefit of U.S. domiciled ceding insurers of any member of the group as additional security for these liabilities; and

(e) Within ninety (90) days after its financial statements are due to be filed with the group's domiciliary regulator, make available to the commissioner an annual certification of each underwriter member's solvency by the member's domiciliary regulator and financial statements of each underwriter member of the group prepared by its independent public accountant.

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d. For the purposes of this paragraph 11., the term "liabilities" shall mean the assuming insurer's gross liabilities attributable to reinsurance ceded by U.S. domiciled insurers excluding liabilities that are otherwise secured by acceptable means, and shall include:

i. For business ceded by domestic insurers authorized to write accident and health, and property and casualty insurance:

(a) Losses and allocated loss expenses paid by the ceding insurer, recoverable from the assuming insurer;

(b) Reserves for losses reported and outstanding;

(c) Reserves for losses incurred but not reported;

(d) Reserves for allocated loss expenses; and

(e) Unearned premiums.

ii. For business ceded by domestic insurers authorized to write life, health and annuity insurance:

(a) Aggregate reserves for life policies and contracts net of policy loans and net due and deferred premiums;

(b) Aggregate reserves for accident and health policies;

(c) Deposit funds and other liabilities without life or disability contingencies; and

(d) Liabilities for policy and contract claims.

12. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that has been certified as a reinsurer in the domestic state of the ceding insurer and secures its obligations in accordance with the requirements of this paragraph 12.

a. In order to be eligible for certification, the assuming insurer shall meet the following requirements:

i. The assuming insurer must be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction, as determined by the domestic state of the ceding insurer pursuant to paragraphs 12.c. and 12.k. of this subsection;

ii. The assuming insurer must maintain minimum capital and surplus, or its equivalent, in an amount as provided in paragraph 12.i.iii.(b) of this appendix;

iii. The assuming insurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the domestic state of the ceding insurer, as provided in paragraph 12.i.iii.(c) of this appendix;

iv. The assuming insurer must agree to submit to the jurisdiction of the domestic state of the ceding insurer, appoint the commissioner of the domestic state of the ceding insurer as its agent for service of process in that state, and agree to provide security for 100 percent of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers if it resists enforcement of a final U.S. judgment;

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v. The assuming insurer must agree to meet applicable information filing requirements as determined by the domestic state of the ceding insurer, both with respect to an initial application for certification and on an ongoing basis; and

vi. The assuming insurer must satisfy any other requirements for certification deemed relevant by the domestic state of the ceding insurer.

b. An association including incorporated and individual unincorporated underwriters may be a certified reinsurer. In order to be eligible for certification, in addition to satisfying requirements of paragraph 12.a. of this appendix:

i. The association shall satisfy its minimum capital and surplus requirements through the capital and surplus equivalents (net of liabilities) of the association and its members, which shall include a joint central fund that may be applied to any unsatisfied obligation of the association or any of its members, in an amount determined by the domestic state of the ceding insurer to provide adequate protection;

ii. The incorporated members of the association shall not be engaged in any business other than underwriting as a member of the association and shall be subject to the same level of regulation and solvency control by the association's domiciliary regulator as are the unincorporated members; and

iii. Within ninety (90) days after its financial statements are due to be filed with the association's domiciliary regulator, the association shall provide to the domestic state of the ceding insurer an annual certification by the association's domiciliary regulator of the solvency of each underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the association.

c. The domestic state of the ceding insurer shall create and publish a list of qualified jurisdictions, under which an assuming insurer licensed and domiciled in such jurisdiction is eligible to be considered for certification by the domestic state of the ceding insurer as a certified reinsurer.

i. In order to determine whether the domiciliary jurisdiction of a non-U.S. assuming insurer is eligible to be recognized as a qualified jurisdiction, the domestic state of the ceding insurer shall evaluate the appropriateness and effectiveness of the reinsurance supervisory system of the jurisdiction, both initially and on an ongoing basis, and consider the rights, benefits and the extent of reciprocal recognition afforded by the non-U.S. jurisdiction to reinsurers licensed and domiciled in the U.S. A qualified jurisdiction must agree to share information and cooperate with the domestic state of the ceding insurer with respect to all certified reinsurers domiciled within that jurisdiction. A jurisdiction may not be recognized as a qualified jurisdiction if the domestic state of the ceding insurer has determined that the jurisdiction does not adequately and promptly enforce final U.S. judgments and arbitration awards. Additional factors may be considered in the discretion of the domestic state of the ceding insurer.

ii. A list of qualified jurisdictions shall be published through the NAIC Committee Process. The domestic state of the ceding insurer shall consider this list in determining qualified jurisdictions. If the domestic state of the ceding insurer approves a jurisdiction as qualified that does not appear on the list of qualified

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jurisdictions, the state shall provide thoroughly documented justification in accordance with criteria to be developed under regulations.

iii. U.S. jurisdictions that meet the requirement for accreditation under the NAIC financial standards and accreditation program shall be recognized as qualified jurisdictions.

iv. If a certified reinsurer's domiciliary jurisdiction ceases to be a qualified jurisdiction, the domestic state of the ceding insurer has the discretion to suspend the reinsurer's certification indefinitely, in lieu of revocation.

d. The domestic state of the ceding insurer shall assign a rating to each certified reinsurer, giving due consideration to the financial strength ratings that have been assigned by rating agencies deemed acceptable to the commissioner pursuant to regulation. The domestic state of the ceding insurer shall publish a list of all certified reinsurers and their ratings.

e. A certified reinsurer shall secure obligations assumed from U.S. ceding insurers under this subsection at a level consistent with its rating, as specified in paragraph 12.h.i. of this appendix.

i. In order for a domestic ceding insurer to qualify for full financial statement credit for reinsurance ceded to a certified reinsurer, the certified reinsurer shall maintain security in a form acceptable to the domestic state of the ceding insurer and consistent with the provisions of paragraph 19 of this appendix, or in a multibeneficiary trust in accordance with paragraph 11 of this appendix, except as otherwise provided in paragraph 12.e.ii. through 12.e.v. of this appendix.

ii. If a certified reinsurer maintains a trust to fully secure its obligations subject to paragraph 11 of this appendix, and chooses to secure its obligations incurred as a certified reinsurer in the form of a multibeneficiary trust, the certified reinsurer shall maintain separate trust accounts for its obligations incurred under reinsurance agreements issued or renewed as a certified reinsurer with reduced security as permitted by paragraph 12, or comparable laws of other U.S. jurisdictions, and for its obligations subject to paragraph 11 of this appendix. It shall be a condition to the grant of certification under paragraph 12 of this appendix that the certified reinsurer shall have bound itself, by the language of the trust and agreement with the commissioner with principal regulatory oversight of each such trust account, to fund, upon termination of any such trust account, out of the remaining surplus of such trust any deficiency of any other such trust account.

iii. The minimum trusteed surplus requirements provided in paragraph 11 of this appendix are not applicable with respect to a multibeneficiary trust maintained by a certified reinsurer for the purpose of securing obligations incurred under this subsection, except that such trust shall maintain a minimum trusteed surplus of $10,000,000.

iv. With respect to obligations incurred by a certified reinsurer under paragraph 12 of this appendix, if the security is insufficient, the allowable reinsurance credit shall be reduced by an amount proportionate to the deficiency, and the domestic state of the ceding insurer has the discretion to impose further reductions in allowable credit upon finding that there is a material risk that the certified reinsurer's obligations will not be paid in full when due.

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v. For purposes of paragraph 12, a certified reinsurer whose certification has been terminated for any reason shall be treated as a certified reinsurer required to secure 100 percent of its obligations.

(a) As used in paragraph 12.e.v., the term "terminated" refers to revocation, suspension, voluntary surrender and inactive status.

(b) If the domestic state of the ceding insurer continues to assign a higher rating as permitted by other provisions of paragraph 12, this requirement does not apply to a certified reinsurer in inactive status or to a reinsurer whose certification has been suspended.

f. If an applicant for certification has been certified as a reinsurer in an NAIC accredited jurisdiction, the domestic state of the ceding insurer has the discretion to defer to that jurisdiction's certification, and has the discretion to defer to the rating assigned by that jurisdiction, and such assuming insurer shall be considered to be a certified reinsurer in the domestic state of the ceding insurer.

g. A certified reinsurer that ceases to assume new business in this state may request to maintain its certification in inactive status in order to continue to qualify for a reduction in security for its in-force business. An inactive certified reinsurer shall continue to comply with all applicable requirements of paragraph 12, and the domestic state of the ceding insurer shall assign a rating that takes into account, if relevant, the reasons why the reinsurer is not assuming new business.

h. The credit allowed under paragraph 12 shall be based upon the security held by or on behalf of the ceding insurer in accordance with a rating assigned to the certified reinsurer by the commissioner. The security shall be in a form consistent with the provisions of paragraph 12 and paragraph 19 of this appendix, and paragraphs 20-51 of this appendix, as applicable. The amount of security required in order for full credit to be allowed shall correspond with the following requirements:

i.

Ratings	**Security Required**
Secure – 1	0%
Secure – 2	10%
Secure – 3	20%
Secure – 4	50%
Secure – 5	75%
Vulnerable – 6	100%

ii. Affiliated reinsurance transactions shall receive the same opportunity for reduced security requirements as all other reinsurance transactions.

iii. The commissioner shall require the certified reinsurer to post one hundred percent (100%), for the benefit of the ceding insurer or its estate, security upon the entry of an order of rehabilitation, liquidation or conservation against the ceding insurer.

iv. In order to facilitate the prompt payment of claims, a certified reinsurer shall not be required to post security for catastrophe recoverables for a period of one year from the date of the first instance of a liability reserve entry by the ceding company as a result of a loss from a catastrophic occurrence as recognized by the commissioner. The one year deferral period is contingent upon the certified

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reinsurer continuing to pay claims in a timely manner. Reinsurance recoverables for only the following lines of business as reported on the NAIC annual financial statement related specifically to the catastrophic occurrence will be included in the deferral:

(a) Line 1: Fire

(b) Line 2: Allied Lines

(c) Line 3: Farmowners multiple peril

(d) Line 4: Homeowners multiple peril

(e) Line 5: Commercial multiple peril

(f) Line 9: Inland Marine

(g) Line 12: Earthquake

(h) Line 21: Auto physical damage

v. Credit for reinsurance under paragraph 12 of this appendix shall apply only to reinsurance contracts entered into or renewed on or after the effective date of the certification of the assuming insurer. Any reinsurance contract entered into prior to the effective date of the certification of the assuming insurer that is subsequently amended after the effective date of the certification of the assuming insurer, or a new reinsurance contract, covering any risk for which collateral was provided previously, shall only be subject to this section with respect to losses incurred and reserves reported from and after the effective date of the amendment or new contract.

vi. Nothing in paragraph 12 of this appendix shall prohibit the parties to a reinsurance agreement from agreeing to provisions establishing security requirements that exceed the minimum security requirements established for certified reinsurers under this section.

i. Certification Procedure

i. The commissioner of the domestic state of the ceding insurer shall post notice on the insurance department's website promptly upon receipt of any application for certification, including instructions on how members of the public may respond to the application. The commissioner may not take final action on the application until at least thirty (30) days after posting the notice required by this paragraph.

ii. The commissioner of the domestic state of the ceding insurer shall issue written notice to an assuming insurer that has made application and been approved as a certified reinsurer. Included in such notice shall be the rating assigned the certified reinsurer in accordance with paragraph 12.h. of this appendix. The commissioner shall publish a list of all certified reinsurers and their ratings.

iii. In order to be eligible for certification, the assuming insurer shall meet the following requirements:

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(a) The assuming insurer must be domiciled and licensed to transact insurance or reinsurance in a Qualified Jurisdiction, as determined by the commissioner pursuant to paragraph 12.c. and 12.k. of this appendix.

(b) The assuming insurer must maintain capital and surplus, or its equivalent, of no less than $250,000,000 calculated in accordance with paragraph 12.i.iv.(h) of this appendix. This requirement may also be satisfied by an association including incorporated and individual unincorporated underwriters having minimum capital and surplus equivalents (net of liabilities) of at least $250,000,000 and a central fund containing a balance of at least $250,000,000.

(c) The assuming insurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the commissioner. These ratings shall be based on interactive communication between the rating agency and the assuming insurer and shall not be based solely on publicly available information. These financial strength ratings will be one factor used by the commissioner in determining the rating that is assigned to the assuming insurer. Acceptable rating agencies include the following:

(1) Standard & Poor's;

(2) Moody's Investors Service;

(3) Fitch Ratings;

(4) A.M. Best Company; or

(5) Any other Nationally Recognized Statistical Rating Organization.

(d) The certified reinsurer must comply with any other requirements reasonably imposed by the commissioner of the domestic state of the ceding insurer.

iv. Each certified reinsurer shall be rated on a legal entity basis, with due consideration being given to the group rating where appropriate, except that an association including incorporated and individual unincorporated underwriters that has been approved to do business as a single certified reinsurer may be evaluated on the basis of its group rating. Factors that may be considered as part of the evaluation process include, but are not limited to, the following:

(a) The certified reinsurer's financial strength rating from an acceptable rating agency. The maximum rating that a certified reinsurer may be assigned will correspond to its financial strength rating as outlined in the table below. The commissioner shall use the lowest financial strength rating received from an approved rating agency in establishing the maximum rating of a certified reinsurer. A failure to obtain or maintain at least two financial strength ratings from acceptable rating agencies will result in loss of eligibility for certification:

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Ratings	Best	S&P	Moody's	Fitch
Secure – 1	A++	AAA	Aaa	AAA
Secure – 2	A+	AA+, AA, AA-	Aa1, Aa2, Aa3	AA+, AA, AA-
Secure – 3	A	A+, A	A1, A2	A+, A
Secure – 4	A-	A-	A3	A-
Secure – 5	B++, B+	BBB+, BBB, BBB-	Baa1, Baa2, Baa3	BBB+, BBB, BBB-
Vulnerable – 6	B, B-C++, C+, C, C-, D, E, F	BB+, BB, BB-, B+, B, B-, CCC, CC, C, D, R	Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, C	BB+, BB, BB-, B+, B, B-, CCC+, CC, CCC-, DD

(b) The business practices of the certified reinsurer in dealing with its ceding insurers, including its record of compliance with reinsurance contractual terms and obligations;

(c) For certified reinsurers domiciled in the U.S., a review of the most recent applicable NAIC annual statement blank, either Schedule F (for property/casualty reinsurers) or Schedule S (for life and health reinsurers);

(d) For certified reinsurers not domiciled in the U.S., a review annually of Form CR-F (for property/casualty reinsurers) or Form CR-S (for life and health reinsurers);

(e) The reputation of the certified reinsurer for prompt payment of claims under reinsurance agreements, based on an analysis of ceding insurers' Schedule F reporting of overdue reinsurance recoverables, including the proportion of obligations that are more than ninety (90) days past due or are in dispute, with specific attention given to obligations payable to companies that are in administrative supervision or receivership;

(f) Regulatory actions against the certified reinsurer;

(g) The report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in paragraph (h) below;

(h) For certified reinsurers not domiciled in the U.S., audited financial statements, regulatory filings, and actuarial opinion (as filed with the non-U.S. jurisdiction supervisor, with a translation into English). Upon the initial application for certification, the commissioner will consider

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audited financial statements for the last two (2) years filed with its non-U.S. jurisdiction supervisor;

(i) The liquidation priority of obligations to a ceding insurer in the certified reinsurer's domiciliary jurisdiction in the context of an insolvency proceeding;

(j) A certified reinsurer's participation in any solvent scheme of arrangement, or similar procedure, which involves U.S. ceding insurers. The commissioner shall receive prior notice from a certified reinsurer that proposes participation by the certified reinsurer in a solvent scheme of arrangement; and

(k) Any other information deemed relevant by the commissioner.

v. Based on the analysis conducted under paragraph 12.i.iv.(e) of a certified reinsurer's reputation for prompt payment of claims, the commissioner may make appropriate adjustments in the security the certified reinsurer is required to post to protect its liabilities to U.S. ceding insurers, provided that the commissioner shall, at a minimum, increase the security the certified reinsurer is required to post by one rating level under paragraph 12.h. if the commissioner finds that:

(a) more than fifteen percent (15%) of the certified reinsurer's ceding insurance clients have overdue reinsurance recoverables on paid losses of ninety (90) days or more which are not in dispute and which exceed $100,000 for each cedent; or

(b) the aggregate amount of reinsurance recoverables on paid losses which are not in dispute that are overdue by ninety (90) days or more exceeds $50,000,000.

vi. The assuming insurer must submit a properly executed Form CR-1 as evidence of its submission to the jurisdiction of this state, appointment of the commissioner as an agent for service of process in this state, and agreement to provide security for one hundred percent (100%) of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers if it resists enforcement of a final U.S. judgment. The commissioner shall not certify any assuming insurer that is domiciled in a jurisdiction that the commissioner has determined does not adequately and promptly enforce final U.S. judgments or arbitration awards.

vii. The certified reinsurer must agree to meet applicable information filing requirements as determined by the commissioner, both with respect to an initial application for certification and on an ongoing basis. All information submitted by certified reinsurers which are not otherwise public information subject to disclosure shall be exempted from disclosure under [cite state law equivalent of Freedom of Information Act] and shall be withheld from public disclosure. The applicable information filing requirements are, as follows:

(a) Notification within ten (10) days of any regulatory actions taken against the certified reinsurer, any change in the provisions of its domiciliary license or any change in rating by an approved rating agency, including a statement describing such changes and the reasons therefore;

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(b) Annually, Form CR-F or CR-S, as applicable;

(c) Annually, the report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in paragraph 12.i.vii.(d) below;

(d) Annually, the most recent audited financial statements, regulatory filings, and actuarial opinion (as filed with the certified reinsurer's supervisor, with a translation into English). Upon the initial certification, audited financial statements for the last two (2) years filed with the certified reinsurer's supervisor;

(e) At least annually, an updated list of all disputed and overdue reinsurance claims regarding reinsurance assumed from U.S. domestic ceding insurers;

(f) A certification from the certified reinsurer's domestic regulator that the certified reinsurer is in good standing and maintains capital in excess of the jurisdiction's highest regulatory action level; and

(g) Any other information that the commissioner may reasonably require.

j. Change in Rating or Revocation of Certification

i. In the case of a downgrade by a rating agency or other disqualifying circumstance, the commissioner shall upon written notice assign a new rating to the certified reinsurer in accordance with the requirements of paragraph 12.i.

ii. The commissioner shall have the authority to suspend, revoke, or otherwise modify a certified reinsurer's certification at any time if the certified reinsurer fails to meet its obligations or security requirements under this section, or if other financial or operating results of the certified reinsurer, or documented significant delays in payment by the certified reinsurer, lead the commissioner to reconsider the certified reinsurer's ability or willingness to meet its contractual obligations.

iii. If the rating of a certified reinsurer is upgraded by the commissioner, the certified reinsurer may meet the security requirements applicable to its new rating on a prospective basis, but the commissioner shall require the certified reinsurer to post security under the previously applicable security requirements as to all contracts in force on or before the effective date of the upgraded rating. If the rating of a certified reinsurer is downgraded by the commissioner, the commissioner shall require the certified reinsurer to meet the security requirements applicable to its new rating for all business it has assumed as a certified reinsurer.

iv. Upon revocation of the certification of a certified reinsurer by the commissioner, the assuming insurer shall be required to post security in accordance with paragraph 19 in order for the ceding insurer to continue to take credit for reinsurance ceded to the assuming insurer. If funds continue to be held in trust in accordance with paragraph 11, the commissioner may allow additional credit equal to the ceding insurer's *pro rata* share of such funds, discounted to reflect the risk of uncollectibility and anticipated expenses of trust administration. Notwithstanding the change of a certified reinsurer's rating or revocation of its certification, a domestic insurer that has ceded reinsurance to that certified

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reinsurer may not be denied credit for reinsurance for a period of three (3) months for all reinsurance ceded to that certified reinsurer, unless the reinsurance is found by the commissioner to be at high risk of uncollectibility.

k. Qualified Jurisdictions

i. If, upon conducting an evaluation with respect to the reinsurance supervisory system of any non-U.S. assuming insurer, the commissioner of the domestic state of the ceding insurer determines that the jurisdiction qualifies to be recognized as a qualified jurisdiction, the commissioner shall publish notice and evidence of such recognition in an appropriate manner. The commissioner may establish a procedure to withdraw recognition of those jurisdictions that are no longer qualified.

ii. In order to determine whether the domiciliary jurisdiction of a non-U.S. assuming insurer is eligible to be recognized as a qualified jurisdiction, the commissioner shall evaluate the reinsurance supervisory system of the non-U.S. jurisdiction, both initially and on an ongoing basis, and consider the rights, benefits and the extent of reciprocal recognition afforded by the non-U.S. jurisdiction to reinsurers licensed and domiciled in the U.S. The commissioner shall determine the appropriate approach for evaluating the qualifications of such jurisdictions, and create and publish a list of jurisdictions whose reinsurers may be approved by the commissioner as eligible for certification. A qualified jurisdiction must agree to share information and cooperate with the commissioner with respect to all certified reinsurers domiciled within that jurisdiction. Additional factors to be considered in determining whether to recognize a qualified jurisdiction, in the discretion of the commissioner, include but are not limited to the following:

(a) The framework under which the assuming insurer is regulated.

(b) The structure and authority of the domiciliary regulator with regard to solvency regulation requirements and financial surveillance.

(c) The substance of financial and operating standards for assuming insurers in the domiciliary jurisdiction.

(d) The form and substance of financial reports required to be filed or made publicly available by reinsurers in the domiciliary jurisdiction and the accounting principles used.

(e) The domiciliary regulator’s willingness to cooperate with U.S. regulators in general and the commissioner in particular.

(f) The history of performance by assuming insurers in the domiciliary jurisdiction.

(g) Any documented evidence of substantial problems with the enforcement of final U.S. judgments in the domiciliary jurisdiction. A jurisdiction will not be considered to be a qualified jurisdiction if the commissioner has determined that it does not adequately and promptly enforce final U.S. judgments or arbitration awards.

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(h) Any relevant international standards or guidance with respect to mutual recognition of reinsurance supervision adopted by the International Association of Insurance Supervisors or successor organization.

(i) Any other matters deemed relevant by the commissioner.

iii. A list of qualified jurisdictions shall be published through the NAIC Committee Process. The commissioner shall consider this list in determining qualified jurisdictions. If the commissioner approves a jurisdiction as qualified that does not appear on the list of qualified jurisdictions, the commissioner shall provide thoroughly documented justification with respect to the criteria provided under paragraphs 12.k.ii.(a) to (i).

iv. U.S. jurisdictions that meet the requirements for accreditation under the NAIC financial standards and accreditation program shall be recognized as qualified jurisdictions.

l. Recognition of Certification Issued by an NAIC Accredited Jurisdiction

i. If an applicant for certification has been certified as a reinsurer in an NAIC accredited jurisdiction, the commissioner has the discretion to defer to that jurisdiction's certification, and to defer to the rating assigned by that jurisdiction, if the assuming insurer submits a properly executed Form CR-1 and such additional information as the commissioner requires. The assuming insurer shall be considered to be a certified reinsurer in this State.

ii. Any change in the certified reinsurer's status or rating in the other jurisdiction shall apply automatically in this State as of the date it takes effect in the other jurisdiction. The certified reinsurer shall notify the commissioner of any change in its status or rating within 10 days after receiving notice of the change.

iii. The commissioner may withdraw recognition of the other jurisdiction's rating at any time and assign a new rating in accordance with paragraph 12.j. of this appendix.

iv. The commissioner may withdraw recognition of the other jurisdiction's certification at any time, with written notice to the certified reinsurer. Unless the commissioner suspends or revokes the certified reinsurer's certification in accordance with paragraph 12.j. of this appendix, the certified reinsurer's certification shall remain in good standing in the domestic state of the ceding insurer for a period of three (3) months, which shall be extended if additional time is necessary to consider the assuming insurer's application for certification in this State.

m. Mandatory Funding Clause. In addition to the clauses required under *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* and *SSAP No. 62R—Property and Casualty Reinsurance*, reinsurance contracts entered into or renewed under paragraph 12 of this appendix shall include a proper funding clause, which requires the certified reinsurer to provide and maintain security in an amount sufficient to avoid the imposition of any financial statement penalty on the ceding insurer under this section for reinsurance ceded to the certified reinsurer.

n. The commissioner shall comply with all reporting and notification requirements that may be established by the NAIC with respect to certified reinsurers and qualified jurisdictions.

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13. Credit shall be allowed when the reinsurance is ceded to an assuming insurer meeting each of the conditions set forth in paragraphs 13.a. through 13.h. Credit shall be allowed for reinsurance ceded by a domestic insurer to an assuming insurer that is licensed to write reinsurance by, and has its head office or is domiciled in, a Reciprocal Jurisdiction, and which meets the other requirements of paragraph 13.

a. The assuming insurer must have its head office or be domiciled in, as applicable, and be licensed in a Reciprocal Jurisdiction. A "Reciprocal Jurisdiction" is a jurisdiction that meets one of the following:

i. A non-U.S. jurisdiction that is subject to an in-force covered agreement with the United States, each within its legal authority or, in the case of a covered agreement between the United States and European Union, is a member state of the European Union. For purposes of this subsection, a "covered agreement" is an agreement entered into pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act, 31 U.S.C. §§ 313 and 314, that is currently in effect or in a period of provisional application and addresses the elimination, under specified conditions, of collateral requirements as a condition for entering into any reinsurance agreement with a ceding insurer domiciled in this state or for allowing the ceding insurer to recognize credit for reinsurance;

ii. A U.S. jurisdiction that meets the requirements for accreditation under the NAIC financial standards and accreditation program; or

iii. A qualified jurisdiction, as determined by the commissioner, which is not otherwise described in paragraphs 13.a.i. or 13.a.ii. and which the commissioner determines meets all of the following additional requirements:

(a) Provides that an insurer which has its head office or is domiciled in such qualified jurisdiction shall receive credit for reinsurance ceded to a U.S.-domiciled assuming insurer in the same manner as credit for reinsurance is received for reinsurance assumed by insurers domiciled in such qualified jurisdiction;

(b) Does not require a U.S.-domiciled assuming insurer to establish or maintain a local presence as a condition for entering into a reinsurance agreement with any ceding insurer subject to regulation by the non-U.S. jurisdiction or as a condition to allow the ceding insurer to recognize credit for such reinsurance;

(c) Recognizes the U.S. state regulatory approach to group supervision and group capital, by providing written confirmation by a competent regulatory authority, in such qualified jurisdiction, that insurers and insurance groups that are domiciled or maintain their headquarters in this state or another jurisdiction accredited by the NAIC shall be subject only to worldwide prudential insurance group supervision including worldwide group governance, solvency and capital, and reporting, as applicable, by the commissioner or the commissioner of the domiciliary state and will not be subject to group supervision at the level of the worldwide parent undertaking of the insurance or reinsurance group by the qualified jurisdiction; and

(d) Provides written confirmation by a competent regulatory authority in such qualified jurisdiction that information regarding insurers and their parent, subsidiary, or affiliated entities, if applicable, shall be provided to

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the commissioner in accordance with a memorandum of understanding or similar document between the commissioner and such qualified jurisdiction, including but not limited to the International Association of Insurance Supervisors Multilateral Memorandum of Understanding or other multilateral memoranda of understanding coordinated by the NAIC.

b. The assuming insurer must have and maintain on an ongoing basis minimum capital and surplus, or its equivalent, calculated on at least an annual basis as of the preceding December 31 or at the annual date otherwise statutorily reported to the Reciprocal Jurisdiction, and confirmed as set forth in paragraph 13.g. according to the methodology of its domiciliary jurisdiction, in the following amounts:

i. No less than $250,000,000; or

ii. If the assuming insurer is an association, including incorporated and individual unincorporated underwriters:

(a) Minimum capital and surplus equivalents (net of liabilities) or own funds of the equivalent of at least $250,000,000; and

(b) A central fund containing a balance of the equivalent of at least $250,000,000.

c. The assuming insurer must have and maintain on an ongoing basis a minimum solvency or capital ratio, as applicable, as follows:

i. If the assuming insurer has its head office or is domiciled in a Reciprocal Jurisdiction as defined in paragraph 13.a.i., the ratio specified in the applicable covered agreement;

ii. If the assuming insurer is domiciled in a Reciprocal Jurisdiction as defined in paragraph 13.a.ii., a risk-based capital (RBC) ratio of three hundred percent (300%) of the authorized control level, calculated in accordance with the formula developed by the NAIC; or

iii. If the assuming insurer is domiciled in a Reciprocal Jurisdiction as defined in paragraph 13.a.iii., after consultation with the Reciprocal Jurisdiction and considering any recommendations published through the NAIC Committee Process, such solvency or capital ratio as the commissioner determines to be an effective measure of solvency.

d. The assuming insurer must agree and provide adequate assurance to the commissioner, in a form of a properly executed Form RJ-1, as follows:

i. The assuming insurer must provide prompt written notice and explanation to the commissioner if it falls below the minimum requirements set forth in paragraphs 13.b. or 13.c., or if any regulatory action is taken against it for serious noncompliance with applicable law;

ii. The assuming insurer must consent in writing to the jurisdiction of the courts of this state and to the appointment of the commissioner as agent for service of process. The commissioner may require that consent for service of process be provided to the commissioner and included in each reinsurance agreement. Nothing in this provision shall limit, or in any way alter, the capacity of parties to

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a reinsurance agreement to agree to alternative dispute resolution mechanisms, except to the extent such agreements are unenforceable under applicable insolvency or delinquency laws;

iii. The assuming insurer must consent in writing to pay all final judgments, wherever enforcement is sought, obtained by a ceding insurer or its legal successor, that have been declared enforceable in the jurisdiction where the judgment was obtained;

iv. Each reinsurance agreement must include a provision requiring the assuming insurer to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities attributable to reinsurance ceded pursuant to that agreement if the assuming insurer resists enforcement of a final judgment that is enforceable under the law of the jurisdiction in which it was obtained or a properly enforceable arbitration award, whether obtained by the ceding insurer or by its legal successor on behalf of its resolution estate; and

v. The assuming insurer must confirm that it is not presently participating in any solvent scheme of arrangement which involves this state's ceding insurers, and agree to notify the ceding insurer and the commissioner and to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities to the ceding insurer, should the assuming insurer enter into such a solvent scheme of arrangement. Such security shall be in a form consistent with the provisions of paragraph 12 and paragraph 19. The term "solvent scheme of arrangement" means a foreign or alien statutory or regulatory compromise procedure subject to requisite majority creditor approval and judicial sanction in the assuming insurer's home jurisdiction either to finally commute liabilities of duly noticed classed members or creditors of a solvent debtor, or to reorganize or restructure the debts and obligations of a solvent debtor on a final basis, and which may be subject to judicial recognition and enforcement of the arrangement by a governing authority outside the ceding insurer's home jurisdiction.

vi. The assuming insurer must agree in writing to meet the applicable information filing requirements as set forth in paragraph 13.e.

e. The assuming insurer or its legal successor must provide, if requested by the commissioner, on behalf of itself and any legal predecessors, the following documentation to the commissioner:

i. For the two years preceding entry into the reinsurance agreement and on an annual basis thereafter, the assuming insurer's annual audited financial statements, in accordance with the applicable law of the jurisdiction of its head office or domiciliary jurisdiction, as applicable, including the external audit report;

ii. For the two years preceding entry into the reinsurance agreement, the solvency and financial condition report or actuarial opinion, if filed with the assuming insurer's supervisor;

iii. Prior to entry into the reinsurance agreement and not more than semi-annually thereafter, an updated list of all disputed and overdue reinsurance claims outstanding for 90 days or more, regarding reinsurance assumed from ceding insurers domiciled in the United States; and

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iv. Prior to entry into the reinsurance agreement and not more than semi-annually thereafter, information regarding the assuming insurer's assumed reinsurance by ceding insurer, ceded reinsurance by the assuming insurer, and reinsurance recoverable on paid and unpaid losses by the assuming insurer to allow for the evaluation of the criteria set forth in paragraph 13.f.

f. The assuming insurer must maintain a practice of prompt payment of claims under reinsurance agreements. The lack of prompt payment will be evidenced if any of the following criteria is met:

i. More than fifteen percent (15%) of the reinsurance recoverables from the assuming insurer are overdue and in dispute as reported to the commissioner;

ii. More than fifteen percent (15%) of the assuming insurer's ceding insurers or reinsurers have overdue reinsurance recoverable on paid losses of 90 days or more which are not in dispute and which exceed for each ceding insurer $100,000, or as otherwise specified in a covered agreement; or

iii. The aggregate amount of reinsurance recoverable on paid losses which are not in dispute, but are overdue by 90 days or more, exceeds $50,000,000, or as otherwise specified in a covered agreement.

g. The assuming insurer's supervisory authority must confirm to the commissioner on an annual basis, as of the preceding December 31 or at the annual date otherwise statutorily reported to the Reciprocal Jurisdiction, that the assuming insurer complies with the requirements set forth in paragraphs 13.b. and 13.c.

h. Nothing in this provision precludes an assuming insurer from providing the commissioner with information on a voluntary basis.

i. The commissioner shall timely create and publish a list of Reciprocal Jurisdictions.

i. A list of Reciprocal Jurisdictions is published through the NAIC Committee Process. The commissioner's list shall include any Reciprocal Jurisdiction as defined under paragraphs 13.a.i. and 13.a.ii., and shall consider any other Reciprocal Jurisdiction included on the NAIC list. The commissioner may approve a jurisdiction that does not appear on the NAIC list of Reciprocal Jurisdictions.

ii. The commissioner may remove a jurisdiction from the list of Reciprocal Jurisdictions upon a determination that the jurisdiction no longer meets one or more of the requirements of a Reciprocal Jurisdiction, except that the commissioner shall not remove from the list a Reciprocal Jurisdiction as defined under paragraphs 13.a.i. and 13.a.ii. Upon removal of a Reciprocal Jurisdiction from this list credit for reinsurance ceded to an assuming insurer domiciled in that jurisdiction shall be allowed, if otherwise allowed pursuant to this appendix.

j. The commissioner shall timely create and publish a list of assuming insurers that have satisfied the conditions set forth in paragraph 13 and to which cessions shall be granted credit in accordance with paragraph 13.

i. If an NAIC accredited jurisdiction has determined that the conditions set forth in paragraph 13 have been met, the commissioner has the discretion to defer to that jurisdiction's determination, and add such assuming insurer to the list of assuming insurers to which cessions shall be granted credit in accordance with

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this subsection. The commissioner may accept financial documentation filed with another NAIC accredited jurisdiction or with the NAIC in satisfaction of the requirements of paragraph 13.b., 13.c. and 13.d.

ii. When requesting that the commissioner defer to another NAIC accredited jurisdiction's determination, an assuming insurer must submit a properly executed Form RJ-1 and additional information as the commissioner may require. A state that has received such a request will notify other states through the NAIC Committee Process and provide relevant information with respect to the determination of eligibility.

k. If the commissioner determines that an assuming insurer no longer meets one or more of the requirements under this section, the commissioner may revoke or suspend the eligibility of the assuming insurer for recognition under this section.

i. While an assuming insurer's eligibility is suspended, no reinsurance agreement issued, amended or renewed after the effective date of the suspension qualifies for credit except to the extent that the assuming insurer's obligations under the contract are secured in accordance with paragraph 19.

ii. If an assuming insurer's eligibility is revoked, no credit for reinsurance may be granted after the effective date of the revocation with respect to any reinsurance agreements entered into by the assuming insurer, including reinsurance agreements entered into prior to the date of revocation, except to the extent that the assuming insurer's obligations under the contract are secured in a form acceptable to the commissioner and consistent with the provisions of paragraph 19.

l. Before denying statement credit or imposing a requirement to post security with respect to paragraph 13.k. or adopting any similar requirement that will have substantially the same regulatory impact as security, the commissioner shall:

i. Communicate with the ceding insurer, the assuming insurer, and the assuming insurer's supervisory authority that the assuming insurer no longer satisfies one of the conditions listed in paragraphs 13.a., 13.b. and 13.c.;

ii. Provide the assuming insurer with 30 days from the initial communication to submit a plan to remedy the defect, and 90 days from the initial communication to remedy the defect, except in exceptional circumstances in which a shorter period is necessary for policyholder and other consumer protection;

iii. After the expiration of 90 days or less, as set out in paragraph 13.l.ii., if the commissioner determines that no or insufficient action was taken by the assuming insurer, the commissioner may impose any of the requirements as set out in this subsection; and

iv. Provide a written explanation to the assuming insurer of any of the requirements set out in paragraph 13.l.

m. If subject to a legal process of rehabilitation, liquidation or conservation, as applicable, the ceding insurer, or its representative, may seek and, if determined appropriate by the court in which the proceedings are pending, may obtain an order requiring that the assuming insurer post security for all outstanding liabilities.

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n. Nothing in this subsection shall limit or in any way alter the capacity of parties to a reinsurance agreement to agree on requirements for security or other terms in that reinsurance agreement, except as expressly prohibited by this appendix.

o. Credit may be taken under this subsection only for reinsurance agreements entered into, amended, or renewed on or after the effective date of the statute adding this subsection, and only with respect to losses incurred and reserves reported on or after the later of (i) the date on which the assuming insurer has met all eligibility requirements pursuant to paragraphs 13.a. through 13.h., and (ii) the effective date of the new reinsurance agreement, amendment, or renewal.

i. This paragraph does not alter or impair a ceding insurer's right to take credit for reinsurance, to the extent that credit is not available under this subsection, as long as the reinsurance qualifies for credit under any other applicable provision of this appendix.

ii. Nothing in this subsection shall authorize an assuming insurer to withdraw or reduce the security provided under any reinsurance agreement except as permitted by the terms of the agreement.

iii. Nothing in this subsection shall limit, or in any way alter, the capacity of parties to any reinsurance agreement to renegotiate the agreement.

14. Credit shall be allowed when the reinsurance is ceded to an assuming insurer not meeting the requirements of paragraphs 8, 9, 10, 11, 12 or 13 of this appendix, but only as to the insurance of risks located in jurisdictions where the reinsurance is required by applicable law or regulation of that jurisdiction.

15. If the assuming insurer is not licensed, accredited or certified to transact insurance or reinsurance in the domiciliary state of the ceding insurer, the credit allowed by paragraphs 10 and 11 of this appendix shall not be allowed unless the assuming insurer agrees in the reinsurance agreements:

a. i. That in the event of the failure of the assuming insurer to perform its obligations under the terms of the reinsurance agreement, the assuming insurer, at the request of the ceding insurer, shall submit to the jurisdiction of any court of competent jurisdiction in any state of the United States, will comply with all requirements necessary to give the court jurisdiction, and will abide by the final decision of the court or of any appellate court in the event of an appeal.

ii. To designate the commissioner or a designated attorney as its true and lawful attorney upon whom may be served any lawful process in any action, suit or proceeding instituted by or on behalf of the ceding insurer.

b. This paragraph 15 is not intended to conflict with or override the obligation of the parties to a reinsurance agreement to arbitrate their disputes, if this obligation is created in the agreement.

16. If the assuming insurer does not meet the requirements of paragraphs 8, 9 or 10, the credit allowed by paragraph 11 or 12 of this appendix shall not be allowed unless the assuming insurer agrees in the trust agreements to the following conditions:

a. Notwithstanding any other provisions in the trust instrument, if the trust fund is inadequate because it contains an amount less than the amount required by paragraph 11 c. of this appendix, or if the grantor of the trust has been declared insolvent or placed into

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receivership, rehabilitation, liquidation or similar proceedings under the laws of its state or country of domicile, the trustee shall comply with an order of the commissioner with regulatory oversight over the trust or with an order of a court of competent jurisdiction directing the trustee to transfer to the commissioner with regulatory oversight all of the assets of the trust fund.

b. The assets shall be distributed by and claims shall be filed with and valued by the commissioner with regulatory oversight in accordance with the laws of the state in which the trust is domiciled that are applicable to the liquidation of domestic insurance companies.

c. If the commissioner with regulatory oversight determines that the assets of the trust fund or any part thereof are not necessary to satisfy the claims of the U.S. ceding insurers of the grantor of the trust, the assets or part thereof shall be returned by the commissioner with regulatory oversight to the trustee for distribution in accordance with the trust agreement.

d. The grantor shall waive any right otherwise available to it under U.S. law that is inconsistent with this provision.

17. If an accredited or certified reinsurer ceases to meet the requirements for accreditation or certification, the domestic state of the ceding insurer may suspend or revoke the reinsurer's accreditation or certification.

a. The domestic state of the ceding insurer must give the reinsurer notice an opportunity for hearing. The suspension or revocation may not take effect until after the state's order on hearing, unless:

i. The reinsurer waives its right to hearing;

ii. The state's order is based on regulatory action by the reinsurer's domiciliary jurisdiction or the voluntary surrender or termination of the reinsurer's eligibility to transact insurance or reinsurance business in its domiciliary jurisdiction or in the primary certifying state of the reinsurer under paragraph 12.f. of this appendix; or

iii. The domestic state of the ceding insurer finds that an emergency requires immediate action and a court of competent jurisdiction has not stayed the state's action.

b. While a reinsurer's accreditation or certification is suspended, no reinsurance contract issued or renewed after the effective date of the suspension qualifies for credit except to the extent that the reinsurer's obligations under the contract are secured in accordance with paragraph 19. If a reinsurer's accreditation or certification is revoked, no credit for reinsurance may be granted after the effective date of the revocation except to the extent that the reinsurer's obligations under the contract are secured in accordance with paragraph 12.e. or paragraph 19.

Valuation of and Requirements for Trust Assets

18. Assets deposited in the trust shall be valued according to their current fair market value and shall consist only of cash in U.S. dollars, certificates of deposit issued by a U.S. financial institution as defined in paragraph 53, clean, irrevocable, unconditional and "evergreen" letters of credit issued or confirmed by a qualified U.S. financial institution, as defined in paragraph 53, and investments of the type specified in this paragraph, but investments in or issued by an entity controlling, controlled by or under common

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control with either the grantor or beneficiary of the trust shall not exceed five percent (5%) of total investments. No more than twenty percent (20%) of the total of the investments in the trust may be foreign investments authorized under paragraphs 18.a.v., 18.c., 18.f.ii. or 18.g., and no more than ten percent (10%) of the total of the investments in the trust may be securities denominated in foreign currencies. For purposes of applying the preceding sentence, a depository receipt denominated in U.S. dollars and representing rights conferred by a foreign security shall be classified as a foreign investment denominated in a foreign currency. The assets of a trust shall be invested only as follows:

a. Government obligations that are not in default as to principal or interest, that are valid and legally authorized and that are issued, assumed or guaranteed by:

i. The United States or by any agency or instrumentality of the United States;

ii. A state of the United States;

iii. A territory, possession or other governmental unit of the United States;

iv. An agency or instrumentality of a governmental unit referred to in paragraphs 18.a.i. and 18.a.ii. if the obligations shall be by law (statutory of otherwise) payable, as to both principal and interest, from taxes levied or by law required to be levied or from adequate special revenues pledged or otherwise appropriated or by law required to be provided for making these payments, but shall not be obligations eligible for investment under this paragraph if payable solely out of special assessments on properties benefited by local improvements; or

v. The government of any other country that is a member of the Organization for Economic Cooperation and Development and whose government obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC;

b. Obligations that are issued in the United States, or that are dollar denominated and issued in a non-U.S. market, by a solvent U.S. institution (other than an insurance company) or that are assumed or guaranteed by a solvent U.S. institution (other than an insurance company) and that are not in default as to principal or interest if the obligations:

i. Are rated A or higher (or the equivalent) by a securities rating agency recognized by the Securities Valuation Office of the NAIC, or if not so rated, are similar in structure and other material respects to other obligations of the same institution that are so rated;

ii. Are insured by at least one authorized insurer (other than the investing insurer or a parent, subsidiary or affiliate of the investing insurer) licensed to insure obligations in this state and, after considering the insurance, are rated AAA (or the equivalent) by a securities rating agency recognized by the Securities Valuation Office of the NAIC; or

iii. Have been designated as Class One or Class Two by the Securities Valuation Office of the NAIC;

c. Obligations issued, assumed or guaranteed by a solvent non U.S. institution chartered in a country that is a member of the Organization for Economic Cooperation and Development or obligations of U.S. corporations issued in a non-U.S. currency, provided that in either case the obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC;

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d. An investment made pursuant to the provisions of paragraphs 18.a., 18.b. or 18.c. shall be subject to the following additional limitations:

i. An investment in or loan upon the obligations of an institution other than an institution that issues mortgage-related securities shall not exceed five percent (5%) of the assets of the trust;

ii. An investment in any one mortgage-related security shall not exceed five percent (5%) of the assets of the trust;

iii. The aggregate total investment in mortgage-related securities shall not exceed twenty-five percent (25%) of the assets of the trust; and

iv. Preferred or guaranteed shares issued or guaranteed by a solvent U.S. institution are permissible investments if all of the institution's obligations are eligible as investments under paragraphs 18.b.i. and 18.b.iii., but shall not exceed two percent (2%) of the assets of the trust.

e. As used in this appendix:

i. "Mortgage-related security" means an obligation that is rated AA or higher (or the equivalent) by a securities rating agency recognized by the Securities Valuation Office of the NAIC and that either:

(a) Represents ownership of one or more promissory notes or certificates of interest or participation in the notes (including any rights designed to assure servicing of, or the receipt or timeliness of receipt by the holders of the notes, certificates, or participation of amounts payable under, the notes, certificates or participation), that:

(1) Are directly secured by a first lien on a single parcel of real estate, including stock allocated to a dwelling unit in a residential cooperative housing corporation, upon which is located a dwelling or mixed residential and commercial structure, or on a residential manufactured home as defined in 42 U.S.C.A. Section 5402(6), whether the manufactured home is considered real or personal property under the laws of the state in which it is located; and

(2) Were originated by a savings and loan association, savings bank, commercial bank, credit union, insurance company, or similar institution that is supervised and examined by a federal or state housing authority, or by a mortgagee approved by the Secretary of Housing and Urban Development pursuant to 12 U.S.C.A. Sections 1709 and 1715-b, or, where the notes involve a lien on the manufactured home, by an institution or by a financial institution approved for insurance by the Secretary of Housing and Urban Development pursuant to 12 U.S.C.A. Section 1703; or

(b) Is secured by one or more promissory notes or certificates of deposit or participations in the notes (with or without recourse to the insurer of the notes) and, by its terms, provides for payments of principal in relation to payments, or reasonable projections of payments, or notes meeting the requirements of paragraphs 18.e.i.(a)(1) and 18.e.i.(a)(2);

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ii. "Promissory note," when used in connection with a manufactured home, shall also include a loan, advance or credit sale as evidenced by a retail installment sales contract or other instrument.

f. Equity interests

i. Investments in common shares or partnership interests of a solvent U.S. institution are permissible if:

(a) Its obligations and preferred shares, if any, are eligible as investments under this paragraph; and

(b) The equity interests of the institution (except an insurance company) are registered on a national securities exchange as provided in the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a to 78kk or otherwise registered pursuant to that Act, and if otherwise registered, price quotations for them are furnished through a nationwide automated quotations system approved by the Financial Industry Regulatory Authority, or successor organization. A trust shall not invest in equity interests under this paragraph an amount exceeding one percent (1%) of the assets of the trust even though the equity interests are not so registered and are not issued by an insurance company.

ii. Investments in common shares of a solvent institution organized under the laws of a country that is a member of the Organization for Economic Cooperation and Development, if:

(a) All its obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC; and

(b) The equity interests of the institution are registered on a securities exchange regulated by the government of a country that is a member of the Organization for Economic Cooperation and Development.

iii. An investment in or loan upon any one institution's outstanding equity interests shall not exceed one percent (1%) of the assets of the trust. The cost of an investment in equity interests made pursuant to this paragraph, when added to the aggregate cost of other investments in equity interests then held pursuant to this paragraph, shall not exceed ten percent (10%) of the assets in the trust;

g. Obligations issued, assumed or guaranteed by a multinational development bank, provided the obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC.

h. Investment companies:

i. Securities of an investment company registered pursuant to the Investment Company Act of 1940, 15 U.S.C. § 802, are allowable investments if the investment company:

(a) Invests at least ninety percent (90%) of its assets in the types of securities that qualify as an investment under paragraphs 18.a., 18.b., or 18.c., or invests in securities that are determined to be substantively similar to the types of securities set forth in paragraphs 18.a., 18.b., or 18.c.; or

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(b) Invests at least ninety percent (90%) of its assets in the types of equity interests that qualify as an investment under paragraph 18.f.i.;

ii. Investments made by a trust in investment companies under this paragraph shall not exceed the following limitations:

(a) An investment in an investment company qualifying under paragraph 18.h.i.(a) shall not exceed ten percent (10%) of the assets in the trust and the aggregate amount of investment in qualifying investment companies shall not exceed twenty-five percent (25%) of the assets in the trust; and

(b) Investments in an investment company qualifying under paragraph 18.h.i.(b) of this paragraph shall not exceed five percent (5%) of the assets in the trust and the aggregate amount of investment in qualifying investment companies shall be included when calculating the permissible aggregate value of equity interests pursuant to paragraph 18.f.i.

i. Letters of Credit

i. In order for a letter of credit to qualify as an asset of the trust, the trustee shall have the right and the obligation pursuant to the deed of trust or some other binding agreement (as duly approved by the commissioner), to immediately draw down the full amount of the letter of credit and hold the proceeds in trust for the beneficiaries of the trust if the letter of credit will otherwise expire without being renewed or replaced.

ii. The trust agreement shall provide that the trustee shall be liable for its negligence, willful misconduct or lack of good faith. The failure of the trustee to draw against the letter of credit in circumstances where such draw would be required shall be deemed to be negligence and/or willful misconduct.

Asset or Reduction from Liability for Reinsurance Ceded by a Domestic Insurer to an Assuming Insurer not Meeting the Requirements detailed above under "Credit Allowed a Domestic Ceding Insurer" (paragraphs 7-18)

19. An asset or a reduction from liability for the reinsurance ceded by a domestic insurer to an assuming insurer not meeting the requirements under "Credit Allowed a Domestic Ceding Insurer" (paragraphs 7-18) shall be allowed in an amount not exceeding the liabilities carried by the ceding insurer. The reduction shall be in the amount of funds held by or on behalf of the ceding insurer, including funds held in trust for the ceding insurer, under a reinsurance contract with the assuming insurer as security for the payment of obligations thereunder, if the security is held in the United States subject to withdrawal solely by, and under the exclusive control of, the ceding insurer; or, in the case of a trust, held in a qualified U.S. financial institution, as defined under "Qualified U.S. Financial Institutions" at paragraph 54. This security may be in the form of:

a. Cash;

b. Securities listed by the Securities Valuation Office of the National Association of Insurance Commissioners, including those deemed exempt from filing as defined by the *Purposes and Procedures Manual of the NAIC Securities Valuation Office*, and qualifying as admitted assets;

Drafting Note: The Purposes and Procedures Manual of the NAIC Securities Valuation Office has been renamed the Purposes and Procedures Manual of the NAIC Investment Analysis Office; however, the Model law refers to the previous name.

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c. i. Clean, irrevocable, unconditional and evergreen letters of credit, issued or confirmed by a qualified U.S. financial institution, as defined in paragraph 53, effective no later than December 31 of the year for which the filing is being made, and in the possession of, or in trust for, the ceding insurer on or before the filing date of its annual statement;

ii. Letters of credit meeting applicable standards of issuer acceptability as of the dates of their issuance (or confirmation) shall, notwithstanding the issuing (or confirming) institution's subsequent failure to meet applicable standards of issuer acceptability, continue to be acceptable as security until their expiration, extension, renewal, modification or amendment, whichever first occurs.

d. An admitted asset or a reduction from liability for reinsurance ceded to an unauthorized assuming insurer pursuant to this appendix shall be allowed only when the requirements of paragraph 15 and the applicable portions under the sections below titled "Trust Agreements Qualified under Paragraph 19", "Letters of Credit Qualified under Paragraph 19", and "Other Security" at paragraph 51.

Trust Agreements Qualified under Paragraph 19

20. The trust agreement shall be entered into between the beneficiary, the grantor and a trustee, which shall be a qualified U.S. financial institution as defined in paragraph 54.

21. The trust agreement shall create a trust account into which assets shall be deposited.

22. All assets in the trust account shall be held by the trustee at the trustee's office in the United States.

23. The trust agreement shall provide that:

a. The beneficiary shall have the right to withdraw assets from the trust account at any time, without notice to the grantor, subject only to written notice from the beneficiary to the trustee;

b. No other statement or document is required to be presented to withdraw assets, except that the beneficiary may be required to acknowledge receipt of withdrawn assets;

c. It is not subject to any conditions or qualifications outside of the trust agreement; and

d. It shall not contain references to any other agreements or documents except as provided for in paragraph 30.

24. The trust agreement shall be established for the sole benefit of the beneficiary.

25. The trust agreement shall require the trustee to:

a. Receive assets and hold all assets in a safe place;

b. Determine that all assets are in such form that the beneficiary, or the trustee upon direction by the beneficiary, may whenever necessary negotiate any such assets, without consent or signature from the grantor or any other person or entity;

c. Furnish to the grantor and the beneficiary a statement of all assets in the trust account upon its inception and at intervals no less frequent than the end of each calendar quarter;

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d. Notify the grantor and the beneficiary within ten (10) days, of any deposits to or withdrawals from the trust account;

e. Upon written demand of the beneficiary, immediately take any and all steps necessary to transfer absolutely and unequivocally all right, title and interest in the assets held in the trust account to the beneficiary and deliver physical custody of the assets to the beneficiary; and

f. Allow no substitutions or withdrawals of assets from the trust account, except on written instructions from the beneficiary, except that the trustee may, without the consent of but with notice to the beneficiary, upon call or maturity of any trust asset, withdraw such asset upon condition that the proceeds are paid into the trust account.

26. The trust agreement shall provide that at least thirty (30) days, but not more than forty-five (45) days, prior to termination of the trust account, written notification of termination shall be delivered by the trustee to the beneficiary.

27. The trust agreement shall be made subject to and governed by the laws of the state in which the trust is domiciled.

28. The trust agreement shall prohibit invasion of the trust corpus for the purpose of paying compensation to, or reimbursing the expenses of, the trustee. In order for a letter of credit to qualify as an asset of the trust, the trustee shall have the right and the obligation pursuant to the deed of trust or some other binding agreement, as duly approved by the commissioner, to immediately draw down the full amount of the letter of credit and hold the proceeds in trust for the beneficiaries of the trust if the letter of credit will otherwise expire without being renewed or replaced.

29. The trust agreement shall provide that the trustee shall be liable for its negligence, willful misconduct or lack of good faith. The failure of the trustee to draw against the letter of credit in circumstances where such draw would be required shall be deemed to be negligence and/or willful misconduct.

30. Notwithstanding other provisions of this appendix, when a trust agreement is established in conjunction with a reinsurance agreement covering risks other than life, annuities and accident and health, where it is customary practice to provide a trust agreement for a specific purpose, the trust agreement may provide that the ceding insurer shall undertake to use and apply amounts drawn upon the trust account, without diminution because of the insolvency of the ceding insurer or the assuming insurer, only for the following purposes:

a. To pay or reimburse the ceding insurer for the assuming insurer's share under the specific reinsurance agreement regarding any losses and allocated loss expenses paid by the ceding insurer, but not recovered from the assuming insurer, or for unearned premiums due to the ceding insurer if not otherwise paid by the assuming insurer;

b. To make payment to the assuming insurer of any amounts held in the trust account that exceed 102 percent of the actual amount required to fund the assuming insurer's obligations under the specific reinsurance agreement; or

c. Where the ceding insurer has received notification of termination of the trust account and where the assuming insurer's entire obligations under the specific reinsurance agreement remain unliquidated and undischarged ten (10) days prior to the termination date, to withdraw amounts equal to the obligations and deposit those amounts in a separate account, in the name of the ceding insurer in any qualified U.S. financial institution as defined in paragraph 54 apart from its general assets, in trust for such uses and purposes

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specified in paragraphs 30.a. and 30.b. as may remain executory after such withdrawal and for any period after the termination date.

31. Notwithstanding other provisions of this appendix, when a trust agreement is established to meet the requirements of paragraph 19 in conjunction with a reinsurance agreement covering life, annuities or accident and health risks, where it is customary to provide a trust agreement for a specific purpose, the trust agreement may provide that the ceding insurer shall undertake to use and apply amounts drawn upon the trust account, without diminution because of the insolvency of the ceding insurer or the assuming insurer, only for the following purposes:

a. To pay or reimburse the ceding insurer for:

i. The assuming insurer's share under the specific reinsurance agreement of premiums returned, but not yet recovered from the assuming insurer, to the owners of policies reinsured under the reinsurance agreement on account of cancellations of the policies; and

ii. The assuming insurer's share under the specific reinsurance agreement of surrenders and benefits or losses paid by the ceding insurer, but not yet recovered from the assuming insurer, under the terms and provisions of the policies reinsured under the reinsurance agreement;

b. To pay to the assuming insurer amounts held in the trust account in excess of the amount necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer; or

c. Where the ceding insurer has received notification of termination of the trust and where the assuming insurer's entire obligations under the specific reinsurance agreement remain unliquidated and undischarged ten (10) days prior to the termination date, to withdraw amounts equal to the assuming insurer's share of liabilities, to the extent that the liabilities have not yet been funded by the assuming insurer, and deposit those amounts in a separate account, in the name of the ceding insurer in any qualified U. S. financial institution apart from its general assets, in trust for the uses and purposes specified in paragraphs 31.a. and 31.b. as may remain executory after withdrawal and for any period after the termination date.

32. Either the reinsurance agreement or the trust agreement must stipulate that assets deposited in the trust account shall be valued according to their current fair market value and shall consist only of cash in United States dollars, certificates of deposit issued by a United States bank and payable in United States dollars, and investments permitted by the Insurance Code or any combination of the above, provided investments in or issued by an entity controlling, controlled by or under common control with either the grantor or the beneficiary of the trust shall not exceed five percent (5%) of total investments. The agreement may further specify the types of investments to be deposited. If the reinsurance agreement covers life, annuities or accident and health risks, then the provisions required by this paragraph must be included in the reinsurance agreement.

33. Notwithstanding any other provisions in the trust instrument, if the grantor of the trust has been declared insolvent or placed into receivership, rehabilitation, liquidation or similar proceedings under the laws of its state or country of domicile, the trustee shall comply with an order of the commissioner with regulatory oversight over the trust or court of competent jurisdiction directing the trustee to transfer to the commissioner with regulatory oversight or other designated receiver all of the assets of the trust fund. The assets shall be applied in accordance with the priority statutes and laws of the state in which the trust is domiciled applicable to the assets of insurance companies in liquidation. If the commissioner with regulatory oversight determines that the assets of the trust fund or any part thereof are not necessary to

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satisfy claims of the U.S. beneficiaries of the trust, the assets or any part of them shall be returned to the trustee for distribution in accordance with the trust agreement.

34. The trust agreement may provide that the trustee may resign upon delivery of a written notice of resignation, effective not less than ninety (90) days after the beneficiary and grantor receive the notice and that the trustee may be removed by the grantor by delivery to the trustee and the beneficiary of a written notice of removal, effective not less than ninety (90) days after the trustee and the beneficiary receive the notice, provided that no such resignation or removal shall be effective until a successor trustee has been duly appointed and approved by the beneficiary and the grantor and all assets in the trust have been duly transferred to the new trustee.

35. The grantor may have the full and unqualified right to vote any shares of stock in the trust account and to receive from time to time payments of any dividends or interest upon any shares of stock or obligations included in the trust account. Any interest or dividends shall be either forwarded promptly upon receipt to the grantor or deposited in a separate account established in the grantor's name.

36. The trustee may be given authority to invest, and accept substitutions of, any funds in the account, provided that no investment or substitution shall be made without prior approval of the beneficiary, unless the trust agreement specifies categories of investments acceptable to the beneficiary and authorizes the trustee to invest funds and to accept substitutions that the trustee determines are at least equal in market value to the assets withdrawn and that are consistent with the restrictions in paragraph 39.b.

37. The trust agreement may provide that the beneficiary may at any time designate a party to which all or part of the trust assets are to be transferred. Transfer may be conditioned upon the trustee receiving, prior to or simultaneously, other specified assets.

38. The trust agreement may provide that, upon termination of the trust account, all assets not previously withdrawn by the beneficiary shall, with written approval by the beneficiary, be delivered over to the grantor.

39. A reinsurance agreement may contain provisions that:

a. Require the assuming insurer to enter into a trust agreement and to establish a trust account for the benefit of the ceding insurer, and specifying what the agreement is to cover;

b. Require the assuming insurer, prior to depositing assets with the trustee, to execute assignments or endorsements in blank, or to transfer legal title to the trustee of all shares, obligations or any other assets requiring assignments, in order that the ceding insurer, or the trustee upon the direction of the ceding insurer, may whenever necessary negotiate these assets without consent or signature from the assuming insurer or any other entity;

c. Require that all settlements of account between the ceding insurer and the assuming insurer be made in cash or its equivalent; and

d. Stipulate that the assuming insurer and the ceding insurer agree that the assets in the trust account, established pursuant to the provisions of the reinsurance agreement, may be withdrawn by the ceding insurer at any time, notwithstanding any other provisions in the reinsurance agreement, and shall be utilized and applied by the ceding insurer or its successors in interest by operation of law, including without limitation any liquidator, rehabilitator, receiver or conservator of such company, without diminution because of insolvency on the part of the ceding insurer or the assuming insurer, only for the following purposes:

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i. To pay or reimburse the ceding insurer for:

(a) The assuming insurer's share under the specific reinsurance agreement of premiums returned, but not yet recovered from the assuming insurer, to the owners of policies reinsured under the reinsurance agreement because of cancellations of such policies;

(b) The assuming insurer's share of surrenders and benefits or losses paid by the ceding insurer pursuant to the provisions of the policies reinsured under the reinsurance agreement; and

(c) Any other amounts necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer;

ii. To make payment to the assuming insurer of amounts held in the trust account in excess of the amount necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer.

40. The reinsurance agreement also may contain provisions that:

a. Give the assuming insurer the right to seek approval from the ceding insurer, which shall not be unreasonably or arbitrarily withheld, to withdraw from the trust account all or any part of the trust assets and transfer those assets to the assuming insurer, provided:

i. The assuming insurer shall, at the time of withdrawal, replace the withdrawn assets with other qualified assets having a current fair market value equal to the market value of the assets withdrawn so as to maintain at all times the deposit in the required amount; or

ii. After withdrawal and transfer, the current fair market value of the trust account is no less than 102 percent of the required amount.

b. Provide for the return of any amount withdrawn in excess of the actual amounts required for paragraph 39.d., and for interest payments at a rate not in excess of the prime rate of interest on such amounts;

c. Allow the award by any arbitration panel or court of competent jurisdiction of:

i. Interest at a rate different from that provided in paragraph 40.b.;

ii. Court or arbitration costs;

iii. Attorney's fees; and

iv. Any other reasonable expenses.

41. Financial Reporting - A trust agreement may be used to reduce any liability for reinsurance ceded to an unauthorized assuming insurer in statutory financial statements when established on or before the date of filing of the statutory financial statement of the ceding insurer. Further, the reduction for the existence of an acceptable trust account may be up to the current fair market value of acceptable assets available to be withdrawn from the trust account at that time, but such reduction shall be no greater than the specific obligations under the reinsurance agreement that the trust account was established to secure.

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42. The failure of any trust agreement to specifically identify the beneficiary as defined in paragraph 4 shall not be construed to affect any actions or rights that the commissioner may take or possess pursuant to the provisions of the laws of the domiciliary state.

Letters of Credit Qualified under Paragraph 19

43. The letter of credit must be clean, irrevocable, unconditional and issued or confirmed by a qualified U.S. financial institution as defined in paragraph 53. The letter of credit shall contain an issue date and expiration date and shall stipulate that the beneficiary need only draw a sight draft under the letter of credit and present it to obtain funds and that no other document need be presented. The letter of credit also shall indicate that it is not subject to any condition or qualifications outside of the letter of credit. In addition, the letter of credit itself shall not contain reference to any other agreements, documents or entities, except as provided in paragraph 50.a. If a court of law appoints a successor in interest to the named beneficiary, then the named beneficiary includes and is limited to the court appointed domiciliary receiver (including conservator, rehabilitator or liquidator).

44. The heading of the letter of credit may include a boxed section containing the name of the applicant and other appropriate notations to provide a reference for the letter of credit. The boxed section shall be clearly marked to indicate that such information is for internal identification purposes only.

45. The letter of credit shall contain a statement to the effect that the obligation of the qualified U.S. financial institution under the letter of credit is in no way contingent upon reimbursement with respect thereto.

46. The term of the letter of credit shall be for at least one year and shall contain an "evergreen clause" that prevents the expiration of the letter of credit without due notice from the issuer. The "evergreen clause" shall provide for a period of no less than thirty (30) days prior to the expiration date or nonrenewal.

47. The letter of credit shall state whether it is subject to and governed by the laws of the ceding insurers state or the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce (Publication 600) or International Standby Practices of the International Chamber of Commerce Publication 590 (ISP98), or any successor publication, and all drafts drawn thereunder shall be presentable at an office in the United States of a qualified U.S. financial institution.

48. If the letter of credit is made subject to the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce Publication 600 (UCP 600) or International Standby Practices of the International Chamber of Commerce Publication 590 (ISP98), or any successor publication, then the letter of credit shall specifically address and provide for an extension of time to draw against the letter of credit in the event that one or more of the occurrences specified in Article 36 of Publication 600 or any other successor publication, occur.

49. If the letter of credit is issued by a financial institution authorized to issue letters of credit, other than a qualified U.S. financial institution as described in paragraph 43, then the following additional requirements shall be met:

a. The issuing financial institution shall formally designate the confirming qualified U.S. financial institution as its agent for the receipt and payment of the drafts; and

b. The "evergreen clause" shall provide for thirty (30) days notice prior to expiration date for nonrenewal.

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50. Reinsurance agreement provisions:

a. The reinsurance agreement in conjunction with which the letter of credit is obtained may contain provisions that:

i. Require the assuming insurer to provide letters of credit to the ceding insurer and specify what they are to cover;

ii. Stipulate that the assuming insurer and ceding insurer agree that the letter of credit provided by the assuming insurer pursuant to the provisions of the reinsurance agreement may be drawn upon at any time, notwithstanding any other provisions in the agreement, and shall be utilized by the ceding insurer or its successors in interest only for one or more of the following reasons:

(a) To pay or reimburse the ceding insurer for:

(1) The assuming insurer's share under the specific reinsurance agreement of premiums returned, but not yet recovered from the assuming insurers, to the owners of policies reinsured under the reinsurance agreement on account of cancellations of such policies;

(2) The assuming insurer's share, under the specific reinsurance agreement, of surrenders and benefits or losses paid by the ceding insurer, but not yet recovered from the assuming insurers, under the terms and provisions of the policies reinsured under the reinsurance agreement; and

(3) Any other amounts necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer;

(b) Where the letter of credit will expire without renewal or be reduced or replaced by a letter of credit for a reduced amount and where the assuming insurer's entire obligations under the reinsurance agreement remain unliquidated and undischarged ten (10) days prior to the termination date, to withdraw amounts equal to the assuming insurer's share of the liabilities, to the extent that the liabilities have not yet been funded by the assuming insurer and exceed the amount of any reduced or replacement letter of credit, and deposit those amounts in a separate account in the name of the ceding insurer in a qualified U.S. financial institution apart from its general assets, in trust for such uses and purposes specified in paragraph 50.a.ii.(a) as may remain after withdrawal and for any period after the termination date.

iii. All of the provisions of paragraph 50.a. shall be applied without diminution because of insolvency on the part of the ceding insurer or assuming insurer.

b. Nothing contained in paragraph 50.a. shall preclude the ceding insurer and assuming insurer from providing for:

i. An interest payment, at a rate not in excess of the prime rate of interest, on the amounts held pursuant to paragraph 50.a.ii.; or

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ii. The return of any amounts drawn down on the letters of credit in excess of the actual amounts required for the above or any amounts that are subsequently determined not to be due.

Other Security

51. A ceding insurer may take credit for unencumbered funds withheld by the ceding insurer in the United States subject to withdrawal solely by the ceding insurer and under its exclusive control.

52. Credit will not be granted, nor an asset or reduction from liability allowed, to a ceding insurer for reinsurance effected with assuming insurers meeting the requirements of this appendix or otherwise in compliance with this appendix unless the reinsurance agreement:

a. Includes a proper insolvency clause, which stipulates that reinsurance is payable directly to the liquidator or successor without diminution regardless of the status of the ceding company;

b. Includes a provision pursuant to Section [cite state law equivalent to Section 2 of the Credit for Reinsurance Model Law] whereby the assuming insurer, if an unauthorized assuming insurer, has submitted to the jurisdiction of an alternative dispute resolution panel or court of competent jurisdiction within the United States, has agreed to comply with all requirements necessary to give the court or panel jurisdiction, has designated an agent upon whom service of process may be effected, and has agreed to abide by the final decision of the court or panel; and

c. Includes a proper reinsurance intermediary clause, if applicable, which stipulates that the credit risk for the intermediary is carried by the assuming insurer.

Qualified U.S. Financial Institutions

53. For purposes of paragraphs 18, 19.c., 43 and 49, a "qualified U.S. financial institution" means an institution that:

a. Is organized or (in the case of a U.S. office of a foreign banking organization) licensed, under the laws of the United States or any state thereof;

b. Is regulated, supervised and examined by U.S. federal or state authorities having regulatory authority over banks and trust companies; and

c. Has been determined by either the commissioner or the Securities Valuation Office of the National Association of Insurance Commissioners to meet such standards of financial condition and standing as are considered necessary and appropriate to regulate the quality of financial institutions whose letters of credit will be acceptable to the commissioner.

54. A "qualified U.S. financial institution" means, for purposes of those provisions of this appendix specifying those institutions that are eligible to act as a fiduciary of a trust, an institution that:

a. Is organized, or in the case of a U.S. branch or agency office of a foreign banking organization, licensed, under the laws of the United States or any state thereof and has been granted authority to operate with fiduciary powers; and

b. Is regulated, supervised and examined by federal or state authorities having regulatory authority over banks and trust companies.

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Life and Health Reinsurance Agreements

Relevant SSAPs:
SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance
SSAP No. 72—Surplus and Quasi-Reorganizations
SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act

Relevant NAIC Model Laws/Regulations:
Credit for Reinsurance Model Law (#785)

Accounting Requirements

1. This Appendix shall not apply to assumption reinsurance, yearly renewable term reinsurance or certain nonproportional reinsurance such as stop loss or catastrophe reinsurance.

Q – Aside from assumption reinsurance, what other types of reinsurance are exempt from the accounting requirements?

A – Yearly renewable term (YRT) and certain nonproportional reinsurance arrangements, such as stop loss and catastrophe reinsurance are exempt because these do not normally provide significant surplus relief and therefore are outside the scope of this Appendix. If a catastrophe arrangement takes a reserve credit for actual losses beyond the attachment point or the unearned premium reserve (UPR) of the current year's premium, there will most likely be no regulatory concern.

Similarly, if a YRT treaty provides incidental reserve credits for the ceding insurer's net amount at risk for the year with no other allowance to enhance surplus, there will most likely be no regulatory concern. For purposes of this exemption, a treaty labeled as YRT does not meet the intended definition of YRT if the surplus relief in the first year is greater than that provided by a YRT treaty with zero first year reinsurance premium and no additional allowance from the reinsurer.

Additional pertinent information applicable to all YRT treaties and to non-proportional reinsurance arrangements is contained in paragraphs 19 and 20 of SSAP No. 61R.

2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:

a. Renewal expense allowances provided or to be provided to the ceding insurer by the reinsurer in any accounting period are not sufficient to cover anticipated allocable renewal expenses of the ceding insurer on the portion of the business reinsured, unless a liability is established for the present value of the shortfall (using assumptions equal to the applicable statutory reserve basis on the business reinsured). Those expenses include commissions, premium taxes and direct expenses including, but not limited to, billing, valuation, claims and maintenance expected by the company at the time the business is reinsured;

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Q – What should be included in the renewal expense allowances with regard to direct expenses? An allocation of salaries? Computer usage? Or just marginal expenses directly related to the business reinsured such as claim payment expenses, postage, etc.?

A – The primary purpose of the accounting requirements is to prohibit credit for reinsurance under financial arrangements where the ceding company enters into an agreement for the principal purpose of producing significant surplus aid for the ceding insurer on a temporary basis, while not transferring all of the significant risks inherent in the business being reinsured.

Paragraph 2.a. implements that purpose by prohibiting credit for reinsurance in certain instances where the ceding insurer is afforded a large ceding commission at the inception of the agreement resulting in a significant increase in surplus only to have such surplus increase be drained away in subsequent periods because renewal expense allowances provided under the agreement are insufficient to cover the direct allocable costs estimated at the time the business is reinsured, which are anticipated to be incurred by the ceding insurer in maintaining the business reinsured.

An exception to complete disallowance of credit for reinsurance is allowed in situations where the ceding insurer reflects a liability for the present value of the shortage between renewal expense allowances provided under the agreement and the direct allocable costs expected in the future by the insurer in maintaining the business reinsured. This liability must be calculated using actuarial assumptions that are consistent with those utilized in the statutory reserve calculation. The expenses to be accounted for in establishing this liability should represent all costs of the ceding insurer in servicing the business that is subject to the agreement.

In determining what the ceding insurer should include in the renewal expenses with regard to direct expenses, there should be an allocation of all renewal expenses anticipated at the time the business is reinsured including salaries, computer usage, postage, etc. This comprehensive calculation should recognize that the anticipated expense levels may be estimated; a comparison with pricing assumptions may be considered in determining the reasonableness of such assumptions.

When an agreement does not comply with paragraph 2.a., this area of non-compliance should be addressed by the posting of a reserve for the present value of the deficiency rather than denial for credit for reinsurance, assuming that no other area of non-compliance is encountered with the agreement and that the assets received corresponding to the ceding commission are in compliance with the Codification, including Appendix A-785. For example, the assets received corresponding to the ceding commission must be admissible and not subject to repayment to the reinsurer.

b. The ceding insurer can be deprived of surplus or assets at the reinsurer's option or automatically upon the occurrence of some event, such as the insolvency of the ceding insurer, except that termination of the reinsurance agreement by the reinsurer for nonpayment of reinsurance premiums or other amounts due, such as modified coinsurance reserve adjustments, interest and adjustments on funds withheld, and tax reimbursements, shall not be considered to be such a deprivation of surplus or assets;

Q – With regard to existing business, should the coinsurance reserve percentage or the coinsurance reserve amount not be allowed to increase in a combination coinsurance/modified coinsurance treaty? How would the rule be applicable to the difference between the total reserve and the amount of funds withheld in a coinsurance with funds withheld treaty?

A – Under a combination coinsurance/modified coinsurance (co/modco) arrangement the ceding company and the reinsurer both establish reserves for future claim payments. Treaty provisions which adjust the reserves each party holds in lieu of transferring funds owed to the reinsurer are acceptable. However, adjustment of reserves in lieu of payment when funds are due to the ceding company is a violation of the

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accounting requirements since it is a depletion of the ceding company's assets. In other words, statutory gains can be used to increase the modified coinsurance reserve but statutory losses cannot be used to reduce the modified coinsurance reserve. This is the case even if the agreement provides for this adjustment at inception and never requires a payment to be owed by the reinsurer.

Under a coinsurance with funds withheld treaty the reinsurer establishes the entire amount of reserve liability on its share of reinsured policies, but the ceding company withholds a portion of the reinsurer's assets typically in an amount less than the reserves, to offset future obligations. Provided the withheld assets are not withheld for any purpose other than the payment of future claims, it is not a violation of the accounting requirements for the reinsurer to require full use of such withheld assets for the payment of claims prior to using any other assets owned by the reinsurer.

Paragraph 2.b. disallows reinsurance credit if the ceding company can be deprived of assets at the reinsurer's option or automatically upon the occurrence of some event. Thus, a provision in a coinsurance with funds withheld or modified coinsurance treaty which unilaterally or automatically allows the reinsurer to convert the treaty to coinsurance at some later date would be of concern. Although the parties could have entered a coinsurance agreement at inception, regulators are concerned that the reinsurer would take invested assets from the ceding company at a time which would be to the detriment of the ceding company's policyholders. Therefore, a conversion provision will not violate paragraph 2.b. only if all of the following are met:

i) the triggers for conversion are limited to ceding company violations of treaty provisions, including complying representations and warranties; the occurrence of a violation has been determined; and the ceding company has been given an opportunity and refuses to promptly remedy the violation;

ii) the conversion is structured so that the surplus of the ceding company will remain unchanged immediately following the conversion;

iii) the invested assets to be transferred upon conversion are less than or equal to the modco reserve, in the case of modco or co/modco, or to the Funds Withheld, in the case of coinsurance funds withheld, and have been maintained in a Trust or Escrow Account since inception of the agreement; and

iv) the reinsurance complies with Credit for Reinsurance requirements (see Appendix A-785) immediately upon conversion.

c. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement, except that neither offsetting experience refunds against current and prior years' losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years' losses under the agreement upon voluntary termination of in force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience. Voluntary termination does not include situations where termination occurs because of unreasonable provisions which allow the reinsurer to reduce its risk under the agreement. An example of such a provision is the right of the reinsurer to increase reinsurance premiums or risk and expense charges to excessive levels forcing the ceding company to prematurely terminate the reinsurance treaty;

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Q – If group term life business is reinsured under a YRT reinsurance agreement (which includes risk-limiting features such as with an experience refund provision which offsets refunds against current and/or prior years' losses (i.e., a "loss carryforward" provision), under what circumstances would any provisions of the reinsurance agreement be considered "unreasonable provisions which allow the reinsurer to reduce its risk under the agreement" thereby violating subsection 2.c.?

A – Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide. So long as the reinsurer cannot charge premiums in excess of the premium received by the ceding insurer under the provisions of the YRT reinsurance agreement, such provisions would not be considered unreasonable. Any provision in the YRT reinsurance agreement which allows the reinsurer to charge reinsurance premiums in excess of the proportionate premium received by the ceding insurer would be considered unreasonable. The revisions to this QA regarding group term life yearly renewable term agreements is effective for contracts in effect as of January 1, 2021.

d. The ceding insurer must, at specific points in time scheduled in the agreement, terminate or automatically recapture all or part of the reinsurance ceded;

e. The reinsurance agreement involves the possible payment by the ceding insurer to the reinsurer of amounts other than from income realized from the reinsured policies. For example, it is improper for a ceding company to pay reinsurance premiums, or other fees or charges to a reinsurer which are greater than the direct premiums collected by the ceding company;

Q – Should a reinsurer have a unilateral right to establish underlying cost of insurance rates or credited interest rates for policies which are wholly or partially reinsured?

A – No, only the ceding company has the right to set the cost of insurance rates charged policyholders and to set the rates of interest credited to them. However, a representation (but not a warranty) that the ceding company shall vary nonguaranteed elements reinsured in a manner consistent with the ceding company's documented procedures, in effect at the time the agreement was entered into, does not violate the accounting requirements.

Q – May a reinsurance contract allow the reinsurer to change the cost of insurance that the ceding company must pay under the treaty?

A – So long as the aggregate amounts payable by the ceding company in any settlement period do not exceed the income of the reinsured policies during that period, the treaty's structure would not be in violation of paragraph 2.e. There is not compliance if any changes could cause payments made by the ceding company to exceed income from the reinsured business, unless the change is necessary to conform to the documented procedures represented to the reinsurer at the time the treaty was entered into and as long as the ceding company has the ability to change the insurance rates it charges policyholders by at least as much as was included in the original representation.

Q – If a reinsured policy allows the ceding company to guarantee rates of interest to be credited to the policyholder which are greater than those guaranteed by the policy, may a reinsurance contract allow the reinsurer to limit its participation in such credited rate as long as it at least provides for the amount based on the rate guaranteed in the contract?

A – So long as the aggregate amounts payable by the ceding company in any settlement period do not exceed the income of the reinsured policies during that period, the treaty's structure would not be in violation of paragraph 2.e. There is not compliance if any changes could cause payments made by the

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ceding company to exceed income from the reinsured business, unless the limited participation reflects a change in declared interest rates which is necessary to conform to the documented procedures represented to the reinsurer at the time the treaty was entered into and as long as the ceding company has the ability to change the declared interest rates to be credited to policyholders by at least as much as was included in the original representation.

f. The treaty does not transfer all of the significant risk inherent in the business being reinsured. The following table identifies for a representative sampling of products or type of business, the risks which are considered to be significant. For products not specifically included, the risks determined to be significant shall be consistent with this table.

Risk categories:

i. Morbidity

ii. Mortality

iii. Lapse

This is the risk that a policy will voluntarily terminate prior to the recoupment of a statutory surplus strain experienced at issue of the policy.

iv. Credit Quality

This is the risk that invested assets supporting the reinsured business will decrease in value. The main hazards are that assets will default or that there will be a decrease in earning power. It excludes market value declines due to changes in interest rate.

v. Reinvestment

This is the risk that interest rates will fall and funds reinvested (coupon payments or monies received upon asset maturity or call) will therefore earn less than expected. If asset durations are less than liability durations, the mismatch will increase.

vi. Disintermediation

This is the risk that interest rates rise and policy loans and surrenders increase or maturing contracts do not renew at anticipated rates of renewal. If asset durations are greater than the liability durations, the mismatch will increase. Policyholders will move their funds into new products offering higher rates. The company may have to sell assets at a loss to provide for these withdrawals.

\+ - Significant 0 - Insignificant

RISK CATEGORY

	i.	ii.	iii.	iv.	v.	vi.
Health Insurance - other than LTC/LTD*	+	0	+	0	0	0
Health Insurance - LTC/LTD*	+	0	+	+	+	0

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Immediate Annuities	0	+	0	+	+	0
Single Premium Deferred Annuities	0	0	+	+	+	+
Flexible Premium Deferred Annuities	0	0	+	+	+	+
Guaranteed Interest Contracts	0	0	0	+	+	+
Other Annuity Deposit Business	0	0	+	+	+	+
Single Premium Whole Life	0	+	+	+	+	+
Traditional Non-Par Permanent	0	+	+	+	+	+
Traditional Non-Par Term	0	+	+	0	0	0
Traditional Par Permanent	0	+	+	+	+	+
Traditional Par Term	0	+	+	0	0	0
Adjustable Premium Permanent	0	+	+	+	+	+
Indeterminate Premium Permanent	0	+	+	+	+	+
Universal Life Flexible Premium	0	+	+	+	+	+
Universal Life Fixed Premium	0	+	+	+	+	+
Universal Life Fixed Premium dump-in premiums allowed	0	+	+	+	+	+

*LTC = Long Term Care Insurance

LTD = Long Term Disability Insurance

Q – If a company cedes health insurance business that is subject to a Medical Loss Ratio (MLR), or similar statutorily required refunds / rebates, must the reinsurer participate in the payment of any refunds / rebates?

A – The reinsurer needs to participate in the payment of its share of any statutorily required MLR or similar refund or rebate based on loss ratio calculations to the extent that the experience of the health business reinsured, during the period that it is reinsured, contributes to the calculation of the refund. Although the payment of such a refund based on the experience of business that is currently reinsured could result in a reduction of surplus on the part of the ceding insurer, if the reduction in surplus of the ceding insurer is entirely attributable to the experience prior to the effective date of the reinsurance, then it is outside of the contract requirements. Accordingly, such a provision should not cause a reinsurance agreement to be out of compliance with Appendix A-791 of the Accounting Practices and Procedure Manual. It is recognized that some refund calculations may involve multiple years.

Furthermore, just as an experience refund is not considered in the determination as to whether a reinsurance agreement is proportional, the requirement for the payment of a refund to policyholders based on a Medical Loss Ratio requirement should also not be considered.

Note: This Q&A only applies to refunds related to a statutory MLR or similar refund or rebate requirement for health insurance and should not be applied to any other situation.

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g. i. The credit quality, reinvestment, or disintermediation risk is significant for the business reinsured and the ceding company does not (other than for the classes of business excepted in paragraph g.ii.) either transfer the underlying assets to the reinsurer or legally segregate such assets in a trust or escrow account or otherwise establish a satisfactory mechanism which legally segregates, by contract or contract provision, the underlying assets.

Q – Is asset segmentation an acceptable mechanism for legal segregation of assets?

A – Generally no. Segmentation involves the allocation of a company's general account investment earnings over several lines of business, or various groups of policies within those lines, such that the performance of one corporate bond, for example, may affect the earnings of several segments within a company. The accounting for the segmentation is largely internal, and the detail of the record keeping varies from company to company.

The fundamental purpose of the requirement for a reinsurance treaty to employ the use of a segregated asset portfolio ("SAP") is that all payments (interest, benefits, allowances, etc.) must be made from the SAP, so as to eliminate any problems that could arise in determining what asset or assets should be sold, and to avoid disputes in the event of insolvency. Any sale of assets that could affect policies not subject to reinsurance, or policies subject to reinsurance with other reinsurers is problematic.

In addition, auditing the performance of a treaty using traditional segmentation methods would be extremely difficult and prone to disagreement, which could provide a reinsurer with broad leverage to contest amounts due that reinsurer, especially in the event of insolvency or rehabilitation of the ceding company.

It is important to determine that the arrangement in place does in fact transfer all of the risks of the underlying assets supporting the reinsured business to the reinsurer.

Q – If a percentage of all policies in a block of business is reinsured, must the company segregate that percentage of the assets supporting the business, or can it segregate all the assets?

A – The company may segregate only assets supporting the reinsured portion or the segregated asset portfolio may represent the entire block of business if the reinsured portion is the same for all policies. In the latter case, the reinsurer would take its proportionate share of the SAP performance.

Q – If the ceding company cedes a portion of each policy in a block of business to one reinsurer and a portion to another, while retaining some itself, does it have to segregate assets separately for each reinsurer, or is it acceptable to have all the assets segregated together with each reinsurer responsible for its portion of the investment risk?

A – The ceding company does not need to segregate assets separately for each reinsurer if the treaties are virtually identical.

Q – At the time assets are legally segregated under a coinsurance with funds withheld treaty, should they be valued at market value, statutory value, or some combination?

A – The assets should be valued at their statutory admitted value.

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Q – When the assets are legally segregated, how are the funds withheld payables and receivables reported?

A – The payables and receivables are recorded in the same manner as in a funds withheld treaty where the assets are not legally segregated and will usually mirror the value of the funds withheld account. However, the funds withheld account, which reflects the statutory admitted value of the assets in the SAP, will fluctuate, and thus may differ from the reserves on the reinsured business.

ii. Notwithstanding the requirements of paragraph g.i., the assets supporting the reserves for the following classes of business and any classes of business which do not have a significant credit quality, reinvestment or disintermediation risk may be held by the ceding company without segregation of such assets:

(a) Health Insurance - LTC/LTD

(b) Traditional Non-Par Permanent

(c) Traditional Par Permanent

(d) Adjustable Premium Permanent

(e) Indeterminate Premium Permanent

(f) Universal Life Fixed Premium

(no dump-in premiums allowed)

The associated formula for determining the reserve interest rate adjustment must use a formula which reflects the ceding company's investment earnings and incorporates all realized and unrealized gains and losses reflected in the statutory statement. The following is an acceptable formula:

$$\text{Rate} = \frac{2\,(I + CG)}{X + Y - I - CG}$$

Where:

I is the net investment income

CG is capital gains less capital losses

X is the current year cash and invested assets plus investment income due and accrued less borrowed money

Y is the same as X but for the prior year

h. Settlements are made less frequently than quarterly or payments due from the reinsurer are not made in cash within ninety (90) days of the settlement date.

i. The ceding insurer is required to make representations or warranties not reasonably related to the business being reinsured.

j. The ceding insurer is required to make representations or warranties about future performance of the business being reinsured.

k. The reinsurance agreement is entered into for the principal purpose of producing significant surplus aid for the ceding insurer, typically on a temporary basis, while not transferring all of the significant risks inherent in the business reinsured and, in substance or effect, the expected potential liability to the ceding insurer remains basically unchanged.

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3. Any increase in surplus net of federal income tax resulting from reinsurance agreements entered into or amended after the effective date of the Codification which involve the reinsurance of business issued prior to the effective date of the agreements shall be identified separately on the insurer's statutory financial statement as a surplus item and recognition of the surplus increase as income shall be reflected on a net of tax basis as earnings emerge from the business reinsured.

{For example, on the last day of calendar year N, company XYZ pays a $20 million initial commission and expense allowance to company ABC for reinsuring an existing block of business. Assuming a 34% tax rate, the net increase in surplus at inception is $13.2 million ($20 million - $6.8 million) which is reported on the "Aggregate write-ins for gains and losses in surplus" line in the Capital and Surplus account. $6.8 million (34% of $20 million) is reported as income on the "Commissions and expense allowances on reinsurance ceded" line of the Summary of Operations.

At the end of year N+1 the business has earned $4 million. ABC has paid $.5 million in profit and risk charges in arrears for the year and has received a $1 million experience refund. Company ABC's annual statement would report $1.65 million (66% of ($4 million - $1 million - $.5 million) up to a maximum of $13.2 million) on the "Commissions and expense allowance on reinsurance ceded" line of the Summary of Operations, and -$1.65 million on the "Aggregate write-ins for gains and losses in surplus" line of the Capital and Surplus account. The experience refund would be reported separately as a miscellaneous income item in the Summary of Operations.}

Written Agreements

4. No reinsurance agreement or amendment to any agreement may be used to reduce any liability or to establish any asset in any financial statement, unless the agreement, amendment or a binding letter of intent has been duly executed by both parties no later than the "as of date" of the financial statement.

5. In the case of a letter of intent, a reinsurance agreement or an amendment to a reinsurance agreement must be executed within a reasonable period of time, not exceeding ninety (90) days from the execution date of the letter of intent, in order for credit to be granted for the reinsurance ceded.

6. The reinsurance agreement shall contain provisions which provide that:

a. The agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder and that there are no understandings between the parties other than as expressed in the agreement; and

b. Any change or modification to the agreement shall be null and void unless made by amendment to the agreement and signed by both parties.

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Appendix A-812

Smoker/Nonsmoker Mortality Tables for Use in Determining Minimum Reserve Liabilities

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 56—Separate Accounts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Purpose

1. The purpose of this Appendix is to permit the use of mortality tables that reflect differences in mortality between smokers and nonsmokers in determining minimum reserve liabilities for plans of insurance with separate premium rates for smokers and nonsmokers.

Definitions

2. As used in this Appendix, "1980 CSO Table, with or without Ten-Year Select Mortality Factor" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the Society of Actuaries Committee to Recommend New Mortality Tables for Valuation of Standard Individual Ordinary Life Insurance, referred to as the Commissioners 1980 Standard Ordinary Mortality Table. The same select factors will be used for both smokers and nonsmokers tables.

3. As used in this Appendix, "1980 CET Table" means that mortality table consisting of separate rates of mortality for male and female lives, developed by the Society of Actuaries Committee to Recommend New Mortality Tables for Valuation of Standard Individual Ordinary Life Insurance, and referred to as the Commissioners 1980 Extended Term Insurance Table.

4. As used in this Appendix, the phrase "smoker and nonsmoker mortality tables" refers to the mortality tables with separate rates of mortality for smokers and nonsmokers derived from the tables defined in paragraphs 2-3 which were developed by the Society of Actuaries Task Force on Smoker/Nonsmoker Mortality and the California Insurance Department staff and recommended by the NAIC Technical Staff Actuarial Group.

5. As used in this Appendix, the phrase "composite mortality tables" refers to the mortality tables defined in paragraphs 2-3 as they were originally published with rates of mortality that do not distinguish between smokers and nonsmokers.

Alternate Tables

6. For any policy of insurance delivered or issued for delivery after the effective date of Codification, at the option of the company and subject to the conditions stated in paragraph 7 of this Appendix;

a. The 1980 CSO Smoker and Nonsmoker Mortality Tables, with or without Ten-Year Select Mortality Factors, may be substituted for the 1980 CSO Table, with or without Ten-Year Select Mortality Factors, and

b. The 1980 CET Smoker and Nonsmoker Mortality Tables may be substituted for the 1980 CET Table for use in determining minimum reserve liabilities.

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Conditions

7. For each plan of insurance with separate rates for smokers and nonsmokers an insurer may

   a. Use composite mortality tables to determine minimum reserve liabilities,

   b. Use smoker and nonsmoker mortality tables to determine the valuation net premiums and additional minimum reserves, if any, required by Appendix A-820 and use composite mortality tables to determine the basic minimum reserves, or

   c. Use smoker and nonsmoker mortality to determine minimum reserve liabilities.

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Appendix A-815

Model Regulation Permitting the Recognition of Preferred Mortality Tables for Use in Determining Minimum Reserve Liabilities

Relevant SSAPs:
SSAP No. 51R—Life Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Valuation of Life Insurance Policies Model Regulation (#830)

Purpose

1. The purpose of this regulation is to recognize, permit and prescribe the use of mortality tables that reflect differences in mortality between preferred and standard lives in determining minimum reserve liabilities in accordance with paragraph 3.a.iii. of Appendix A-820 Standard Valuation Law and paragraphs 16 and 17 of Appendix A-830 Valuation of Life Insurance Model Regulation.

2. **Definitions**

a. "2001 CSO Mortality Table" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the American Academy of Actuaries CSO Task Force from the Valuation Basic Mortality Table developed by the Society of Actuaries Individual Life Insurance Valuation Mortality Task Force, and adopted by the NAIC in December 2002. The 2001 CSO Mortality Table is included in the *Proceedings of the NAIC (2nd Quarter 2002)* and supplemented by the 2001 CSO Preferred Class Structure Mortality Table defined below in Subsection B. Unless the context indicates otherwise, the "2001 CSO Mortality Table" includes both the ultimate form of that table and the select and ultimate form of that table and includes both the smoker and nonsmoker mortality tables and the composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality tables. Mortality tables in the 2001 CSO Mortality Table include the following:

i. "2001 CSO Mortality Table (F)" means that mortality table consisting of the rates of mortality for female lives from the 2001 CSO Mortality Table.

ii. "2001 CSO Mortality Table (M)" means that mortality table consisting of the rates of mortality for male lives from the 2001 CSO Mortality Table.

iii. "Composite mortality tables" means mortality tables with rates of mortality that do not distinguish between smokers and nonsmokers.

iv. "Smoker and nonsmoker mortality tables" means mortality tables with separate rates of mortality for smokers and nonsmokers.

b. "2001 CSO Preferred Class Structure Mortality Table" means mortality tables with separate rates of mortality for super preferred nonsmokers, preferred nonsmokers, residual standard nonsmokers, preferred smokers, and residual standard smoker splits of the 2001 CSO Nonsmoker and Smoker Tables, as adopted by the NAIC at the September, 2006 national meeting and published in the *NAIC Proceedings {3rd Quarter 2006}*. Unless the context indicates otherwise, the "2001 CSO Preferred Class Structure Mortality Table" includes both the ultimate form of that table and the select and ultimate

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form of that table. It includes both the smoker and nonsmoker mortality tables. It includes both the male and female mortality tables and the gender composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality table.

c. "Statistical agent" means an entity with proven systems for protecting the confidentiality of individual insured and insurer information; demonstrated resources for and history of ongoing electronic communications and data transfer ensuring data integrity with insurers, which are its members or subscribers; and a history of and means for aggregation of data and accurate promulgation of the experience modifications in a timely manner.

2001 CSO Preferred Class Structure Table

3. At the election of the company, for each calendar year of issue, for any one or more specified plans of insurance and subject to satisfying the conditions stated in this regulation, the 2001 CSO Preferred Class Structure Mortality Table may be substituted in place of the 2001 CSO Smoker or Nonsmoker Mortality Table as the minimum valuation standard for policies issued on or after January 1, 2007. For policies issued on or after January 1, 2004 (effective date of adoption of the 2001 CSO Mortality Table for Use in Determining Minimum Reserve Liabilities and Nonforfeiture Benefits), and prior to January 1, 2007, these tables may be substituted with the consent of the commissioner and subject to the conditions of paragraph 4. In determining such consent, the commissioner may rely on the consent of the commissioner of the company's state of domicile. No such election shall be made until the company demonstrates at least 20% of the business to be valued on this table is in one or more of the preferred classes. A table from the 2001 CSO Preferred Class Structure Mortality Table used in place of a 2001 CSO Mortality Table, pursuant to the requirements of this rule, will be treated as part of the 2001 CSO Mortality Table only for purposes of reserve valuation pursuant to the requirements of the NAIC model regulation, "Recognition of the 2001 CSO Mortality Table For Use In Determining Minimum Reserve Liabilities And Nonforfeiture Benefits Model Regulation."

4. **Conditions**

a. For each plan of insurance with separate rates for preferred and standard nonsmoker lives, an insurer may use the super preferred nonsmoker, preferred nonsmoker, and residual standard nonsmoker tables to substitute for the nonsmoker mortality table found in the 2001 CSO Mortality Table to determine minimum reserves. At the time of election and annually thereafter, except for business valued under the residual standard nonsmoker table, the appointed actuary shall certify that:

i. The present value of death benefits over the next ten years after the valuation date, using the anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the valuation basic table corresponding to the valuation table being used for that class.

ii. The present value of death benefits over the future life of the contracts, using anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the valuation basic table corresponding to the valuation table being used for that class.

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b. For each plan of insurance with separate rates for preferred and standard smoker lives, an insurer may use the preferred smoker and residual standard smoker tables to substitute for the smoker mortality table found in the 2001 CSO Mortality Table to determine minimum reserves. At the time of election and annually thereafter, for business valued under the preferred smoker table, the appointed actuary shall certify that:

i. The present value of death benefits over the next ten years after the valuation date, using the anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the preferred smoker valuation basic table corresponding to the valuation table being used for that class.

ii. The present value of death benefits over the future life of the contracts, using anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the preferred smoker valuation basic table.

c. Unless exempted by the commissioner, every authorized insurer using the 2001 CSO Preferred Class Structure Table shall annually file with the commissioner, with the NAIC, or with a statistical agent designated by the NAIC and acceptable to the commissioner, statistical reports showing mortality and such other information as the commissioner may deem necessary or expedient for the administration of the provisions of this regulation. The form of the reports shall be established by the commissioner or the commissioner may require the use of a form established by the NAIC or by a statistical agent designated by the NAIC and acceptable to the commissioner.

d. The use of the 2001 CSO Preferred Class Structure Table for the valuation of policies issued prior to January 1, 2007 shall not be permitted in any statutory financial statement in which a company reports, with respect to any policy or portion of a policy coinsured, either of the following:

i. In cases where the mode of payment of the reinsurance premium is less frequent than the mode of payment of the policy premium, a reserve credit that exceeds, by more than the amount specified in this paragraph as Y, the gross reserve calculated before reinsurance. Y is the amount of the gross reinsurance premium that (a) provides coverage for the period from the next policy premium due date to the earlier of the end of the policy year and the next reinsurance premium due date, and (b) would be refunded to the ceding entity upon the termination of the policy.

ii. In cases where the mode of payment of the reinsurance premium is more frequent than the mode of payment of the policy premium, a reserve credit that is less than the gross reserve, calculated before reinsurance, by an amount that is less than the amount specified in this paragraph as Z. Z is the amount of the gross reinsurance premium that the ceding entity would need to pay the assuming company to provide reinsurance coverage from the period of the next reinsurance premium due date to the next policy premium due date minus any liability established for the proportionate amount not remitted to the reinsurer.

For purposes of this condition, both the reserve credit and the gross reserve before reinsurance (i) for the mean reserve method shall be defined as the mean reserve minus the deferred premium asset, and (ii) for the mid-terminal reserve method shall include the unearned premium reserve. A company may estimate and adjust its accounting on an

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aggregate basis in order to meet the conditions to use the 2001 CSO Preferred Class Structure Table.

Effective Date

5. The effective date of this regulation is after January 1, 2007.

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Appendix A-817

Preneed Life Insurance Minimum Standards for Determining Reserve Liabilities and Nonforfeiture Values

Relevant SSAPs:
SSAP No. 51R—Life Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Scope

1. This rule applies to preneed insurance contracts, as defined in paragraph 5 and to similar policies and certificates.

Purpose

2. The purpose of this appendix is to establish for preneed insurance products minimum mortality standards for reserves and nonforfeiture values, and to require the use of the 1980 Commissioners Standard Ordinary (CSO) Life Valuation Mortality Table for use in determining the minimum standard of valuation of reserves and the minimum standard nonforfeiture values for preneed insurance products.

Definitions

3. The term "**2001 CSO Mortality Table**" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the American Academy of Actuaries CSO Task Force from the Valuation Basic Mortality Table developed by the Society of Actuaries Individual Life Insurance Valuation Mortality Task Force, and adopted by the NAIC in December 2002. The 2001 CSO Mortality Table is included in the *Proceedings of the NAIC (2nd Quarter 2002)*. Unless the context indicates otherwise, the "2001 CSO Mortality Table" includes both the ultimate form of that table and the select and ultimate form of that table and includes both the smoker and nonsmoker mortality tables and the composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality tables.

4. The term "**Ultimate 1980 CSO**" means the Commissioners' 1980 Standard Ordinary Life Valuation Mortality Tables (1980 CSO) without ten-year (10-year) selection factors, incorporated into the 1980 amendments to the NAIC Standard Valuation Law approved in December 1983.

5. For the purposes of this guidance, preneed insurance is any life insurance policy or certificate that is issued in combination with, in support of, with an assignment to, or as a guarantee for a prearrangement agreement for goods and services to be provided at the time of and immediately following the death of the insured. Goods and services may include, but are not limited to embalming, cremation, body preparation, viewing or visitation, coffin or urn, memorial stone, and transportation of the deceased. The status of the policy or contract as preneed insurance is determined at the time of issue in accordance with the policy form filing.

Minimum Valuation Mortality Standards

6. For preneed insurance contracts, as defined in paragraph 5, and similar policies and contracts, the minimum mortality standard for determining reserve liabilities and nonforfeiture values for both male and female insureds shall be the Ultimate 1980 CSO.

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Minimum Valuation Interest Rate Standards

7. The interest rates used in determining the minimum standard for valuation of preneed insurance shall be the calendar year statutory valuation interest rates as defined in *Appendix A-820—Minimum Life and Annuity Reserve Standards*, paragraphs 5-8.

8. The interest rates used in determining the minimum standard for nonforfeiture values for preneed insurance shall be the calendar year statutory nonforfeiture interest rates.

Minimum Valuation Method Standards

9. The method used in determining the standard for the minimum valuation of reserves of preneed insurance shall be the method defined in *Appendix A-820—Minimum Life and Annuity Reserve Standards*, paragraphs 9-11.

Transition Rules

10. For preneed insurance policies issued on or after the effective date of this appendix and before January 1, 2012, the 2001 CSO may be used as the minimum standard for reserves and minimum standard for nonforfeiture benefits for both male and female insureds.

11. If an insurer elects to use the 2001 CSO as a minimum standard for any policy issued on or after the effective date of this appendix and before January 1, 2012, the insurer shall provide, as a part of the actuarial opinion memorandum submitted in support of the company's asset adequacy testing, an annual written notification to the domiciliary commissioner. The notification shall include:

a. A complete list of all preneed policy forms that use the 2001 CSO as a minimum standard;

b. A certification signed by the appointed actuary stating that the reserve methodology employed by the company in determining reserves for the preneed policies issued after the effective date and using the 2001 CSO as a minimum standard, develops adequate reserves (For the purposes of this certification, the preneed insurance policies using the 2001 CSO as a minimum standard cannot be aggregated with any other policies.); and

c. Supporting information regarding the adequacy of reserves for preneed insurance policies issued after the effective date of this guidance and using the 2001 CSO as a minimum standard for reserves.

12. Preneed insurance policies issued on or after January 1, 2012, must use the Ultimate 1980 CSO in the calculation of minimum nonforfeiture values and minimum reserves.

Effective Date

13. This rule is applicable to preneed insurance policies and certificates and similar contracts and certificates, as specified in paragraph 5, issued on or after January 1, 2011.

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Appendix A-818

Determining Reserve Liabilities for Credit Life Insurance Model Regulation

Relevant SSAPs:
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Definitions

1. "2001 CSO Mortality Table" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the American Academy of Actuaries CSO Task Force from the Valuation Basic Mortality Table developed by the Society of Actuaries Individual Life Insurance Valuation Mortality Task Force, and adopted by the NAIC in December 2002. The 2001 CSO Mortality Table is included in the *Proceedings of the NAIC (2nd Quarter 2002)*. Unless the context indicates otherwise, the "2001 CSO Mortality Table" includes both the ultimate form of that table and the select and ultimate form of that table and includes both the smoker and nonsmoker mortality tables and the composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality tables.

2. "Composite mortality tables" means mortality tables with rates of mortality that do not distinguish between smokers and nonsmokers.

3. "Credit life insurance" means insurance on a debtor or debtors, pursuant to or in connection with a specific loan or other credit transaction, to provide for satisfaction of a debt, in whole or in part, upon the death of an insured debtor.

4. Credit life insurance does NOT include:

   a. Insurance written in connection with a credit transaction that is:

      i. Secured by a first mortgage or deed of trust; and

      ii. Made to finance the purchase of real property or the construction of a dwelling thereon, or to refinance a prior credit transaction made for such a purpose;

   b. Insurance sold as an isolated transaction on the part of the insurer and not related to an agreement or a plan for insuring debtors of the creditor.

   c. Insurance for which no identifiable charge is made to the debtor.

   d. Insurance on accounts receivable.

5. This rule applies to credit life insurance policies and certificates, and those similar policies and certificates where there is no identifiable charge made to the debtor.

2001 CSO Male Composite Ultimate Mortality Table

6. The minimum standard for both male and female insureds shall be 2001 CSO Male Composite Ultimate Mortality Table.

7. Where the credit life insurance policy or certificate insures two lives, the minimum standard shall be twice the mortality in the 2001 CSO Male Composite Ultimate Mortality Table based on the age of the older insured.

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Minimum Standards

8. Appendix A-830 shall not apply to credit life insurance.

9. The interest rates used in determining the minimum standard for valuation shall be the calendar year statutory valuation interest rates as defined in Appendix A-820, paragraphs 7-10.

10. The method used in determining the minimum standard for valuation shall be the commissioners reserve valuation method as defined in Appendix A-820, paragraphs 11-13.

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Appendix A-820

Minimum Life and Annuity Reserve Standards

Relevant SSAPs:
SSAP No. 35R—Guaranty Fund and Other Assessments
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 56—Separate Accounts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts
SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities

Relevant NAIC Model Laws/Regulations:
Preneed Life Insurance Minimum Standards for Determining Reserve Liabilities and Nonforfeiture Values Model Regulation (#817)
NAIC Model Rule for Recognizing a New Annuity Mortality Table for Use in Determining Reserve Liabilities for Annuities (#821)

Definitions

1. For the purposes of this Appendix, the following definitions shall apply on or after the operative date of the *Valuation Manual*:

a. The term "accident and health insurance" means contracts that incorporate morbidity risk and provide protection against economic loss resulting from accident, sickness, or medical conditions and as may be specified in the *Valuation Manual*.

b. The term "appointed actuary" means a qualified actuary who is appointed in accordance with the *Valuation Manual* to prepare the actuarial opinion.

c. The term "company" means an entity, which (a) has written, issued, or reinsured life insurance contracts, accident and health insurance contracts, or deposit-type contracts in a U.S. State, district or territory and has at least one such policy in force or on claim or (b) has written, issued, or reinsured life insurance contracts, accident and health insurance contracts, or deposit-type contracts in any U.S. State, district or territory and is required to hold a certificate of authority to write life insurance, accident and health insurance, or deposit-type contracts in a U.S. State, district or territory.

d. The term "deposit-type contract" means contracts that do not incorporate mortality or morbidity risks and as may be specified in the *Valuation Manual*.

e. The term "life insurance" means contracts that incorporate mortality risk, including annuity and pure endowment contracts, and as may be specified in the *Valuation Manual*.

f. The term "NAIC" means the National Association of Insurance Commissioners.

g. The term "policyholder behavior" means any action a policyholder, contract holder or any other person with the right to elect options, such as a certificate holder, may take under a policy or contract subject to this Appendix including, but not limited to, lapse, withdrawal, transfer, deposit, premium payment, loan, annuitization, or benefit elections prescribed by the policy or contract but excluding events of mortality or morbidity that result in benefits prescribed in their essential aspects by the terms of the policy or contract.

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h. The term "principle-based valuation" means a reserve valuation that uses one or more methods or one or more assumptions determined by the insurer and is required to comply with paragraphs 25-27 of this Appendix as specified in the *Valuation Manual*.

i. The term "qualified actuary" means an individual who is qualified to sign the applicable statement of actuarial opinion in accordance with the American Academy of Actuaries qualification standards for actuaries signing such statements and who meets the requirements specified in the *Valuation Manual*.

j. The term "tail risk" means a risk that occurs either where the frequency of low probability events is higher than expected under a normal probability distribution or where there are observed events of very significant size or magnitude.

k. The term "*Valuation Manual*" means the manual of valuation instructions adopted by the NAIC as specified in this Appendix or as subsequently amended.

Valuation Requirements

2. Reserves reported in the financial statements shall:

a. Be computed in accordance with presently accepted actuarial standards;

b. Be based on actuarial assumptions that produce reserves at least as great as those called for in any contract provision as to reserve basis and method, and are in accordance with all other contract provisions. The reported reserves and related actuarial items held in support of the policies and contracts when considered in light of the assets held by the company with respect to the reserves and related actuarial items, including but not limited to the investment earnings on the assets and the considerations anticipated to be received and retained under the policies and contracts, make adequate provision for the company's obligations under the policies and contracts, including but not limited to the benefits under and expenses associated with the policies and contracts;

c. Be computed on the basis of assumptions consistent with those used in computing the corresponding items in the annual statement of the preceding year-end with any exceptions disclosed in the notes to the financial statements; and

d. Include provision for all actuarial reserves and related statement items which ought to be established.

Policies and Contracts Issued On or After the Operative Date of the Valuation Manual

3. The provisions set forth in paragraphs 23-27 of this Appendix shall apply to all policies and contracts issued on or after the January 1, 2017, operative date of the *Valuation Manual*.

Policies and Contracts Issued Prior to the Operative Date of the Valuation Manual

4. The provisions set forth in paragraphs 5-22 of this Appendix shall apply to all policies and contracts, as appropriate, subject to this Appendix prior to the January 1, 2017, operative date of the *Valuation Manual* and the provisions set forth in paragraphs 23-27 of this Appendix shall not apply to any such policies and contracts.

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Computation of Minimum Standard for Life Insurance and Endowment Benefits – Policies and Contracts Issued Prior to the Operative Date of the Valuation Manual

5. The minimum standard for the valuation of all life insurance and endowment policies and contracts shall be the commissioners reserve valuation methods defined in paragraphs 11-13, valuation interest rates provided in paragraphs 7-10, and the following tables:

a. For ordinary policies of life insurance issued on the standard basis on or after January 1, 2004, excluding preneed policies (which follow Appendix A-817) any disability and accidental death benefits in the policies:

i. The Commissioners 2001 Standard Ordinary Mortality Table;

ii. At the election of the company for any one or more specified plans of life insurance, the Commissioners 2001 Standard Ordinary Mortality Table with 25-Year Select Mortality Factors; or

iii. Any ordinary mortality table adopted subsequently by the NAIC for use in determining the minimum standard for valuation for such policies;

b. For ordinary policies of life insurance issued on the standard basis, prior to January 1, 2004, excluding any disability and accidental death benefits in the policies and including preneed policies issued on or after January 1, 2012 (see A-817):

i. The Commissioners 1980 Standard Ordinary Mortality Table;

ii. At the election of the company for any one or more specified plans of life insurance, the Commissioners 1980 Standard Ordinary Mortality Table with Ten-Year Select Mortality Factors;

c. For industrial life insurance policies issued on the standard basis, excluding any disability and accidental death benefits in the policies, the Commissioners 1961 Standard Industrial Mortality Table or any industrial mortality table adopted after 1980 by the NAIC for use in determining the minimum standard of valuation for the policies;

d. For total and permanent disability benefits in or supplementary to ordinary policies or contracts, the tables of Period 2 disablement rates and the 1930 to 1950 termination rates of the 1952 Disability Study of the Society of Actuaries, with due regard to the type of benefit or any tables of disablement rates and termination rates adopted after 1980 by the NAIC, for use in determining the minimum standard of valuation for those policies. Any such table shall, for active lives, be combined with a mortality table permitted for calculating the reserves for life insurance policies;

e. For accidental death benefits in or supplementary to policies, the 1959 Accidental Death Benefits Table or any accidental death benefits table adopted after 1980 by the NAIC for use in determining the minimum standard of valuation for those policies. The table shall be combined with a mortality table for calculating the reserves for life insurance policies; and

f. For group life insurance, life insurance issued on the substandard basis and other special benefits: tables which provide for an adequate reserve.

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Computation of Minimum Standard for Annuities

6. The minimum standard of valuation for individual annuity and pure endowment contracts and for annuities and pure endowments purchased under group annuity and pure endowment contracts, shall be the commissioners annuity reserve valuation methods defined in paragraphs 14 and 15, valuation interest rates provided in paragraphs 7-10, and the tables defined in Appendix A-821.

Computation of Minimum Standard Valuation Interest Rates by Calendar Year of Issue - All Business

7. The interest rates used in determining the minimum standard for the valuation of policies issued on or after the effective date of the Codification shall be the calendar year statutory valuation interest rates as defined below:

a. Calendar Year Statutory Valuation Interest Rates

i. The calendar year statutory valuation interest rates, I, shall be determined as follows and the results rounded to the nearer one-quarter of one percent (1/4 of 1%):

(a) For life insurance:

$$I = .03 + W(R_1 - .03) + \frac{W}{2}(R_2 - .09);$$

(b) For single premium immediate annuities and for annuity benefits involving life contingencies arising from other annuities with cash settlement options and from guaranteed interest contracts with cash settlement options:

$$I = .03 + W(R - .03)$$

Where R_1 is the lesser of R and .09,

R_2 is the greater of R and .09,

R is the reference interest rate defined in paragraph 9,

and W is the weighting factor defined in paragraph 8;

(c) For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on an issue year basis, except as stated in subparagraph (b) above, the formula for life insurance stated in subparagraph (a) above shall apply to annuities and guaranteed interest contracts with guarantee durations in excess of ten (10) years and the formula for single premium immediate annuities stated in subparagraph (b) above shall apply to annuities and guaranteed interest contracts with guarantee duration of ten (10) years or less;

(d) For other annuities with no cash settlement options and for guaranteed interest contracts with no cash settlement options, the formula for single premium immediate annuities stated in subparagraph (b) above shall apply.

(e) For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a change in fund basis,

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the formula for single premium immediate annuities stated in subparagraph (b) above shall apply.

ii. However, if the calendar year statutory valuation interest rate for a life insurance policy issued in any calendar year determined without reference to this sentence differs from the corresponding actual rate for similar policies issued in the immediately preceding calendar year by less than one-half of one percent (1/2 of 1%), the calendar year statutory valuation interest rate for the life insurance policies shall be equal to the corresponding actual rate for the immediately preceding calendar year.

Weighting Factors

8. The weighting factors referred to in the formulas stated above are given in the following tables:

a. Weighting Factors for Life Insurance:

Guarantee Duration (Years)	Weighting Factors
10 or less	.50
More than 10, but not more than 20	.45
More than 20	.35

For life insurance, the guarantee duration is the maximum number of years the life insurance can remain in force on a basis guaranteed in the policy or under options to convert to plans of life insurance with premium rates or nonforfeiture values or both which are guaranteed in the original policy;

b. Weighting factor for single premium immediate annuities and for annuity benefits involving life contingencies arising from other annuities with cash settlement options and guaranteed interest contracts with cash settlement options:

.80

c. Weighting factors for other annuities and for guaranteed interest contracts, except as stated in subparagraph (b) above, shall be as specified in items i., ii. and iii. below, according to the rules and definitions in items iv., v. and vi. below:

i. For annuities and guaranteed interest contracts valued on an issue year basis:

Guarantee Duration (Years)	Weighting Factor for Plan Type A	B	C
5 or less:	.80	.60	.50
More than 5, but not more than 10:	.75	.60	.50
More than 10, but not more than 20:	.65	.50	.45
More than 20:	.45	.35	.35

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		Plan Type		
		A	B	C
ii.	For annuities and guaranteed interest contracts valued on a change in fund basis, the factors shown in item i. above increased by:	.15	.25	.05

		Plan Type		
		A	B	C
iii.	For annuities and guaranteed interest contracts valued on an issue year basis (other than those with no cash settlement options) that do not guarantee interest on considerations received more than one year after issue or purchase and for annuities and guaranteed interest contracts valued on a change in fund basis that do not guarantee interest rates on considerations received more than twelve (12) months beyond the valuation date, the factors shown in item i. or derived in item ii. increased by:	.05	.05	.05

iv. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, the guarantee duration is the number of years for which the contract guarantees interest rates in excess of the calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty (20) years. For other annuities with no cash settlement options and for guaranteed interest contracts with no cash settlement options, the guaranteed duration is the number of years from the date of issue or date of purchase to the date annuity benefits are scheduled to commence.

v. Plan type as used in the above tables is defined as follows:

(a) Plan Type A: At any time policyholder may withdraw funds only (l) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) without an adjustment but installments over five years or more, or (3) as an immediate life annuity, or (4) no withdrawal permitted.

(b) Plan Type B: Before expiration of the interest rate guarantee, policyholder may withdraw funds only (1) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) without an adjustment but in installments over five years or more, or (3) no withdrawal permitted. At the end of interest rate guarantee, funds may be withdrawn without an adjustment in a single sum or installments over less than five years.

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(c) Plan Type C: Policyholder may withdraw funds before expiration of interest rate guarantee in a single sum or installments over less than five years either (1) without adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) subject only to a fixed surrender charge stipulated in the contract as a percentage of the fund.

vi. A company may elect to value guaranteed interest contracts with cash settlement options and annuities with cash settlement options on either an issue year basis or on a change in fund basis. Guaranteed interest contracts with no cash settlement options and other annuities with no cash settlement options must be valued on an issue year basis. An issue year basis of valuation refers to a valuation basis under which the interest rate used to determine the minimum valuation standard for the entire duration of the annuity or guaranteed interest contract is the calendar year valuation interest rate for the year of issue or year of purchase of the annuity or guaranteed interest contract, and the change in fund basis of valuation refers to a valuation basis under which the interest rate used to determine the minimum valuation standard applicable to each change in the fund held under the annuity or guaranteed interest contract is the calendar year valuation interest rate for the year of the change in the fund.

Reference Interest Rate

9. The reference interest rate referred to in paragraph 7 of this Appendix shall be defined as follows:

a. For life insurance, the lesser of the average over a period of thirty-six (36) months and the average over a period of twelve (l2) months, ending on June 30 of the calendar year preceding the year of issue, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

b. For single premium immediate annuities and for annuity benefits involving life contingencies arising from other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or year of purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

c. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a year of issue basis, except as stated in subparagraph (b) above, with guarantee duration in excess of ten (10) years, the lesser of the average over a period of thirty-six (36) months and the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

d. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a year of issue basis, except as stated in subparagraph (b) above, with guarantee duration of ten (10) years or less, the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

e. For other annuities with no cash settlement options and for guaranteed interest contracts with no cash settlement options, the average over a period of twelve (12) months, ending

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on June 30 of the calendar year of issue or purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

f. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a change in fund basis, except as stated in subparagraph b. above, the average over a period of twelve (12) months, ending on June 30 of the calendar year of the change in the fund, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.

10. Alternative Method for Determining Reference Interest Rates – In the event that the monthly average of the composite yield on seasoned corporate bonds is no longer published by Moody's Investors Service, Inc. or in the event that the NAIC determines that the monthly average of the composite yield on seasoned corporate bonds as published by Moody's Investors Service, Inc. is no longer appropriate for the determination of the reference interest rate, then an alternative method for determination of the reference interest rate adopted by the NAIC may be substituted.

Reserve Valuation Method—Life Insurance and Endowment Benefits

11. Except as otherwise provided in this Appendix, reserves according to the commissioners reserve valuation method, for the life insurance and endowment benefits of policies providing for a uniform amount of insurance and requiring the payment of uniform premiums shall be the excess, if any, of the present value, at the date of valuation, of the future guaranteed benefits provided for by those policies, over the then present value of any future modified net premiums therefore. The modified net premiums for a policy shall be the uniform percentage of the respective contract premiums for the benefits such that the present value, at the date of issue of the policy, of all modified net premiums shall be equal to the sum of the then present value of the benefits provided for by the policy and the excess of a. over b., as follows:

a. A net level annual premium equal to the present value, at the date of issue, of the benefits provided for after the first policy year, divided by the present value, at the date of issue, of an annuity of one per annum payable on the first and each subsequent anniversary of the policy on which a premium falls due. However, the net level annual premium shall not exceed the net level annual premium on the nineteen-year premium whole life plan for insurance of the same amount at an age one year higher than the age at issue of the policy.

b. A net one-year term premium for the benefits provided for in the first policy year.

12. For a life insurance policy for which the contract premium in the first policy year exceeds that of the second year and for which no comparable additional benefit is provided in the first year for the excess and which provides an endowment benefit or a cash surrender value or a combination in an amount greater than the excess premium, the reserve according to the commissioners reserve valuation method as of any policy anniversary occurring on or before the assumed ending date defined herein as the first policy anniversary on which the sum of any endowment benefit and any cash surrender value then available is greater than the excess premium shall, except as otherwise provided in paragraphs 19 and 20, be the greater of the reserve as of the policy anniversary calculated as described in the preceding paragraph and the reserve as of the policy anniversary calculated as described in those paragraphs, but with (i) the value defined in that paragraph being reduced by fifteen percent (15%) of the amount of such excess first year premium, (ii) all present values of benefits and premiums being determined without reference to premiums or benefits provided for by the policy after the assumed ending date, (iii) the policy being assumed to mature on that date as an endowment, and (iv) the cash surrender value provided on that date being considered as an endowment benefit. In making the above comparison the mortality stated in paragraph 5 and interest bases stated in paragraphs 7-10 shall be used.

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13. Reserves according to the commissioners reserve valuation method shall be calculated by a method consistent with the principles of paragraphs 11 and 12 for:

a. Life insurance policies providing for a varying amount of insurance or requiring the payment of varying premiums;

b. Group annuity and pure endowment contracts purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer (including a partnership or sole proprietorship) or by an employee organization, or by both, other than a plan providing individual retirement accounts or individual retirement annuities under Section 408 of the Internal Revenue Code, as now or hereafter amended;

c. Disability and accidental death benefits in all policies and contracts; and

d. All other benefits, except life insurance and endowment benefits in life insurance policies and benefits provided by all other annuity and pure endowment contracts.

Reserve Valuation Method—Annuity and Pure Endowment Benefits

14. Paragraph 15 shall apply to all annuity and pure endowment contracts other than group annuity and pure endowment contracts purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer (including a partnership or sole proprietorship) or by an employee organization, or by both, other than a plan providing individual retirement accounts or individual retirement annuities under Section 408 of the Internal Revenue Code, as now or hereafter amended.

15. Reserves according to the commissioners annuity reserve method for benefits under annuity or pure endowment contracts, excluding any disability and accidental death benefits in the contracts, shall be the greatest of the respective excesses of the present values, at the date of valuation, of the future guaranteed benefits, including guaranteed nonforfeiture benefits, provided for by the contracts at the end of each respective contract year, over the present value, at the date of valuation, of any future valuation considerations derived from future gross considerations, required by the terms of the contract, that become payable prior to the end of the respective contract year. The future guaranteed benefits shall be determined by using the mortality table, if any, and the interest rate, or rates, specified in the contracts for determining guaranteed benefits. The valuation considerations are the portions of the respective gross considerations applied under the terms of the contracts to determine nonforfeiture values.

Minimum Reserves

16. In no event shall a company's aggregate reserves for all life insurance policies, excluding disability and accidental death benefits be less than the aggregate reserves calculated in accordance with the methods set forth in paragraphs 11-15, paragraphs 19-21, and the mortality table or tables and rate or rates of interest used in calculating nonforfeiture benefits for the policies.

Optional Reserve Calculation

17. Reserves for any category of policies, contracts or benefits, may be calculated, at the option of the company, according to any standards that produce greater aggregate reserves for the category than those calculated according to the minimum standard provided herein, but the rate or rates of interest used for policies and contracts, other than annuity and pure endowment contracts, shall not be greater than the corresponding rate or rates of interest used in calculating any nonforfeiture benefits provided in the policies or contracts.

18. A company which adopts at any time a standard of valuation producing greater aggregate reserves than those calculated according to the minimum standard provided herein may, adopt a lower standard of

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valuation, but not lower than the minimum provided herein; provided that the holding of additional reserves previously determined by the appointed actuary shall not be deemed to be the adoption of a higher standard of valuation.

Reserve Calculation—Valuation Net Premium Exceeding the Gross Premium Charged

19. If in any contract year the gross premium charged by a company on a policy or contract is less than the valuation net premium for the policy or contract calculated by the method used in calculating the reserve but using the minimum valuation standards of mortality and rate of interest, the minimum reserve required for the policy or contract shall be the greater of either the reserve calculated according to the mortality table, rate of interest, and method actually used for the policy or contract, or the reserve calculated by the method actually used for the policy or contract but using the minimum valuation standards of mortality and rate of interest and replacing the valuation net premium by the actual gross premium in each contract year for which the valuation net premium exceeds the actual gross premium. The minimum valuation standards of mortality and rate of interest to be used are those standards stated in paragraph 5 and paragraphs 7-10 of this Appendix.

20. For a life insurance policy for which the gross premium in the first policy year exceeds that of the second year and for which no comparable additional benefit is provided in the first year for the excess and which provides an endowment benefit or a cash surrender value or a combination in an amount greater than the excess premium, the provisions of paragraphs 19 and 20 shall be applied as if the method actually used in calculating the reserve for the policy were the method described in paragraph 11. The minimum reserve at each policy anniversary of such a policy shall be the greater of the minimum reserve calculated in accordance with paragraphs 11 and 12 and the minimum reserve calculated in accordance with paragraphs 19 and 20.

Reserve Calculation—Indeterminate Premium Plans

21. In the case of a plan of life insurance that provides for future premium determination, the amounts of which are to be determined by the insurance company based on then estimates of future experience, or in the case of a plan of life insurance or annuity that is of such a nature that the minimum reserves cannot be determined by the methods described above, the reserves that are held under the plan shall:

a. Be appropriate in relation to the benefits and the pattern of premiums for that plan; and

b. Be computed by a method that is consistent with the principles of this Appendix.

Minimum Standard for Accident and Health Insurance Contracts On or After the Operative Date of the Valuation Manual

22. For accident and health insurance contracts issued on or after the operative date of the *Valuation Manual*, the standard prescribed in the *Valuation Manual* is the minimum standard of valuation required under paragraph 3. For [disability, accident and sickness, accident and health] insurance contracts issued on or after January 1, 2017, and prior to the operative date of the *Valuation Manual* the minimum standard of valuation is the standard adopted by the commissioner by regulation.

Valuation Manual for Policies Issued On or After the Operative Date of the Valuation Manual

23. For policies issued on or after the operative date of the *Valuation Manual*, the standard prescribed in the *Valuation Manual* is the minimum standard of valuation required under paragraph 3.

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24. The *Valuation Manual* must specify all of the following:

a. Minimum valuation standards for and definitions of the policies or contracts subject to paragraph 3. Such minimum valuation standards shall be:

i. The commissioners reserve valuation method for life insurance contracts, or other than annuity contracts, subject to paragraph 3;

ii. The commissioners annuity reserve valuation method for annuity contracts subject to paragraph 3; and

iii. Minimum reserves for all other policies or contracts subject to paragraph 3.

b. Which policies or contracts or types of policies or contracts that are subject to the requirements of a principle-based valuation in paragraph 25 and the minimum valuation standards consistent with those requirements;

c. For policies and contracts subject to a principle-based valuation under paragraphs 25-27:

i. Requirements for the format of reports to the commissioner under paragraph 26.c. and which shall include information necessary to determine if the valuation is appropriate and in compliance with this Appendix;

ii. Assumptions shall be presecribed for risks over which the company does not have significant control or influence; and

iii. Procedures for corporate governance and oversight of the actuarial function, and a process for appropriate waiver or modification of such procedures.

d. For policies not subject to a principle-based valuation under paragraph 25-27, the minimum valuation standard shall either:

i. Be consistent with the minimum standard of valuation prior to the operative date of the *Valuation Manual*; or

ii. Develop reserves that quantify the benefits and guarantees, and the funding, associated with the contracts and their risks at a level of conservatism that reflects conditions that include unfavorable events that have a reasonable probability of occurring.

e. Other requirements, including, but not limited to, those relating to reserve methods, models for measuring risk, generation of economic scenarios, assumptions, margins, use of company experience, risk measurement, disclosure, certifications, reports, actuarial opinions and memorandums, transition rules and internal controls; and

f. The data and form of the data required under paragraph 28, with whom the data must be submitted, and may specify other requirements including data analyses and reporting of analyses.

Requirements of a Principle-Based Valuation

25. A company must establish reserves using a principle-based valuation that meets the following conditions for policies or contracts as specified in the *Valuation Manual*:

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a. Quantify the benefits and guarantees, and the funding, associated with the contracts and their risks at a level of conservatism that reflects conditions that include unfavorable events that have a reasonable probability of occurring during the lifetime of the contracts. For polices or contracts with significant tail risk, reflects conditions appropriately adverse to quantify the tail risk.

b. Incorporate assumptions, risk analysis methods and financial models and management techniques that are consistent with, but not necessarily identical to, those utilized within the company's overall risk assessment process, while recognizing potential differences in financial reporting structures and any prescribed assumptions or methods.

c. Incorporate assumptions that are derived in one of the following manners:

i. The assumption is prescribed in the *Valuation Manual*.

ii. For assumptions that are not prescribed, the assumptions shall:

(a) Be established utilizing the company's available experience, to the extent it is relevant and statistically credible; or

(b) To the extent that company data is not available, relevant, or statistically credible, be established utilizing other relevant, statistically credible experience.

d. Provide margins for uncertainty including adverse deviation and estimation error, such that the greater the uncertainty, the larger the margin and resulting reserve.

26. A company using a principle-based valuation for one or more policies or contracts subject to paragraphs 25-27 as specified in the *Valuation Manual* shall:

a. Establish procedures for corporate governance and oversight of the actuarial valuation function consistent with those described in the *Valuation Manual*.

b. Provide to the commissioner and the board of directors an annual certification of the effectiveness of the internal controls with respect to the principle-based valuation. Such controls shall be designed to assure that all material risks inherent in the liabilities and associated assets subject to such valuation are included in the valuation, and that valuations are made in accordance with the *Valuation Manual*. The certification shall be based on the controls in place as of the end of the preceding calendar year.

c. Develop, and file with the commissioner upon request, a principle-based valuation report that complies with standards prescribed in the *Valuation Manual*.

27. A principle-based valuation may include a prescribed formulaic reserve component.

Experience Reporting for Policies In Force On or After the Operative Date of the Valuation Manual

28. A company shall submit mortality, morbidity, policyholder behavior, or expense experience and other data as prescribed in the *Valuation Manual*.

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Appendix A-821

Annuity Mortality Table for Use in Determining Reserve Liabilities for Annuities

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 56—Separate Accounts

Purpose

1. The purpose of this Appendix is to recognize the following mortality tables for use in determining the minimum standard of valuation for annuity and pure endowment contracts: the 1983 Table "a," the Annuity 2000 Mortality Table, the 2012 Individual Annuity Reserving (2012 IAR) Table and the 1994 Group Annuity Reserving (1994 GAR) Table.

Definitions

2. As used in this Appendix "1983 Table 'a'" means that mortality table developed by the Society of Actuaries Committee to Recommend a New Mortality Basis for Individual Annuity Valuation and adopted as a recognized mortality table for annuities in June 1982 by the National Association of Insurance Commissioners.

3. As used in this Appendix "1994 GAR Table" means that mortality table developed by the Society of Actuaries Group Annuity Valuation Table Task Force and shown in the *Proceedings of the NAIC*.

4. As used in this Appendix "Annuity 2000 Mortality Table" means that mortality table developed by the Society of Actuaries Committee on Life Insurance Research and shown in the Proceedings of the NAIC.

5. As used in this Appendix, "Period table" means a table of mortality rates applicable to a given calendar year (the Period).

6. As used in this Appendix, "Generational mortality table" means a mortality table containing a set of mortality rates that decrease for a given age from one year to the next based on a combination of a Period table and a projection scale containing rates of mortality improvement.

7. As used in this Appendix, "2012 IAR Table" means that Generational mortality table developed by the Society of Actuaries Committee on Life Insurance Research and containing rates, qx2012+n, derived from a combination of the 2012 IAM Period Table and Projection Scale G2, using the methodology stated in paragraphs 13 and 14.

8. As used in this Appendix, "2012 Individual Annuity Mortality Period Life (2012 IAM Period) Table" means the Period table containing loaded mortality rates for calendar year 2012. This table contains rates, qx2012, developed by the Society of Actuaries Committee on Life Insurance Research and is shown in Appendices I and II.

9. As used in this Appendix, "Projection Scale G2 (Scale G2)" is a table of annual rates, $G2_x$, of mortality improvement by age for projecting future mortality rates beyond calendar year 2012. This table was developed by the Society of Actuaries Committee on Life Insurance Research and is shown in Appendices III and IV.

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Individual Annuity or Pure Endowment Contracts

10. Except as provided in paragraph 12 of this Appendix, the Annuity 2000 Mortality Table shall be used for determining the minimum standard of valuation for any individual annuity or pure endowment contract issued on or after January 1, 2001, through December 31, 2014.

11. Except as provided in paragraph 12, the 2012 IAR Mortality Table shall be used for determining the minimum standard of valuation for any individual annuity or pure endowment contract issued on or after January 1, 2015.

12. The 1983 Table "a" without projection is to be used for determining the minimum standards of valuation for an individual annuity or pure endowment contract solely when the contract is based on life contingencies and is issued to fund periodic benefits arising from:

a. Settlements of various forms of claims pertaining to court settlements or out of court settlements from tort actions;

b. Settlements involving similar actions such as workers' compensation claims; or

c. Settlements of long term disability claims where a temporary or life annuity has been used in lieu of continuing disability payments.

Application of the 2012 IAR Mortality Table

13. In using the 2012 IAR Mortality Table, the mortality rate for a person age x in year (2012 + n) is calculated as follows:

$$q_x^{2012+n} = q_x^{2012} (1 - G2_x)^n$$

14. The resulting q_x^{2012+n} shall be rounded to three decimal places per 1,000, e.g., 0.741 deaths per 1,000. Also, the rounding shall occur according to the formula above, starting at the 2012 period table rate. For example, for a male age 30, $q_x^{2012} = 0.741$.

$q_x^{2013} = 0.741 * (1 – 0.010) ^ 1 = 0.73359$, which is rounded to 0.734
$q_x^{2014} = 0.741 * (1 – 0.010) ^ 2 = 0.7262541$, which is rounded to 0.726

A method leading to incorrect rounding would be to calculate q_x^{2014} as $q_x^{2013} * (1 – 0.010)$, or $0.734 * 0.99 = 0.727$. It is incorrect to use the already rounded q_x^{2013} to calculate q_x^{2014}.

Group Annuity or Pure Endowment Contracts

15. The 1994 GAR Table shall be used for determining the minimum standard of valuation for any annuity or pure endowment purchased under a group annuity or pure endowment contract.

Application of the 1994 GAR Table

16. In using the 1994 GAR Table, the mortality rate for a person age x in year (1994 + n) is calculated as follows:

$$q_x^{1994+n} = q_x^{1994} (1 - AA_x)^n$$

where the q_x^{1994} and AA_xs are as specified in the 1994 GAR Table.

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APPENDIX I

2012 IAM Period Table
Female, Age Nearest Birthday

AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$
0	**1.621**	30	**0.300**	60	**3.460**	90	**88.377**
1	**0.405**	31	**0.321**	61	**3.916**	91	**97.491**
2	**0.259**	32	**0.338**	62	**4.409**	92	**107.269**
3	**0.179**	33	**0.351**	63	**4.933**	93	**118.201**
4	**0.137**	34	**0.365**	64	**5.507**	94	**130.969**
5	**0.125**	35	**0.381**	65	**6.146**	95	**146.449**
6	**0.117**	36	**0.402**	66	**6.551**	96	**163.908**
7	**0.110**	37	**0.429**	67	**7.039**	97	**179.695**
8	**0.095**	38	**0.463**	68	**7.628**	98	**196.151**
9	**0.088**	39	**0.504**	69	**8.311**	99	**213.150**
10	**0.085**	40	**0.552**	70	**9.074**	100	**230.722**
11	**0.086**	41	**0.600**	71	**9.910**	101	**251.505**
12	**0.094**	42	**0.650**	72	**10.827**	102	**273.007**
13	**0.108**	43	**0.697**	73	**11.839**	103	**295.086**
14	**0.131**	44	**0.740**	74	**12.974**	104	**317.591**
15	**0.156**	45	**0.780**	75	**14.282**	105	**340.362**
16	**0.179**	46	**0.825**	76	**15.799**	106	**362.371**
17	**0.198**	47	**0.885**	77	**17.550**	107	**384.113**
18	**0.211**	48	**0.964**	78	**19.582**	108	**400.000**
19	**0.221**	49	**1.051**	79	**21.970**	109	**400.000**
20	**0.228**	50	**1.161**	80	**24.821**	110	**400.000**
21	**0.234**	51	**1.308**	81	**28.351**	111	**400.000**
22	**0.240**	52	**1.460**	82	**32.509**	112	**400.000**
23	**0.245**	53	**1.613**	83	**37.329**	113	**400.000**
24	**0.247**	54	**1.774**	84	**42.830**	114	**400.000**
25	**0.250**	55	**1.950**	85	**48.997**	115	**400.000**
26	**0.256**	56	**2.154**	86	**55.774**	116	**400.000**
27	**0.261**	57	**2.399**	87	**63.140**	117	**400.000**
28	**0.270**	58	**2.700**	88	**71.066**	118	**400.000**
29	**0.281**	59	**3.054**	89	**79.502**	119	**400.000**
						120	**1000.000**

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APPENDIX II

2012 IAM Period Table
Male, Age Nearest Birthday

AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$
0	**1.605**	30	**0.741**	60	**5.096**	90	**109.993**
1	**0.401**	31	**0.751**	61	**5.614**	91	**123.119**
2	**0.275**	32	**0.754**	62	**6.169**	92	**137.168**
3	**0.229**	33	**0.756**	63	**6.759**	93	**152.171**
4	**0.174**	34	**0.756**	64	**7.398**	94	**168.194**
5	**0.168**	35	**0.756**	65	**8.106**	95	**185.260**
6	**0.165**	36	**0.756**	66	**8.548**	96	**197.322**
7	**0.159**	37	**0.756**	67	**9.076**	97	**214.751**
8	**0.143**	38	**0.756**	68	**9.708**	98	**232.507**
9	**0.129**	39	**0.800**	69	**10.463**	99	**250.397**
10	**0.113**	40	**0.859**	70	**11.357**	100	**268.607**
11	**0.111**	41	**0.926**	71	**12.418**	101	**290.016**
12	**0.132**	42	**0.999**	72	**13.675**	102	**311.849**
13	**0.169**	43	**1.069**	73	**15.150**	103	**333.962**
14	**0.213**	44	**1.142**	74	**16.860**	104	**356.207**
15	**0.254**	45	**1.219**	75	**18.815**	105	**380.000**
16	**0.293**	46	**1.318**	76	**21.031**	106	**400.000**
17	**0.328**	47	**1.454**	77	**23.540**	107	**400.000**
18	**0.359**	48	**1.627**	78	**26.375**	108	**400.000**
19	**0.387**	49	**1.829**	79	**29.572**	109	**400.000**
20	**0.414**	50	**2.057**	80	**33.234**	110	**400.000**
21	**0.443**	51	**2.302**	81	**37.533**	111	**400.000**
22	**0.473**	52	**2.545**	82	**42.261**	112	**400.000**
23	**0.513**	53	**2.779**	83	**47.441**	113	**400.000**
24	**0.554**	54	**3.011**	84	**53.233**	114	**400.000**
25	**0.602**	55	**3.254**	85	**59.855**	115	**400.000**
26	**0.655**	56	**3.529**	86	**67.514**	116	**400.000**
27	**0.688**	57	**3.845**	87	**76.340**	117	**400.000**
28	**0.710**	58	**4.213**	88	**86.388**	118	**400.000**
29	**0.727**	59	**4.631**	89	**97.634**	119	**400.000**
						120	**1000.000**

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APPENDIX III

Projection Scale G2
Female, Age Nearest Birthday

AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$
0	**0.010**	30	**0.010**	60	**0.013**	90	**0.006**
1	**0.010**	31	**0.010**	61	**0.013**	91	**0.006**
2	**0.010**	32	**0.010**	62	**0.013**	92	**0.005**
3	**0.010**	33	**0.010**	63	**0.013**	93	**0.005**
4	**0.010**	34	**0.010**	64	**0.013**	94	**0.004**
5	**0.010**	35	**0.010**	65	**0.013**	95	**0.004**
6	**0.010**	36	**0.010**	66	**0.013**	96	**0.004**
7	**0.010**	37	**0.010**	67	**0.013**	97	**0.003**
8	**0.010**	38	**0.010**	68	**0.013**	98	**0.003**
9	**0.010**	39	**0.010**	69	**0.013**	99	**0.002**
10	**0.010**	40	**0.010**	70	**0.013**	100	**0.002**
11	**0.010**	41	**0.010**	71	**0.013**	101	**0.002**
12	**0.010**	42	**0.010**	72	**0.013**	102	**0.001**
13	**0.010**	43	**0.010**	73	**0.013**	103	**0.001**
14	**0.010**	44	**0.010**	74	**0.013**	104	**0.000**
15	**0.010**	45	**0.010**	75	**0.013**	105	**0.000**
16	**0.010**	46	**0.010**	76	**0.013**	106	**0.000**
17	**0.010**	47	**0.010**	77	**0.013**	107	**0.000**
18	**0.010**	48	**0.010**	78	**0.013**	108	**0.000**
19	**0.010**	49	**0.010**	79	**0.013**	109	**0.000**
20	**0.010**	50	**0.010**	80	**0.013**	110	**0.000**
21	**0.010**	51	**0.010**	81	**0.012**	111	**0.000**
22	**0.010**	52	**0.011**	82	**0.012**	112	**0.000**
23	**0.010**	53	**0.011**	83	**0.011**	113	**0.000**
24	**0.010**	54	**0.011**	84	**0.010**	114	**0.000**
25	**0.010**	55	**0.012**	85	**0.010**	115	**0.000**
26	**0.010**	56	**0.012**	86	**0.009**	116	**0.000**
27	**0.010**	57	**0.012**	87	**0.008**	117	**0.000**
28	**0.010**	58	**0.012**	88	**0.007**	118	**0.000**
29	**0.010**	59	**0.013**	89	**0.007**	119	**0.000**
						120	**0.000**

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APPENDIX IV

Projection Scale G2
Male, Age Nearest Birthday

AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$
0	**0.010**	30	**0.010**	60	**0.015**	90	**0.007**
1	**0.010**	31	**0.010**	61	**0.015**	91	**0.007**
2	**0.010**	32	**0.010**	62	**0.015**	92	**0.006**
3	**0.010**	33	**0.010**	63	**0.015**	93	**0.005**
4	**0.010**	34	**0.010**	64	**0.015**	94	**0.005**
5	**0.010**	35	**0.010**	65	**0.015**	95	**0.004**
6	**0.010**	36	**0.010**	66	**0.015**	96	**0.004**
7	**0.010**	37	**0.010**	67	**0.015**	97	**0.003**
8	**0.010**	38	**0.010**	68	**0.015**	98	**0.003**
9	**0.010**	39	**0.010**	69	**0.015**	99	**0.002**
10	**0.010**	40	**0.010**	70	**0.015**	100	**0.002**
11	**0.010**	41	**0.010**	71	**0.015**	101	**0.002**
12	**0.010**	42	**0.010**	72	**0.015**	102	**0.001**
13	**0.010**	43	**0.010**	73	**0.015**	103	**0.001**
14	**0.010**	44	**0.010**	74	**0.015**	104	**0.000**
15	**0.010**	45	**0.010**	75	**0.015**	105	**0.000**
16	**0.010**	46	**0.010**	76	**0.015**	106	**0.000**
17	**0.010**	47	**0.010**	77	**0.015**	107	**0.000**
18	**0.010**	48	**0.010**	78	**0.015**	108	**0.000**
19	**0.010**	49	**0.010**	79	**0.015**	109	**0.000**
20	**0.010**	50	**0.010**	80	**0.015**	110	**0.000**
21	**0.010**	51	**0.011**	81	**0.014**	111	**0.000**
22	**0.010**	52	**0.011**	82	**0.013**	112	**0.000**
23	**0.010**	53	**0.012**	83	**0.013**	113	**0.000**
24	**0.010**	54	**0.012**	84	**0.012**	114	**0.000**
25	**0.010**	55	**0.013**	85	**0.011**	115	**0.000**
26	**0.010**	56	**0.013**	86	**0.010**	116	**0.000**
27	**0.010**	57	**0.014**	87	**0.009**	117	**0.000**
28	**0.010**	58	**0.014**	88	**0.009**	118	**0.000**
29	**0.010**	59	**0.015**	89	**0.008**	119	**0.000**
						120	**0.000**

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Appendix A-822

Asset Adequacy Analysis Requirements

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 56—Separate Accounts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Asset adequacy analysis" means an analysis of the adequacy of reserves and related actuarial items, in light of the assets supporting such reserves and related items, to meet the obligations of an insurer.

Asset Adequacy Analysis

2. The reserves and related items, when considered in light of the assets held by the company with respect to such reserves and related actuarial items including, but not limited to, the investment earnings on the assets, and the considerations anticipated to be received and retained under the policies and contracts, shall make adequate provision, according to presently accepted actuarial standards of practice, for the anticipated cash flows required by the contractual obligations and related expenses of the company.

3. If the company determines as the result of asset adequacy analysis that a reserve should be held in addition to the aggregate reserve held and calculated in accordance with methods set forth in Appendix A-820, the company shall establish the additional reserve.

4. Additional reserves established above and deemed not necessary in subsequent years may be released. The release of such reserves would not be deemed an adoption of a lower standard of valuation.

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Appendix A-830

Valuation of Life Insurance Policies
(Including the Introduction and Use of New Select Mortality Factors)

Relevant SSAPs:
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Actuarial Opinion and Memorandum Regulation (#822)

Purpose

1. The purpose of this appendix is to provide:

   a. Tables of select mortality factors and rules for their use;

   b. Rules concerning a minimum standard for the valuation of plans with nonlevel premiums or benefits; and

   c. Rules concerning a minimum standard for the valuation of plans with secondary guarantees.

2. The method for calculating basic reserves defined in this appendix will constitute the Commissioners' Reserve Valuation Method for policies to which this appendix is applicable.

Applicability

3. This appendix shall apply to all life insurance policies, with or without nonforfeiture values, issued on or after the effective date of this appendix, subject to the following exceptions and conditions. Nothing in this section shall be construed to expand the applicability of the Valuation of Life Insurance Policies Model Regulation to include life insurance policies exempted under this section.

   a. Exceptions

      i. This appendix shall not apply to any individual life insurance policy issued on or after the effective date of this appendix if the policy is issued in accordance with and as a result of the exercise of a reentry provision contained in the original life insurance policy of the same or greater face amount, issued before the effective date of this appendix, that guarantees the premium rates of the new policy. This appendix also shall not apply to subsequent policies issued as a result of the exercise of such a provision, or a derivation of the provision, in the new policy.

      ii. This appendix shall not apply to any universal life policy that meets all the following requirements:

         (a) Secondary guarantee period, if any, is five (5) years or less;

         (b) Specified premium for the secondary guarantee period is not less than the net level reserve premium for the secondary guarantee period based on the CSO valuation tables as defined in paragraph 9 and the applicable

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valuation interest rate. For contracts issued beginning January 1, 2004, the net level reserve premium is based on the ultimate mortality rates in the 2001 CSO Mortality Table; and

(c) The initial surrender charge is not less than 100 percent of the first year annualized specified premium for the secondary guarantee period.

Drafting Note: Policies with a secondary guarantee are described in paragraph 29.

iii. This appendix shall not apply to any variable life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts.

iv. This appendix shall not apply to any variable universal life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts.

v. This appendix shall not apply to a group life insurance certificate unless the certificate provides for a stated or implied schedule of maximum gross premiums required in order to continue coverage in force for a period in excess of one year.

vi. This appendix shall not apply to preneed policies, which follow the requirements of A-817.

b. Conditions

i. Calculation of the minimum valuation standard for policies with guaranteed nonlevel gross premiums or guaranteed nonlevel benefits (other than universal life policies), or both, shall be in accordance with the provisions of paragraphs 21-28.

ii. Calculation of the minimum valuation standard for flexible premium and fixed premium universal life insurance policies, that contain provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period shall be in accordance with the provisions of paragraphs 29-32.

Definitions

4. "Basic reserves" means reserves calculated in accordance with Appendix A-820, paragraphs 11-13.

5. "Contract segmentation method" means the method of dividing the period from issue to mandatory expiration of a policy into successive segments, with the length of each segment being defined as the period from the end of the prior segment (from policy inception, for the first segment) to the end of the latest policy year as determined below. For contracts beginning January 1, 2004, all calculations are made using the 2001 CSO Mortality Rate, and, if elected, the optional minimum mortality standard for deficiency reserves stipulated in paragraph 17. (or any other valuation mortality table adopted by the National Association of Insurance Commissioners (NAIC) after the effective date of this appendix for this purpose), and, if elected, the optional minimum mortality standard for deficiency reserves stipulated in paragraph 17 of this appendix. The length of a particular contract segment shall be set equal to the minimum of the value t for which G_t is greater than R_t (if G_t never exceeds R_t the segment length is deemed to be the number of years from the beginning of the segment to the mandatory expiration date of the policy), where G_t and R_t are defined as follows:

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Attachment 1

$$G_t = \frac{GPx+k+t}{GP_{x+k+t-1}}$$

where: x = original issue age;

k = the number of years from the date of issue to the beginning of the segment;

t = 1, 2, ...; *t* is reset to 1 at the beginning of each segment;

$GP_{x+k+t-1}$ = Guaranteed gross premium per thousand of face amount for year *t* of the segment, ignoring policy fees only if level for the premium paying period of the policy.

$R_t = \frac{q_{x+k+t}}{q_{x+k+t-1}}$ However, R_t may be increased or decreased by one percent in any policy year, at the company's option, but R_t shall not be less than one;

where: x, k and t are as defined above, and

The value of "$q_{x+k+t-1}$" is the valuation mortality rate for deficiency reserves in policy year k+t, but using the unmodified select mortality rates if modified select mortality rates are used in the computation of deficiency reserves.

However, if GP_{x+k+t} is greater than 0 and $GP_{x+k+t-1}$ is equal to 0, G_t shall be deemed to be 1000. If GP_{x+k+t} and $GP_{x+k+t-1}$ are both equal to 0, G_t shall be deemed to be 0.

Drafting Note: The purpose of the one percent tolerance in the R factor is to prevent irrational segment lengths due to such things as premium rounding. For example, consider a plan in which gross premiums are designed at some point to be a ratio times the underlying ultimate mortality rates, where the ratio varies by issue age. The resulting segments may be greater than one year, because the guaranteed gross premiums are not expressed in fractional cents. The tolerance factor allows the creation of one year segments for a plan in which premiums parallel the underlying valuation mortality table.

6. "Deficiency reserves" means the excess, if greater than zero, of

a. Minimum reserves calculated in accordance with Appendix A-820, paragraphs 19 and 20, over

b. Basic reserves.

7. "Guaranteed gross premiums" means the premiums under a policy of life insurance that are guaranteed and determined at issue.

8. "Maximum valuation interest rates" means the interest rates defined in Appendix A-820, paragraphs 7-10 (Computation of Minimum Standard by Calendar Year of Issue – All Business) that are to be used in determining the minimum standard for the valuation of life insurance policies.

9. "1980 CSO valuation tables" means the Commissioners' 1980 Standard Ordinary Mortality Table (1980 CSO Table) without ten-year selection factors, referenced in Appendix A-820, and variations of the 1980 CSO Table approved by the NAIC, such as the smoker and nonsmoker versions approved in

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December 1983.

Drafting Note: This appendix defines the 1980 CSO Tables without the existing ten -year select mortality factors to assure that, if select mortality factors are elected, only one set of factors may be applied to the base valuation mortality table.

10. "Scheduled gross premium" means the smallest illustrated gross premium at issue for other than universal life insurance policies. For universal life insurance policies, scheduled gross premium means the smallest specified premium described in paragraph 29.c., if any, or else the minimum premium described in paragraph 29.d.

11. a. "Segmented reserves" means reserves, calculated using segments produced by the contract segmentation method, equal to the present value of all future guaranteed benefits less the present value of all future net premiums to the mandatory expiration of a policy, where the net premiums within each segment are a uniform percentage of the respective guaranteed gross premiums within the segment. The uniform percentage for each segment is such that, at the beginning of the segment, the present value of the net premiums within the segment equals:

i. The present value of the death benefits within the segment, plus

ii. The present value of any unusual guaranteed cash value (see paragraph 24) occurring at the end of the segment, less

iii. Any unusual guaranteed cash value occurring at the start of the segment, plus

iv. For the first segment only, the excess of the Item (a) over Item (b), as follows:

(a) A net level annual premium equal to the present value, at the date of issue, of the benefits provided for in the first segment after the first policy year, divided by the present value, at the date of issue, of an annuity of one per year payable on the first and each subsequent anniversary within the first segment on which a premium falls due. However, the net level annual premium shall not exceed the net level annual premium on the nineteen-year premium whole life plan of insurance of the same renewal year equivalent level amount at an age one year higher than the age at issue of the policy.

(b) A net one-year term premium for the benefits provided for in the first policy year.

b. The length of each segment is determined by the "contract segmentation method," as defined in paragraph 5.

c. The interest rates used in the present value calculations for any policy may not exceed the maximum valuation interest rate, determined with a guarantee duration equal to the sum of the lengths of all segments of the policy.

d. For both basic reserves and deficiency reserves computed by the segmented method, present values shall include future benefits and net premiums in the current segment and in all subsequent segments.

Drafting Note: The segmentation requirement should not be limited to plans with no cash surrender values; otherwise companies could avoid segmentation entirely by designing policies with minimal (positive) cash values. Segmentation for plans with cash surrender values should be based solely upon

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gross premium levels. Basing segmentation upon the level of cash surrender values introduces complications because of the inter-relationship between minimum cash surrender values and gross premium patterns. The requirements of this appendix relating to reserves for plans with unusual cash values and to reserves if cash values exceed calculated reserves serve to link required reserves and cash surrender values. The calculation of segmented reserves shall not be linked to the occurrence of a positive unitary terminal reserve at the end of a segment. The requirement of this appendix to hold the greater of the segmented reserve or the unitary reserve eliminates the need for any linkage.

12. "Tabular cost of insurance" means the net single premium at the beginning of a policy year for one-year term insurance in the amount of the guaranteed death benefit in that policy year.

13. "Ten-year select factors" means the select factors referenced in Appendix A-820.

14. a. "Unitary reserves" means the present value of all future guaranteed benefits less the present value of all future modified net premiums, where:

i. Guaranteed benefits and modified net premiums are considered to the mandatory expiration of the policy; and

ii. Modified net premiums are a uniform percentage of the respective guaranteed gross premiums, where the uniform percentage is such that, at issue, the present value of the net premiums equals the present value of all death benefits and pure endowments, plus the excess of Item (a) over Item (b), as follows:

(a) A net level annual premium equal to the present value, at the date of issue, of the benefits provided for after the first policy year, divided by the present value, at the date of issue, of an annuity of one per year payable on the first and each subsequent anniversary of the policy on which a premium falls due. However, the net level annual premium shall not exceed the net level annual premium on the nineteen-year premium whole life plan of insurance of the same renewal year equivalent level amount at an age one year higher than the age at issue of the policy.

(b) A net one year term premium for the benefits provided for in the first policy year.

b. The interest rates used in the present value calculations for any policy may not exceed the maximum valuation interest rate, determined with a guarantee duration equal to the length from issue to the mandatory expiration of the policy.

Drafting Note: The purpose of this paragraph is to define as specifically as possible what has become commonly called the unitary method. Appendix A-820 does not define the term "unitary" for policies with nonlevel premiums or benefits; its requirement for reserves "computed by a method that is consistent with the principles of Appendix A-820" has not been uniformly interpreted.

15. "Universal life insurance policy" means any individual life insurance policy under the provisions of which separately identified interest credits (other than in connection with dividend accumulations, premium deposit funds, or other supplementary accounts) and mortality or expense charges are made to the policy.

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General Calculation Requirements for Basic Reserves and Premium Deficiency Reserves

16. Prior to January 1, 2004, at the election of the company for any one or more specified plans of life insurance, the minimum mortality standard for basic reserves may be calculated using the 1980 CSO valuation tables with select mortality factors. Effective January 1, 2004, the 2001 CSO Mortality Table is the minimum standard for basic reserves (or any other valuation mortality table adopted by the NAIC after the effective date of the 2001 CSO table for this purpose). Prior to January 1, 2004 if select mortality factors are elected, they may be:

a. The ten-year select mortality factors referenced in Appendix A-820;

b. The select mortality factors in Attachment 1 of this appendix; or

Drafting Note: The select mortality factors for duration 1 through 15 in Attachment 1 of this appendix reflect the Society of Actuaries' data for the years 1983 through 1986, split by sex and smoking status, with fifteen years of mortality improvement, based on Society of Actuaries' Projection Scale A applied. A 50% margin was added. The factors were then graded to the 1980 CSO Tables over the next five durations. A 50% margin was deemed appropriate to provide a reasonable margin, with little likelihood that actual experience for significant blocks of business would exceed it.

c. Any other table of select mortality factors adopted by the NAIC after the effective date of this appendix for the purpose of calculating basic reserves.

17. Deficiency reserves, if any, are calculated for each policy as the excess, if greater than zero, of the quantity A over the basic reserve. The quantity A is obtained by recalculating the basic reserve for the policy using guaranteed gross premiums instead of net premiums when the guaranteed gross premiums are less than the corresponding net premiums. At the election of the company for any one or more specified plans of insurance, the quantity A and prior to January 1, 2004 the corresponding net premiums used in the determination of quantity A may be based upon the 1980 CSO valuation tables with select mortality factors (or any other valuation mortality table adopted by the NAIC after the effective date of this appendix). If select mortality factors are elected, they may be:

a. The ten-year select mortality factors referenced in Appendix A-820;

b. The select mortality factors in Attachment 1 of this appendix;

Effective January 1, 2004, the 2001 CSO Mortality Table is the minimum standard for deficiency reserves. If select mortality rates are used, they may be multiplied by X percent for durations in the first segment, subject to the conditions specified in Sections 17c. to iv. (a). In demonstrating compliance with those conditions, the demonstrations may not combine the results of tests that utilize the 1980 CSO Mortality Table with those tests that utilize the 2001 CSO Mortality Table, unless the combination is explicitly required by regulation or necessary to be in compliance with relevant Actuarial Standards of Practice.

Drafting Note: The select mortality factors in Attachment 1 of this appendix do not reflect the underwriting risk classes that have evolved since the period of the underlying experience. In light of this consideration and the recent recognition of the regulatory value of actuarial opinions, this appendix allows actuarial judgment to be used for deficiency reserves.

c. For durations in the first segment, X percent of the select mortality factors in Attachment 1 of this appendix, subject to the following:

i. X may vary by policy year, policy form, underwriting classification, issue age, or any other policy factor expected to affect mortality experience;

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ii. X is such that, when using the valuation interest rate used for basic reserves, Item (a) is greater than or equal to Item (b);

(a) The actuarial present value of future death benefits, calculated using the mortality rates resulting from the application of X;

(b) The actuarial present value of future death benefits calculated using anticipated mortality experience without recognition of mortality improvement beyond the valuation date;

iii. X is such that the mortality rates resulting from the application of X are at least as great as the anticipated mortality experience, without recognition of mortality improvement beyond the valuation date, in each of the first five (5) years after the valuation date;

iv. The appointed actuary shall increase X at any valuation date where it is necessary to continue to meet all the requirements of paragraph 17.c.;

v. The appointed actuary may decrease X at any valuation date as long as X continues to meet all the requirements of paragraph 17.c.; and

vi. The appointed actuary shall specifically take into account the adverse effect on expected mortality and lapsation of any anticipated or actual increase in gross premiums.

(a) If X is less than 100 percent at any duration for any policy, the following requirements shall be met:

(i) The appointed actuary shall annually prepare an actuarial opinion and memorandum for the company in conformance with the asset adequacy analysis requirements as outlined in Appendix A-822;

(ii) The appointed actuary shall disclose, in the Regulatory Asset Adequacy Issues Summary, the impact of the insufficiency of assets to support the payment of benefits and expenses and the establishment of statutory reserves during one or more interim periods; and

(iii) The appointed actuary shall annually opine for all policies subject to this appendix as to whether the mortality rates resulting from the application of X meet the requirements of paragraph 17.c. This opinion shall be supported by an actuarial report, subject to appropriate Actuarial Standards of Practice promulgated by the Actuarial Standards Board of the American Academy of Actuaries. The X factors shall reflect anticipated future mortality, without recognition of mortality improvement beyond the valuation date, taking into account relevant emerging experience.

d. Any other table of select mortality factors adopted by the NAIC after the effective date of this appendix for the purpose of calculating deficiency reserves.

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18. This paragraph applies to both basic reserves and deficiency reserves. Any set of select mortality factors may be used only for the first segment. However, if the first segment is less than ten (10) years, the appropriate ten-year select mortality factors referenced in Appendix A-820 may be used thereafter through the tenth policy year from the date of issue.

Drafting Note: This appendix does not allow the use of select mortality factors beyond the first segment. The rationale is that the result of a premium increase that is sufficient to require a new segment will be increased lapsation, leading to mortality deterioration after the increase. Also, for policies that have reentry provisions, select mortality factors shall not be used in segments beginning after reentry unless a new policy is actually issued. However, this appendix allows the use of the ten-year select mortality factors referenced in Appendix A-820 beyond the first segment (but in no case beyond the tenth policy year) in recognition that the mortality deterioration is unlikely to occur to a significant degree within the first ten (10) years.

19. In determining basic reserves or deficiency reserves, guaranteed gross premiums without policy fees may be used where the calculation involves the guaranteed gross premium but only if the policy fee is a level dollar amount after the first policy year. In determining deficiency reserves, policy fees may be included in guaranteed gross premiums, even if not included in the actual calculation of basic reserves.

20. Reserves for policies that have changes to guaranteed gross premiums, guaranteed benefits, guaranteed charges, or guaranteed credits that are unilaterally made by the insurer after issue and that are effective for more than one year after the date of the change shall be the greatest of the following: (1) reserves calculated ignoring the guarantee, (2) reserves assuming the guarantee was made at issue, and (3) reserves assuming that the policy was issued on the date of the guarantee.

Calculation of Minimum Valuation Standard for Policies with Guaranteed Nonlevel Gross Premiums or Guaranteed Nonlevel Benefits (Other than Universal Life Policies)

21. Basic Reserves

a. Basic reserves shall be calculated as the greater of the segmented reserves and the unitary reserves. Both the segmented reserves and the unitary reserves for any policy shall use the same valuation mortality table and selection factors. At the option of the insurer, in calculating segmented reserves and net premiums, either of the adjustments described in subparagraph i. or ii. below may be made:

i. Treat the unitary reserve, if greater than zero, applicable at the end of each segment as a pure endowment and subtract the unitary reserve, if greater than zero, applicable at the beginning of each segment from the present value of guaranteed life insurance and endowment benefits for each segment.

ii. Treat the guaranteed cash surrender value, if greater than zero, applicable at the end of each segment as a pure endowment; and subtract the guaranteed cash surrender value, if greater than zero, applicable at the beginning of each segment from the present value of guaranteed life insurance and endowment benefits for each segment.

22. Deficiency Reserves

a. The deficiency reserve at any duration shall be calculated:

i. On a unitary basis if the corresponding basic reserve determined by paragraph 21 is unitary;

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ii. On a segmented basis if the corresponding basic reserve determined by paragraph 21 is segmented; or

iii. On the segmented basis if the corresponding basic reserve determined by paragraph 21 is equal to both the segmented reserve and the unitary reserve.

b. Paragraph 22 shall apply to any policy for which the guaranteed gross premium at any duration is less than the corresponding modified net premium calculated by the method used in determining the basic reserves, but using the minimum valuation standards of mortality (specified in paragraph 17) and rate of interest.

c. Deficiency reserves, if any, shall be calculated for each policy as the excess if greater than zero, for the current and all remaining periods, of the quantity A over the basic reserve, where A is obtained as indicated in paragraph 17.

d. For deficiency reserves determined on a segmented basis, the quantity A is determined using segment lengths equal to those determined for segmented basic reserves.

23. Minimum Value

a. Basic reserves may not be less than the tabular cost of insurance for the balance of the policy year, if mean reserves are used. Basic reserves may not be less than the tabular cost of insurance for the balance of the current modal period or to the paid-to-date, if later, but not beyond the next policy anniversary, if mid-terminal reserves are used. The tabular cost of insurance shall use the same valuation mortality table and interest rates as that used for the calculation of the segmented reserves. However, if select mortality factors are used, they shall be the ten-year select factors referenced in Appendix A-820. In no case may total reserves (including basic reserves, deficiency reserves and any reserves held for supplemental benefits that would expire upon contract termination) be less than the amount that the policyowner would receive (including the cash surrender value of the supplemental benefits, if any, referred to above), exclusive of any deduction for policy loans, upon termination of the policy. Effective January 1, 2004, the valuation mortality table used in determining the tabular cost of insurance shall be the ultimate mortality rates in the 2001 CSO Mortality Table.

24. Unusual Pattern of Guaranteed Cash Surrender Values

Drafting Note: This requirement is independent of both the segmentation process and the unitary process. After the greater of the segmented or the unitary reserve has been determined, then this paragraph imposes an additional floor on the ultimate reserve. The purpose of this paragraph is to assure adequate funding of significant increases in guaranteed cash surrender values.

a. For any policy with an unusual pattern of guaranteed cash surrender values, the reserves actually held prior to the first unusual guaranteed cash surrender value shall not be less than the reserves calculated by treating the first unusual guaranteed cash surrender value as a pure endowment and treating the policy as an *n* year policy providing term insurance plus a pure endowment equal to the unusual cash surrender value, where *n* is the number of years from the date of issue to the date the unusual cash surrender value is scheduled.

b. The reserves actually held subsequent to any unusual guaranteed cash surrender value shall not be less than the reserves calculated by treating the policy as an *n* year policy providing term insurance plus a pure endowment equal to the next unusual guaranteed

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cash surrender value, and treating any unusual guaranteed cash surrender value at the end of the prior segment as a net single premium, where

i. *n* is the number of years from the date of the last unusual guaranteed cash surrender value prior to the valuation date to the earlier of:

(a) The date of the next unusual guaranteed cash surrender value, if any, that is scheduled after the valuation date; or

(b) The mandatory expiration date of the policy; and

ii. The net premium for a given year during the *n* year period is equal to the product of the net to gross ratio and the respective gross premium; and

iii. The net to gross ratio is equal to Item (a) divided by Item (b) as follows:

(a) The present value, at the beginning of the *n* year period, of death benefits payable during the *n* year period plus the present value, at the beginning of the n year period, of the next unusual guaranteed cash surrender value, if any, minus the amount of the last unusual guaranteed cash surrender value, if any, scheduled at the beginning of the *n* year period.

(b) The present value, at the beginning of the *n* year period, of the scheduled gross premiums payable during the *n* year period.

c. For purposes of this paragraph, a policy is considered to have an unusual pattern of guaranteed cash surrender values if any future guaranteed cash surrender value exceeds the prior year's guaranteed cash surrender value by more than the sum of:

i. One hundred ten percent (110%) of the scheduled gross premium for that year;

ii. One hundred ten percent (110%) of one year's accrued interest on the sum of the prior year's guaranteed cash surrender value and the scheduled gross premium using the nonforfeiture interest rate used for calculating policy guaranteed cash surrender values; and

iii. Five percent (5%) of the first policy year surrender charge, if any.

25. Optional Exemption for Yearly Renewable Term Reinsurance. At the option of the company, the following approach for reserves on YRT reinsurance may be used:

Drafting Note: Traditional reserves for yearly renewable term (YRT) reinsurance, the calculations of which this section describes, are already adequate and sufficient. However, without this option in the appendix, YRT reinsurance would be subject to the more complex segmentation calculations.

a. Calculate the valuation net premium for each future policy year as the tabular cost of insurance for that future year.

b. Basic reserves shall never be less than the tabular cost of insurance for the appropriate period, as defined in paragraph 23.

c. Deficiency reserves.

i. For each policy year, calculate the excess, if greater than zero, of the valuation net premium over the respective maximum guaranteed gross premium.

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ii. Deficiency reserves shall never be less than the sum of the present values, at the date of valuation, of the excesses determined in accordance with subparagraph i. above.

d. Prior to January 1, 2004, for purposes of this paragraph, the calculations use the maximum valuation interest rate and the 1980 CSO mortality tables with or without ten-year select mortality factors, or any other table adopted after the effective date of this appendix by the NAIC for this purpose. Effective January 1, 2004, the calculations specified in this paragraph (25) shall use the ultimate mortality rates in the 2001 CSO Mortality Table.

e. A reinsurance agreement shall be considered YRT reinsurance for purposes of this paragraph if only the mortality risk is reinsured.

f. If the assuming company chooses this optional exemption, the ceding company's reinsurance reserve credit shall be limited to the amount of reserve held by the assuming company for the affected policies.

26. Optional Exemption for Attained-Age-Based Yearly Renewable Term Life Insurance Policies. At the option of the company, the following approach for reserves for attained-age-based YRT life insurance policies may be used:

Drafting Note: Traditional reserves for attained-age-based YRT policies, the calculations of which this subsection describes, are already adequate and sufficient. However, without this option in the appendix, these policies would be subject to the more complex segmentation calculations.

a. Calculate the valuation net premium for each future policy year as the tabular cost of insurance for that future year.

b. Basic reserves shall never be less than the tabular cost of insurance for the appropriate period, as defined in paragraph 23.

c. Deficiency reserves.

i. For each policy year, calculate the excess, if greater than zero, of the valuation net premium over the respective maximum guaranteed gross premium.

ii. Deficiency reserves shall never be less than the sum of the present values, at the date of valuation, of the excesses determined in accordance with subparagraph i. above.

d. Prior to January 1, 2004, for purposes of this paragraph, the calculations use the maximum valuation interest rate and the 1980 CSO valuation tables with or without ten-year select mortality factors, or any other table adopted after the effective date of this appendix by the NAIC for this purpose. Effective January 1, 2004, the calculations specified in this paragraph shall use the ultimate mortality rates in the 2001 CSO Mortality Table.

e. A policy shall be considered an attained-age-based YRT life insurance policy for purposes of this subsection if:

i. The premium rates (on both the initial current premium scale and the guaranteed maximum premium scale) are based upon the attained age of the insured such

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that the rate for any given policy at a given attained age of the insured is independent of the year the policy was issued; and

ii. The premium rates (on both the initial current premium scale and the guaranteed maximum premium scale) are the same as the premium rates for policies covering all insureds of the same sex, risk class, plan of insurance and attained age.

f. For policies that become attained-age-based YRT policies after an initial period of coverage, the approach of this subsection may be used after the initial period if:

i. The initial period is constant for all insureds of the same sex, risk class and plan of insurance; or

ii. The initial period runs to a common attained age for all insureds of the same sex, risk class and plan of insurance; and

iii. After the initial period of coverage, the policy meets the conditions of paragraph 26.e. above.

g. If this election is made, this approach shall be applied in determining reserves for all attained-age-based YRT life insurance policies issued on or after the effective date of this appendix.

27. Exemption from Unitary Reserves for Certain *n*-Year Renewable Term Life Insurance Polices. Unitary basic reserves and unitary deficiency reserves need not be calculated for a policy if the following conditions are met:

Drafting Note: Without this exemption, companies issuing certain *n*-year renewable term policies could be forced to hold reserves higher than *n*-year term reserves, even though in many cases gross premiums are well above valuation mortality rates.

a. The policy consists of a series of *n*-year periods, including the first period and all renewal periods, where *n* is the same for each period, except that for the final renewal period, n may be truncated or extended to reach the expiry age, provided that this final renewal period is less than 10 years and less than twice the size of the earlier n-year periods, and for each period, the premium rates on both the initial current premium scale and the guaranteed maximum premium scale are level;

b. Prior to January 1, 2004, the guaranteed gross premiums in all *n*-year periods are not less than the corresponding net premiums based upon the 1980 CSO Table with or without the ten-year select mortality factors. Effective January 1, 2004, the calculations specified in this paragraph shall use the ultimate mortality rates in the 2001 CSO Mortality Table; and

c. There are no cash surrender values in any policy year.

28. Exemption from Unitary Reserves for Certain Juvenile Policies. Unitary basic reserves and unitary deficiency reserves need not be calculated for a policy if the following conditions are met, based upon the initial current premium scale at issue:

a. At issue, the insured is age twenty-four (24) or younger;

b. Until the insured reaches the end of the juvenile period, which shall occur at or before age twenty-five (25), the gross premiums and death benefits are level, and there are no cash surrender values; and

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c. After the end of the juvenile period, gross premiums are level for the remainder of the premium paying period, and death benefits are level for the remainder of the life of the policy.

Drafting Note: The jumping juvenile policy described has traditionally been valued in two segments. This exemption will allow that practice to continue without requiring the calculation of reserves on a unitary basis. However, within each segment, both basic and deficiency reserves shall comply with the segmented reserve requirements.

Calculation of Minimum Valuation Standard for Flexible Premium and Fixed Premium Universal Life Insurance Policies That Contain Provisions Resulting in the Ability of a Policyowner to Keep a Policy in Force Over a Secondary Guarantee Period

29. General

a. Policies with a secondary guarantee include:

i. A policy with a guarantee that the policy will remain in force at the original schedule of benefits, subject only to the payment of specified premiums;

ii. Prior to January 1, 2004 a policy in which the minimum premium at any duration is less than the corresponding one year valuation premium, calculated using the maximum valuation interest rate and the 1980 CSO valuation tables with or without ten-year select mortality factors, or any other table adopted after the effective date of this appendix by the NAIC for this purpose. Effective January 1, 2004, the one-year valuation premium shall be calculated using the ultimate mortality rates in the 2001 CSO Mortality Table; or

iii. A policy with any combination of subparagraph i. and ii.

Drafting Note: Universal life and variable universal life policies with secondary guarantees that meet the requirements of paragraph 3.a.ii. are not subject to this appendix.

b. A secondary guarantee period is the period for which the policy is guaranteed to remain in force subject only to a secondary guarantee. When a policy contains more than one secondary guarantee, the minimum reserve shall be the greatest of the respective minimum reserves at that valuation date of each unexpired secondary guarantee, ignoring all other secondary guarantees. Secondary guarantees that are unilaterally changed by the insurer after issue shall be considered to have been made at issue. Reserves described in paragraphs 30 and 31 below shall be recalculated from issue to reflect these changes.

c. Specified premiums mean the premiums specified in the policy, the payment of which guarantees that the policy will remain in force at the original schedule of benefits, but which otherwise would be insufficient to keep the policy in force in the absence of the guarantee if maximum mortality and expense charges and minimum interest credits were made and any applicable surrender charges were assessed.

d. For purposes of this paragraph, the minimum premium for any policy year is the premium that, when paid into a policy with a zero account value at the beginning of the policy year, produces a zero account value at the end of the policy year. The minimum premium calculation shall use the policy cost factors (including mortality charges, loads and expense charges) and the interest crediting rate, which are all guaranteed at issue.

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e. The one-year valuation premium means the net one-year premium based upon the original schedule of benefits for a given policy year. The one-year valuation premiums for all policy years are calculated at issue. The select mortality factors defined in paragraphs 17.b., 17.c. and 17.d. may not be used to calculate the one-year valuation premiums.

f. The one-year valuation premium should reflect the frequency of fund processing, as well as the distribution of deaths assumption employed in the calculation of the monthly mortality charges to the fund.

30. Basic Reserves for the Secondary Guarantees. Basic reserves for the secondary guarantees shall be the segmented reserves for the secondary guarantee period. In calculating the segments and the segmented reserves, the gross premiums shall be set equal to the specified premiums, if any, or otherwise to the minimum premiums, that keep the policy in force and the segments will be determined according to the contract segmentation method as defined in paragraph 5.

31. Deficiency Reserves for the Secondary Guarantees. Deficiency reserves, if any, for the secondary guarantees shall be calculated for the secondary guarantee period in the same manner as described in paragraph 22 with gross premiums set equal to the specified premiums, if any, or otherwise to the minimum premiums that keep the policy in force.

32. Minimum Reserves. The minimum reserves during the secondary guarantee period are the greater of:

a. The basic reserves for the secondary guarantee plus the deficiency reserve, if any, for the secondary guarantees; or

b. The minimum reserves required by other appendices governing universal life plans.

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Attachment 1

SELECT MORTALITY FACTORS

This Attachment contains tables of select mortality factors that are the bases to which the respective percentage of paragraphs 16.b., 17.b. and 17.c. are applied.

The six tables of select mortality factors contained herein include: (1) male aggregate, (2) male nonsmoker, (3) male smoker, (4) female aggregate, (5) female nonsmoker, and (6) female smoker.

These tables apply to both age last birthday and age nearest birthday mortality tables.

For sex-blended mortality tables, compute select mortality factors in the same proportion as the underlying mortality. For example, for the 1980 CSO-B Table, the calculated select mortality factors are eighty percent (80%) of the appropriate male table in this Attachment, plus twenty percent (20%) of the appropriate female table in this Attachment.

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Attachment 1

SELECT MORTALITY FACTORS

Male, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	96	98	98	99	99	100	100	90	92	92	92	92	93	93	96	97	98	98	99	100
19	83	84	84	87	87	87	79	79	79	81	81	82	82	82	85	88	91	94	97	100
20	69	71	71	74	74	69	69	67	69	70	71	71	71	71	74	79	84	90	95	100
21	66	68	69	71	66	66	67	66	67	70	70	70	70	71	71	77	83	88	94	100
22	65	66	66	63	63	64	64	64	65	68	68	68	68	69	71	77	83	88	94	100
23	62	63	59	60	62	62	63	63	64	65	65	67	67	69	70	76	82	88	94	100
24	60	56	56	59	59	60	61	61	61	64	64	64	66	67	70	76	82	88	94	100
25	52	53	55	56	58	58	60	60	60	63	62	63	64	67	69	75	81	88	94	100
26	51	52	55	56	58	58	57	61	61	62	63	64	66	69	66	73	80	86	93	100
27	51	52	55	57	58	60	61	61	60	63	63	64	67	66	67	74	80	87	93	100
28	49	51	56	58	60	60	61	62	62	63	64	66	65	66	68	74	81	87	94	100
29	49	51	56	58	60	61	62	62	62	64	64	62	66	67	70	76	82	88	94	100
30	49	50	56	58	60	60	62	63	63	64	62	63	67	68	71	77	83	88	94	100
31	47	50	56	58	60	62	63	64	64	62	63	66	68	70	72	78	83	89	94	100
32	46	49	56	59	60	62	63	66	62	63	66	67	70	72	73	78	84	89	95	100
33	43	49	56	59	62	63	64	62	65	66	67	70	72	73	75	80	85	90	95	100
34	42	47	56	60	62	63	61	63	66	67	70	71	73	75	76	81	86	90	95	100
35	40	47	56	60	63	61	62	65	67	68	71	73	74	76	76	81	86	90	95	100
36	38	42	56	60	59	61	63	65	67	68	70	72	74	76	77	82	86	91	95	100
37	38	45	56	57	61	62	63	65	67	68	70	72	74	76	76	81	86	90	95	100
38	37	44	53	58	61	62	65	66	67	69	69	73	75	76	77	82	86	91	95	100
39	37	41	53	58	62	63	65	65	66	68	69	72	74	76	76	81	86	90	95	100
40	34	40	53	58	62	63	65	65	66	68	68	71	75	76	77	82	86	91	95	100
41	34	41	53	58	62	63	65	64	64	66	68	70	74	76	77	82	86	91	95	100
42	34	43	53	58	61	62	63	63	63	64	66	69	72	75	77	82	86	91	95	100
43	34	43	54	59	60	61	63	62	62	64	66	67	72	74	77	82	86	91	95	100
44	34	44	54	58	59	60	61	60	61	62	64	67	71	74	77	82	86	91	95	100
45	34	45	53	58	59	60	60	60	59	60	63	66	71	74	77	82	86	91	95	100
46	31	43	52	56	57	58	59	59	59	60	63	67	71	74	75	80	85	90	95	100
47	32	42	50	53	55	56	57	58	59	60	65	68	71	74	75	80	85	90	95	100
48	32	41	47	52	54	56	57	57	57	61	65	68	72	73	74	79	84	90	95	100
49	30	40	46	49	52	54	55	56	57	61	66	69	72	73	74	79	84	90	95	100
50	30	38	44	47	51	53	54	56	57	61	66	71	72	73	75	80	85	90	95	100
51	28	37	42	46	49	53	54	56	57	61	66	71	72	73	75	80	85	90	95	100
52	28	35	41	45	49	51	54	56	57	61	66	71	72	74	75	80	85	90	100	100
53	27	35	39	44	48	51	53	55	57	61	67	71	74	75	76	81	86	100	100	100
54	27	33	38	44	48	50	53	55	57	61	67	72	74	75	76	81	100	100	100	100
55	25	32	37	43	47	50	53	55	57	61	68	72	74	75	78	100	100	100	100	100

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Attachment 1

Male, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	25	32	37	43	47	49	51	54	56	61	67	70	73	74	100	100	100	100	100	100
57	24	31	38	43	47	49	51	54	56	59	66	69	72	100	100	100	100	100	100	100
58	24	31	38	43	48	48	50	53	56	59	64	67	100	100	100	100	100	100	100	100
59	23	30	39	43	48	48	51	53	55	58	63	100	100	100	100	100	100	100	100	100
60	23	30	39	43	48	47	50	52	53	57	100	100	100	100	100	100	100	100	100	100
61	23	30	39	43	49	49	50	52	53	75	100	100	100	100	100	100	100	100	100	100
62	23	30	39	44	49	49	51	52	75	75	100	100	100	100	100	100	100	100	100	100
63	22	30	39	45	50	50	52	75	75	75	100	100	100	100	100	100	100	100	100	100
64	22	30	39	45	50	51	75	75	75	75	100	100	100	100	100	100	100	100	100	100
65	22	30	39	45	50	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
66	22	30	39	45	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
67	22	30	39	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
68	23	32	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
69	23	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
70	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
71	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
72	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
73	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
74	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
75	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
76	48	52	55	60	60	65	70	70	70	100	100	100	100	100	100	100	100	100	100	100
77	48	52	55	60	60	65	70	70	100	100	100	100	100	100	100	100	100	100	100	100
78	48	52	55	60	60	65	70	100	100	100	100	100	100	100	100	100	100	100	100	100
79	48	52	55	60	60	65	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	48	52	55	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	48	52	55	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	48	52	55	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	48	52	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	48	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

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Attachment 1

Male, Non-Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	93	95	96	98	99	100	100	90	92	92	92	92	95	95	96	97	98	98	99	100
19	80	81	83	86	87	87	79	79	79	81	81	82	83	83	86	89	92	94	97	100
20	65	68	69	72	74	69	69	67	69	70	71	71	72	72	75	80	85	90	95	100
21	63	66	68	71	66	66	67	66	67	70	70	70	71	71	73	78	84	89	95	100
22	62	65	66	62	63	64	64	64	67	68	68	68	70	70	73	78	84	89	95	100
23	60	62	58	60	62	62	63	63	64	67	68	68	67	69	71	77	83	88	94	100
24	59	55	56	58	59	60	61	61	63	65	67	66	66	69	71	77	83	88	94	100
25	52	53	55	56	58	58	60	60	61	64	64	64	64	67	70	76	82	88	94	100
26	51	53	55	56	58	60	61	61	61	63	64	64	66	69	67	74	80	87	93	100
27	51	52	55	58	60	60	61	61	62	63	64	66	67	66	67	74	80	87	93	100
28	49	52	57	58	60	61	63	62	62	64	66	66	63	66	68	74	81	87	94	100
29	49	51	57	60	61	61	62	62	63	64	66	63	65	67	68	74	81	87	94	100
30	49	51	57	60	61	62	63	63	63	64	62	63	66	68	70	76	82	88	94	100
31	47	50	57	60	60	62	63	64	64	62	63	65	67	70	71	77	83	88	94	100
32	46	50	57	60	62	63	64	64	62	63	65	66	68	71	72	78	83	89	94	100
33	45	49	56	60	62	63	64	62	63	65	66	68	71	73	74	79	84	90	95	100
34	43	48	56	62	63	64	62	62	65	66	67	70	72	74	74	79	84	90	95	100
35	41	47	56	62	63	61	62	63	66	67	68	70	72	74	75	80	85	90	95	100
36	40	47	56	62	59	61	62	63	66	67	68	70	72	74	75	80	85	90	95	100
37	38	45	56	58	59	61	62	63	66	67	67	69	71	73	74	79	84	90	95	100
38	38	45	53	58	61	62	63	65	65	67	68	70	72	74	73	78	84	89	95	100
39	37	41	53	58	61	62	63	64	65	67	68	70	71	73	73	78	84	89	95	100
40	34	41	53	58	61	62	63	64	64	66	67	69	71	73	72	78	83	89	94	100
41	34	41	53	58	61	61	62	62	63	65	65	67	69	71	71	77	83	88	94	100
42	34	43	53	58	60	61	62	61	61	63	64	66	67	69	71	77	83	88	94	100
43	32	43	53	58	60	61	60	60	60	60	62	64	66	68	69	75	81	88	94	100
44	32	44	52	57	59	60	60	59	59	58	60	62	65	67	69	75	81	88	94	100
45	32	44	52	57	59	60	59	57	57	57	59	61	63	66	68	74	81	87	94	100
46	32	42	50	54	56	57	57	56	55	56	59	61	63	65	67	74	80	87	93	100
47	30	40	48	52	54	55	55	54	54	55	59	61	62	63	66	73	80	86	93	100
48	30	40	46	49	51	52	53	53	54	55	57	61	62	63	63	70	78	85	93	100
49	29	39	43	48	50	51	50	51	53	54	57	61	61	62	62	70	77	85	92	100
50	29	37	42	45	47	48	49	50	51	54	57	61	61	61	61	69	77	84	92	100
51	27	35	40	43	45	47	48	50	51	53	57	60	61	61	62	70	77	85	92	100
52	27	34	39	42	44	45	48	49	50	53	56	60	60	62	62	70	77	85	100	100
53	25	31	37	41	44	45	47	49	50	51	56	59	61	61	62	70	77	100	100	100
54	25	30	36	39	43	44	47	48	49	51	55	59	59	61	62	70	100	100	100	100
55	24	29	35	38	42	43	45	48	49	50	56	58	59	61	62	100	100	100	100	100

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Attachment 1

Male, Non-Smoker

Issue	Duration																			
Age	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**	**13**	**14**	**15**	**16**	**17**	**18**	**19**	**20+**
56	23	29	35	38	42	42	44	47	48	50	55	57	58	59	100	100	100	100	100	100
57	23	28	35	38	42	42	43	45	47	49	53	55	56	100	100	100	100	100	100	100
58	22	28	33	37	41	41	43	45	45	47	51	53	100	100	100	100	100	100	100	100
59	22	26	33	37	41	41	42	44	44	46	50	100	100	100	100	100	100	100	100	100
60	20	26	33	37	41	40	41	42	42	45	100	100	100	100	100	100	100	100	100	100
61	20	26	33	37	41	40	41	42	42	75	100	100	100	100	100	100	100	100	100	100
62	19	25	32	38	40	40	41	42	75	75	100	100	100	100	100	100	100	100	100	100
63	19	25	33	36	40	40	41	75	75	75	100	100	100	100	100	100	100	100	100	100
64	18	24	32	36	39	40	75	75	75	75	100	100	100	100	100	100	100	100	100	100
65	18	24	32	36	39	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
66	18	24	32	36	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
67	18	24	32	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
68	18	24	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
69	18	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
70	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
71	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
72	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
73	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
74	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
75	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
76	48	52	55	60	60	65	70	70	70	100	100	100	100	100	100	100	100	100	100	100
77	48	52	55	60	60	65	70	70	100	100	100	100	100	100	100	100	100	100	100	100
78	48	52	55	60	60	65	70	100	100	100	100	100	100	100	100	100	100	100	100	100
79	48	52	55	60	60	65	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	48	52	55	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	48	52	55	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	48	52	55	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	48	52	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	48	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

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Attachment 1

Male, Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
19	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
20	98	100	100	100	100	100	100	99	99	99	100	99	99	99	100	100	100	100	100	100
21	95	98	99	100	95	96	96	95	96	97	97	96	96	96	96	97	98	98	99	100
22	92	95	96	90	90	93	93	92	93	95	95	93	93	92	93	94	96	97	99	100
23	90	92	85	88	88	89	89	89	90	90	90	90	89	90	92	94	95	97	98	100
24	87	81	82	85	84	86	88	86	86	88	88	86	86	88	89	91	93	96	98	100
25	77	78	79	82	81	83	83	82	83	85	84	84	84	85	86	89	92	94	97	100
26	75	77	79	82	82	83	83	82	83	84	84	84	84	85	81	85	89	92	96	100
27	73	75	78	82	82	83	83	82	82	82	82	84	84	80	81	85	89	92	96	100
28	71	73	79	82	81	82	83	81	81	82	82	82	80	80	81	85	89	92	96	100
29	69	72	78	81	81	82	82	81	81	81	81	77	80	80	81	85	89	92	96	100
30	68	71	78	81	81	81	82	81	81	81	76	77	80	80	81	85	89	92	96	100
31	65	70	77	81	79	81	82	81	81	76	77	79	81	81	83	86	90	93	97	100
32	63	67	77	78	79	81	81	81	76	77	77	80	83	83	85	88	91	94	97	100
33	60	65	74	78	79	79	81	76	77	77	79	80	83	85	85	88	91	94	97	100
34	57	62	74	77	79	79	75	76	77	79	79	81	83	85	87	90	92	95	97	100
35	53	60	73	77	79	75	75	76	77	79	80	82	84	86	88	90	93	95	98	100
36	52	59	71	75	74	75	75	76	77	79	79	81	83	85	87	90	92	95	97	100
37	49	58	70	71	74	74	75	76	77	78	79	81	84	86	86	89	92	94	97	100
38	48	55	66	70	72	74	74	75	76	78	79	81	83	85	87	90	92	95	97	100
39	45	50	65	70	72	72	74	74	75	77	79	81	84	86	86	89	92	94	97	100
40	41	49	63	68	71	72	73	74	74	76	78	80	83	85	86	89	92	94	97	100
41	40	49	63	68	71	72	72	72	73	75	76	78	81	84	85	88	91	94	97	100
42	40	49	62	68	70	71	71	71	71	73	75	76	81	83	85	88	91	94	97	100
43	39	50	62	67	69	69	70	70	70	71	73	76	79	83	85	88	91	94	97	100
44	39	50	60	66	68	69	68	69	69	69	71	74	79	81	85	88	91	94	97	100
45	37	50	60	66	68	68	68	67	67	67	69	73	78	81	85	88	91	94	97	100
46	37	48	58	63	65	67	66	66	66	67	71	74	78	81	84	87	90	94	97	100
47	36	47	55	61	63	64	64	64	65	67	71	75	79	81	84	87	90	94	97	100
48	35	46	53	58	60	62	63	63	65	67	72	75	79	81	83	86	90	93	97	100
49	34	45	51	56	58	59	61	62	63	67	72	77	80	81	83	86	90	93	97	100
50	34	43	49	53	55	57	60	61	63	67	73	78	80	81	81	85	89	92	96	100
51	32	42	47	52	55	57	60	61	63	67	73	78	80	83	84	87	90	94	97	100
52	32	40	46	50	54	56	60	61	63	67	73	78	81	84	85	88	91	94	100	100
53	30	37	44	49	54	56	59	61	65	67	74	79	83	85	87	90	92	100	100	100
54	30	36	43	48	53	55	59	61	65	67	74	80	84	85	89	91	100	100	100	100
55	29	35	42	47	53	55	59	61	65	67	75	80	84	86	90	100	100	100	100	100

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Attachment 1

Male, Smoker

Issue	Duration																			
Age	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**	**13**	**14**	**15**	**16**	**17**	**18**	**19**	**20+**
56	28	35	42	47	53	55	57	60	63	68	74	79	83	85	100	100	100	100	100	100
57	28	35	42	47	53	54	57	60	64	67	74	78	81	100	100	100	100	100	100	100
58	26	33	43	48	54	54	56	59	63	67	73	78	100	100	100	100	100	100	100	100
59	26	33	43	48	54	53	57	59	63	66	73	100	100	100	100	100	100	100	100	100
60	25	33	43	48	54	53	56	58	62	66	100	100	100	100	100	100	100	100	100	100
61	25	33	43	49	55	55	57	59	63	75	100	100	100	100	100	100	100	100	100	100
62	25	33	43	50	56	56	58	61	75	75	100	100	100	100	100	100	100	100	100	100
63	24	33	45	51	56	56	59	75	75	75	100	100	100	100	100	100	100	100	100	100
64	24	34	45	51	57	57	75	75	75	75	100	100	100	100	100	100	100	100	100	100
65	24	34	45	52	57	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
66	24	35	45	53	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
67	25	35	45	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
68	25	36	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
69	27	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
70	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
71	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
72	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
73	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
74	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
75	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
76	48	52	55	60	60	65	70	70	70	100	100	100	100	100	100	100	100	100	100	100
77	48	52	55	60	60	65	70	70	100	100	100	100	100	100	100	100	100	100	100	100
78	48	52	55	60	60	65	70	100	100	100	100	100	100	100	100	100	100	100	100	100
79	48	52	55	60	60	65	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	48	52	55	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	48	52	55	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	48	52	55	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	48	52	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	48	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

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Attachment 1

Female, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	99	100	100	100	100	100	100	100	93	95	96	97	97	100	100	100	100	100	100	100
18	83	83	84	84	84	84	86	78	78	79	82	84	85	88	88	90	93	95	98	100
19	65	66	68	68	68	68	63	63	64	66	69	71	72	74	75	80	85	90	95	100
20	48	50	51	51	51	47	48	48	49	51	56	57	58	61	63	70	78	85	93	100
21	47	48	50	51	47	47	48	49	51	53	57	60	61	64	64	71	78	86	93	100
22	44	47	48	45	47	47	48	49	53	54	60	61	63	64	66	73	80	86	93	100
23	42	45	44	45	47	47	49	51	53	54	61	64	64	67	69	75	81	88	94	100
24	39	40	42	44	47	47	50	51	54	56	64	64	66	69	70	76	82	88	94	100
25	34	38	41	44	47	47	50	53	56	57	64	67	69	71	73	78	84	89	95	100
26	34	38	41	45	49	49	51	56	58	59	66	69	70	73	70	76	82	88	94	100
27	34	38	41	47	50	51	54	57	59	60	69	70	73	70	71	77	83	88	94	100
28	34	37	43	47	53	53	56	59	62	63	70	73	70	72	74	79	84	90	95	100
29	34	38	43	49	54	56	58	60	63	64	73	70	72	74	75	80	85	90	95	100
30	35	38	43	50	56	56	59	63	66	67	70	71	74	75	76	81	86	90	95	100
31	35	38	43	51	56	58	60	64	67	65	71	72	74	75	76	81	86	90	95	100
32	35	39	45	51	56	59	63	66	65	66	72	72	75	76	76	81	86	90	95	100
33	36	39	44	52	58	62	64	65	66	67	72	74	75	76	76	81	86	90	95	100
34	36	40	45	52	58	63	63	66	67	68	74	74	76	76	76	81	86	90	95	100
35	36	40	45	53	59	61	65	67	68	70	75	74	75	76	75	80	85	90	95	100
36	36	40	45	53	55	62	65	67	68	70	74	74	74	75	75	80	85	90	95	100
37	36	41	47	52	57	62	65	67	68	69	72	72	73	75	74	79	84	90	95	100
38	34	41	44	52	57	63	66	68	69	70	72	71	72	74	75	80	85	90	95	100
39	34	40	45	53	58	63	66	68	69	69	70	70	70	73	74	79	84	90	95	100
40	32	40	45	53	58	65	65	67	68	69	70	69	70	73	73	78	84	89	95	100
41	32	40	45	53	57	63	64	67	68	68	69	69	69	73	74	79	84	90	95	100
42	32	40	45	52	56	61	63	65	66	68	69	68	70	74	75	80	85	90	95	100
43	31	39	45	51	55	59	61	65	65	66	68	69	69	74	77	82	86	91	95	100
44	31	39	45	50	54	58	61	63	64	66	67	68	71	75	78	82	87	91	96	100
45	31	38	44	49	53	56	59	62	63	65	67	68	71	77	79	83	87	92	96	100
46	29	37	43	48	51	54	59	62	63	65	67	69	71	77	78	82	87	91	96	100
47	28	35	41	46	49	54	57	61	62	66	68	69	71	77	77	82	86	91	95	100
48	28	35	41	44	49	52	57	61	63	66	68	71	72	75	77	82	86	91	95	100
49	26	34	39	43	47	52	55	61	63	67	69	71	72	75	75	80	85	90	95	100
50	25	32	38	41	46	50	55	61	63	67	69	72	72	75	74	79	84	90	95	100
51	25	32	38	41	45	50	55	61	63	66	68	69	71	74	74	79	84	90	95	100
52	23	30	36	41	45	51	56	61	62	65	66	68	68	73	73	78	84	89	100	100
53	23	30	36	41	47	51	56	61	62	63	65	66	68	72	72	78	83	100	100	100
54	22	29	35	41	47	53	57	61	61	62	62	66	66	69	70	76	100	100	100	100
55	22	29	35	41	47	53	57	61	61	61	62	63	64	68	69	100	100	100	100	100

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Attachment 1

Female, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	22	29	35	41	45	51	56	59	60	61	62	63	64	67	100	100	100	100	100	100
57	22	29	35	41	45	50	54	56	58	59	61	62	63	100	100	100	100	100	100	100
58	22	30	36	41	44	49	53	56	57	57	61	62	100	100	100	100	100	100	100	100
59	22	30	36	41	44	48	51	53	55	56	59	100	100	100	100	100	100	100	100	100
60	22	30	36	41	43	47	50	51	53	55	100	100	100	100	100	100	100	100	100	100
61	22	29	35	39	42	46	49	50	52	80	100	100	100	100	100	100	100	100	100	100
62	20	28	33	39	41	45	47	49	80	80	100	100	100	100	100	100	100	100	100	100
63	20	28	33	38	41	44	46	80	80	80	100	100	100	100	100	100	100	100	100	100
64	19	27	32	36	40	42	80	80	80	80	100	100	100	100	100	100	100	100	100	100
65	19	25	30	35	39	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
66	19	25	30	35	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
67	19	25	30	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
68	19	25	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
69	19	64	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
70	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
71	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
72	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
73	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
74	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
75	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
76	60	60	64	68	68	72	75	75	80	100	100	100	100	100	100	100	100	100	100	100
77	60	60	64	68	68	72	75	75	100	100	100	100	100	100	100	100	100	100	100	100
78	60	60	64	68	68	72	75	100	100	100	100	100	100	100	100	100	100	100	100	100
79	60	60	64	68	68	72	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	60	60	64	68	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	60	60	64	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	60	60	64	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

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Attachment 1

Female, Non-Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	96	98	98	98	98	99	99	99	92	92	93	95	95	97	99	99	99	100	100	100
18	78	80	80	80	80	81	81	74	75	75	78	79	82	83	85	88	91	94	97	100
19	60	62	63	63	63	65	59	59	60	60	64	67	67	70	72	78	83	89	94	100
20	42	44	45	45	45	42	42	42	45	45	50	51	53	56	58	66	75	83	92	100
21	41	42	44	45	41	42	42	44	47	47	51	53	54	57	59	67	75	84	92	100
22	39	41	44	41	41	42	44	45	49	49	54	56	57	58	60	68	76	84	92	100
23	38	41	38	40	41	42	44	46	49	50	56	57	58	60	62	70	77	85	92	100
24	36	36	38	40	41	42	46	47	50	51	58	59	60	62	63	70	78	85	93	100
25	32	34	37	40	41	43	46	49	51	53	59	60	62	63	64	71	78	86	93	100
26	32	34	37	41	43	45	47	50	53	53	60	62	63	64	62	70	77	85	92	100
27	32	34	38	43	46	47	49	51	53	55	62	63	64	62	62	70	77	85	92	100
28	30	34	39	43	47	49	51	53	56	58	63	63	61	62	63	70	78	85	93	100
29	30	35	40	45	50	51	52	55	58	59	64	61	62	63	63	70	78	85	93	100
30	31	35	40	46	51	52	53	56	59	60	62	62	63	65	65	72	79	86	93	100
31	31	35	40	46	51	53	55	58	60	58	62	62	63	65	65	72	79	86	93	100
32	32	35	40	45	51	53	56	59	57	58	62	63	63	65	64	71	78	86	93	100
33	32	36	41	47	52	55	58	55	58	59	63	63	65	65	65	72	79	86	93	100
34	33	36	41	47	52	55	55	57	58	59	63	65	64	65	64	71	78	86	93	100
35	33	36	41	47	52	53	57	58	59	61	63	64	64	64	64	71	78	86	93	100
36	33	36	41	47	49	53	57	58	59	61	63	64	63	64	63	70	78	85	93	100
37	32	36	41	44	49	53	57	58	59	60	62	62	61	62	63	70	78	85	93	100
38	32	37	39	45	50	54	57	58	60	60	61	61	61	62	61	69	77	84	92	100
39	30	35	39	45	50	54	57	58	60	59	60	60	59	60	61	69	77	84	92	100
40	28	35	39	45	50	54	56	57	59	59	60	59	59	59	60	68	76	84	92	100
41	28	35	39	45	49	52	55	55	58	57	58	59	58	59	60	68	76	84	92	100
42	27	35	39	44	49	52	54	55	56	57	57	57	58	60	61	69	77	84	92	100
43	27	34	39	44	47	50	53	53	55	55	56	57	56	60	61	69	77	84	92	100
44	26	34	38	42	47	50	52	53	54	55	55	55	56	61	62	70	77	85	92	100
45	26	33	38	42	45	48	51	51	52	53	54	55	56	61	62	70	77	85	92	100
46	24	32	37	40	43	47	49	51	52	53	54	55	56	60	61	69	77	84	92	100
47	24	30	35	39	42	45	47	49	51	53	54	55	56	59	60	68	76	84	92	100
48	23	30	35	37	40	44	47	49	50	53	54	55	55	59	57	66	74	83	91	100
49	23	29	33	35	39	42	45	48	50	53	54	55	55	57	56	65	74	82	91	100
50	21	27	32	34	37	41	44	48	50	53	54	55	55	56	55	64	73	82	91	100
51	21	26	30	34	37	41	44	48	49	51	53	53	54	55	55	64	73	82	91	100
52	20	25	30	33	37	41	44	47	48	50	50	51	51	55	53	62	72	81	100	100
53	19	24	29	32	37	41	43	47	48	48	49	49	51	52	52	62	71	100	100	100
54	18	24	29	32	37	41	43	45	47	47	47	49	49	51	51	61	100	100	100	100
55	18	23	28	32	37	41	43	45	45	45	46	46	47	50	50	100	100	100	100	100

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Attachment 1

Female, Non-Smoker

Issue	Duration																			
Age	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**	**13**	**14**	**15**	**16**	**17**	**18**	**19**	**20+**
56	18	23	28	32	36	39	42	44	44	45	46	46	46	49	100	100	100	100	100	100
57	18	23	28	31	35	38	41	42	44	44	45	45	46	100	100	100	100	100	100	100
58	17	23	26	31	35	36	38	41	41	42	45	45	100	100	100	100	100	100	100	100
59	17	23	26	30	33	35	38	39	40	41	44	100	100	100	100	100	100	100	100	100
60	17	23	26	30	32	34	36	38	39	40	100	100	100	100	100	100	100	100	100	100
61	17	22	25	29	32	33	35	36	38	80	100	100	100	100	100	100	100	100	100	100
62	16	22	25	28	30	32	34	35	80	80	100	100	100	100	100	100	100	100	100	100
63	16	20	24	28	30	32	34	80	80	80	100	100	100	100	100	100	100	100	100	100
64	14	21	24	27	29	30	80	80	80	80	100	100	100	100	100	100	100	100	100	100
65	15	19	23	25	28	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
66	15	19	23	25	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
67	15	19	22	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
68	13	18	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
69	13	64	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
70	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
71	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
72	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
73	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
74	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
75	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
76	60	60	64	68	68	72	75	75	80	100	100	100	100	100	100	100	100	100	100	100
77	60	60	64	68	68	72	75	75	100	100	100	100	100	100	100	100	100	100	100	100
78	60	60	64	68	68	72	75	100	100	100	100	100	100	100	100	100	100	100	100	100
79	60	60	64	68	68	72	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	60	60	64	68	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	60	60	64	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	60	60	64	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

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Attachment 1

Female, Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	99	100	100	100	100	100	100	95	96	97	100	100	100	100	100	100	100	100	100	100
19	87	89	92	92	92	92	84	84	86	86	92	93	95	96	99	99	99	100	100	100
20	74	77	80	80	80	73	73	73	75	77	83	83	86	88	90	92	94	96	98	100
21	71	74	78	78	71	71	73	74	77	79	85	86	88	89	90	92	94	96	98	100
22	68	71	75	70	71	71	73	74	78	79	88	90	89	89	92	94	95	97	98	100
23	65	69	67	70	70	70	73	77	79	81	89	90	90	92	92	94	95	97	98	100
24	62	60	64	69	70	70	74	77	79	81	92	90	92	93	93	94	96	97	99	100
25	53	58	63	67	69	70	74	78	81	82	92	93	93	95	95	96	97	98	99	100
26	53	58	63	69	71	72	75	79	82	82	93	93	95	96	90	92	94	96	98	100
27	52	56	63	70	74	74	78	81	82	84	93	95	95	90	90	92	94	96	98	100
28	52	56	64	71	75	77	79	82	85	86	95	95	90	92	92	94	95	97	98	100
29	51	56	64	71	78	78	81	84	86	88	95	90	90	92	92	94	95	97	98	100
30	51	56	64	72	79	79	82	85	88	89	90	90	92	93	93	94	96	97	99	100
31	51	56	64	72	78	81	84	84	88	84	90	90	92	93	93	94	96	97	99	100
32	51	56	64	71	78	81	85	86	84	85	90	90	92	94	93	94	96	97	99	100
33	51	57	62	71	78	82	85	83	84	85	90	92	93	93	93	94	96	97	99	100
34	51	56	62	71	78	82	81	83	85	86	90	92	92	94	93	94	96	97	99	100
35	51	56	62	71	78	79	83	84	85	86	90	91	91	93	93	94	96	97	99	100
36	49	56	62	71	74	79	83	84	85	86	90	90	91	93	92	94	95	97	98	100
37	48	55	62	67	74	79	83	84	85	86	89	90	89	92	91	93	95	96	98	100
38	47	55	57	66	72	77	81	84	86	86	87	88	88	90	91	93	95	96	98	100
39	45	50	57	66	72	77	81	83	85	86	86	87	86	89	90	92	94	96	98	100
40	41	50	57	66	72	77	81	83	84	85	86	86	86	89	89	91	93	96	98	100
41	40	50	57	65	71	76	79	81	83	84	85	86	85	89	90	92	94	96	98	100
42	40	49	57	65	69	74	77	80	82	83	84	85	86	90	92	94	95	97	98	100
43	39	49	55	63	69	73	76	78	80	82	83	84	85	92	93	94	96	97	99	100
44	39	48	55	62	67	71	75	78	80	80	82	84	86	93	96	97	98	98	99	100
45	37	47	55	61	65	70	73	76	78	80	81	84	86	94	97	98	98	99	99	100
46	36	46	53	59	63	68	71	75	77	79	83	85	86	93	96	97	98	98	99	100
47	34	44	51	57	62	66	70	75	77	80	83	85	86	93	94	95	96	98	99	100
48	34	44	50	54	60	64	69	74	77	80	84	86	87	92	92	94	95	97	98	100
49	33	42	48	53	58	63	68	74	77	81	84	86	87	92	91	93	95	96	98	100
50	31	41	46	51	57	61	67	74	77	81	85	87	87	91	90	92	94	96	98	100
51	30	39	45	51	56	61	67	74	75	80	83	85	85	90	90	92	94	96	98	100
52	29	38	45	50	56	62	68	74	75	79	81	83	84	90	90	92	94	96	100	100
53	28	37	43	49	57	62	68	73	74	77	79	81	83	89	89	91	93	100	100	100
54	28	36	43	49	57	63	69	73	74	75	78	80	81	87	89	91	100	100	100	100
55	26	35	42	49	57	63	69	73	73	74	76	78	79	86	87	100	100	100	100	100

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Attachment 1

Female, Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	26	35	42	49	56	62	67	71	72	74	76	78	79	85	100	100	100	100	100	100
57	26	35	42	49	55	61	66	69	72	73	76	78	79	100	100	100	100	100	100	100
58	28	36	43	49	55	59	63	68	69	72	76	78	100	100	100	100	100	100	100	100
59	28	36	43	49	54	57	63	67	68	70	76	100	100	100	100	100	100	100	100	100
60	28	36	43	49	53	57	61	64	67	69	100	100	100	100	100	100	100	100	100	100
61	26	35	42	48	52	56	59	63	66	80	100	100	100	100	100	100	100	100	100	100
62	26	33	41	47	51	55	58	62	80	80	100	100	100	100	100	100	100	100	100	100
63	25	33	41	46	51	55	57	80	80	80	100	100	100	100	100	100	100	100	100	100
64	25	33	40	45	50	53	80	80	80	80	100	100	100	100	100	100	100	100	100	100
65	24	32	39	44	49	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
66	24	32	39	44	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
67	24	32	39	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
68	24	32	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
69	24	64	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
70	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
71	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
72	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
73	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
74	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
75	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
76	60	60	64	68	68	72	75	75	80	100	100	100	100	100	100	100	100	100	100	100
77	60	60	64	68	68	72	75	75	100	100	100	100	100	100	100	100	100	100	100	100
78	60	60	64	68	68	72	75	100	100	100	100	100	100	100	100	100	100	100	100	100
79	60	60	64	68	68	72	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	60	60	64	68	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	60	60	64	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	60	60	64	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

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Appendix B
Interpretations of Statutory Accounting Principles

Introduction

Appendix B includes the final interpretations (INTs) of statutory accounting principles (SAPs) through December 2023. Reporting entities should note that interpretations are generally effective when finalized; therefore, the *Accounting Practices and Procedures Manual* (Manual) may not include every interpretation currently in effect due to the fact that it is published annually. As revisions are adopted, updates to the interpretations are tracked in the subsequent version of the Manual.

Historical

EITF Review/Rejected EITF Tracking

Beginning January 1, 1999, the Emerging Accounting Issues (E) Working Group (EAIWG) began addressing the Emerging Issues Task Force (EITF) opinions issued subsequent to 1996. In 2009, the EAIWG reached a consensus to incorporate rejected and non-applicable FASB EITFs that do not provide additional statutory accounting guidance in a listing within a designated interpretation. This interpretation (INT 99-00) included reference to all FASB EITFs, including those previously included in Appendix B as a statutory accounting interpretation, that were 1) rejected as not applicable to statutory accounting; 2) rejected without providing additional statutory guidance; or 3) rejected on the basis of issues rejected in a statement of statutory accounting principles (SSAP). In 2014, the Statutory Accounting Principles (E) Working Group (SAPWG) adopted a proposal to move all references to rejected GAAP material from INT 99-00 into *Issue Paper No. 99—Nonapplicable GAAP Pronouncements*. In 2015, Issue Paper No. 99 was moved to *Appendix D, Nonapplicable GAAP Pronouncements*.

Superseded SSAPs and Nullified INTs

In 2013, the SAPWG adopted a proposal to remove *Appendix H, Superseded SSAPs and Nullified Interpretations* from the Manual. Currently, these items are posted for public reference on the Statutory Accounting Principles (E) Working Group web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

Development Responsibilities

In 2015, the EAIWG was disbanded and its duties were absorbed by the SAPWG. The SAPWG is responsible for developing interpretations to address issues requiring interpretation, application or clarification of existing SAP.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-03: Illustration of the Accounting/Reporting of Deposit-Type Contracts in Accordance with SSAP Nos. 51R, 52 and 56

INT 00-03 Dates Discussed

December 6, 1999; March 13, 2000

INT 00-03 References

Current:
SSAP No. 51R—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

INT 00-03 Issue

1. Deposit-type contracts, as defined in SSAP No. 52 may be maintained in the general account or transferred to the separate account of an insurance company. During the process of preparing Blanks proposals to conform the reporting requirements to the SSAPs, the Impact of Codification on NAIC Publications Working Group noted an inconsistency in the reporting of deposit-type contracts between SSAP No. 52 and SSAP No. 56. At the 1999 NAIC Fall National Meeting, SSAP No. 56 was amended to clarify that the requirements of SSAP No. 52 are applicable to separate account deposit-type contracts.

2. Exhibit A is included as an illustration of accounting/reporting of separate account deposit-type contracts in accordance with SSAP Nos. 51, 52 and 56. Is this illustration consistent with the intent of the Codification of Statutory Accounting Principles (E) Working Group?

INT 00-03 Discussion

3. The Working Group reached a consensus that Exhibit A is consistent with the intent of the SSAPs.

INT 00-03 Status

4. No further discussion is planned.

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Illustrative Example of the Accounting/Reporting of Deposit-Type Contracts in Accordance with SSAPs 51R/52

NOTE: Entries presented in this illustration may not reflect all accounting entries associated with the activity, e.g., some "due from" or "due to" entries are eliminated to simplify the example.

1. Contractholder surrendered an ordinary life insurance policy and elected to place the proceeds ($100,000) under a supplementary contract without life contingencies (SCWOLC).

General Account Statement

a.	Surrender Benefits & Withdrawals	$100,000	
	Liability for Deposit –Type Contracts		$100,000
b.	Aggregate Reserves for Life Policies	$100,000	
	Increase in Aggregate Reserves for Life Policies		$100,000

2. Insurer transfers, pursuant to contract provisions, $95,000 to separate account fund for SCWOLC contracts from general account fund for SCWOLC contracts; $5,000 is retained in the general account.

General Account Statement

a.	Liability for Deposit –Type Contracts	$95,000	
	Transfers to Separate Accounts		$95,000
b.	Transfers to Separate Account	$95,000	
	Cash		$95,000

Separate Accounts Statement

c.	Other transfers from General Account (net)	$95,000	
	Transfers on account of deposit-type contracts		$95,000
d.	Cash	$95,000	
	Other Transfers from General Account		$95,000
e.	Increase in liability for deposit-type contracts	$95,000	
	Liability for Deposit-Type Contracts		$95,000

3. Insurer establishes a $4,000 CARVM valuation allowance for this contract in the separate account fund.

Separate Accounts Statement

a.	Liability for Deposit-Type Contracts	$4,000	
	Increase in liability for deposit-type contracts		$4,000
b.	Change in expense allowances recognized in reserves	$4,000	
	Other transfers from General Account (net)		$4,000

General Account Statement

c.	Transfers to Separate Accounts (net)	$4,000	
	Transfer to/or (from) Separate Accounts		$4,000

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4. Insurer's separate account fund for SCWOLC contracts assets earns $2,000 investment income that is immediately credited to the separate account fund for SCWOLC contracts.

Separate Accounts Statement			
a.	Cash	$2,000	
	Net investment income		$2,000
b.	Increase in liability for deposit-type contracts	$2,000	
	Liability for Deposit-Type Contracts		$2,000

5. Contractholder is paid a $1,000 SCWOLC contract benefit from the separate account fund. The example has been simplified to show the cash flows from the Separate Account to the General Account and the payment to the contractholder from the General Account.

General Account Statement			
a.	Cash	$1,000	
	Liability for Deposit-Type Contracts		$1,000
b.	Liability for Deposit-Type Contracts	$1,000	
	Cash		$1,000
Separate Accounts Statement			
c.	Transfers on account of deposit-type contracts	$1,000	
	Cash		$1,000
d.	Liability for Deposit-type Contracts	$1,000	
	Increase in liability for deposit-type contracts		$1,000

6. Contractholder requests the insurer to purchase a variable annuity contract (insurance product) with $25,000 drawn from the separate account fund supporting the SCWOLC contract (deposit-type contract) and transfer it to a separate fund supporting variable annuities. This example has been simplified and ignores the internal cash exchange.

General Account Statement			
a.	Transfers to Separate Accounts	$25,000	
	Premiums and Annuity Considerations		$25,000
Separate Accounts Statement			
b.	Liability for Deposit-Type Contracts	$25,000	
	Increase in liability for deposit-type contracts		$25,000
c.	Transfers on account of deposit-type contracts	$25,000	
	Other transfers to general account (net)		$25,000
d.	Other transfers to general account (net)	$25,000	
	Net Premiums and Annuity Considerations		$25,000
e.	Increase in aggregate reserve for life, annuity	$25,000	
	Aggregate Reserve for life, annuity		$25,000

7. Contractholder in accordance with a Group GIC contract requests that $15,000 be withdrawn from the Group GIC Separate Account fund maintained by the insurer and transferred to the contractholder's Separate Account fund supporting the SCWOLC contract.

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Separate Accounts Statement

a.	Liability for Deposit-Type Contracts (GIC)	$15,000	
	Increase in liability for deposit-type contracts		$15,000
b.	Transfers on account of deposit-type contracts	$15,000	
	Cash		$15,000
c.	Cash	$15,000	
	Transfers on account of deposit-type contracts		$15,000
d.	Increase in liability for deposit-type contracts	$15,000	
	Liability for Deposit-Type Contracts (SCWOLC)		$15,000

General Accounts Statement

e.	Other transfers to separate account (net)	$15,000	
	Liability for Deposit-Type Contracts (SCWOLC)		$15,000
f.	Liability for Deposit-Type Contracts (SCWOLC)	$15,000	
	Other transfers to separate account (net)		$15,000

8. Contractholder is assessed the annual administration fee of $100 for the SCWOLC contract.

Separate Accounts Statement

a.	Administration fees	$100	
	Cash		$100
b.	Liability for Deposit-type contracts	$100	
	Increase in liability for deposit-type contracts		$100

General Account Statement

c.	Cash	$100	
	Management fees		$100

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"T" Accounts

General Account Statement

Balance Sheet

Cash

Xaction Ref.	Debit	Credit
Begin Bal.	100,000	
2b		95,000
5a	1,000	
5b		1,000
8c	100	
Total	101,100	96,000
Net	5,100	

Aggregate Reserves for Life Policies etc.

Xaction Ref.	Debit	Credit
Begin Bal.		100,000
1b	100,000	

Liab for Deposit-Type Contracts

Xaction Ref.	Debit	Credit
1a		100,000
2a	95,000	
5a		1,000
5b	1,000	
7e		15,000
7f	15,000	
Total	111,000	116,000
Net		5,000

Transfers to Sep Accts Pybl

Xaction Ref.	Debit	Credit
2a		95,000
2b	95,000	
3c	4,000	
7e	15,000	
7f		15,000
Total	114,000	110,000
Net	4,000	

Summary of Operations

Premiums & Considerations

Xaction Ref.	Debit	Credit
6a		25,000

Income from Fees . . From Sep Accts

Xaction Ref.	Debit	Credit
8c		100

Surrender Benefits

Xaction Ref.	Debit	Credit
1a	100,000	

Increase in Agg Res for Life Pol etc.

Xaction Ref.	Debit	Credit
1b		100,000

Transfers to Sep Accts

Xaction Ref.	Debit	Credit
3c		4,000
6a	25,000	
Total	25,000	4,000
Net	21,000	

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Separate Accounts Statement

Balance Sheet

Cash

Xaction Ref.	Debit	Credit
Begin Bal.	15,000	
2d	95,000	
4a	2,000	
5c		1,000
7b		15,000
7c	15,000	
8a		100
Total	127,000	16,100
Net	110,900	

Aggregate Reserves for Life Policies etc.

Xaction Ref.	Debit	Credit
6e		25,000

Liab for Deposit-Type Contracts

Xaction Ref.	Debit	Credit
Begin Bal.		15,000
2e		95,000
3a	4,000	
4b		2,000
5d	1,000	
6b	25,000	
7a	15,000	
7d		15,000
8b	100	
Total	45,100	127,000
Net		81,900

Transfers to Gen Acct Pybl

Xaction Ref.	Debit	Credit
2c	95,000	
2d		95,000
3b		4,000
6c		25,000
6d	25,000	
Total	120,000	124,000
Net		4,000

Summary of Operations

Premiums & Considerations

Xaction Ref.	Debit	Credit
6d		25,000

Deposits Acct of Deposit-Type Contracts

Xaction Ref.	Debit	Credit
2c		95,000
5c	1,000	
6c	25,000	
7b	15,000	
7c		15,000
Total	41,000	110,000
Net		69,000

Net Invest Inc & Cap Gains

Xaction Ref.	Debit	Credit
4a		2,000

Change in Expense Allow

Xaction Ref.	Debit	Credit
3b	4,000	

Fees Assoc with Charges for Inv Mgmt etc.

Xaction Ref.	Debit	Credit
8a	100	

Increase in Agg Res for Life Cont etc.

Xaction Ref.	Debit	Credit
6e	25,000	

Increase in Liab for Deposit-Type Contracts

Xaction Ref.	Debit	Credit
2e	95,000	
3a		4,000
4b	2,000	
5d		1,000
6b		25,000
7a		15,000
7d	15,000	
8b		100
Total	112,000	45,100
Net	66,900	

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General Account Instructions

NOTES TO FINANCIAL STATEMENTS

19. Separate Accounts

Illustration B:

Reconciliation of Net Transfers To or (From) Separate Accounts

1. Transfers as reported in the Summary of Operations of the Separate Accounts Statement:

a.	Transfers to Separate Accounts	$ 25,000
b.	Transfers from Separate Accounts	$ 4,000
c.	Net transfers to or (From) Separate Accounts (a) – (b)	$ 21,000

2. Reconciling Adjustments:

a.	_____	$_____
b.	_____	$_____
c.	_____	$_____

3. Transfers as Reported in the Summary of Operations of the Life, Accident & Health Annual Statement

(1c) + (2) =	$ 21,000

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Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

ASSETS	Current Year			Prior Year
	1 General Account Basis	2 Fair Value Basis	3 Total (Cols. 1 + 2)	4 Total
1. Bonds (Schedule D)				
2. Stocks (Schedule D):				
2.1 Preferred stocks				
2.2 Common stocks				
3. Mortgage loans on real estate (Schedule B)				
4. Real estate (Schedule A):				
4.1 Properties held for the production of income (less $……encumbrances)				
4.2 Properties held for sale (less $……encumbrances)				
5. Policy loans				
6. Cash (Schedule E-Part 1)		110,900	110,900	
7. Short-term investments (Schedule DA)				
8. Other invested assets (Schedule BA)				
9. Aggregate write-ins for invested assets				
10. Subtotals—Cash and invested assets (Lines 1 to 9)		110,900	110,900	
11. Investment income due and accrued				
12. Receivable for securities				
13. Net adjustment in assets and liabilities due to foreign exchange rates				
14. Aggregate write-ins for other-than-invested assets				
15. Lines 10 to 14		110,900	110,900	
DETAILS OF WRITE-INS				
0901.				
0902.				
0903.				
0998. Summary of remaining write-ins Line 9 from overflow page				
0999. Totals (Lines 0901 through 0903 + 0998) (Line 9 above)				
1401.				
1402.				
1403.				
1498. Summary of remaining write-ins for Line 14 from overflow page				
1499. Totals (Lines 1401 through 1403 plus 1498) (Line 14 above)				

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Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

LIABILITIES AND SURPLUS	Current Year			Prior Year
	1 General Account Basis	2 Fair Value Basis	3 Total (Cols. 1 +2)	4 Total
1. Aggregate reserve for life, annuity and accident and health policies and contracts (Exhibit 6, Line 9999999, Col. 2)	.....	25,000	25,000	.....
2. Liability for deposit-type contracts (Exhibit 7, Line 9, Col. 1)	.....	81,900	81,900	.....
3. Interest Maintenance Reserve	.....	.....	.....	.....
4. Charges for investment management, administration and contract guarantees due or accrued	.....	.....	.....	.....
5. Investment expenses due or accrued (Exhibit 4, Line 24)	.....	.....	.....	.....
6. Investment taxes, licenses and fees due or accrued, excluding federal income taxes (Exhibit 5, Line 8)	.....	.....	.....	.....
7. Federal and foreign income taxes due or accrued (excluding deferred taxes)	.....	.....	.....	.....
8. Reserve for future federal income taxes	.....	.....	.....	.....
9. Unearned investment income (Exhibit 2, Line 14, Col. 2)	.....	.....	.....	.....
10. Other transfers to general account due or accrued (net) (including $..... accrued expense allowances recognized in reserves)	.....	4,000	4,000	.....
11. Remittances and items not allocated	.....	.....	.....	.....
12. Payable for securities	.....	.....	.....	.....
13. Net adjustment in assets and liabilities due to foreign exchange rates	.....	.....	.....	.....
14. Aggregate write-ins for liabilities				
15. Total Liabilities (including $.....due or accrued net transfers to or (from) the general account)		110,900	110,900	
16. Contributed surplus	.....	.....	.....	.....
17. Aggregate write-ins for special surplus funds	.....	.....	.....	.....
18. Unassigned funds				
19. Surplus (Lines 16 through 18)				
20. Totals		110,900	110,900	
DETAILS OF WRITE-INS				
1401.	.....	.....	.....	.....
1402.	.....	.....	.....	.....
1403.	.....	.....	.....	.....
1498. Summary of remaining write-ins for Line 14 from overflow page	.....	.....	.....	.....
1499. Totals (Lines 1401 through 1403 plus 1498) (Line 14 above)				
1701.	.....	.....	.....	.....
1702.	.....	.....	.....	.....
1703.	.....	.....	.....	.....
1798. Summary of remaining write-ins for Line 17 from overflow page	.....	.....	.....	.....
1799. Totals (Lines 1701 through 1703 plus 1798) (Line 17 above)				

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Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

SUMMARY OF OPERATIONS	1 Current Year	2 Prior Year
1. Transfers to Separate Accounts:		
1.1 Net premiums and annuity considerations for life and accident and health policies and contracts	25,000	
1.2 Considerations for supplementary contracts with life contingencies		
1.3 Aggregate write-ins for other transfers to Separate Accounts		
1.4 Totals (Lines 1.1 to 1.3)	25,000	
2. Transfers on account of deposit-type contracts (including $110,000 deposits less $41,000 withdrawals)	69,000	
3. Net investment income and capital gains and losses (Exhibit 1, Line 9)	2,000	
4. Aggregate write-ins for other income		
5. Totals (Lines 1.4 to 4)	96,000	
DEDUCT:		
6. Transfers from the Separate Account on account of contract benefits:		
6.1 Death benefits		
6.2 Matured endowments		
6.3 Annuity benefits		
6.4 Payments on supplementary contracts with life contingencies		
6.5 Accident and health benefits		
6.6 Surrender benefits and withdrawals for life contracts		
6.7 Aggregate write-ins for other transfers from Separate Accounts on account of contract benefits		
7. Transfers on account of policy loans		
8. Net transfer of reserves from or (to) Separate Accounts		
9. Other transfers from the Separate Accounts:		
9.1 Federal and foreign income taxes incurred		
9.2 Change in expense allowances recognized in reserves	4,000	
9.3 Aggregate write-ins for other transfers from Separate Accounts		
10. Subtotals (Lines 6.1 to 9.3)	4,000	
11. Fees associated with charges for investment management, administration and contract guarantees	100	
12. Increase in aggregate reserve for life and accident and health policies and contracts	25,000	
13. Increase in reserve for variable dividend accumulations		
14. Increase in liability for deposit-type contracts	66,900	
15. Increase in reserve for future federal income taxes		
16. Aggregate write-ins for reserves and funds		
17. Totals (Lines 10 to 16)	96,000	
18. Net gain from operations (including $…….unrealized capital gains) (Line 5 minus Line 17)	0	
SURPLUS ACCOUNT		
19. Surplus, December 31, prior year		
20. Net gain from operations (Line 18)		
21. Surplus contributed or (withdrawn) during year		
22. Change in reserve on account of change in valuation basis, (increase) or decrease		
23. Transfer from Separate Accounts of the change in expense allowances charged or credited to surplus		
24. Aggregate write-ins for gains and losses in surplus		
25. Surplus, December 31, current year (Page 3, Line 19)		
DETAILS OF WRITE-INS		
01.301.		
01.302.		
01.303.		
01.398. Summary of remaining write-ins for Line 1.3 from overflow page		
01.399. Totals (Lines 01.301 through 01.303 plus 01.398) (Line 1.3 above)		
0401.		
0402.		
0403.		
0498. Summary of remaining write-ins for Line 4 from overflow page		
0499. Totals (Lines 0401 through 0403 plus 0498) (Line 4 above)		
06.701.		
06.702.		
06.703.		
06.798. Summary of remaining write-ins for Line 6.7 from overflow page		
06.799. Totals (Lines 06.701 through 06.703 plus 06.798) (Line 6.7 above)		
09.301.		
09.302.		
09.303.		
09.398. Summary of remaining write-ins for Line 9.3 from overflow page		
09.399. Totals (Lines 09.301 through 09.303 plus 09.398) (Line 9.3 above)		
1601.		
1602.		
1603.		
1698. Summary of remaining write-ins for Line 16 from overflow page		
1699. Totals (Lines 1601 through 1603 plus 1698) (Line 16 above)		
2401.		
2402.		
2403.		
2498. Summary of remaining write-ins for Line 24 from overflow page		
2499. Totals (Lines 2401 through 2403 plus 2498) (Line 24 above)		

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Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
1. Bonds				
2. Stocks:				
2.1 Preferred stocks (Schedule D, Part 2, Section 1)				
2.2 Common stocks (Schedule D, Part 2, Section 2)				
3. Mortgage loans on real estate (Schedule B, Part 1):				
3.1 First liens				
3.2 Other than first liens				
4. Real estate (Schedule A):				
4.1 Properties occupied by the company (less $..... encumbrances)				
4.2 Properties held for the production of income (less $..... encumbrances)				
4.3 Properties held for sale (less $..... encumbrances)				
5. Policy loans				
6. Premium notes, including $..... for first year premiums				
7. Cash ($...……., Schedule E, Part 1) and short-term investments ($...…….…., Schedule DA, Part 2)	5,100		5,100	
8. Other invested assets (Schedule BA, Part 1)				
9. Receivable for securities				
10. Aggregate write-ins for invested assets				
11. Subtotals, cash and invested assets (Lines 1 to 10)	5,100		5,100	
12. Reinsurance ceded:				
12.1 Amounts recoverable from reinsurers (Schedule S, Part 2)				
12.2 Commissions and expense allowances due				
12.3 Experience rating and other refunds due				
12.4 Other amounts receivable under reinsurance contracts				
13. Electronic data processing equipment and software				
14. Federal and foreign income tax recoverable and interest thereon (including $…… net deferred tax asset)				
15. Guaranty funds receivable or on deposit				
16. Life insurance premiums and annuity considerations deferred and uncollected on in force business (less premiums on reinsurance ceded and less $.....loading)				
17. Accident and health premiums due and unpaid				
18. Investment income due and accrued (Exhibit 2)				
19. Net adjustment in assets and liabilities due to foreign exchange rates				
20. Receivable from parent, subsidiaries and affiliates				
21. Amounts receivable relating to uninsured accident and health plans				
22. Amounts due from agents				
23. Other assets nonadmitted (Exhibit 12)				
24. Aggregate write-ins for other-than-invested assets				
25. Total assets excluding Separate Accounts business (Lines 11 to 24)	5,100		5,100	
26. From Separate Accounts Statement	110,900		110,900	
27. Total (Lines 25 and 26)	116,000		116,000	
DETAILS OF WRITE-INS				
1001.				
1002.				
1003.				
1098. Summary of remaining write-ins for Line 10 from overflow page				
1099. Totals (Lines 1001 through 1003 + 1098) (Line 10 above)				
2401.				
2402.				
2403.				
2498. Summary of remaining write-ins for Line 24 from overflow page				
2499. Totals (Lines 2401 through 2403 + 2498) (Line 24 above)				

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LIABILITIES, SURPLUS AND OTHER FUNDS	1 Current Year	2 Prior Year
1. Aggregate reserve for life policies and contracts $.....(Exhibit 8, Line 9999999) less $ .included in Line 6.3 (including $ Modco Reserve	.....	.....
2. Aggregate reserve for accident and health policies (Exhibit 9, Line 17, Col. 1) (including $.....Modco Reserve)	.....	.....
3. Liability for deposit-type contracts (Exhibit 10, Line 14, Col. 1) (including $.....Modco Reserve)	5,000	.....
4. Policy and contract claims:		
4.1 Life (Exhibit 11, Part 1, Line 4.4, Col. 1 less sum of Cols. 9, 10 and 11)	.....	.....
4.2 Accident and health (Exhibit 11, Part 1, Line 4.4, sum of Cols. 9, 10 and 11)	.....	.....
5. Policyholders' dividends $.....and coupons $.....due and unpaid (Exhibit 7, Line 10)	.....	.....
6. Provision for policyholders' dividends and coupons payable in following calendar year—estimated amounts:		
6.1 Dividends apportioned for payment to ....., 20 ..... (including $ ..... Modco Reserve)	.....	.....
6.2 Dividends not yet apportioned (including $ ..... Modco Reserve)	.....	.....
6.3. Coupons and similar benefits (including $ ..... Modco Reserve)	.....	.....
7. Amount provisionally held for deferred dividend policies not included in Line 6	.....	.....
8. Premiums and annuity considerations for life and accident and health policies and contracts received in advance less $.....discount; including $.....accident and health premiums (Exhibit 1, Part 1, Col. 1, sum of Lines 4 and 14)	.....	.....
9. Policy and contract liabilities not included elsewhere:		
9.1 Surrender values on canceled policies	.....	.....
9.2 Provision for experience rating refunds, including $..... accident and health experience rating refunds	.....	.....
9.3 Other amounts payable on reinsurance, including $.....assumed and $.....ceded	.....	.....
9.4 Interest Maintenance Reserve (Page 33, Line 6)	.....	.....
10. Commissions to agents due or accrued-life and annuity contracts $..... accident and health $……. and deposit-type contract funds $	.....	.....
11. Commissions and expense allowances payable on reinsurance assumed	.....	.....
12. General expenses due or accrued (Exhibit 5, Line 12, Col. 5)	.....	.....
13. Transfers to Separate Accounts due or accrued (net) (including ($ 4,000) accrued for expense allowances recognized in reserves)	(4,000)	.....
14. Taxes, licenses and fees due or accrued, excluding federal income taxes (Exhibit 6, Line 9, Col. 5)	.....	.....
15. Federal and foreign income taxes, including $.....on realized capital gains (losses) (including $.. net-deferred tax liability)	.....	.....
16. Unearned investment income (Exhibit 2, Line 9, Col. 2)	.....	.....
17. Amounts withheld or retained by company as agent or trustee	.....	.....
18. Amounts held for agents' account, including $..... agents' credit balances	.....	.....
19. Remittances and items not allocated	.....	.....
20. Net adjustment in assets and liabilities due to foreign exchange rates	.....	.....
21. Liability for benefits for employees and agents if not included above	.....	.....
22. Borrowed money $.....and interest thereon $	.....	.....
23. Dividends to stockholders declared and unpaid	.....	.....
24. Miscellaneous liabilities:		
24.1 Asset valuation reserve (Page 34, Line 15, Col. 7)	.....	.....
24.2 Reinsurance in unauthorized companies	.....	.....
24.3 Funds held under reinsurance treaties with unauthorized reinsurers	.....	.....
24.4 Payable to parent, subsidiaries and affiliates	.....	.....
24.5 Drafts outstanding	.....	.....
24.6 Liability for amounts held under uninsured accident and health plans	.....	.....
24.7 Funds held under coinsurance	.....	.....
24.8 Payable for securities	.....	.....
24.9 Capital notes $…… and interest thereon $…….	.....	.....
25. Aggregate write-ins for liabilities		
26. Total liabilities excluding Separate Accounts business (Lines 1 to 25)	1,000	
27. From Separate Accounts statement	110,900	.....
28. Total liabilities (Lines 26 and 27)	111,900	
29. Common capital stock	.....	.....
30. Preferred capital stock	.....	.....
31. Aggregate write-ins for other than special surplus funds	.....	.....
32. Surplus notes	.....	.....
33. Gross paid in and contributed surplus (Page 3, Line 33, Col. 2 plus Page 4, Line 51.1, Col. 1)	.....	.....
34. Aggregate write-ins for special surplus funds	.....	.....
35. Unassigned funds (surplus)	.....	
36. Less treasury stock, at cost:		.....
36.1 ..... shares common (value included in Line 29 $ .....)	.....	.....
36.2 ..... shares preferred (value included in Line 30 $ .....)	.....	.....
37. Surplus (total Lines 31 + 32 + 33 + 34 + 35 - 36) (Including $.....in Separate Accounts Statement)		
38. Totals of Lines 29, 30 and 37 (Page 4, Line 55)		
39. Totals of Lines 28 and 38 (Page 2, Line 27, Col. 3)		
DETAILS OF WRITE-INS		
2501.	.....	.....
2502.	.....	.....
2503.	.....	.....
2598. Summary of remaining write-ins for Line 25 from overflow page	.....	.....
2599. Totals (Lines 2501 through 2503 plus 2598) (Line 25 above)		
3101.	.....	.....
3102.	.....	.....
3103.	.....	.....
3198. Summary of remaining write-ins for Line 31 from overflow page	.....	.....
3199. Totals (Lines 3101 through 3103 plus 3198) (Line 31 above)		
3401.	.....	.....
3402.	.....	.....
3403.	.....	.....
3498. Summary of remaining write-ins for Line 34 from overflow page	.....	.....
3499. Totals (Lines 3401 through 3403 plus 3498) (Line 34 above)		

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SUMMARY OF OPERATIONS (Excluding Unrealized Capital Gains and Losses)	1 Current Year	2 Prior Year
1. Premiums and annuity considerations for life and accident and health policies and contracts (Exhibit 1, Part 1, Line 20.4, Col. 1, less Col. 11)	25,000	
2. Considerations for supplementary contracts with life contingencies		
3. Net investment income (Exhibit 2, Line 16)		
4. Amortization of Interest Maintenance Reserve (IMR) (Page 33, Line 5)		
5. Separate Accounts net gain from operations excluding unrealized gains or losses		
6. Commissions and expense allowances on reinsurance ceded (Exhibit 1, Part 2, Line 26.1, Col. 1)		
7. Reserve adjustments on reinsurance ceded		
8. Miscellaneous Income:		
8.1 Income from fees associated with investment management, administration and contract guarantees from Separate Accounts	100	
8.2 Charges and fees for deposit-type contracts		
8.3 Aggregate write-ins for miscellaneous income		
9. Totals (Lines 1 to 8.3)	25,100	
10. Death benefits		
11. Matured endowments (excluding guaranteed annual pure endowments)		
12. Annuity benefits (Exhibit 11, Part 2, Line 6.4, Cols. 4 + 8)		
13. Disability benefits and benefits under accident and health policies		
14. Coupons, guaranteed annual pure endowments and similar benefits		
15. Surrender benefits and withdrawals for life contracts	100,000	
16. Group conversions		
17. Interest and adjustments on policy or deposit-type contract funds		
18. Payments on supplementary contracts with life contingencies		
19. Increase in aggregate reserves for life and accident and health policies and contracts	(100,000)	
20. Totals (Lines 10 to 19)	0	
21. Commissions on premiums, annuity considerations and deposit-type contract funds (direct business only) (Exhibit 1, Part 2, Line 31, Col. 1, less Col. 11)		
22. Commissions and expense allowances on reinsurance assumed (Exhibit 1, Part 2, Line 26.2, Col. 1, less Col. 11)		
23. General insurance expenses (Exhibit 5, Line 10, Cols. 1 + 2 + 3)		
24. Insurance taxes, licenses and fees, excluding federal income taxes (Exhibit 6, Line 7, Cols. 1 + 2 + 3)		
25. Increase in loading on deferred and uncollected premiums		
26. Net transfers to or (from) Separate Accounts	21,000	
27. Aggregate write-ins for deductions		
28. Totals (Lines 20 to 27)	21,000	
29. Net gain from operations before dividends to policyholders and federal income taxes (Line 9 minus Line 28)	4,100	
30. Dividends to policyholders		
31. Net gain from operations after dividends to policyholders and before federal income taxes (Line 29 minus Line 30)		
32. Federal and foreign income taxes incurred (excluding tax on capital gains)		
33. Net gain from operations after dividends to policyholders and federal income taxes and before realized capital gains or (losses) (Line 31 minus Line 32)		
34. Net realized capital gains or (losses) less capital gains tax and transferred to the IMR (Exhibit 3, Footnote (a), Line 3C)		
35. Net income (Line 33 plus Line 34)		
CAPITAL AND SURPLUS ACCOUNT		
36. Capital and surplus, December 31, prior year (Page 3, Line 38, Col. 2)		
37. Net income (Line 35)		
38. Change in net unrealized capital gains (losses)		
39. Change in net unrealized foreign exchange capital gain (loss)		
40. Change in net deferred income tax		
41. Change in nonadmitted assets and related items (Exhibit 12, Line 6, Col. 3)		
42. Change in liability for reinsurance in unauthorized companies		
43. Change in reserve on account of change in valuation basis, (increase) or decrease (Exhibit 8A, Line 9999999, Col. 4)		
44. Change in asset valuation reserve (Page 34, Lines 2 through 4 plus 8, 11 and 12, Col. 7)		
45. Change in treasury stock (Page 3, Lines 36.1 and 36.2 Col. 2 minus Col. 1)		
46. Surplus (contributed to) withdrawn from Separate Accounts during period		
47. Other changes in surplus in Separate Accounts statement		
48. Change in surplus notes		
49. Cumulative effect of changes in accounting principles		
50. Capital changes:		
50.1 Paid in		
50.2 Transferred from surplus (Stock Dividend)		
50.3 Transferred to surplus		
51. Surplus adjustment:		
51.1 Paid in		
51.2 Transferred to capital (Stock Dividend)		
51.3 Transferred from capital		
51.4 Change in surplus as a result of reinsurance		
52. Dividends to stockholders		
53. Aggregate write-ins for gains and losses in surplus		
54. Net change in capital and surplus for the year (Lines 37 through 53)		
55. Capital and surplus, December 31, current year (Lines 36 + 54) (Page 3, Line 38)		
DETAILS OF WRITE-INS		
08.301.		
08.302.		
08.303.		
08.398. Summary of remaining write-ins for Line 8.3 from overflow page		
08.399. Totals (Lines 08.301 through 08.303 plus 08.398) (Line 8.3 above)		
2701.		
2702.		
2703.		
2798. Summary of remaining write-ins for Line 27 from overflow page		
2799. Totals (Lines 2701 through 2703 plus 2798) (Line 27 above)		
5301.		
5302.		
5303.		
5398. Summary of remaining write-ins for Line 53 from overflow page		
5399. Totals (Lines 5301 through 5303 plus 5398) (Line 53 above)		

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CASH FLOW

		1 Current Year	2 Prior Year
	Cash from Operations		
1.	Premiums and annuity considerations for life and accident and health policies and contracts	25,000	
2.	Charges and fees for deposit-type contracts		
3.	Considerations for supplementary contracts with life contingencies		
4.	Net investment income		
5.	Commissions and expense allowances on reinsurance ceded		
6.	Fees associated with investment management, administration and contract guarantees from Separate Accounts	100	
7.	Aggregate write-ins for miscellaneous income		
8.	Total (Lines 1 to 7)	25,100	
9.	Death benefits		
10.	Matured endowments		
11.	Annuity benefits		
12.	Disability benefits and benefits under accident and health policies		
13.	Coupons, guaranteed annual pure endowments and similar benefits		
14.	Surrender benefits and withdrawals for life contracts	100,000	
15.	Group conversions		
16.	Interest and adjustments on policy or deposit-type contract funds		
17.	Payments on supplementary contracts with life contingencies		
18.	Total (Lines 9 to 17)	100,000	
19.	Commissions on premiums, annuity considerations and deposit-type contract funds		
20.	Commissions and expense allowances on reinsurance assumed		
21.	General insurance expenses		
22.	Insurance taxes, licenses and fees, excluding federal income taxes		
23.	Net transfers to or (from) Separate Accounts	25,000	
24.	Aggregate write-ins for deductions		
25.	Total (Lines 18 to 24)	125,000	
26.	Dividends paid to policyholders		
27.	Federal income taxes (excluding tax on capital gains)		
28.	Total (Lines 25 to 27)	125,000	
29.	Net cash from operations (Line 8 minus Line 28)	(99,900)	
	Cash from Investments		
30.	Proceeds from investments sold, matured or repaid:		
	30.1 Bonds		
	30.2 Stocks		
	30.3 Mortgage loans		
	30.4 Real estate		
	30.5 Other invested assets		
	30.6 Net gains (losses) on cash and short-term investments		
	30.7 Miscellaneous proceeds		
	30.8 Total investment proceeds (Lines 30.1 to 30.7)		
31.	Net tax on capital gains (losses)		
32.	Total (Line 30.8 minus Line 31)		
33.	Cost of investments acquired (long-term only):		
	33.1 Bonds		
	33.2 Stocks		
	33.3 Mortgage loans		
	33.4 Real estate		
	33.5 Other invested assets		
	33.6 Miscellaneous applications		
	33.7 Total investments acquired (Lines 33.1 to 33.6)		
34.	Net increase (or decrease) in policy loans and premium notes		
35.	Net cash from investments (Line 32 minus Line 33.7 minus Line 34)		
	Cash from Financing and Miscellaneous Sources		
36.	Cash provided:		
	36.1 Surplus notes, capital and surplus paid in		
	36.2 Borrowed money $.....less amounts repaid $		
	36.3 Capital notes $..... less amounts repaid $.....		
	36.4 Deposits on deposit-type contract funds and other liabilities without life or disability contingencies	115,000	
	36.5 Other cash provided		
	36.6 Total (Lines 36.1 to 36.5)	115,000	
37.	Cash applied:		
	37.1 Dividends to stockholders paid		
	37.2 Interest on indebtedness		
	37.3 Withdrawals on deposit-type contract funds and other liabilities without life or disability contingencies	110,000	
	37.4 Other applications (net)		
	37.5 Total (Lines 37.1 to 37.4)	110,000	
38.	Net cash from financing and miscellaneous sources (Line 36.6 minus Line 37.5)	5,000	
	RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS		
39.	Net change in cash and short-term investments (Line 29, plus Line 35, plus Line 38)	(94,900)	
40.	Cash and short-term investments:		
	40.1 Beginning of year	100,000	
	40.2 End of year (Line 39 plus Line 40.1)	5,100	
	DETAILS OF WRITE-INS		
0701.			
0702.			
0703.			
0798.	Summary of remaining write-ins for Line 7 from overflow page		
0799.	Totals (Lines 0701 through 0703 plus 0798) (Line 7 above)		
2401.			
2402.			
2403.			
2498.	Summary of remaining write-ins for Line 24 from overflow page		
2499.	Totals (Lines 2401 through 2403 plus 2498) (Line 24 above)		

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EXHIBIT 7—DEPOSIT TYPE CONTRACTS

	1 Total	2 Guaranteed Interest Contracts	3 Supplemental Contracts and Annuities Certain	4 Dividend Accumulations or Refunds	5 Premium and Other Deposit Funds	6 Other
1. Balance at the beginning of the year	15,000	15,000	.....	.....	.....	.....
2. Deposits received during the year	110,000	.....	110,000	.....	.....	.....
3. Investment earnings credited to the account	2,000	.....	2,000	.....	.....	.....
4. Other net change in reserves	(4,000)	.....	(4,000)	.....	.....	.....
5. Fees and other charges assessed	100	.....	100	.....	.....	.....
6. Surrender charges	.....	.....	.....	.....	.....	.....
7. Net surrender or withdrawal payments	41,000	15,000	26,000	.....	.....	.....
8. Other net transfers to or (from) General Accounts	.....	.....	.....	.....	.....	.....
9. Balance at the end of current year(Lines 1+2+3+4-5-6-7-8)	81,900	0	81,900			

Reconciliation of Exh. 7 to Summary of Operations:

Exh. 7, Column 1, Line 9	81,900
Exh. 7, Column 1, Line 1	15,000
Summary of Operations, Column 1, Line 14	66,900

Exh. 7, Column 1, Line 2	110,000
Exh. 7, Column 1, Line 7	41,000
Summary of Operations, Column 1, Line 2	69,000

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EXHIBIT 10—DEPOSIT TYPE CONTRACTS

	1 Total	2 Guaranteed Interest Contracts	3 Supplemental Contracts and Annuities Certain	4 Dividend Accumulations or Refunds	5 Premium and Other Deposit Funds	6 Other
1. Balance at the beginning of the year before reinsurance						
2. Deposits received during the year	115,000		115,000			
3. Investment earnings credited to the account						
4. Other net change in reserves						
5. Fees and other charges assessed						
6. Surrender charges						
7. Net surrender or withdrawal payments	41,000	15,000	26,000			
8. Other net transfers to or (from) Separate Accounts	69,000	(15,000)	84,000			
9. Balance at the end of current year before reinsurance (Lines 1+2+3+4-5-6-7-8)	5,000	0	5,000			
10. Reinsurance balance at the beginning of the year						
11. Net change in reinsurance assumed						
12. Net change in reinsurance ceded						
13. Reinsurance balance at the end of the year (Lines 10+11-12)						
14. Net balance at the end of current year after reinsurance (Lines 9-13)						

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-20: Application of SEC SAB No. 99, Materiality to the Preamble of the AP&P Manual

INT 00-20 Dates Discussed

June 12, 2000; September 20, 2000; June 11, 2001; October 16, 2001

INT 00-20 References

Current:
Preamble to the NAIC *Accounting Practices and Procedures Manual* (Preamble)

INT 00-20 Issue

1. In summary, SEC Staff Accounting Bulletin No. 99, *Materiality* (SAB No. 99) addresses two issues; 1) may a company or auditor assume the immateriality of items that fall below a percentage threshold set by management or its auditors to determine whether amounts and items are material to the financial statements? and 2) may a company make intentional immaterial misstatements in its financial statements? The SEC staff answers each question as NO and gives numerous references to FASB guidelines to support their opinion.

2. The issue is whether the responses outlined in SAB No. 99 can be applied to statutory accounting and the concept of materiality as defined in paragraphs 48-53 of the Preamble.

INT 00-20 Discussion

3. At the 2000 Spring National Meeting, the Statutory Accounting Principles (E) Working Group (SAPWG) reviewed SAB No. 99 for incorporation into the *Accounting Practices and Procedures Manual* (AP&P Manual or Manual). The SAPWG determined that no modifications to the Preamble were warranted and referred the issue to the NAIC/AICPA Working Group for their consideration. The SAPWG felt the SAB had applicability to management of reporting entities, independent auditors and State Examiners. The NAIC/AICPA WG reviewed the SAB and determined that an interpretation of the Preamble was a more effective way to adopt the SAB for statutory accounting. The NAIC/AICPA WG felt that the AP&P Manual reached a larger audience than the A/S Instructions or Examiner's Handbook.

4. The Working Group reached a consensus to adopt an interpretation of the concept of materiality based on certain matters outlined in SAB No. 99. The Working Group believes the responses below provide additional support for the concepts delineated in Section VII of the Preamble. The SAB contains numerous references to SEC guidelines and GAAP pronouncements that are not reflected in this interpretation as such matters are not necessarily applicable or appropriate for statutory financial reporting. The interpretative responses (as modified by this interpretation) are as follows:

> **QUESTION:** Paragraph 53 of the Preamble states "The provisions of this Manual need not be applied to immaterial items." May a reporting entity's management, state examiner or independent auditor of the entity's financial statements assume the immateriality of items that fall below a percentage threshold set by management, state examiner or independent auditor to determine whether amounts and items are material to the financial statements?
>
> **INTERPRETIVE RESPONSE** No. Over time, the NAIC is aware that reporting entities have developed quantitative thresholds as "rules of thumb" to assist in the preparation of their financial statements, and that state examiners and independent auditors also have used these thresholds in

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their evaluation of whether items might be considered material to users of a reporting entity's financial statements. One rule of thumb in particular suggests that the misstatement or omission of an item that falls under a 5% of surplus threshold is not material in the absence of particularly egregious circumstances, such as self-dealing or misappropriation by senior management. Exclusive reliance on this or any percentage or numerical threshold has no basis in the accounting literature or the law.

The use of a percentage as a numerical threshold, such as 5% of surplus, may provide the basis for a preliminary assumption that - without considering all relevant circumstances - a deviation of less than the specified percentage with respect to a particular item on the reporting entity's financial statements is unlikely to be material. The NAIC has no objection to such a "rule of thumb" as an initial step in assessing materiality. But quantifying, in percentage terms, the magnitude of a misstatement is only the beginning of an analysis of materiality; it cannot appropriately be used as a substitute for a full analysis of all relevant considerations. Materiality concerns the significance of an item to users of the reporting entity's financial statements. A matter is "material" if there is a substantial likelihood that a reasonable person would consider it important.

QUESTION: May a reporting entity make intentional immaterial misstatements in its financial statements?

INTERPRETIVE RESPONSE No. In certain circumstances, intentional immaterial misstatements are unlawful.

Each reporting entity must make and keep books, records, and accounts, that, in reasonable detail, accurately and fairly reflect the acquisitions and dispositions of assets of the reporting entity and must maintain internal control that is sufficient to provide reasonable, but not absolute, assurances that, among other things, transactions are recorded as necessary to permit the preparation of financial statements in conformity with the revised *Accounting Practices and Procedures Manual*. In this context, determinations of what constitutes "reasonable assurance" and "reasonable detail" are based not on a "materiality" analysis but on the level of detail and degree of assurance that would satisfy prudent individuals in the conduct of their own affairs. It is unlikely that it is ever "reasonable" for a reporting entity to record misstatements or not to correct known misstatements as part of an ongoing effort directed by or known to senior management for the purpose of "managing" reported results or financial position.

The National Commission on Fraudulent Financial Reporting, also known as the Treadway Commission, in its 1987 report:

> The tone set by top management - the corporate environment or culture within which financial reporting occurs - is the most important factor contributing to the integrity of the financial reporting process. Notwithstanding an impressive set of written rules and procedures, if the tone set by management is lax, fraudulent financial reporting is more likely to occur.

Statement on Auditing Standards No. ("SAS") 54, "Illegal Acts by Clients," and SAS No. 82, "Consideration of Fraud in a Financial Statement Audit" provide guidance to the independent auditor. Pursuant to paragraph 38 of SAS 82, if the independent auditor determines there is evidence that fraud may exist, the independent auditor must discuss the matter with the appropriate level of management. The auditor must report directly to the audit committee fraud involving senior management and fraud that causes a material misstatement of the financial statements. Paragraph 4 of SAS No. 82 states that "misstatements arising from fraudulent financial reporting are intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users." SAS No. 82 further states that

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fraudulent financial reporting may involve falsification or alteration of accounting records; misrepresenting or omitting events, transactions or other information in the financial statements; and the intentional misapplication of accounting principles relating to amounts, classifications, the manner of presentation, or disclosures in the financial statements. The clear implication of SAS No. 82 is that immaterial misstatements may be fraudulent financial reporting.

Independent auditors that learn of intentional misstatements may also be required to (1) re-evaluate the degree of audit risk involved in the audit engagement, (2) determine whether to revise the nature, timing, and extent of audit procedures accordingly, and (3) consider whether to resign.

Intentional misstatements also may signal the existence of reportable conditions or material weaknesses in the reporting entity's system of internal accounting control designed to detect and deter improper accounting and financial reporting.

An auditor is required to report to the audit committee any reportable conditions or material weaknesses in a reporting entity's system of internal accounting control that the auditor discovers in the course of the examination of the registrant's financial statements.

INT 00-20 Status

5. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-24: EITF 98-13: Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of the Investee and EITF 99-10: Percentage Used to Determine the Amount of Equity Method Losses

INT 00-24 Dates Discussed

June 12, 2000; September 11, 2000

INT 00-24 References

Current:
SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities

Superseded:
SSAP No. 46—Investments in Subsidiary, Controlled, and Affiliated Entities
SSAP No. 88—Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46

INT 00-24 Issue

1. EITF 98-13 and Topic No. D-68, *Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of an Investee* (EITF 98-13 or Topic D-68) provides the FASB staff position that Accounting Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock* (APB No. 18) requires an investor that owns common (or other voting) stock and also (a) owns debt securities (including mandatorily redeemable preferred stock), (b) owns preferred stock, or (c) has extended loans to the investee to continue to report losses. Paragraph 13 of FASB Statement 114, *Accounting by Creditors for Impairment of a Loan* (FAS 114) as amended by FASB Statement 118, *Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures* (FAS 118) provides that when a loan is impaired, a creditor shall measure impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate. Paragraph 12 of FASB Statement 115, *Accounting for Certain Investments in Debt and Equity Securities* (FAS 115) provides that investments in both debt securities not held to maturity and equity securities that have readily determinable fair values shall be carried at fair value.

2. EITF 99-10, *Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of an Investee* (EITF 99-10) and Topic No. D-68 provides the FASB staff position on an investor's accounting when more than one type of interest is held. Specifically, the FASB staff announced that APB No. 18 requires that when an investor owns common stock and also (a) owns debt securities (including mandatorily redeemable preferred stock), (b) owns preferred stock, or (c) has extended loans to the investee (collectively referred to as "other investments"), the equity method investor should continue to report losses up to the investor's investment carrying value, including any additional financial support made or committed to by the investor. EITF 98-13 provides guidance on the interaction between the applicable literature for those instruments and APB No. 18 for situations in which an investee is incurring losses and (a) an investor is not required to advance additional funds to the investee and (b) previous losses have reduced the common stock investment account to zero. However, neither Topic D-68 nor EITF 98-13 provides guidance on how an investor should calculate the amount of equity method losses or subsequent income in that circumstance.

3. The issue is, when an investor is required to account for a common stock investment using the equity method, how the equity method loss pickup from the application of APB No. 18 (when the

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carrying amount of the common stock has been reduced to zero) interacts with the applicable literature relating to investments in the other securities of the investee (either FAS 114 or FAS 115), and if an investor owns common stock and "other investments" in an investee and is not required to advance additional funds to the investee and if previous losses have reduced the common stock investment account to zero, how additional equity method losses should be measured and recognized by the investor.

INT 00-24 Discussion

4. The Working Group reached a consensus to adopt the final conclusions reached in EITF 98-13 and 99-10 with modification as follows:

5. The EITF reached a consensus that in situations where (a) an investor is not required to advance additional funds to the investee and (b) previous losses have reduced the common stock investment account to zero, the investor should continue to report its share of equity method losses in its statement of operations to the extent of and as an adjustment to the adjusted basis of the other investments in the investee. The order in which those equity method losses should be applied to the other investments should follow the seniority of the other investments (that is, priority in liquidation). For each period, the adjusted basis of the other investments should be adjusted for the equity method losses, then the investor should apply SSAP No. 97 to the other investments, as applicable.

6. For purposes of this consensus, other investments in the investee include, but are not limited to, preferred stock, debt securities, and loans to the investee (collectively referred to as loans and securities). The cost basis of the other investments is the original cost of those investments adjusted for the effects of other-than-temporary write-downs, unrealized gains and losses, and amortization of any discount or premium on debt securities or loans. The adjusted basis is the cost basis adjusted for the valuation allowance account for an investee loan and the cumulative equity method losses applied to the other investments. Equity method income subsequently recorded should be applied to the adjusted basis of the other investments in reverse order of the application of the equity method losses (that is, equity method income is applied to the more senior securities first).

7. When the investor has loans and securities of the investee that are within the scopes of SSAP No. 97, the investor should perform the following in order to determine the amount of equity method loss to report at the end of a period:

a. Apply SSAP No. 97 to determine the maximum amount of equity method losses.

b. Determine whether the adjusted basis of the other investment(s) in the investee is positive.

i. When the adjusted basis is positive, the adjusted basis of the other investments should be adjusted for the amount of the equity method loss based on its seniority. For investments accounted for in accordance with *SSAP No. 30R—Unaffiliated Common Stock*, this adjusted basis becomes the security's basis from which subsequent changes in fair value are measured.

ii. When the adjusted basis reaches zero, equity method losses should cease being reported; however, the investor should continue to track the amount of unreported equity method losses for purposes of applying SSAP No. 97. (If one of the other investments is sold at a time when its carrying value exceeds its adjusted basis, the difference between the cost basis of that other investment and its adjusted basis at the time of sale represents equity method losses that were originally applied to that other investment but effectively reversed upon its sale. Accordingly, that excess represents unreported equity method losses that should continue to be tracked before future equity method income can be reported.

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c. After applying SSAP No. 97, apply SSAP No. 30R to the adjusted basis of the other investments in the investee, as applicable. Apply appropriate statutory accounting principles to other investments that are not within the scope of SSAP No. 30R.

8. The EITF reached a consensus that an investor should not recognize equity method losses based solely on the percentage of investee common stock held by the investor.

9. The EITF observed that an entity should utilize a single entity-wide approach to determine the amount of its equity method losses when previous losses have reduced the common stock investment account to zero and that the selected policy should be disclosed in the footnotes to the financial statements.

10. The provisions of these consensuses are effective for interim or annual periods beginning after January 1, 2001.

11. Refer to Exhibit 00-24A for an example that illustrates application of these consensuses.

INT 00-24 Status

12. No further discussion is planned.

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Exhibit 00-24A
ILLUSTRATION OF THE APPLICATION OF THE INT 00-24 CONSENSUS'S

XYZ Investment in ABC Company

1. ABC Company is a life insurance company, formed January 2, 20X1 to sell health insurance in the state of New York. On January 2, 20X1, XYZ Insurance Company invested $500,000 in ABC, and purchased 100,000 shares of common stock at par, and 40,000 shares of preferred stock at par. ABC Preferred stock is non-voting, 5% cumulative.

2. XYZ determined it has obtained a controlling interest in ABC as XYZ owns 50% of the voting interests of ABC. XYZ accounted for its investment in ABC Insurance Company under the statutory equity method of accounting. The following table is selected information from the financial statements of ABC Insurance Company.

	1/2/20X1	12/31/20X1	12/31/20X2	12/31/20X3	12/31/20X4
Capital and Surplus:					
Common stock, $1 par, 200,000 shares issued and outstanding	$ 200,000	$ 200,000	$ 200,000	$ 200,000	$ 200,000
Preferred stock, $10 par, 100,000 shares issued and outstanding	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Surplus Notes			$ 500,000	$ 500,000	$ 500,000
Unassigned Funds (Surplus)		$ 130,000	($ 180,000)	($ 630,000)	($1,430,000)
Total Capital and Surplus	$1,200,000	$1,330,000	$1,520,000	$ 1,070,000	$ 270,000

	12/31/20X5	12/31/20X6	12/31/20X7	12/31/20X8	12/31/20X9
Capital and Surplus:					
Common stock, $1 par, 200,000 shares issued and outstanding	$ 200,000	$ 200,000	$ 200,000	$ 200,000	$ 200,000
Preferred stock, $10 par, 100,000 shares issued and outstanding	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Surplus Notes	$ 500,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Unassigned Funds (Surplus)	($1,980,000)	($1,830,000)	($1,280,000)	($ 430,000)	$ 820,000
Total Capital and Surplus	($280,000)	$ 370,000	$ 920,000	$1,770,000	$3,020,000

3. At 1/2/20X1, XYZ recorded the following entry to record its investment in ABC:

Investment in ABC Common stock	$ 100,000	
Investment in ABC Preferred stock	$ 400,000	
Cash		$ 500,000

To record initial investment in ABC Insurance Company.

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4. During the year ended 12/31/20X1, ABC had statutory net income before dividends of $200,000. At 12/31/20X1, ABC declared and paid a 5% preferred dividend, and a common stock dividend of $.10 per share. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X1.

Investment in ABC Common stock	$ 75,000	
Unrealized Gain/Loss		$ 75,000

To record 20X1 unrealized gain on investment in ABC Common. (($200,000 - $50,000) * 50%)

Cash	$ 10,000	
Unrealized Gain/Loss	$ 10,000	
Dividend Income		$ 10,000
Investment in ABC Common stock		$ 10,000

To record 20X1 dividend on ABC Common. (100,000 shares * $.10)

5. During the year ended 12/31/20X2, ABC issued an 8% surplus note of $500,000. XYZ purchased 100% of the surplus note. During that same year, ABC incurred a statutory net loss before dividends of $250,000. At 12/31/20X2, ABC declared and paid a 5% preferred dividend, and a common stock dividend of $.05 per share. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Investment in ABC Surplus Notes	$ 500,000	
Cash		$ 500,000

To record investment in ABC Insurance Company surplus notes.

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X2.

Unrealized Gain/Loss	$ 150,000	
Investment in ABC Common stock		$ 150,000

To record 20X2 unrealized loss on investment in ABC Common. (($-250,000 - $50,000) * 50%)

Cash	$ 5,000	
Unrealized Gain/Loss	$ 5,000	
Dividend Income		$ 5,000
Investment in ABC Common stock		$ 5,000

To record 20X2 dividend on ABC Common. (100,000 shares * $.05)

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6. During the year ended 12/31/20X3, ABC Insurance Company incurred a statutory net loss before dividends of $400,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X3.

Unrealized Gain/Loss	$ 182,000	
Investment in ABC Preferred stock		$ 172,000
Investment in ABC Common stock		$ 10,000

To record 20X3 unrealized loss on investment in ABC Common and Preferred.

Total net loss and preferred stock dividend ($450,000).
Common stock component reduces the Investment in ABC Common stock component to $0. (20,000 * 50%)

Total net loss and preferred dividend (-$400,000 - $50,000)	$450,000
Less amount used to reduce common stock investment to $0	20,000
Amount remaining to be allocated to investment in preferred	430,000
XYZ ownership % of preferred	40%
XYZ reduction in investment in preferred	$172,000

7. During the year ended 12/31/20X4, ABC Insurance Company incurred a statutory net loss before dividends of $750,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X4.

Unrealized Gain/Loss	$ 458,000	
Investment in ABC Preferred stock		$ 228,000
Investment in ABC Surplus note		$ 230,000

To record 20X4 unrealized loss on investment in ABC Preferred and Surplus Notes.

Total net loss and preferred stock dividend ($800,000).
Common stock component reduces the Investment in ABC Preferred stock component to $0. (570,000 * 40%)
Preferred stock component calculated as:

Total net loss and preferred dividend (-$750,000 - $50,000)	$800,000
Less amount used to reduce preferred stock investment to $0	570,000
Amount remaining to be allocated to investment in surplus note	230,000
XYZ ownership % of surplus note	100%
XYZ reduction in investment in ABC Surplus Notes	$230,000

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8. During the year ended 12/31/20X5, ABC Insurance Company incurred a statutory net loss before dividends of $500,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X5.

Unrealized Gain/Loss	$ 270,000	
Investment in ABC Surplus note		$ 270,000

To record 20X5 unrealized loss on investment in ABC Surplus Notes.

Total ABC net loss and preferred stock dividend (-$500,000 - $50,000).
Surplus Note component calculated as:

Total net loss and preferred dividend (-$500,000 - $50,000)	$550,000
XYZ ownership % of ABC Surplus Note	100%
	$550,000
Amount of unrealized loss recognized in 20X5	$270,000
Amount of unrealized loss suspended	$280,000

9. Since XYZ has not guaranteed any liabilities of ABC, the reduction they would recognize is limited to their remaining investment in ABC Surplus Notes. Therefore, they would only recognize a 20X5 unrealized loss on their investment in ABC of $270,000.

10. During the year ended 12/31/20X6, ABC Insurance Company realigned their marketing efforts and modified the products they were selling. ABC also issued an additional 8% surplus note of $500,000. This surplus note was purchased by an unaffiliated third party. During the year ended 12/31/X6, ABC Insurance Company had statutory net income before dividends of $200,000. ABC Insurance Company did not declare any dividends on common stock, but declared and paid current and dividends in arrears on preferred. XYZ recorded the following entries:

Cash	$ 80,000	
Dividends Receivable		$ 60,000
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X6, and receipt of preferred dividends receivable for 20X3, 20X4 and 20X5.

11. XYZ did not record any change in their investment in ABC Surplus Notes, ABC Preferred or ABC Common, since ABCs' net income after preferred dividends did not exceed the losses accumulated during the period that XYZ suspended recording unrealized losses.

12. The following amounts were tracked:

Total ABC net income and preferred stock dividend ($200,000 - $50,000).
Surplus Note component calculated as:

Total net income and preferred dividend ($200,000 - $50,000)	$150,000
XYZ ownership % of ABC Surplus Note	50%
Amount of unrealized loss suspended in 20X5	$ 75,000
Remaining amount of unrealized loss suspended	$280,000
	$205,000

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13. During the year ended 12/31/20X7, ABC Insurance Company had statutory net income before dividends of $600,000. At 12/31/20X7, ABC declared and paid a 5% preferred dividend. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X7.

Investment in ABC Surplus Notes	$ 70,000	
Unrealized Gain/Loss		$ 70,000

To record 20X7 unrealized gain on investment in ABC Surplus Notes.

Total ABC net income and preferred stock dividend ($600,000 - $50,000).
Surplus Note component calculated as:

Total net income and preferred dividend ($600,000 - $50,000)	$550,000
XYZ ownership % of ABC Surplus Note	50%
	$275,000
Remaining amount of unrealized loss suspended in 20X5	$205,000
20X7 amount of unrealized gain on investment in ABC Surplus Note	$ 70,000

14. During the year ended 12/31/20X8, ABC Insurance Company had statutory net income before dividends of $900,000. At 12/31/20X8, ABC declared and paid a 5% preferred dividend. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X8.

Total ABC net income and preferred stock dividend ($900,000 - $50,000).
Surplus Note component calculated as:

Total net income and preferred dividend ($900,000 - $50,000)	$850,000
XYZ ownership % of ABC Surplus Note	50%
20X8 amount of unrealized gain on investment in ABC Surplus Note	$425,000

Investment in ABC Surplus Notes	$ 425,000	
Unrealized Gain/Loss		$ 425,000

To record 20X8unrealized gain on investment in ABC Surplus Notes.

15. During the year ended 12/31/20X9, ABC Insurance Company had statutory net income, before interest on surplus notes and dividends, of $1,400,000. The Commissioner approved one year's interest payment on the surplus notes. At 12/31/20X9, ABC declared and paid a 5% preferred dividend, and a $.10 dividend per share on Common stock. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X9.

Cash	$ 40,000	
Interest Income		$ 40,000

To record surplus notes interest income from ABC Insurance Company for 20X9. ($500,000 * 8%)

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Investment in ABC Surplus Notes	$	5,000		
Investment in ABC Preferred Stock	$	400,000		
Investment in ABC Common Stock	$	130,000		
Unrealized Gain/Loss			$	535,000

To record 20X9 unrealized gain on investment in ABC Common, Preferred and Surplus Notes.

Components computed as follows:

Total Net Income net of preferred stock dividend and interest on surplus notes ($1,400,000 - $50,000 - $80,000)	$ 1,270,000
Less amount needed to restore investment in surplus notes	($ 10,000)
Amount available for preferred stock and common stock investment restoration	$ 1,260,000
Amount needed to restore preferred stock component	($ 1,000,000)
Amount available to restore common stock component	$ 260,000

Surplus Notes component ($10,000 * 50%)	$ 5,000
Preferred Stock component ($1,000,000 * 40%)	$ 400,000
Common stock component ($260,000 * 50%)	$ 130,000

Cash	$	10,000		
Unrealized Gain/Loss	$	10,000		
Dividend Income			$	10,000
Investment in ABC Common stock			$	10,000

To record 20X9 dividend on ABC Common. (100,000 shares * $.10)

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-26: EITF 98-3: Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business

INT 00-26 Dates Discussed

June 12, 2000; September 11, 2000; March 5, 2006; June 11, 2006; December 10, 2006; March 10, 2007

INT 00-26 References

Current:
SSAP No. 95—Nonmonetary Transactions

Superseded:
SSAP No. 28—Nonmonetary Transactions

INT 00-26 Issue

1. The basic principle contained in APB Opinion No. 29, *Accounting for Nonmonetary Transactions* (APB No. 29) is that an exchange of nonmonetary assets should be recorded at fair value. Certain modifications to that basic principle are contained in paragraphs 20-23 of APB No. 29. Paragraph 21.b. provides that accounting for an exchange of productive assets for similar productive assets should be based on the recorded amount of the nonmonetary assets relinquished. Paragraph 4 of APB No. 29 states that Opinion is not applicable to business combinations.

2. APB Opinion No. 16, *Business Combinations* (APB No. 16) provides accounting guidance for business combinations. Paragraph 1 of APB No. 16 states that "a business combination occurs when a corporation and one or more incorporated or unincorporated businesses are brought together into one accounting entity. The single entity carries on the activities of the previously separate, independent enterprises."

3. It is not clear whether exchanges of certain types of assets, for example, radio stations, cable systems, and hotels, are considered exchanges of productive assets or business combinations.

4. The issues are whether the exchange of assets or groups of assets involving the receipt of a consolidated business can be considered an exchange of similar productive assets accounted for at historical cost pursuant to paragraph 21 of APB No. 29 and how a "business" should be defined.

5. In December of 2004, the Financial Accounting Standards Board (FASB) issued *FAS 153: Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29* (FAS 153), which addresses the measurement of exchanges of nonmonetary assets. It eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21.b. of APB No. 29, and replaces it with an exception for exchanges that do not have commercial substance. This statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. While the guidance referred to above has been amended, the statutory accounting guidance included in the following discussion is not impacted and remains in effect.

INT 00-26 Discussion

6. The Working Group reached a consensus to update the description of the issue by adding an explanatory paragraph 5, which discusses amendments to APB No. 29 resulting from FAS 153.

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7. The Working Group reached a consensus to adopt the conclusions reached in EITF 98-3 with modification. APB No. 29 is adopted with SSAP No. 95. Although APB No. 16 is rejected in SSAP No. 68, the issues raised in EITF 98-3 are applicable to statutory accounting and SSAP No. 95. The modified conclusions of EITF 98-3 are outlined in paragraphs 8-15.

8. The EITF reached a consensus that the guidance below should be used to evaluate whether a business has been received in a nonmonetary exchange transaction.

9. A business is a self-sustaining integrated set of activities and assets conducted and managed for the purpose of providing a return to investors. A business consists of (a) inputs, (b) processes applied to those inputs, and (c) resulting outputs that are used to generate revenues. For a transferred set of activities and assets to be a business, it must contain all of the inputs and processes necessary for it to continue to conduct normal operations after the transferred set is separated from the transferor, which includes the ability to sustain a revenue stream by providing its outputs to customers.

10. The elements necessary for a transferred set to continue to conduct normal operations will vary by industry and by the operating strategies of the transferred set. An evaluation of the necessary elements should consider:

Inputs

a. Long-lived assets, including intangible assets, or rights to the use of long-lived assets.
b. Intellectual property.
c. The ability to obtain access to necessary materials or rights.
d. Employees.

Processes

e. The existence of systems, standards, protocols, conventions, and rules that act to define the processes necessary for normal, self-sustaining operations, such as (i) strategic management processes, (ii) operational processes, and (iii) resource management processes.

Outputs

f. The ability to obtain access to the customers that purchase the outputs of the transferred set.

11. A transferred set of activities and assets fails the definition of a business if it excludes one or more of the above items such that it is not possible for the set to continue normal operations and sustain a revenue stream by providing its products and/or services to customers. However, if the excluded item or items are only minor (based on the degree of difficulty and the level of investment necessary to obtain access to or to acquire the missing item(s)), then the transferred set is capable of continuing normal operations and is a business. The assessment of whether excluded items are only minor should be made without regard to the attributes of the transferee and should consider such factors as the uniqueness or scarcity of the missing element, the time frame, the level of effort, and the cost required to obtain the missing element. If goodwill is present in a transferred set of activities and assets, it should be presumed that the excluded items are minor and that the transferred set is a business.

12. The assessment of whether a transferred set is a business should be made without regard to how the transferee intends to use the transferred set. In other words, it is not relevant to the evaluation of whether the transferred set is a business whether the transferee will actually operate the set on a stand-alone basis or intends to continue using the transferred set in the same manner as the transferor.

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13. If all but a de minimis amount of the fair value of the transferred set of activities and assets is represented by a single tangible or identifiable intangible asset, the concentration of value in the single asset is an indicator that an asset rather than a business is being received.

14. The level of working capital or the adequacy of financing necessary to conduct normal operations in the transferred set is not an indicator either way as to whether the set meets the definition of a business. Likewise, if the planned principal operations of the transferred set have commenced, the presence and/or expectation of continued operating losses while the set seeks to achieve the level of market share necessary to attain profitability is not an indicator of whether or not the set is a business. However, if the transferred set is in the development stage and has not commenced planned principal operations, the set is presumed not to be a business.

15. The determination of whether a transferred set of assets and activities is or is not a business is a three-step process. First, one must identify the elements included in the transferred set. Second, one must compare the identified elements in the transferred set to the complete set of elements necessary for the transferred set to conduct normal operations in order to identify any missing elements. Third, if there are missing elements, one must make an assessment as to whether the missing elements cause one to conclude that the transferred set is not a business. That assessment is based on the degree of difficulty or the level of investment (relative to the fair value of the transferred set) necessary to obtain access to or to acquire the missing elements. If the degree of difficulty and level of investment necessary to obtain access to or to acquire the missing elements are not significant, then the missing elements are considered minor and their absence would not cause one to conclude that the transferred set is not a business. The determination of the degree of difficulty or level of investment necessary to obtain access to or to acquire the missing elements requires significant judgment and is dependent on the particular facts and circumstances.

INT 00-26 Status

16. On March 10, 2007, the Working Group reached a consensus to remove SSAP No. 68 from the references section of this interpretation; as it should not be used to interpret SSAP No. 68. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-28: EITF 99-12: Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination

INT 00-28 Dates Discussed

June 12, 2000; September 11, 2000

INT 00-28 References

Current:
SSAP No. 68—Business Combinations and Goodwill

INT 00-28 Issue

1. APB No. 16, *Business Combinations* (APB No. 16) appears to include contradictory guidance about the date that should be used to value equity securities issued to effect a business combination accounted for using the purchase method. Paragraph 74 of APB No. 16 states that "the market price for a reasonable period before and after the date the terms of the acquisition are agreed to and announced should be considered in determining the fair value of securities issued." However, paragraph 94 of APB No. 16 refers to determining the cost of an acquired company as of the date of acquisition, which is defined in paragraph 93 as, "ordinarily . . . the date assets are received and other assets are given or securities are issued." This Issue addresses that apparent contradiction.

2. The interval between initiating and completing a business combination may involve an extended period of time. Although management of the companies involved may agree to and announce the terms of a business combination at the initiation date, internal or external contingencies, such as the need to obtain shareholder or regulatory approvals, may exist and prevent concurrent consummation of the combination. Because of the length of time that may be required to resolve those contingencies, the market price of the securities that are expected to be issued to effect a purchase business combination may fluctuate. As a result, the total cost of the acquired company assigned by the acquirer may vary significantly depending on the date that is used to value the securities that are issued.

3. The issues are:

a. The date that should be used to value marketable equity securities of the acquirer issued to effect a business combination accounted for using the purchase method when the number of the acquirer's shares or amount of other consideration is not subject to change pursuant to the existing terms of the acquisition agreement

b. The date that should be used as the measurement date to value equity securities of the acquirer issued in a purchase business combination if the number of the acquirer's shares or amount of other consideration to be issued could change pursuant to a formula in the initial acquisition agreement.

INT 00-28 Discussion

4. The Working Group reached a consensus to adopt the final conclusions reached in EITF 99-12, *Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination* (EITF 99-12) with modification. Although APB 16 is rejected in SSAP No. 68, the issues identified in EITF 99-12 are applicable to paragraph 3 of SSAP No. 68. The issue of cost is defined as:

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> 3. The statutory purchase method of accounting is defined as accounting for a business combination as the acquisition of one entity by another. It shall be used for all purchases of SCA entities including partnerships, joint ventures, and limited liability companies. The acquiring reporting entity shall record its investment at cost. Cost is defined as the sum of: (a) any cash payment, (b) the fair value of other assets distributed, (c) the fair value of any liabilities assumed, and (d) any direct costs of the acquisition. Contingent consideration issued in a purchase business combination that is embedded in a security or that is in the form of a separate financial instrument shall be recorded by the issuer at fair value at the acquisition date.

5. As shown in subsection b of the excerpted paragraph above, SSAP No. 68 does not address the timing issues raised in EITF 99-12 of "other assets distributed".

6. The modifications to the conclusions reached in EITF 99-12 are as follows:

7. The EITF reached a consensus on Issue 1 that the value of the acquirer's marketable equity securities issued to effect a purchase business combination should be determined, pursuant to the guidance in paragraph 74 of APB No. 16, based on the market price of the securities over a reasonable period of time before and after the terms of the acquisition are agreed to and announced. In other words, the date of measurement of the value of the acquirer's marketable equity securities should not be influenced by the need to obtain shareholder or regulatory approvals. EITF members observed that the reasonable period of time referred to in paragraph 74 of APB No. 16 is intended to be very short, such as a few days before and after the acquisition is agreed to and announced. EITF members also observed that in transactions involving a hostile tender offer, the measurement date for the value of the acquirer's marketable equity securities occurs when the proposed transaction is announced and sufficient shares have been tendered to make the offer binding or when the proposed acquisition becomes nonhostile, as evidenced by the target company's agreement to the purchase price.

8. The EITF also reached a consensus that if the purchase price (the number of shares or the amount of other consideration) is subsequently changed as a result of further negotiations or a revised acquisition agreement, a new measurement date for valuing the acquirer's marketable equity securities that will be issued to effect the combination is established as of the date of the change. The Working Group clarified that if the change in the number of shares or other consideration is not substantive, a new measurement date does not result from the change.

9. The EITF addressed the accounting for contingent consideration issued to effect a purchase business combination in Issue No. 97-8, *Accounting for Contingent Consideration Issued in a Purchase Business Combination* (EITF 97-8). The measurement guidance in this Issue is to be applied to the acquirer's equity securities issued to effect a business combination accounted for using the purchase method, including those instruments that meet the criteria in EITF 97-8 for recording as part of the cost of the business acquired. (EITF 97-8 was adopted by the Working Group in SSAP No. 68.)

10. The EITF reached a consensus on Issue 2 that if the application of the formula results in a change to the number of shares or the amount of other consideration to be issued in the purchase business combination, then the first date on which the number of acquirer shares and the amount of other consideration become fixed without subsequent revision is the measurement date. That is, the measurement date is the earliest date, from the date the terms of the acquisition are agreed to and announced to the date of final application of the formula pursuant to the acquisition agreement, on which subsequent applications of the formula do not result in a change in the number of shares or the amount of other consideration. For example, assume the terms of a purchase business combination are agreed to and announced on March 1, 1999. Also assume that the purchase agreement includes a formula arrangement that specifies that an adjustment will be made to the number of shares issued in the business combination if the average closing security price for the 10 days ending June 30, 1999, is less than $16. If the 10-day average closing security price drops below $16 for the first time on June 1, 1999, and does not subsequently recover to an amount equal to or greater than $16 from June 1, 1999 through June 30, 1999, June 1, 1999 is the measurement date. However, if the originally announced number of shares or amount

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of other consideration does not change as a result of final application of the formula, then the initial date that the terms were agreed to and announced is the measurement date. The EITF noted that a new measurement date does not occur as a result of the application of a nonsubstantive formula in the original agreement.

11. As another example, assume that the terms of the acquisition are agreed to and announced on March 31, 1999. The number of shares to be issued in the business combination is equal to $20 million divided by the June 30, 1999 closing market price of the acquirer's common stock; however, if the June 30, 1999 closing market price of the acquirer's common stock is less than $16 or greater than $24, the exchange ratio is adjusted as follows: (a) if the closing market price is less than $16, the acquirer will issue 1,250,000 shares of its common stock for the outstanding common shares of the target company, and (b) if the closing market price is greater than $24, the acquirer will issue 833,000 shares of its common stock for the outstanding common shares of the target company. The variable exchange ratio represents a formula and, as a result, if the stock price changes during the period from March 31, 1999 through June 30, 1999, but remains within the $16-$24 range, the measurement date is June 30, 1999. However, if the acquirer's closing common stock price exceeds $24 on June 1, 1999, and remains above $24 through June 30, 1999, the number of shares to be issued in the transaction becomes fixed on June 1, 1999, and that date is the measurement date.

12. The EITF also reached a consensus that the securities should be valued based on market prices a few days before and after the measurement date determined in Issue 2 but that the measurement period would not include any dates after the date the business combination is consummated.

13. The EITF reached a consensus that the consensus reached on Issue 1 should only be applied prospectively to purchase business combinations consummated on or after January 1, 2001. The EITF reached a consensus that the consensuses reached on Issue 2 should be applied prospectively to purchase business combinations initiated on or after January 1, 2001. An entity should apply its existing policy prior to the effective date of the consensus on Issue 2.

INT 00-28 Status

14. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 01-18: Consolidated or Legal Entity Level – Limitations on EDP Equipment, Goodwill and Deferred Tax Assets Admissibility

INT 01-18 Dates Discussed

March 26, 2001; June 11, 2001

INT 01-18 References

Current:
SSAP No. 16R—Electronic Data Processing Equipment and Software
SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements
SSAP No. 68—Business Combinations and Goodwill
SSAP No. 101—Income Taxes

Superseded:
SSAP No. 79—Depreciation of Nonoperating System Software – An Amendment to SSAP No. 16—Electronic Data Processing Equipment and Software
SSAP No. 10R—Income Taxes—A Temporary Replacement of SSAP No. 10

INT 01-18 Issue

1. Case Number 1: The reporting entity has several wholly-owned insurance company subsidiaries. The reporting entity will account for its investment in these subsidiaries at their underlying statutory equity in accordance with *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

2. Case Number 2: A reporting entity has deferred tax assets (DTAs) in excess of those that are allowed to be admitted in accordance with the guidance in SSAP No. 101 paragraph 11. The reporting entity files a consolidated tax return with one or more affiliates. Those affiliates have deferred tax liabilities (DTLs) that exceed the remaining DTAs available for admission after application of paragraphs 11.a. and 11.b. of SSAP No. 101 at the affiliates' legal entity level.

3. The accounting issues are:

Case Number 1:

When applying the limitations described in paragraph 11 of SSAP No. 101, paragraph 4 of SSAP No. 16R, and paragraph 7 of SSAP No. 68 to the parent reporting entity's adjusted capital and surplus, is the reporting entity required to exclude any net deferred tax assets, EDP equipment and operating system software, and net positive goodwill included in its insurance subsidiaries' valuation? Or, is the limitation calculated solely based on the legal entity's adjusted capital and surplus?

The effect of looking solely at the legal entity is to allow for the "stacking" of intangibles, so that the parent reporting entity may effectively have more than the defined limitations "invested" in deferred tax assets, EDP equipment and operating system software and goodwill. These assets are limited at each subsidiary legal entity level.

Case Number 2:

Can the reporting entity offset its DTAs against existing gross DTLs of an affiliated entity? This offset would be pursuant to the allowance of an offset against existing DTLs under SSAP No. 101

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paragraph 11.c. This offset would occur only after application of paragraphs 11.a. and 11.b. for both the reporting entity and the affiliate. The premise for the offset is that both entities file a consolidated federal income tax return and that future deductible items of the reporting entity are, by current tax law, able to offset future income items of the affiliate. The affiliates for this purpose would have to have a tax sharing agreement that required payment from one affiliate to another for loss usage.

INT 01-18 Discussion

4. The Working Group reached a consensus as follows:

Case Number 1:

The Working Group reached a consensus that in applying the limitations described in paragraph 11.b.ii. of SSAP No. 101, paragraph 4 of SSAP No. 16R, and paragraph 7 of SSAP No. 68 to the parent reporting entity's adjusted capital and surplus, the reporting entity shall not exclude any net deferred tax assets, EDP equipment, operating system software, and net positive goodwill included in its insurance subsidiaries valuation.

Case Number 2:

The Working Group reached a consensus that the reporting entity shall not offset it's DTAs against existing gross DTLs of an affiliated entity.

INT 01-18 Status

5. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 01-25: Accounting for U.S. Treasury Inflation-Indexed Securities

INT 01-25 Dates Discussed

June 11, 2001; October 16, 2001; September 10, 2002; December 8, 2002; December 10, 2016; April 8, 2017

INT 01-25 References

Current:
SSAP No. 26R—Bonds

INT 01-25 Issue

1. Treasury inflation-indexed securities are direct obligations of the United States government, and are backed by the full faith and credit of the government.[1] The principal is protected against inflation. Since the principal is indexed to the Consumer Price Index and grows with inflation, the investor is guaranteed that the real purchasing power of the principal will keep pace with the rate of inflation (Based on the Reference CPI-U, which has a three-month lag). Although deflation could cause the principal to decline, Treasury will pay at maturity an amount that is no less than the par amount as of the date the security was first issued.

2. Interest is also protected from inflation. The investor will receive semiannual interest payments, based on a fixed semiannual interest rate applied to the inflation-adjusted principal, so that the investor is guaranteed a real rate of return above inflation.

Summary of the Structure and Index:

Principal amount. The principal amount of Treasury inflation-indexed securities will be adjusted for changes in the level of inflation. The inflation-adjusted principal amount of the securities can be calculated daily. However, the inflation adjustment will not be payable by Treasury until maturity, when the securities will be redeemed at the greater of their inflation-adjusted principal amount or the principal amount of the securities on the date of original issuance (i.e., par).

Index. The index for measuring the inflation rate will be the nonseasonally adjusted CPI-U (U.S. City Average All Items Consumer Price Index for All Urban Consumers). CPI-U was selected by Treasury because it is the best known and most widely accepted measure of inflation.

Interest payments. Every six months Treasury will pay interest based on a fixed rate of interest determined at auction. Semiannual interest payments are determined by multiplying the inflation-adjusted principal amount by one-half the stated rate of interest on each interest payment date.

Payment at maturity. If at maturity the inflation-adjusted principal is less than the par amount of the security (due to deflation), the final payment of principal of the security by Treasury will not be less than the par amount of the security at issuance. In such a circumstance, Treasury will pay an additional amount at maturity so that the additional amount plus the inflation-adjusted principal amount will equal the par amount of the securities on the date of original issuance. Initially, the securities will be issued with a 10-year maturity; however, Treasury expects to issue other maturities over time.

[1] The guidance prescribed within this interpretation is limited to treasury inflation-indexed securities backed by the full faith and credit of the United States Government. Inflation-indexed securities of foreign governments shall not follow the guidance within this interpretation and shall be accounted for and reported according to the applicable SSAP without adjustments for the inflation factor.

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Stripping. The securities will be eligible for the STRIPS program (Separate Trading of Registered Interest and Principal of Securities) as of the first issue date. Unlike the conventional STRIPS program, however, interest components stripped from different inflation-indexed securities, at least initially, will not be interchangeable or fungible with interest components from other securities, even if they have the same payment or maturity date.

3. The accounting issue is how should changes to inflation-adjusted principal be recorded?

4. At the September 10, 2002 and December 8, 2002 the Working Group expanded this interpretation to address specific questions regarding U.S. Treasury Inflation-Indexed Securities purchased at either a premium or discount and how the inflation adjustment interacts with any such premium or discount, as well as the calculation of each of these amounts.

5. The following example will be used to highlight issues concerning the amortization of premium and inflation adjustment for a typical security:

Assume:	
Par value of TIP security	$500,000
Inflation factor at date of purchase	1.12075
Price at date of purchase	102.96875
Original issue date 6/30/X0	
Purchase date 06/30/X6	
Maturity date 06/30/X10	
Amount of inflation adjustment at date of purchase ($500,000 * .12075)	$60,375
Total purchase price ($500,000*1.12075*1.0296875)	$577,011
Premium at date of purchase ($577,011 - $500,000 - $60,375)	$16,636

6. The issues are:

Issue a. – If accretion or amortization should be recognized over the period of time the security is owned.

Issue b. – Assuming that at the end of the accounting period, 12/31/X6, the inflation factor is 1.13000, what the correct book value of the security would be.

Issue c. – Assuming that at the end of the accounting period, 12/31/X6, the inflation factor is 1.12000, what the correct value of the security would be.

Issue d. – How changes in accounting treatment would be handled.

INT 01-25 Discussion

7. At its October 16, 2001 meeting, the Working Group reached a consensus that the inflation adjustment be recognized as an unrealized gain until such time as it is paid, at which time it should be recognized as a realized gain. If there is a deflation adjustment, such amounts should only be recognized to the extent of any previously recognized inflation adjustment for that particular security, (reduce any unrealized gain on that security to zero) as the investor is guaranteed at maturity to receive at least the par amount of the security. (See paragraph 8.c. below for amendments to this paragraph adopted at the December 8, 2002 meeting.)

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8. At its December 8, 2002 meeting, the Working Group reached a consensus on the following issues related to the purchase of a treasury inflation-indexed security at either a premium or a discount, how the inflation adjustment interacts with any such premium or discount, as well as the calculation of each of these amounts.

Issue a. – The $16,636 premium paid for the security should be amortized over the remaining life of the security. Therefore, if the inflation adjustment factor never changed from the 1.12075 at date of purchase, the security would have a book value at maturity of $560,375, the amount the reporting entity would receive at maturity date ($500,000*1.12075).

Issue b. – The reporting entity should record the unrealized gain/loss based on the difference in the inflation factor times the par amount, and amortize the premium over the remaining life of the security.

Issue c. – In the case where the inflation factor is reduced to a factor not less than 1.0000, the reporting entity should reflect the change in the inflation adjustment as well as amortization of premium. Paragraph 7 of this interpretation is amended as follows:

> 7. The Working Group reached a consensus that the inflation adjustment be recognized as an unrealized gain until such time as it is paid, at which time it should be recognized as a realized gain. If there is a deflation adjustment, such amounts should only be recognized to the extent the inflation factor is not reduced to an amount less than 1.0000 as the investor is guaranteed at maturity to receive at least the par amount of the security.

Issue d. - A change in accounting principle should be recorded per the requirements of *SSAP No. 3—Accounting Changes and Corrections of Errors*, paragraph 5:

> 5. The cumulative effect of changes in accounting principles shall be reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle. The cumulative effect is the difference between the amount of capital and surplus at the beginning of the year and the amount of capital and surplus that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods.

In the specific question noted, if the reporting entity is currently recognizing both amortization of premium as well as the change in the inflation adjustment factor as amortization of premium, there should not be a cumulative effect on surplus to record.

INT 01-25 Status

9. No further discussion is planned.

10. On April 8, 2017, the Statutory Accounting Principles (E) Working Group modified this interpretation, adding footnote 1 to clarify that the guidance within this interpretation is only applicable to Treasury inflation-indexed securities backed by the full faith and credit of the United States Government.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 01-31: Assets Pledged as Collateral

INT 01-31 Dates Discussed

October 16, 2001; December 10, 2001; March 18, 2002; September 12, 2004; December 5, 2004; March 3, 2012; August 31, 2012

INT 01-31 References

Current:
SSAP No. 4—Assets and Nonadmitted Assets
SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
INT 20-06: Participation in the 2020 TALF Program

Superseded/Nullified:
SSAP No. 18—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
SSAP No. 33—Securitization
SSAP No. 45—Repurchase Agreements, Reverse Repurchase Agreements and Dollar Repurchase Agreements
SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
INT 99-02: Accounting for Collateral in Excess of Debt Principal

INT 01-31 Issue

1. Insurers may enter into certain transactions that require the granting of a security interest in certain assets to another party to serve as collateral for their performance under a contract. The arrangement is commonly referred to as a pledge, typically accomplished by delivery of assets to the secured party or to an independent custodian. In these transactions, the pledging insurer typically (1) continues to receive the income on the pledged collateral and (2) can remove and substitute other securities with little or no advance notice to the secured party as long as they comply with related investment quality and market value agreement provisions. Examples include collateral pledged under investment, derivative, debt obligations and policyholder transactions.

2. Specific examples of collateral pledged for derivative and investment transactions include but are not limited to: (1) securities posted with a broker as margin for futures and options transactions, (2) securities pledged to secure credit exposure with swap counterparties, (3) securities pledged under reverse repurchase agreements or securitizations that are accounted for as secured borrowing transactions and (4) securities pledged under securities lending transactions.

3. Specific examples of collateral pledged for debt obligations and policyholder transactions include but are not limited to assets pledged to secure (1) debt borrowings from or insurance contracts issued to banking entities and (2) insurance contracts issued to governmental entities such as municipalities.

4. Under these transactions, the fair value of the securities pledged as collateral may exceed the contract balance (swap fair value, advance balance, policyholder account balance, etc). For this interpretation, this excess carrying value of securities pledged over the corresponding asset or contract balance is called the "overcollateralization" amount.

5. The accounting issue is whether the assets pledged as collateral under the various transactions mentioned above should be considered admitted assets.

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INT 01-31 Discussion

6. The Working Group reached a consensus that if the collateral had not been pledged in the examples described above, it is assumed the underlying asset would be recorded as an admitted asset under SSAP No. 4 (e.g. they are readily marketable assets available to meet both current and future policyholder obligations). In addition, it is assumed that the asset would not be considered impaired under SSAP No. 5R due to a default, fair value decline, or other loss contingency.

7. Therefore, for the examples described above, the pledging insurer would record the collateral (including the overcollateralization amount) as an admitted asset until they have committed a contract default that has not been cured in accordance with the contract provisions. This accounting is in accordance with the provisions of SSAP No. 103R. This consensus of reporting collateral as an admitted asset is further supported by SSAP Nos. 4 and 5 since generally, the insurer can readily substitute pledged assets. Additionally, an insurer may typically unwind the transaction allowing the assets to be available to the pledging insurer to meet policyholder obligations. Furthermore, no event has occurred to indicate an impairment or potential loss contingency with respect to such pledged assets. The fact that some pledged assets may constitute an overcollaterlization amount does not change this analysis. Accordingly, all assets pledged in support of these type transactions should also be admitted.

8. At the time of an uncured default, the provisions of paragraph 20 of SSAP No. 103R shall be used to determine the appropriate accounting treatment for the collateral. If the secured party utilizes collateral to offset all or a portion of the liability owed by the pledging insurer as a result of the default, then the collateral amount utilized to offset the liability shall be removed from the balance sheet. At the same time, the amount of the liability that was offset should be removed from the balance sheet since that obligation has been satisfied through the secured party's utilization of that collateral. To the extent that an uncured default remains without the secured party utilizing the collateral to offset the obligation, the pledging insurer should only record an admitted asset for the amount of collateral that it can redeem.

INT 01-31 Status

9. As of March 18, 2002, the consensus position of this interpretation is consistent with the position of the NAIC Invested Asset (E) Working Group. This interpretation will be reviewed by the FAS 140 Subgroup of the NAIC Statutory Accounting Principles (E) Working Group in conjunction of its consideration of incorporating GAAP pronouncement *FAS 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, a replacement of FASB Statement 125* into the statutory accounting model. As such, this interpretation is subject to amendment pending disposition of the FAS 140 Subgroup's review of collateral and FAS 140 in its entirety.

10. On September 12, 2004, the Working Group noted that the review of FAS 140 was complete and INT 01-31 was listed as an interpretation of SSAP No. 91R. On March 3, 2012, the Working Group adopted with modification *FAS 166—Accounting for Transfers of Financial Assets, an Amendment of FAS 140* (FAS 166). With this adoption, there was no change to the consensus opinion within this interpretation, and this INT was listed as an interpretation of SSAP No. 103R.

11. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 02-22: Accounting for the U.S. Terrorism Risk Insurance Program

INT 02-22 Dates Discussed

December 8, 2002; March 9, 2003; March 24, 2018

INT 02-22 References

Current:
SSAP No. 35R—Guaranty Fund and Other Assessments
SSAP No. 62R—Property and Casualty Reinsurance

INT 02-22 Issue

1. The Terrorism Risk Insurance Act of 2002 establishes a temporary Federal program in the Department of the Treasury that provides for a system of shared public and private compensation for insured losses resulting from acts of terrorism, i.e., subject losses. The Terrorism Insurance Program (or the "Program") requires that all entities that meet the definition of an insurer under the act (generally, commercial property/casualty insurers that are licensed in the U.S.) participate in the Program. The Program becomes effective upon enactment and runs through December 31, 2005. (For purposes of the act, there is a "Transition Period" that runs from enactment through December 31, 2002, and three "Program Years" that run from January 1st through December 31st of 2003, 2004, and 2005, respectively.) The amount of compensation paid to participating insurers under the Program is 90% of subject losses, after an insurer deductible, and subject to an annual cap. The deductible under the Program is 1% for the Transition Period, 7% for Program Year 1, 10% for Program Year 2, and 15% for Program Year 3. In each case, the deductible percentage is multiplied times the insurer's direct earned premiums from the calendar year immediately preceding the respective Transition or Program year. The annual cap limits the amount of terrorism losses paid by insurers and the amount of Federal reimbursement and is $100 billion for Program Year 1 (combined with the Transition Period), Program Year 2, and Program Year 3

2. The Program provides for the establishment of a mandatory surcharge on all covered policyholders to provide for recoupment of defined losses paid by the Department of Treasury. To the extent that the amount of Federal financial assistance exceeds the amount recovered through the mandatory surcharge, the Department of Treasury may impose a second surcharge. The two surcharges combined may not exceed 3% of the annual premium charged for the insured policy. The Program provides that the Department of the Treasury shall collect the surcharges and further provides that insurers shall collect the surcharges and remit such amounts collected to the Department of Treasury.

3. The issues are:

Issue 1: Does the Program result in a transfer of underwriting risk for terrorism losses to the Department of Treasury and, if so, how should the recovery from the Department of Treasury for terrorism losses be accounted for by insurers?

Issue 2: How should the imposition of the surcharges on policyholders by the Department of Treasury be accounted for by insurers?

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INT 02-22 Discussion

4. The Working Group reached a consensus as follows:

Issue 1: Because the Program results in losses from acts of terrorism (above the defined insurer deductibles) being paid by the Department of Treasury, there is a transfer of insurance risk and accordingly, the recovery of such losses should be reported as reinsured losses.

Issue 2: Because the terrorism loss risk-spreading premium is imposed on policyholders as a surcharge and the Department of Treasury provides for insurers to collect the surcharge "and remit amounts collected to the Secretary," the surcharge generally meets the requirements of paragraph 16 of SSAP No. 35R and should be accounted for as such.

INT 02-22 Status

5. No further discussion is planned.

6. This interpretation will remain in effect as long as the Terrorism Risk Insurance Act is authorized by the U.S. Congress.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 03-02: Modification to an Existing Intercompany Pooling Arrangement

INT 03-02 Dates Discussed

March 9, 2003; June 22, 2003

INT 03-02 References

Current:
SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance
SSAP No. 62R—Property and Casualty Reinsurance
SSAP No. 63—Underwriting Pools

INT 03-02 Issue

1. Insurance groups that utilize intercompany pooling arrangements often modify these arrangements from time to time for various business reasons. These business reasons commonly include mergers, acquisitions, dispositions or a restructuring of the group's legal entity structure. As an insurance group's business objectives and strategies evolve, it may be necessary for the insurance group's legal entity structure to similarly evolve in order to address the insurance group's business needs.

2. SSAP No. 63, paragraphs 5 and 7, defines and describes intercompany pooling as an arrangement among affiliated entities whereby "all of the pooled business is ceded to the lead entity and then retroceded back to the pool participants in accordance with their stipulated shares." This arrangement is established through "a conventional quota share reinsurance agreement…" Arrangements whereby there is one lead company that retains 100% of the pooled business and all or some of the affiliated companies have a 0% net share of the pool may qualify as intercompany pooling."

3. Therefore, in order to effectuate a modification to the existing intercompany pooling arrangement, companies must either 1) amend the existing reinsurance agreement, or 2) execute new agreements. The latter scenario may entail executing at least two agreements: a commutation of the existing agreement, and a new quota share agreement(s) that covers both past and future periods.

4. To illustrate, in order to effectuate a relatively simple modification, such as changing pooling participation percentages without changing the pool participants, companies often simply amend the existing pooling agreement. Alternatively, in order to effectuate a more complex modification, such as changing (by adding or removing) the number of pool participants, a company must commute the existing pooling agreement and execute a new quota share agreement(s). In conjunction with executing the appropriate reinsurance agreements, a transfer of assets and liabilities amongst the impacted affiliates is also required in order to implement the new reinsurance agreement(s). At issue is the appropriate valuation basis to be used for assets and liabilities that are transferred pursuant to the new reinsurance agreement(s).

5. Since SSAP No. 63 does not specifically address modifications to intercompany pooling arrangements, insurance groups that modify their intercompany pooling arrangements must refer elsewhere in Statutory Accounting Principles (SAP) for relevant guidance. The obvious guidance for such transactions is SSAP No. 62R since an intercompany pooling arrangement is, by definition, affiliated reinsurance. There is, however, a minority opinion that *SSAP No. 25—Affiliates and Other Related Parties* appears to apply due to the affiliated nature of these transactions. Since the guidance and intent of SSAP No. 62R and SSAP No. 25 provide for different valuation bases, this interpretation serves to provide definitive guidance as to which SSAP is relevant for these transactions and, therefore, clarify the

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appropriate valuation basis to be used for assets and liabilities transferred pursuant to a modification to an intercompany pooling arrangement.

SSAP No. 62R Approach:

6. This approach refers to the guidance and statutory accounting intent from SSAP No. 62R since intercompany pooling arrangements are defined and established through reinsurance. Further, since modifications to intercompany pooling agreements typically involve the transfer of net liabilities incurred since the inception of the existing pooling agreement (i.e., prior to the effective date of the new agreement), the retroactive reinsurance accounting guidance in paragraphs 33-39 of SSAP No. 62R is applicable. Paragraph 33 states that this special accounting treatment is warranted "due to the potential abuses involving the creation of surplus to policyholders and the distortion of underwriting results…" However, paragraph 36.d. specifically applies to intercompany reinsurance arrangements, and amendments to intercompany reinsurance agreements, since the reinsurance agreement is among companies 100% owned by a common parent. This paragraph allows prospective accounting treatment for intercompany reinsurance agreements that do not result in a gain in surplus as a result of the transaction.

7. To provide historical perspective, prior to the adoption (with modification) of FASB *Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts* (FAS 113) as SAP, paragraph 36.d. was added as one of the SAP modifications. The intent of adding paragraph 36.d. was to specifically exclude intercompany reinsurance agreements among entities 100% owned by a common parent from retroactive reinsurance accounting requirements as a result of amending or modifying these agreements, provided there is no surplus gain. The presumption in this intent was that there would be no gains to the ceding entity resulting from implementing amendments or modifications to these types of reinsurance agreements.

8. Therefore, based on the foregoing guidance and background, the statutory accounting intent is to avoid surplus gains for the ceding entity as a result of implementing a modification to an intercompany pooling arrangement. On that basis, such a modification does not represent an economic transaction to the insurance group or to the impacted companies. As such, the transfer of both the assets and the liabilities valued at statutory book value ensures that there is no impact to surplus as a result of implementing a modification to an existing pooling arrangement.

SSAP No. 25 Approach:

9. An approach different from that which refers to reinsurance accounting guidance is to refer to the guidance in SSAP No. 25 since some may view a modification to an intercompany pooling agreement as a related party transaction involving the exchange of assets or liabilities. In this case, paragraphs 14-18 of SSAP No. 25 would appear applicable. This guidance specifies differing valuation bases, depending on whether the transaction is considered an economic or a non-economic transaction. SSAP No. 25, paragraph 15, states that "…The appearance of permanence is also an important criterion is assessing the economic substance of a transaction. In order for a transaction to have economic substance and thus warrant revenue (loss) recognition, it must appear unlikely to be reversed …" Since insurance groups often modify intercompany pooling arrangements, this type of transaction is not permanent, and may be construed as a non-economic transaction. SSAP No. 25, paragraph 19.b., states that "non-economic transactions … shall be recorded at the lower of existing book value or fair value at the date of the transaction."

10. It appears that this guidance is intended to address matters involving discrete or isolated transfers of assets and/or liabilities between affiliates rather than transfers of assets and liabilities effected in relation to executing reinsurance transactions (the guidance for which is SSAP No. 62R). Additionally, application of this guidance would result in a change to the surplus of the insurance group as a result of implementing a modification to an existing intercompany pooling arrangement. As previously stated, the

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statutory accounting intent is to avoid surplus gains for the insurance group as a result of implementing a modification to an intercompany pooling arrangement.

11. The accounting issues are:

a. What is the relevant guidance for modifications to intercompany pooling arrangements?

b. What is the appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement?

INT 03-02 Discussion

The Working Group reached a consensus as follows:

12. SSAP No. 62R provides accounting for property and casualty reinsurance agreements including specific guidance on intercompany pooling agreements. SSAP No. 62R provides two methods of accounting for changes in intercompany pooling agreements, depending on whether or not the pooling results in a gain in surplus.

13. The appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement is statutory book value for assets and statutory value for liabilities. Book value is defined in the glossary of the *Accounting Practices and Procedure Manual*.

INT 03-02 Status

14. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 04-17: Impact of Medicare Modernization Act on Postretirement Benefits

INT 04-17 Dates Discussed

September 14, 2004; December 5, 2004

INT 04-17 References

Current:
SSAP No. 92—Postretirement Benefits Other Than Pensions

Superseded:
SSAP No. 10R—Income Taxes
SSAP No. 14—Postretirement Benefits Other Than Pensions
SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8

INT 04-17 Issue

1. In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) became law. Under the Act, starting in 2006, retirees will have the ability to obtain prescription drug benefits through a new Medicare Part D program and companies that continue to provide postretirement prescription drug benefits to their retirees may be eligible to receive a new federal subsidy.

2. In May 2004, FASB adopted the Board directed FASB Staff Position (FSP) *FAS 106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* (FSP FAS 106-2). The guidance found in FSP FAS 106-2 superseded the earlier guidance in *FSP FAS 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* and was intended as being the final guidance on this subject.

3. Questions have arisen regarding whether an employer that provides postretirement prescription drug coverage should recognize the effects of the Act on the plan's accumulated postretirement benefit obligation (APBO) and the employer's postretirement benefit costs and, if so, when and how to account for those effects.

INT 04-17 Discussion

4. The Working Group reached a consensus to adopt the final conclusions reached in FSP FAS 106-2 with the following modifications:

a. Postretirement benefits should be accounted for in accordance with SSAP No. 92.

b. Income Taxes should be accounted for in accordance with SSAP No. 101.

c. Calculations shall not exclude non-vested employees.

d. Any references to *FSP FAS 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* are removed as this guidance was superseded by FSP FAS 106-2.

e. The effective date is universal for both public and non-public entities.

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5. Per FSP FAS 106-2:

> 3. The guidance in this FSP related to accounting for the subsidy applies only to the sponsor of a single-employer defined benefit postretirement health care plan for which (a) the employer has concluded that prescription drug benefits available under the plan to some or all participants for some or all future years are "actuarially equivalent" to Medicare Part D and thus qualify for the subsidy under the Act and (b) the expected subsidy will offset or reduce the employer's share of the cost of the underlying postretirement prescription drug coverage on which the subsidy is based. This interpretation also provides guidance for the disclosures about the effects of the subsidy for an employer that sponsors a postretirement health care benefit plan that provides prescription drug coverage but for which the employer has not yet been able to determine actuarial equivalency.
>
> 4. Although this FSP provides limited guidance on certain other related aspects of accounting and disclosure necessitated by the Act (for example, changes in assumed participation rates and health care cost trend rates, as well as income tax accounting) that guidance is not intended to supersede or in any way limit the application of other relevant authoritative literature. This FSP does not address the accounting for the subsidy in situations that may arise in which the expected subsidy exceeds the employer's share of the cost of the underlying postretirement prescription drug coverage on which the subsidy is based. It also does not address accounting for the subsidy by multiemployer health and welfare benefit plans or by the sponsors or participating employers of those plans.

6. The Act introduces two new features to Medicare that an employer needs to consider in determining those measurements: (a) a subsidy that is based on 28 percent of an individual beneficiary's annual prescription drug costs between $250 and $5,000 (subject to indexation and the provisions of the Act as to "allowable retiree costs") and (b) the opportunity for a retiree to obtain a prescription drug benefit under Medicare.

7. Per FSP FAS 106-2:

> 9. An employer's eligibility for the 28 percent subsidy depends on whether the prescription drug benefit available under its plan is at least "actuarially equivalent" to the Medicare Part D benefit. At present, detailed regulations necessary to implement the Act have not been issued, including those that would specify the manner in which actuarial equivalency must be determined, the evidence required to demonstrate actuarial equivalency, and the documentation requirements necessary to be entitled to the subsidy.[1] In addition, the magnitude of the subsidy for an employer depends on how many of the employer's Medicare-eligible retired Plan participants choose not to enroll in the *voluntary* Medicare Part D plan. Further, specific regulations regarding the payment/reimbursement mechanism for the subsidy are yet to be defined by the appropriate administrative agency. Accordingly, questions have been raised regarding whether the subsidy is substantively similar to other Medicare benefits that existed when Statement 106 was issued and therefore should be accounted for as a reduction of the APBO and net periodic postretirement benefit cost, or whether the subsidy represents a payment to the employer that is determined by reference to its plan's benefit payments but is not, in and of itself, a direct reduction of postretirement benefit costs. Under either view, there is also a question as to when the subsidy should be given accounting recognition.
>
> Effect on Per Capita Claims Cost
>
> 10. Regardless of the impact of the subsidy, the existence of prescription drug coverage under Medicare Part D may have an effect on an employer's per capita claims cost for a plan that currently provides a prescription drug benefit. That effect depends on (a) whether current and future retirees (or their beneficiaries under the employer-sponsored plan) enroll in the voluntary

[1] Section 1860D-11(c) of the Social Security Act, as amended by the Act, states that "the Secretary [of Health and Human Services] shall establish processes and methods for determining the actuarial valuation of prescription drug coverage."

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Medicare Part D plan and (b) the Act's macro-socioeconomic effects on health care cost trends and consumers' behavior.

Plan Amendments

11. In response to the Act, or for other reasons, an employer may amend an existing plan (or establish a new one). To the extent that an employer amends a plan (positively or negatively), the APBO will be affected by the direct effects of the change in benefits attributed to employee services already rendered. If an amendment changes the determination as to the actuarial equivalency of benefits available under the plan, the expected subsidy to the employer also will change.

Income Tax Accounting

12. The Act excludes receipt of the subsidy from the taxable income of the employer for federal income tax purposes.[2] Accordingly, this interpretation addresses how that provision affects the accounting for the temporary difference related to the employer's accrued postretirement benefit cost under Statement 109, *Accounting for Income Taxes.*

FASB Staff Position

13. Paragraph 35 of Statement 106 specifies that health care coverage provided by Medicare shall be taken into account in measuring the employer's postretirement health care benefit obligation. Paragraph 40 of Statement 106 requires presently enacted changes in relevant laws to be considered in current period measurements of net periodic postretirement benefit cost and the APBO. Therefore, under that guidance, measures of the APBO and net periodic postretirement benefit cost on or after the date of enactment shall reflect the effects of the Act.

Effect of the Subsidy on Benefits Attributable to Past Service

14. When an employer initially accounts for the subsidy pursuant to the effective date and transition guidance in paragraphs 23–32, its effect on the APBO shall be accounted for as an actuarial experience gain pursuant to paragraphs 56 and 59 or 60 of Statement 106.

Effect of the Subsidy on Current Measures of Net Periodic Postretirement Benefit Cost

15. Because the subsidy affects the employer's share of its plan's costs, the subsidy is included in measuring the costs of benefits attributable to current service. Therefore, the subsidy reduces service cost (as defined in paragraph 47 of Statement 106) when it is recognized as a component of net periodic postretirement benefit cost.

Changes in Estimates

16. If an estimate of the expected subsidy subsequently changes—as a result of changes in regulations or legislation, changes in the underlying estimates of postretirement prescription drug costs, or for reasons other than a plan amendment—the effect of the change in estimate is an actuarial experience gain or loss pursuant to paragraph 56 of Statement 106.

Plan Amendments

17. If prescription drug benefits currently available under an existing plan are deemed not actuarially equivalent as of the date of enactment of the Act, but the plan is subsequently amended to provide actuarially equivalent benefits, the direct effect of the plan amendment on the APBO (that is, the effect of only the change in prescription drug coverage) and the effect on the APBO from any resulting subsidy to which the employer is expected to be entitled as a result of the amendment shall be combined. If that combined effect reduces the APBO, it is deemed to be an actuarial experience gain pursuant to paragraph 56 of Statement 106. If the combined effect

[2] New Section 139A of the Internal Revenue Code established by Section 1202 of the Act.

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increases the APBO, it is deemed to be prior service cost that shall be accounted for pursuant to paragraphs 50-54 of Statement 106.

18. A plan that provides prescription drug benefits that previously were deemed actuarially equivalent under the Act may be subsequently amended to reduce its prescription drug coverage and that reduced coverage may not be considered actuarially equivalent. In that circumstance, any actuarial experience gain related to the subsidy previously recognized is unaffected. However, the combined net effect on the APBO of (a) the subsequent plan amendment that reduces benefits under the plan and thus disqualifies the benefits as actuarially equivalent and (b) the elimination of the subsidy shall be accounted for as prior service cost (credit) as of the date the amendment is adopted.

Income Tax Accounting

19. In the periods in which the subsidy affects the employer's accounting for the plan, it shall have no effect on any plan-related temporary difference accounted for under Statement 109 because the subsidy is exempt from federal taxation. That is, the measure of any temporary difference shall continue to be determined as if the subsidy did not exist. To illustrate, consider the following simple example.

> Prior to the adoption of this FSP, an employer's carrying amount of accrued postretirement benefit cost (the amount recognized in the statement of financial position) is $100 for a noncontributory, unfunded prescription drug benefit plan with only inactive participants who are not yet eligible to collect benefits. Assuming a tax rate of 35 percent and no corresponding tax basis for the accrued postretirement benefit cost, the employer would report a $35 deferred tax asset related to that $100 deductible temporary difference. Because the employer has a policy of amortizing gains and losses under paragraph 59 of Statement 106, upon adoption of the FSP and recognition of a $28 actuarial gain resulting from the subsidy, neither the carrying amount of accrued postretirement benefit cost nor the deferred tax asset would change. Subsequently, ignoring interest on the APBO (which includes interest on the subsidy), as the actuarial gain related to the subsidy is amortized as a component of net periodic postretirement benefit cost, the carrying amount of accrued postretirement cost would be reduced. However, the associated temporary difference and deferred tax asset would remain unchanged. That is, after the gain related to the subsidy is amortized in its entirety, the carrying amount of accrued postretirement benefit cost would be $72, and the deferred tax asset would remain at $35.

For purposes of simplicity, this example ignores complexities regarding the amount and timing of the subsidies reflected in the carrying amount of accrued postretirement benefit cost arising from any of the following: (a) netting gains and losses and application of the corridor amortization approach described in paragraph 59 of Statement 106, (b) recognition of additional subsidies through amortization of prior service costs that include effects of the subsidy, or (c) reduction in future service and interest costs. Those complexities must be considered in determining the temporary difference on which the deferred tax effects under Statement 109 will be based. However, providing detailed guidance on the application of Statement 109 to postretirement benefits other than pensions is beyond the scope of this FSP.

INT 04-17 Disclosures

8. Per FSP FAS 106-2:

20. Until an employer is able to determine whether benefits provided by its plan are actuarially equivalent, it shall disclose the following in financial statements for interim or annual periods:

a. The existence of the Act

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b. The fact that measures of the APBO or net periodic postretirement benefit cost do not reflect any amount associated with the subsidy because the employer is unable to conclude whether the benefits provided by the plan are actuarially equivalent to Medicare Part D under the Act.

9. In interim and annual financial statements for the first period in which an employer includes the effects of the subsidy in measuring the net postretirement benefit cost and the first period in which an employer includes the effects of the subsidy in measuring net periodic postretirement benefit cost, it shall disclose the following:

a. The reduction in the net postretirement benefit cost for the subsidy related to benefits attributed to former employees.

b. The effect of the subsidy on the measurement of net periodic postretirement benefit cost for the current period. That effect includes (1) any amortization of the actuarial experience gain in (a) as a component of the net amortization called for by paragraph 49 of SSAP No. 92, (2) the reduction in current period service cost due to the subsidy, and (3) the resulting reduction in interest cost on the net postretirement benefit cost as a result of the subsidy.

c. Any other disclosures required by paragraph 66.p. of SSAP No. 92 which requires disclosure of "An explanation of any significant change in the benefit obligation or plan assets not otherwise apparent in the other disclosures required by this statement."

10. For purposes of the disclosures required by paragraph 66.a. of SSAP No. 92, an employer shall disclose gross benefit payments (paid and expected, respectively), including prescription drug benefits, and separately the gross amount of the subsidy receipts (received and expected, respectively).

INT 04-17 Effective Date and Transition

11. This interpretation is effective for reporting years beginning on or after January 1, 2005 with early adoption allowed. A change resulting from adoption of this interpretation should be accounted for as detailed in paragraphs 12 and 13. A change resulting from the adoption of this interpretation shall be accounted for as a change in accounting principle in accordance with SSAP No. 3.

12. Per FSP FAS 106-2:

> 24. … If the effects of the Act—including the subsidy, if any, changes in participation rates, and changes in estimated health care costs—cause the employer to conclude that enactment of the Act was not a "significant event" pursuant to paragraph 73 of Statement 106, the effects of the Act shall be incorporated in the next measurement of plan assets and obligations otherwise required by Statement 106 following the effective date of this FSP. If an employer concludes that enactment of the Act was a significant event, but either (a) benefits available under its plan are not actuarially equivalent to Medicare Part D or (b) the employer is unable to conclude (refer to paragraph 33) whether any benefits are actuarially equivalent, it shall measure any effects of the Act other than the subsidy (for example, changes in estimated participation rates or health care costs) at the next measurement date for plan assets and obligations required by paragraphs 28–32 of this FSP.

13. Per FSP FAS 106-2:

> 27. For a plan (a) that provides benefits that are considered actuarially equivalent as of the date of enactment, based on information that is available as of the date of adoption of this interpretation, and (b) for which enactment of the Act was a significant event, this interpretation provides two alternative methods of transition—retroactive application to the date of enactment (paragraphs 28–29) or prospective application from the date of adoption (paragraph 30).

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Retroactive application to date of enactment

28. When this FSP is initially adopted, a remeasurement of the plan's assets and APBO, including the effects of the subsidy, if applicable, as well as the other effects of the Act, shall be made as of the earlier of (a) the plan's measurement date that normally would have followed enactment of the Act or (b) the end of the employer's interim or annual period that includes the date of the Act's enactment. As an alternative, employers are permitted, but not required, to perform that remeasurement as of the date of enactment. The measurement of the APBO shall be based on the plan provisions in place on the measurement date. Plan amendments occurring after the measurement date pursuant to (a) or (b) above shall not be anticipated in performing that measurement. However, if prior to the effective date of this FSP, a plan is amended so as to not be considered actuarially equivalent, the employer shall not reflect any effects of the subsidy in the transitional measurements required by this FSP. If the prescription drug coverage provided by a plan was amended after December 8, 2003, but before January 31, 2004 (the date before which plan amendments would not cause the deferral provided by FSP FAS 106-1 to expire), the effects of the prescription drug plan amendment and the consequential effects of the subsidy shall be accounted for pursuant to the applicable guidance in either paragraph 17 or 18 of this FSP.

29. The effects of measuring plan assets and obligations under paragraph 28 generally will not affect the accrued or prepaid postretirement benefit cost reported in the employer's statement of financial position as of the measurement date.[3] However, those measurements will affect net periodic postretirement benefit cost for periods subsequent to the date of the re-measurement.[4] To the extent that previously issued financial reports for periods prior to the effective date of this FSP would have been affected by the remeasurement of plan assets and obligations under paragraph 28, the requirements in paragraph 20 of APB Opinion No. 20, Accounting Changes, and paragraph 10 of FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, as applicable, shall be followed.[5] In calculating the effects on prior periods, the guidance in paragraphs 17 and 18 of this FSP applies to plan amendments adopted subsequent to the measurement date described in paragraph 28 but before the effective date of this FSP. The effects of any such amendment shall be determined as of the date the plan amendment is adopted. The following examples illustrate the application of the provisions in this paragraph.

Example A—Calendar Year-End, September 30 Measurement Date

Calendar Company, a public company, sponsors a postretirement health care benefit plan that provides prescription drug coverage. It has a December 31 year-end for financial reporting purposes and uses a September 30 measurement date pursuant to paragraph 72 of Statement 106. Calendar Company elected to defer any accounting for the effects of the Act pursuant to FSP FAS 106-1 and made that election in the quarter ending March 31, 2004, the first period in which the plan's accounting for the effects of the Act normally would have been reflected in Calendar Company's financial statements.

Calendar Company adopts the guidance in this FSP as of July 1, 2004, the beginning of its third quarter. Calendar Company and its actuarial advisors determine that benefits provided by the plan as of the date of enactment were at least actuarially equivalent to

[3] The paragraph 28 measurement would affect the statement of financial position if, pursuant to paragraph 60 of Statement 106, the employer has a policy of immediately recognizing gains and losses.

[4] Depending on the measurement date selected for the plan pursuant to paragraph 72 of Statement 106, the net periodic postretirement benefit cost may not be affected by the Act in the employer's reporting period immediately following the measurement required by paragraph 28. For example, for a public company with a December 31 fiscal year-end, the end of the employer's interim period that includes the date of enactment would be December 31, 2003. If that employer uses a September 30 measurement date pursuant to paragraph 72 of Statement 106, the effects of the Act on the plan would first affect net periodic postretirement benefit cost in the employer's interim period that begins April 1, 2004.

[5] Paragraph 10 of Statement 3 states that no cumulative effect of a change in accounting principle shall be included in net income of the interim period, other than the first interim period, in which the change is adopted. However, financial information for the pre-change interim periods of the fiscal year in which the change is made shall be restated on the basis of the new accounting principle whenever those pre-change interim periods are subsequently presented.

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Medicare Part D, and, accordingly, Calendar Company will be entitled to the subsidy. Calendar Company performs an interim measurement of the effects of the Act on the APBO as of December 31, 2003, the end of its interim (and annual) period that includes the date of the Act's enactment and determines that the aggregate effect on service cost, interest cost, and amortization of gains and losses results in a reduction of $500 in annual net periodic postretirement benefit cost compared to that amount calculated without considering the effects of the Act.

The effect of applying this FSP has no cumulative effect on Calendar Company's retained earnings as of December 31, 2003. Because Calendar Company uses a September 30 measurement date, the accounting for the plan is reflected in Calendar Company's financial statements on a one-quarter lag. Therefore, the Act had no effect on net periodic postretirement benefit cost for the first quarter. Accordingly, in applying the guidance in Statement 3, Calendar Company reports net periodic postretirement benefit cost for the nine-month period ending September 30, 2004, reflecting $250 (the second and third quarter amounts) of the $500 annual reduction. Net periodic postretirement benefit cost included in third quarter results of operations reflects only that quarter's $125 reduction due to the Act. When presented for comparative purposes, for example in summary quarterly financial information in the annual report or for comparative purposes in the 2005 second quarter financial report, the results of operations for the second quarter of 2004 will be restated to reflect a $125 reduction in net periodic postretirement benefit cost due to the Act.

Example B—April 30 Year-End, April 30 Measurement Date

Spring Company, a public company, sponsors a postretirement health care benefit plan that provides prescription drug coverage. It has an April 30 year-end for financial reporting purposes and uses April 30 as the measurement date for plan assets and obligations under Statement 106. Spring Company elected to defer any accounting for the effects of the Act pursuant to FSP FAS 106-1 and made that election in the quarter ending January 31, 2004, the first period in which the plan's accounting for the effects of the Act normally would have been reflected in Spring Company's financial statements.

Spring Company adopts the guidance in this FSP as of August 1, 2004, the beginning of its second quarter. Spring Company and its actuarial advisors determine that benefits provided by the plan as of the date of enactment were at least actuarially equivalent to Medicare Part D, and, accordingly, Spring Company will be entitled to the subsidy. Spring Company measures the effects of the Act on the APBO as of January 31, 2004, the end of its interim period that includes the date of the Act's enactment and determines that the aggregate effect on service cost, interest cost, and amortization of gains and losses results in a reduction of $500 in annual net periodic postretirement benefit cost compared to that amount calculated without considering the effects of the Act.

Because the date for remeasuring the plan's assets and obligations required by this FSP—for an employer that elects retroactive application—occurs in Spring Company's prior fiscal year, the cumulative effect of applying the guidance in this FSP on Spring Company's retained earnings as of April 30, 2004, is $125 (the fourth quarter effect on net periodic postretirement cost, ignoring any deferred income tax effects, which may be none). That cumulative effect of a change in accounting principle is recognized in Spring Company's net income for the six months ending October 31, 2004. Assuming no other changes in assumptions or other gains and losses arise in the regularly scheduled April 30, 2004 measurement of the plan, pursuant to the guidance in Statement 3, Spring Company reports net periodic postretirement benefit cost for the six-month period ending October 31, 2004, reflecting $250 (the first and second quarter amounts) of the $500 annual reduction. Net periodic postretirement benefit cost included in second quarter results of operations reflects only that quarter's $125 reduction due to the Act. When presented for comparative purposes, for example in summary quarterly financial information in the annual report or for comparative purposes in the next fiscal year's first quarter financial report, the results of operations for the quarter ended July 31, 2004, will

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be restated to reflect the $125 reduction in net periodic postretirement benefit cost due to the Act and the $125 cumulative effect of the change in accounting principle.

Prospective application as of date of adoption

30. When this FSP is initially adopted, a remeasurement of the plan's assets and APBO, including the effects of the subsidy, if applicable, as well as the other effects of the Act, shall be made as of the beginning of the period of adoption pursuant to the guidance in paragraph 73 of Statement 106. The measurement of the APBO shall be based on the plan provisions in place on the measurement date and shall incorporate the best available current information regarding actuarial assumptions and discount rates. The results of that measurement shall be used to determine net periodic postretirement benefit cost in interim periods following the date of adoption until the next measurement date otherwise required by Statement 106. The following example illustrates the application of the provisions of this paragraph.

Example C—Calendar Year-End, September 30 Measurement Date

Calendar Company, a public company, sponsors a postretirement health care benefit plan that provides prescription drug coverage. It has a December 31 year-end for financial reporting purposes and uses a September 30 measurement date pursuant to paragraph 72 of Statement 106. Calendar Company elected to defer any accounting for the effects of the Act pursuant to FSP FAS 106-1 and made that election in the quarter ending March 31, 2004, the first period in which the plan's accounting for the effects of the Act normally would have been reflected in Calendar Company's financial statements.

Calendar Company adopts the guidance in this FSP as of July 1, 2004, the beginning of its third quarter. Calendar Company and its actuarial advisors determine that benefits provided by the plan as of the date of enactment were at least actuarially equivalent to Medicare Part D, and, accordingly, Calendar Company will be entitled to the subsidy. Calendar Company measures the effects of the Act on the APBO as of April 1, 2004, the beginning of the plan's interim period that corresponds to the plan sponsor's first reporting period beginning after June 15, 2004, and determines that the aggregate effect on service cost, interest cost, and amortization of gains and losses results in a reduction of $500 in annual net periodic postretirement benefit cost compared to that amount calculated without considering the effects of the Act.

Net periodic postretirement benefit cost for the quarters ending September 30 and December 31, 2004, reflecting the activity in the plan for the quarters ending June 30 and September 30, 2004, will include a $125 per quarter reduction in net periodic postretirement benefit cost due to the effects of the Act.

Nonpublic entity with only small plans

31. If enactment of the Act constitutes a significant event for a plan, a nonpublic entity that meets the criteria in paragraph 23 may follow the guidance in paragraph 28, including the related transition guidance described in paragraph 29, or may incorporate the effects of the Act prospectively in measures of net periodic postretirement benefit cost and plan assets and obligations for fiscal years beginning after December 15, 2004.

Employer That Did Not Elect Deferral

32. For an employer that did not elect the deferral option provided under FSP FAS 106-1 and whose previous accounting for the effects of the Act differs from the guidance in this FSP, the adoption of this FSP constitutes a change in accounting principle under Opinion 20. Accordingly, the cumulative effect of retroactive application of this FSP to the date of the Act's enactment shall be reflected in the financial statements following the provisions of paragraph 20 of Opinion 20 and paragraphs 9 and 10 of Statement 3, as applicable.

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Subsequent Determination of Actuarial Equivalence Absent a Plan Amendment

33. When adopting this FSP, an employer and its actuarial consultants may be unable to determine the extent to which the benefits provided by a plan are actuarially equivalent as of the date of the initial measurement applying the guidance in this FSP. If clarifying regulations related to the Act or new information about the interpretation or determination of *actuarial equivalency* under the Act becomes available, the employer shall reconsider whether the benefits provided under its plan, as presently constructed, are actuarially equivalent.[6] If that reconsideration results in a conclusion that benefits provided by the plan are actuarially equivalent (or that additional benefits provided by the plan are actuarially equivalent in the case of a plan under which an employer previously had determined that some benefits were actuarially equivalent), that conclusion could be a significant event pursuant to paragraph 73 of Statement 106.[7] If the effects of the subsidy on the plan are significant, a measurement of plan assets and obligations shall be performed as of the date that actuarial equivalency is determined. Any effect on the APBO due to the subsidy shall be reflected as an actuarial gain consistent with the guidance in paragraph 14 of this FSP. Measures of net periodic postretirement benefit cost for subsequent periods would reflect the effects of those measurements (reported on a lag basis, if appropriate; refer to footnote 6). Prior financial statements shall not be retroactively adjusted nor shall a cumulative effect for prior periods be recognized in income.

INT 04-17 Status

14. No further discussion is planned.

[6] The guidance in this paragraph does not apply if a plan amendment is the event that gives rise to the employer's reconsideration of actuarial equivalency. The guidance in paragraphs 17 and 18 of this FSP apply to plan amendments.

[7] To the extent that some benefits under a plan are determined to be actuarially equivalent at the date of adoption of the FSP, the provisions of paragraphs 24–32 apply.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 04-21: EITF 02-9: Accounting for Changes That Result in a Transferor Regaining Control of Financial Assets Sold

INT 04-21 Dates Discussed

December 5, 2004; March 13, 2005; March 3, 2012; August 31, 2012

INT 04-21 References

Current:
SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities

Superseded:
SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities

INT 04-21 Issue

1. EITF No. 02-9, *Accounting for Changes That Result in a Transferor Regaining Control of Financial Assets Sold* (EITF 02-9) expands on a key concept presented in FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (FAS 140), paragraph 55. This key concept requires a transferred financial asset that has been accounted for as sold to be accounted for as "re-purchased" if the basis for that sale accounting subsequently becomes invalid.

2. The following is excerpted from EITF 02-9:

> 1. …One circumstance that has raised questions about the application of paragraph 55 occurs when the provisions of paragraph 55 are triggered because the transferor holds a contingent right such as a contingent call option on the transferred financial assets (for example, a removal of accounts provision or "ROAP") and the contingency has been met. This issue assumes that the transferee is not consolidated by the transferor.
>
> 2. Under Statement 140, rights held by the transferor (typically in the form of purchased options or forward purchase contracts) only preclude sale accounting under paragraph 9.c.(2) if they provide the transferor with (a) the unilateral right to cause the holder to return specific transferred financial assets, and (b) more than a trivial benefit. One class of contingent rights (including certain ROAPs 1) does not preclude sale accounting because it does not include unilateral rights. The most common type of ROAP is a default ROAP, which gives the holder the right but not the obligation to purchase (call) a loan that is in default (the meaning of default typically is specifically defined in each transaction). Such rights are common in credit card securitizations and in securitizations sponsored by the Government National Mortgage Association (GNMA) 2 and other governmental or quasi-governmental agencies. Once the contingency is met (in this case, when a given loan goes into default), the call option on that asset (loan) is no longer contingent. At that point, the transfer fails the criterion in paragraph 9.c.(2) of Statement 140 because the transferor has the unilateral right to purchase a specific transferred financial asset and obtains more than a trivial benefit. Under the requirements of paragraph 55, when a contingency related to a transferor's contingent right has been met, the transferor generally must account for the "re-purchase" of a specific subset of the financial assets transferred to and held by the qualifying entity. The transferor must do so regardless of whether it intends to exercise its call option.

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3. Per EITF 02-9, the issues are:

Issue 1—How the transferor should account for the transferor's beneficial interests when the underlying assets are re-recognized under the provisions of paragraph 55 because the transferor's contingent right (for example, a ROAP or other contingent call option on the transferred financial assets) becomes exercisable, including whether any gain or loss should be recognized by the transferor when paragraph 55 is applied.

Issue 2—Whether under any circumstances a loan loss allowance should initially be recorded for loans that do not meet the definition of a security when they are re-recognized under the provisions of paragraph 55

Issue 3—How re-recognition under paragraph 55 of assets sold affects the accounting for the related servicing asset.

Issue 4—After a paragraph 55 event, how the transferor should account for the transferor's interests (other than the servicing asset).

INT 04-21 Discussion

4. EITF 02-9 consensus on each issue is as follows:

5. The Task Force reached a consensus on Issue 1 that upon application of paragraph 55, no gain or loss should be recognized in earnings with respect to any of the transferor's beneficial interests. Beneficial interests should be evaluated periodically for possible impairment, including at the time paragraph 55 is applied. A gain or loss may be recognized upon the exercise of a ROAP or similar contingent right with respect to the "re-purchased" transferred financial assets that were sold if the ROAP or similar contingent right held by the transferor is not accounted for as a derivative under Statement 133 and is not at-the-money, resulting in the fair value of those repurchased assets being greater or less than the related obligation to the transferee.

6. The Task Force reached a consensus on Issue 3 that under no circumstances should a loan loss allowance be initially recorded for loans that do not meet the definition of a security when they are re-recognized pursuant to paragraph 55.

7. The Task Force reached a consensus on Issue 4 that when a paragraph 55 event occurs, the accounting for the servicing asset related to the previously sold financial assets does not change as a result of the application of paragraph 55. That is, even though the transferor has regained control over the previously sold assets, the cash flows from those assets will contractually be paid to the SPE, which will then distribute the proceeds to satisfy its contractual obligations (including obligations to the beneficial interest holders). Because the transferor, as servicer, is still contractually required to collect the asset's cash flows for the benefit of the SPE and otherwise service the assets, it should continue to recognize the servicing asset and assess the asset for impairment as required by Statement 140.

8. The Task Force reached a consensus on Issue 5 that when a paragraph 55 event occurs, the transferor should continue to account for the transferor's interests in those underlying financial assets apart from any re-recognized financial assets. That is, the transferor's interests should not be combined with and accounted for with the re-recognized financial assets. However, a subsequent event that results in the transferor reclaiming those financial assets from the transferee—for example, the exercise of a ROAP or the consolidation by the transferor of the securitization entity in accordance with applicable generally accepted accounting principles, including Interpretation 46R—would result in a recombination of the transferor's interests with the underlying financial assets.

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5. The Working Group reached a consensus to adopt EITF 02-9 as an interpretation of SSAP No. 103R, with modification as follows:

a. Change references to FAS 140 to SSAP No. 103R including paragraph-specific references. Modify FAS 140, paragraph 55 references to refer to SSAP No. 103R, paragraph 59.

b. Change references to FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* to SSAP No. 86 as an interpretation of SSAP No. 91R.

c. Remove reference to Interpretation 46R as FASB Interpretation No. 46, *Consolidation of Variable Interest Entities,* is pending review for statutory accounting. (The prior GAAP guidance in FASB Interpretation FIN 46 was rejected for statutory accounting in *SSAP No. 3—Accounting Changes and Corrections of Errors*.)

d. Limit the applicability of EITF 02-9, Issue 3 to only valuation allowances applicable to statutory accounting for mortgage loans and real estate under development as provided in *SSAP No. 37—Mortgage Loans* and real estate under development as discussed in *SSAP No. 38—Acquisition, Development and Construction Arrangements*.

6. This interpretation was originally effective for years beginning January 1, 2005, to be consistent with the original effective date of SSAP No. 91R. Revisions adopted to this interpretation on March 3, 2012, are in accordance with the adoption with modification of FAS 166 in a new SSAP to superseded SSAP No. 91R.

INT 04-21 Status

7. In 2009, *FAS 166, Accounting for Transfers of Financial Assets, an Amendment of FAS 140*, was issued. In addition to amending FAS 140, it also amended FASB EITF 02-9. FAS 166 was adopted for statutory accounting in SSAP No. 103R to supersede SSAP No. 91R. On March 3, 2012, corresponding revisions to INT 04-21 were also adopted to reflect the updated GAAP guidance adopted for statutory accounting interpreting SSAP No. 103R. These changes will not be tracked in subsequent editions of the Manual.

8. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group and Statutory Accounting Principles (E) Working Group

INT 05-05: Accounting for Revenues Under Medicare Part D Coverage

INT 05-05 Dates Discussed

September 28, 2005; December 3, 2005; March 24, 2018; August 4, 2018

INT 05-05 References

Current:
SSAP No. 47—Uninsured Plans
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 66—Retrospectively Rated Contracts
SSAP No. 84—Health Care and Government Insured Plan Receivables

INT 05-05 Issue

1. The Medicare Modernization Act of 2003 (MMA) created a new program, commonly known as Medicare Part D, whereby Medicare recipients may obtain prescription coverage offered by insurers who have been approved by the Centers for Medicare and Medicaid Services (CMS). Insurers who offer Medicare Part D coverage will, starting in January 2006, receive several different types of funds relating to the program. Some of these funds relate to portions of the coverage that require an annual reconciliation, resulting in the return of any excess funds received. Other funds may be received (or may be required to be returned) to offset experience that is especially unfavorable (or, respectively, favorable).

2. How should the various components of the funds received or receivable by an insurer from Medicare Part D coverage be accounted for?

INT 05-05 Discussion

3. The attached appendix provides a listing of terms to which CMS ascribes a specific meaning. This list has been enhanced to include other terms in order to facilitate consistent application for accounting and the NAIC's risk-based capital (RBC) formula. It should be noted that the terms included in the attached appendix are, for the most part, defined by CMS. Consequently, the term "reinsurance payment" does not represent actual reinsurance as defined by *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*.

4. The Emerging Accounting Issues (E) Working Group reached a consensus to adopt the following guidance as it applies to the various funds to be received under the Medicare Part D program. The funds should be accounted for in accordance with one of the three SSAP's outlined below:

a. Specific funds received as reimbursements (or advance payments) for uninsured claims under a partially uninsured plan should be accounted for under SSAP No. 47. These funds include "reinsurance payments," "Coverage Gap Discount Program" payments and "low-income subsidy (cost-sharing portion)." These funds are paid by the government for a portion of claims above the out-of-pocket threshold or relate to prescription drug plan (PDP) payments for all or a portion of the deductible, the coinsurance and the co-payment amounts for low-income beneficiaries. CMS provides advance funding to the Part D sponsors. The Part D sponsor uses those advances to provide point-of-sale drug discounts to participants. CMS invoices the prescription drug manufacturers. The payment reconciliation process ensures that the Part D sponsor is paid dollar for dollar for coverage gap discounts advanced at the point of sale, based on accepted prescription drug

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event (PDE) data, and that any unused excess advances from the government are repaid. The Coverage Discount Gap Program does not apply to low-income beneficiaries.

b. Specific funds received by the PDP sponsor from either the Medicare Part D enrollee or the government as payment for standard coverage that will be subject to retrospective premium adjustments should be accounted for under SSAP No. 66. These funds include "direct subsidy," "low-income subsidy (premium portion)," "beneficiary premium (standard coverage portion)," "Part D payment demonstration" and "risk corridor payment adjustment." The funds noted above have a final policy amount that is calculated based on the loss experience of the insured during the term of the policy, therefore should be treated as such.

c. Specific funds received as premiums for coverage that is not retrospectively rated should be accounted for under SSAP No. 54R. These funds include "beneficiary premium (supplemental benefit portion)" as these payments are considered to be standard premium payments that do not meet the definitions under SSAP No. 47 or SSAP No. 66 as defined in paragraph 4.a. and paragraph 4.b. of this interpretation.

5. The collectibility and any nonadmission of amounts receivable from the government insured or uninsured plans are addressed in SSAP No. 84, paragraph 22, and SSAP No. 47, paragraph 10 and paragraph 11, respectively.

INT 05-05 Status

6. On August 4, 2018, the Statutory Accounting Principles (E) Working Group updated this interpretation to add a description of the Coverage Gap Discount Program, amend existing guidance on program payments and update definitions. No further discussion is planned.

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Appendix – Commonly Used Terms for Medicare Part D Coverage

The federal Centers for Medicare and Medicaid Services (CMS) oversees the Medicare Part D prescription drug coverage, including coverage provided through a stand-alone prescription drug plan (PDP) and coverage provided as part of a Medicare Advantage plan. CMS ascribed specific meaning to most of the following terms. Other terms have been defined below in order to facilitate consistent application.

Beneficiary Premium (Standard Coverage Portion) – The amount received from the Part D enrollee (directly, or from CMS after being withheld from Social Security benefits) as payment for the standard coverage. This includes any late enrollment penalties that the PDP sponsor receives for an enrollee. The beneficiary premium is accounted for as health premium.

Beneficiary Premium (Supplemental Benefit Portion) – The amount received from the Part D enrollee (directly, or from CMS after being withheld from Social Security benefits) as payment for supplemental benefits. The beneficiary premium is accounted for as health premium.

Coverage Gap Discount Program – The federal Affordable Care Act amended the Health Care and Education Act of 2010 (H. R. 4872) (HCERA) in 2011 to establish a discount program that would make manufacturer discounts available to applicable Medicare beneficiaries receiving applicable covered Part D drugs while in the coverage gap. Part D sponsors must provide the discounts for the applicable drugs in the coverage gap at point-of-sale. CMS coordinates the collection of discount payments from manufacturers and payment to Part D sponsors that provided the discount to applicable beneficiaries through a contractor. The coordination involves a standard process for paying Part D sponsors based on new information submitted to CMS on prescription drug event data. The Coverage GAP Discount Program is reconciled quarterly.

Coverage Year Reconciliation – A reconciliation made after the close of each calendar year to determine the amounts that a PDP sponsor is entitled to for the low-income subsidy (cost-sharing portion), the reinsurance payment, and the risk corridor payment adjustment. To the extent that interim payments (if any) from CMS exceeded the amounts determined by the reconciliation, the PDP sponsor must return the excess to the government; to the extent that interim payments (if any) from CMS fell short of the amounts determined by the reconciliation, the government will make an additional payment to the PDP sponsor. The coverage year reconciliation results in the low-income subsidy (cost-sharing portion) and the reinsurance payment being essentially a self-insured (by the government) component of the Part D coverage, subject to SSAP No. 47. The coverage year reconciliation also results in the treatment of the risk corridor payment adjustment as a retrospective premium adjustment, subject to SSAP No. 66.

Direct Subsidy – The amount the government pays to the PDP sponsor for the standard coverage. These payments are accounted for as health premium.

Low-Income Subsidy (Cost-Sharing Portion) – The amount the government pays to the PDP sponsor for additional benefits provided to low-income enrollees. The additional benefits may include payment for some or all of the deductible, the coinsurance, and the co-payment above the out-of-pocket threshold. These payments are accounted for as payments made under a self-insured plan.

Low-Income Subsidy (Premium Portion) – The amount the government pays to the PDP sponsor for low-income enrollees in lieu of part or all of the beneficiary premium (standard coverage portion). These payments are accounted for as health premium.

PDP Sponsor – The entity that provides stand-alone Part D coverage (as opposed to Part D coverage provided through a Medicare Advantage plan).

Reinsurance Payment – An amount paid by the government for benefit costs above the out-of-pocket threshold (see "Standard Coverage"). Generally, when costs exceed the out-of-pocket threshold, the government pays a specified percentage of the costs, the enrollee pays a percentage (or the specified co-

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payments which are updated based on cost trends for generic and for brand-name prescriptions), and the PDP sponsor pays the remainder. The amount paid by the government is treated as a claim payment made by a self-insured benefit plan rather than as revenue to the PDP sponsor, and the claims do not flow through the PDP sponsor's income statement. In cases where the government prepays the reinsurance payment on an estimated basis, the prepayment is treated as a deposit, which again does not pass through the PDP sponsor's income statement. The amount paid by the enrollee is paid directly to the pharmacy; therefore there is no required accounting for this amount by the PDP sponsor.

Part D Payment Demonstration – A payment from the government to a PDP sponsor participating in CMS's Part D Payment Demonstration. The payment demonstration is a special arrangement in which the PDP sponsor receives a predetermined per-enrollee capitation payment and the government no longer provides reinsurance for the specified percentage (example 80%) of costs in excess of the out-of-pocket threshold. Rather, the PDP sponsor assumes the risk for the specified percentage (example 80%) of costs, in addition to its normal percentage (example 15%) share of costs in excess of this threshold. However, risk corridor protection does still apply to this specified percentage (example 80%) share of costs. These payments are accounted for as health premium.

Reinsurance Coverage – The Medicare Part D provision under which the PDP sponsor may receive a reinsurance payment. This does not include payments under the Part D Payment Demonstration.

Risk Corridor Payment Adjustment – An amount by which the government adjusts its payments to the PDP sponsor, based on how actual benefit costs vary from the costs anticipated in the PDP sponsor's bid for the Part D contract (the "target amount" of costs). The government establishes thresholds for symmetric risk corridors around the target amount, using percentages of the target amount. If actual costs exceed the target amount but are less than the first threshold upper limit, then no adjustment is made. Risk corridor payment adjustments are accounted for as retrospective premium adjustments on retrospectively rated contracts.

Risk Corridor Protection – The Medicare Part D provision under which the PDP sponsor may receive (or pay) a Risk Corridor Payment Adjustment. Most employer plans providing Medicare Part D are not eligible for Risk Corridor Protection.

Standard Coverage – The Part D benefit design that conforms to certain standards prescribed by the government. The standard coverage comprises: no coverage for an annual initial deductible; coverage net of a coinsurance provision (the percentage of costs are payable by the insured) for costs up to an initial coverage limit; a range beyond the initial coverage limit (sometimes called the "coverage gap") in which the insured drug manufacturers and the PDP sponsor (for example, by 2020 insureds who are eligible for drug manufacturer discounts will pay 25% for qualifying brand and generic drugs, the PDP sponsor will be responsible for 25% of qualifying brand and 75% of generic drugs, and the drug manufacturer will be responsible for 50% of qualifying brand drugs); and an annual out-of-pocket threshold above which the insured pays the greater of a specified co-payment or a specified percentage of the drug cost. The various limits and thresholds are set at specified dollar amounts, which will be increased in later years based on the growth in drug expenditures. Wherever the term "standard coverage" is used as part of these instructions, the same treatment would be applied to coverage that has been approved as actuarially equivalent coverage. With respect to amounts above the out-of-pocket threshold, see the definitions of "Reinsurance Payment" and "Part D Payment Demonstration."

Supplemental Benefits – Benefits in excess of the standard coverage. These benefits typically will cover some portion of the deductible, the co-payments, or the coverage gap between the initial coverage limit and the out-of-pocket threshold. Supplemental benefits are part of an enrollee's Part D coverage, so they are not placed in the "Other" category in the RBC formula. However, they are not subject to either the reinsurance payment or the risk corridor payment adjustment, so they receive less favorable RBC treatment than the standard coverage.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)

INT 06-02 Dates Discussed

March 5, 2006; June 11, 2006; September 10, 2006

INT 06-02 References

Current:
SSAP No. 26R—Bonds
SSAP No. 30R—Unaffiliated Common Stock
SSAP No. 32R—Preferred Stock
SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies

INT 06-02 Issue

1. A certified capital company (CAPCO) is a state legislated venture capital firm that can be a partnership, corporation, trust or limited liability company, profit or not-for-profit, for which investors who invest cash to acquire an equity interest or qualified debt instrument receive state premium or income tax credit. Although these investments are sometimes termed by different acronyms, they will be referred to as a CAPCO for purposes of this issue.

2. A reporting entity that qualifies as a certified investor typically earns, in the year the investment is made, a vested credit against state premium or income taxes equal to greater than 100% of the investor's investment of certified capital, of which a certain percent (varies by state; example: 10%, 25%) may be taken in any taxable year. The credit to be applied in any one year may not exceed the entity's state premium or income tax liability for the taxable year. Any unused tax credit may be carried forward until the premium or income tax credit is used (varies by state; some indefinitely, in other instances there is a specified expiration date, such as 2010; 2020). In some cases, a certified investor may transfer or assign unused premium or income tax credits. In addition to tax credits, the CAPCO often pays a nominal amount of interest and has a specified principal repayment date. The CAPCO often provides for a mechanism that guarantees the principal repayment.

3. Depending on the terms of the agreement, a CAPCO may make prepayments of principal and interest on its indebtedness.

4. The accounting issues are:

Issue 1: How should investments in a CAPCO be accounted for?

Issue 2: If the CAPCO agreement provides for the majority of interest to be paid in advance, how should it be earned?

INT 06-02 Discussion

5. For Issue 1, the Working Group came to a consensus that reporting entities should account and report for investments in CAPCO's consistent with the agreement structure within the guidance provided below:

a. Investment in a debt instrument of a CAPCO shall be reported as a bond in accordance with the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and the designation assigned in the *NAIC Valuations of Securities* product prepared by the

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NAIC Securities Valuation Office (Valuations of Securities manual) as stated in SSAP No. 26R, paragraph 11.

b. Investment in an equity interest of a CAPCO shall be reported as common stock and reported at fair value as stated in SSAP No. 30R, paragraph ~~8~~9.

c. Investment in preferred stock interest of a CAPCO shall be reported as preferred stock in accordance with the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and the designation assigned in the *NAIC Valuations of Securities* product prepared by the NAIC Securities Valuation Office (Valuations of Securities manual) as stated in SSAP No. 32R, paragraphs ~~19-22~~20-23.

d. Investment in a Joint Venture, Partnership and Limited Liability Company (LLC) shall be reported in accordance with SSAP No. 48, paragraphs 5-6. The reported value of the investment shall be decreased in proportion to the premium tax credits utilized.

e. The tax credits shall be recognized as a reduction of the tax liabilities as they are utilized. Tax credits received are not to be included in investment income.

6. For Issue 2, the Working Group came to a consensus that reporting entities should account for any prepaid interest received by the insurer to be recorded as an unearned interest liability and should be amortized over the life of the security. This is consistent with the treatment of prepaid interest in SSAP No. 37 and SSAP No. 49. This is also consistent with SSAP No. 34, which states that gross investment income should be reported as earned, and includes a change in unearned investment income.

INT 06-02 Status

7. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-07: Definition of Phrase "Other Than Temporary"

INT 06-07 Dates Discussed

September 10, 2006; December 10, 2006; December 11, 2023; January 10, 2024

INT 06-07 References

Current:
SSAP No. 26R—Bonds
SSAP No. 30R—Unaffiliated Common Stock
SSAP No. 32R—Preferred Stock
SSAP No. 37—Mortgage Loans
SSAP No. 39—Reverse Mortgages
SSAP No. 41R—Surplus Notes
SSAP No. 43R—Loan-Backed and Structured Securities
SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies
SSAP No. 68—Business Combinations and Goodwill
SSAP No. 93—Low-Income Housing Tax Credit Property Investments
SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities
SSAP No. 105R—Working Capital Finance Investments

Superseded:
SSAP No. 88—Investments in Subsidiary, Controlled, and Affiliated Entities, A Replacement of SSAP No. 46
SSAP No. 98—Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43—Loan-Backed and Structured Securities
SSAP No. 99—Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment

Affects:
Nullifies the prior interpretation on this topic, *INT 02-07 Definition of Phrase "Other Than Temporary"*

INT 06-07 Issue

1. The *Accounting Practices and Procedures Manual* contains guidance for determining when an investment is considered impaired within each of the above identified statements. Those statements should also be used to determine the measurement of an impairment loss. Each of the above statements also makes reference to an "other than temporary" decline in fair value. This interpretation is designed to address questions related to that phrase, as well as summarize the statutory accounting process for determining when an investment is considered impaired.

Step 1: Determine Whether an Investment Is Impaired

2. The decision for determining when an investment is considered impaired is dictated by the applicable SSAP and the respective impairment indicators included in each of the SSAPs. If an impairment indicator is present, the determination of an impairment shall be assessed at the individual security or investment level as reported in the annual statement and supporting schedules. For those SSAPs that require the reporting entity to use the fair value to determine if an impairment has occurred, the determination of that value shall be consistent with how the term fair value is defined within *SSAP No. 100—Fair Value*. Once a reporting entity has determined that an impairment indicator is present, the reporting entity shall continue to evaluate whether the investment is impaired each subsequent reporting

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period until either (a) the investment experiences a recovery of the fair value up to (or beyond) its carrying value or (b) the investor recognizes an other-than-temporary impairment loss.

Step 2: Evaluate Whether an Impairment Is Other Than Temporary

3. There are numerous factors to be considered when determining whether an impairment is other than temporary and their relative significance will vary from case to case. The Emerging Accounting Issues (E) Working Group (Working Group) has been asked if the phrase "other than temporary" should be interpreted to mean "permanent." The Working Group[1] believes the Statutory Accounting Principles (E) Working Group consciously chose the phrase "other than temporary" as the analysis was not intended to determine whether an individual security or investment was "permanently impaired." The fair value of assets may decline for various reasons. The market price may be affected by general market conditions, which reflect prospects for the economy as a whole, or by specific information pertaining to an industry or an individual company. Such declines require further investigation by management. Acting upon the premise that a write-down may be required, management should consider all available evidence to evaluate the fair value of its investment.

4. The Working Group believes that the following items are only a few examples of the factors, which, individually or in combination, indicate that a security's decline in value is specific to an issuer's fundamental credit difficulties, or that a non-interest related decline is other than temporary and that a write-down of the carrying value is required:

a. The length of time and the extent to which the fair value has been less than cost;

b. The financial condition and short-term prospects of the issuer, including any specific events that may influence the operations of the issuer, such as changes in technology, that may impair the earnings potential of the asset or the discontinuance of a segment of the business that may affect the future earnings potential; or

c. The intent and ability of the holder to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in value.

5. An interest related impairment should be deemed other-than-temporary when an investor has the intent to sell an investment, at the reporting date, before recovery of the cost of the investment. The investor should consider whether its cash or working capital requirements and contractual or regulatory obligations indicate that the investment may need to be sold before the forecasted recovery occurs. The term "interest related" includes a declining value due to both increases in the risk free interest rate and general credit spread widening. Credit spreads can widen or contract for a variety of reasons, including supply/demand imbalances in the marketplace or perceived higher/lower risk of an entire sector. If the declining value is caused, in whole or in part, due to credit spreads widening, but not due to fundamental credit problems of the issuer, the change in credit spreads is deemed to be interest related. Fundamental credit problems exist with the issuer when there is evidence of financial difficulty that may result in the issuer being unable to pay principal or interest when due.

6. Unless evidence exists to support the assertion that the decline in fair value below carrying value is temporary, a write-down, accounted for as a realized loss, should be recorded. In accordance with the guidance of the SSAPs, such loss should be recognized in income for the period in which other than temporary impairment is determined to have occurred. The adjusted carrying value reflecting the impairment loss of the individual security or investment shall be the new cost basis of the individual security or investment.

1 The recommendations provided by the Working Group were developed in part from SEC Staff Accounting Bulletin No. 59– *Noncurrent Marketable Equity Securities* (SAB 59). As such, readers of this interpretation should understand that SAB 59 has not been adopted as part of Statutory Accounting Principles as SAB's are not part of the Statutory Hierarchy (see Preamble).

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7. The Working Group has also been asked if it is appropriate for reporting entities, independent auditors or state examiners to apply predefined thresholds to the phrase "other than temporary"? The Working Group is aware that certain insurers, independent auditors and state examiners, over time, have developed quantitative thresholds as "rules of thumb" to assist in the evaluation of asset impairment. One rule of thumb in particular suggests that if the fair value is less than its carrying value by 20 percent or more, then it is considered to be other than temporarily impaired. Another suggests that an asset is other than temporarily impaired if the fair value has been less than cost for more than 6 months. The use of a numerical threshold may provide the basis for a preliminary assumption that – without considering all relevant circumstances – an impairment may have occurred. Identifying the impairment is only the beginning of the analysis; it cannot appropriately be used as a substitute for a full analysis of all relevant qualitative considerations. Exclusive reliance on such thresholds removes the ability of management to apply its judgment, a concept inherent to the impairment model.

Step 3: If the Impairment is Other Than Temporary, the Cost Basis of the Individual Asset Shall Be Written Down to a New Cost Basis and the Amount of the Write-Down Is Accounted for as a Realized Loss

8. If an impairment is considered other than temporary, the cost or carrying value of the asset should be written down to reflect its value in accordance with the relevant SSAP. A company's management should follow the impairment guidance in the SSAP pertaining to that particular asset class while considering various factors on a case-by-case basis in determining the amount of the realized loss that should be recorded.

INT 06-07 Discussion

9. The Working Group reached a consensus to adopt with modification paragraph 6, 7 and 11 of *FSP FAS115-1/124-1: The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (FSP FAS 115-1/124-1). This INT rejects paragraphs 1-5, 8-10, 12-15, and 19 of FSP FAS 115-1/124-1. This INT does not address paragraphs 16-18 and footnote 1 to paragraph 7 of FSP FAS115-1/124-1.

10. Paragraphs 3-8 of this interpretation incorporate the guidance that was in *INT 02-07: Definition of Phrase "Other Than Temporary*," paragraphs 3-9, with an addition to clarify the general credit spread widening that was discussed in INT 02-07, paragraph 6. On final adoption of this interpretation, INT 02-07 is nullified.

11. FSP FAS 115-1/124-1 nullified the requirements of paragraphs 10-18 of EITF 03-01: *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (EITF 03-1) and carried forward the requirements of paragraphs 8, 9, 21 and 22 of the EITF to the FSP. The Working Group notes that the remaining paragraphs of EITF 03-01 either primarily related to the EITF process or are inconsistent with the current statutory model for impairment and are rejected. The Statutory Accounting Principles (E) Working Group is separately considering the disclosures related to the FSP.

12. FSP EITF 03-1-1: Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1 (FSP EITF 03-1-1) was issued by the EITF on September 30, 2004, and delayed the effective date for the measurement and recognition guidance contained in paragraphs 10-20 of EITF 03-1. The delay of the effective date for paragraphs 10-20 of Issue 03-1 was superseded concurrent with the final issuance of FSP FAS 115-1/124-1 and as such, is rejected.

13. Effective December 31, 2023, the Working Group rejected *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases*

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(Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and *ASU 2020-03 Codification Improvements to Financial Instruments*. As a result, companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect prior U.S. GAAP guidance.

INT 06-07 Status

~~13.~~14. INT 06-07 nullifies *INT 02-07: Definition of Phrase "Other Than Temporary."*

~~14.~~15. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-12: Tax Deposits Submitted in Accordance with Section 6603 of the Internal Revenue Service (IRS) Code

INT 06-12 Dates Discussed

September 10, 2006; December 10, 2006

INT 06-12 References

Current:
SSAP No. 101—Income Taxes

Superseded:
SSAP No. 10R—Income Taxes – A Temporary Replacement of SSAP No. 10

INT 06-12 Issue

1. The American Jobs Creation Act of 2004 enacted on October 22, 2004, added new section 6603 to the Internal Revenue Service Code (the Code) to permit a taxpayer to make a deposit with the Internal Revenue Service to suspend the running of interest under section 6601 on a potential underpayment of tax. A deposit may be made with respect to certain underpayments of tax that have not been assessed at the time of the deposit.

2. Section 6603(a) provides that a taxpayer may make a deposit with the Service that may be used by the Secretary to pay any income, gift, estate, or generation-skipping taxes imposed on the taxpayer under the Code, or certain excise taxes imposed on the taxpayer under the Code. Section 6603(b) provides that, to the extent that a deposit is used by the Service to pay tax, the tax shall be treated as paid on the date the deposit is made for purposes of computing interest on underpayments under section 6601.

3. Section 6603(c) provides that the Service will return to the taxpayer any amount of a deposit that the taxpayer requests in writing be returned unless the amount has previously been used to pay tax or the Service determines that collection of tax is in jeopardy.

4. The accounting issue is whether protective tax deposits meet the definition of current income tax recoverable as that term is used in SSAP No. 101, paragraph 9.

INT 06-12 Discussion

5. The Working Group reached a consensus that deposits made with the Internal Revenue Service, as described in paragraphs 1-3 of this interpretation, meet the definition of a current income tax recoverable as defined in SSAP No. 101, paragraph 9, as the reporting entity has made the deposit under its substantial authority and the deposit can be recovered upon written request.

6. Section 6603 tax deposits are admitted assets to the extent the section 6603 tax deposit complies with SSAP No. 101 and this guidance. The reporting entity shall report section 6603 tax deposits as assets within the caption "Current Federal and Foreign Income Tax Recoverable and Interest thereon." The section 6603 tax deposit asset and any related tax liability shall be presented on a gross basis for statutory reporting purposes.

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Calculating Nonadmission

7. The reporting entity shall expense amounts previously used to pay tax.

8. The reporting entity shall nonadmit:

   a. amounts the Service has determined, or the reporting entity estimates it is probable the Service will determine, that collection of the tax from the reporting entity is in jeopardy for section 6603 tax deposit amounts in excess of the specifically established tax liability, or

   b. any portion of the deposit that the reporting entity does not reasonably expect to be recovered in a subsequent accounting period for section 6603 tax deposit amounts in excess of specifically established tax liability.

9. The term "specifically established tax liability" is a liability, that for financial reporting purposes, the reporting entity has recognized relating to the IRS Section 6603 tax deposit. The reporting entity intends this "specifically established tax liability" to be settled by applying the section 6603 tax deposit. In calculating nonadmission discussed in the paragraph 8, the reporting entity shall deduct the specifically accrued tax liability prior to the determination of whether the remaining amounts should be nonadmitted.

10. To illustrate the nonadmission criteria, consider the following two situations:

   a. IAOA insurer has a 6603 tax deposit of $100,000 and a federal income tax liability of $30,000 that IAOA intends to pay in the normal course of business. IAOA would not consider the tax liability when determining nonadmission of the section 6603 tax deposit. IAOA is not aware of any situations which would indicate that use of the deposit is in question and would admit the entire $100,000 tax deposit.

   b. TAI insurer has a $110,000 section 6603 tax deposit and has been notified by its tax department that an adverse tax finding of $45,000 was probable and may result in significant interest penalties. TAI recorded a "specifically established tax liability" of $45,000 and intends to use the section 6603 tax deposit to settle the $45,000 adverse tax finding. In determining the amount of the 6603 tax deposit to nonadmit, TAI would determine the amount in excess of the "specifically established tax liability, which is $65,000 ($110,000 – $45,000). This net amount of $65,000 is then evaluated for nonadmission, based on other relevant factors, if any. To continue the illustration, TAI became aware of an additional situation at the reporting date, which indicated that $10,000 of the section 6603 tax deposit is not reasonably expected to be recovered in a subsequent accounting period . As a result, TAI would nonadmit $10,000 of the tax deposit.

INT 06-12 Status

11. No further discussion is planned. The Working Group noted that *FIN 48: Accounting for Uncertainty in Income Tax, an interpretation of FASB Statement No. 109* (FIN 48) is pending review by the Statutory Accounting Principles (E) Working Group has the potential to impact the consensus in this interpretation. The Working Group will consider if the interpretation requires updating after the review of FIN 48 is complete.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-13: EITF 01-2: Interpretations of APB Opinion No. 29

INT 06-13 Dates Discussed

September 10, 2006; December 10, 2006

INT 06-13 References

Current:
SSAP No. 40R—Real Estate Investments
SSAP No. 95—Nonmonetary Transactions

Superseded:
SSAP No. 77—Real Estate Sales – An Amendment to SSAP No. 40, Real Estate Investments

INT 06-13 Issue

1. The introduction to issues as described in *EITF 01-2: Interpretations of APB Opinion No. 29* is as follows:

> 1. The basic principle in Opinion 29 is that the accounting for nonmonetary transactions should be based on the fair values of the assets (or services) exchanged. The cost of a nonmonetary asset acquired in exchange for another nonmonetary asset is the fair value of the asset surrendered to obtain it, and a gain or loss for the difference between the carrying amount of the surrendered asset and its fair value should be recognized on the exchange. The fair value of the asset received should be used to measure the fair value of the asset surrendered (and the cost of the asset received) if it is more clearly evident than the fair value of the asset surrendered. Opinion 29 includes several modifications to that principle in circumstances in which (a) fair values of the assets exchanged are not readily determinable (paragraph 20.a. of Opinion 29), (b) the assets exchanged are products or properties held for sale in the same line of business to facilitate sales to customers other than the parties to the exchange (paragraph 20.b. of Opinion 29), (c) the assets exchanged are similar productive assets not held for sale in the ordinary course of business, [Note: See paragraph 44 of the STATUS section.] (d) the exchange involves an amount of monetary consideration (paragraph 22 of Opinion 29), and (e) the transaction represents a nonreciprocal transfer to owners (paragraph 23 of Opinion 29). Over the years, the Task Force has addressed several issues relating to the guidance in Opinion 29. The purpose of this Issue is to codify and reconcile the following Issues:
>
> *Issue No. 86-29, "Nonmonetary Transactions: Magnitude of Boot and the Exceptions to the Use of Fair Value"* (paragraphs 4-6, and 18-19)
>
> *Issue No. 87-17, "Spinoffs or Other Distributions of Loans Receivable to Shareholders"* (paragraphs 28-29)
>
> *Issue No. 87-29, "Exchange of Real Estate Involving Boot"* (paragraphs 25-27)
>
> *Issue No. 89-7, "Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity"* (paragraphs 21-24)
>
> *Issue No. 96-2, "Impairment Recognition When a Nonmonetary Asset Is Exchanged or Is Distributed to Owners and Is Accounted for at the Asset's Recorded Amount*" (paragraphs 33-39)
>
> *Issue No. 96-4, "Accounting for Reorganizations Involving a Non–Pro Rata Split-off of Certain Nonmonetary Assets to Owners"* (paragraphs 30-32)

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Issue No. 98-7, "Accounting for Exchanges of Similar Equity Method Investments" (paragraph 11)

Issue No. 00-5, "Determining Whether a Nonmonetary Transaction Is an Exchange of Similar Productive Assets" (paragraphs 2-3, 9-10, and 12-17).

The Task Force observed that the transition guidance for the above Issues is governed by the original consensuses on those Issues.

2. As described in paragraph 44 in the STATUS section of *EITF 01-2, FAS 153: Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29* (FAS 153), was issued in December 2004 and eliminated the fair value measurement exception for nonmonetary exchanges of similar productive assets provided in APB 29 and replaces it with an exception from fair value measurement for nonmonetary exchanges that lack commercial substance. As a result, FAS 153 nullifies Issues 1(b), 1(c), 2-5, and 7 since those issues interpret the exception to fair value measurement for similar productive assets that was eliminated by FAS 153. FAS 153 was adopted with modification in *SSAP No. 95—Nonmonetary Transactions*. *FAS 144: Accounting for the Impairment or Disposal of Long-Lived Assets*, also amended APB 29 and resolved issues 13(a) and 13(b) of EITF 01-2. FAS 144 was adopted with modification in *SSAP No. 90—Impairment or Disposal of Real Estate Investments*. This interpretation addresses the remaining issues of EITF 01-2.

3. The following EITF issues listed above were adopted, rejected or determined to be not applicable to statutory accounting principles in their entirety, as follows:

- *EITF Issue No. 86-29, "Nonmonetary Transactions: Magnitude of Boot and the Exceptions to the Use of Fair Value*" – adopted in *SSAP No. 95—Nonmonetary Transactions*
- *EITF Issue No. 87-17, "Spinoffs or Other Distributions of Loans Receivable to Shareholders"* – determined to be not applicable to statutory accounting principles
- *EITF Issue No. 87-29, "Exchange of Real Estate Involving Boot*" – adopted in *SSAP No. 40R—Real Estate Investments*
- *EITF Issue No. 89-7, "Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity"* – rejected in *SSAP No. 68—Business Combinations and Goodwill*
- *EITF Issue No. 96-4, "Accounting for Reorganizations Involving a Non-Pro Rata Split-off of Certain Nonmonetary Assets to Owners"* – rejected in *SSAP No. 95—Nonmonetary Transactions*

4. As EITF 01-2 was adopted to codify or reconcile the issues included in paragraph 1 of this interpretation, each issue will be described and discussed in paragraphs 5-18 of this interpretation.

INT 06-13 Discussion

5. Issue 6 and guidance per EITF 01-2:

Issue 6—If a nonmonetary exchange is required to be accounted for at fair value, whether full or partial gain recognition is appropriate in a circumstance in which one entity (Entity A) transfers its ownership of either a controlled productive asset or assets or a controlled business to another entity (Entity B) in exchange for a noncontrolling ownership interest in that entity (Entity B).

16. The Task Force reached a consensus on Issue 6 that if the fair value of the asset(s) given up (or of the ownership interest received if the fair value of that asset is more readily determinable) is less than its carrying value, that difference should be recognized as a loss. [Note: See STATUS

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section.] If the fair value of the asset(s) given up (or of the ownership interest received if that asset's fair value is more readily determinable) is greater than its carrying value, then (a) a gain in the amount of that difference should be recognized if the entity accounts for the ownership interest received using the cost method, or (b) a partial gain should be recognized if the entity accounts for the ownership interest received using the equity method. The partial gain should be calculated as the amount described in (a), above, less the portion of that gain represented by the economic interest (which may be different from the voting interest) retained. For example, if Entity A exchanges an asset with a carrying value of $1,000 and a fair value of $2,000 for a 30 percent economic interest in Entity B, Entity A should recognize a gain of $700 [($2,000 - $1,000) × 70%]. Thus, the amount recorded for the ownership interest received is partially based on its fair value at the exchange date and partially based on the carryover amount of the asset(s) surrendered.

17. The Task Force observed that paragraph 20 of Opinion 29 requires that the accounting for a nonmonetary transaction subject to Opinion 29 should not be based on the fair values of the assets transferred unless those fair values are determinable within reasonable limits.

6. The STATUS section of EITF 01-2 states the following relative to Issue 6:

45. Issue 6 addresses whether full or partial gain recognition is appropriate in circumstances in which an entity transfers its ownership of either a controlled productive asset (or assets) or a controlled business to another entity in exchange for a noncontrolling ownership interest in that entity. Statement 153 amends the scope of Opinion 29 to exclude a transfer of assets to an entity in exchange for an equity interest in that entity. Statement 153 also amends Statement 140 to remove the scope exception in Statement 140 for exchanges of equity method investments for similar productive assets. Accordingly, transfers of equity method investments in exchange for other assets should be accounted for in accordance with Statement 140. However, Opinion 29 (as amended by Statement 153) and Statement 140 do not provide guidance on the accounting for transfers of nonfinancial assets in exchange for other assets. Therefore, the guidance in Issue 6 should continue to be applied in circumstances in which an entity transfers a nonfinancial asset (or assets) to another entity in exchange for a noncontrolling ownership interest in that entity and the exchange is required to be accounted for at fair value.

7. The Working Group reached a consensus to adopt the EITF 01-2 for Issue 6 guidance believing the economic interest relates to the ownership interest of Entity B in the above issue. This may or may not be different from the voting interest or controlling interest of Entity B. However, the GAAP guidance above for Issue 6 determines the proper accounting for the transactions between unrelated parties relative to the gain or loss on the nonmonetary transaction. This guidance establishes the cost basis for the ownership interest in Entity B to be recorded by Entity A. Subsequent to the transactions, existing guidance should apply for the ownership interest. For statutory purposes, the valuation of this ownership interest would then follow existing statutory guidance (e.g., *SSAP No. 30R—Unaffiliated Common Stock* for Common Stock, *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* for Joint Ventures, *SSAP No. 97—Investments in Subsidiary, Controlled, and Affiliated Entities* for investments in SCA entities, etc.)

8. Issue 8 and guidance per EITF 01-2:

Exchanges Involving Monetary Consideration (Paragraph 22 of Opinion 29)

Issue 8(a)—What level of monetary consideration in a nonmonetary exchange causes the transaction to be considered monetary in its entirety and, therefore, outside the scope of Opinion 29.

19. The Task Force discussed an exchange of nonmonetary assets that would otherwise be based on recorded amounts but that also involves monetary consideration (boot). The Task Force reached a consensus that that transaction should be considered monetary (rather than nonmonetary) if the boot is significant, and agreed that "significant" should be defined as at least 25 percent of the fair value of the exchange. As a monetary transaction, both parties would record

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the exchange at fair value[1] (as discussed in Issue 8(b), below). If the boot in a transaction is less than 25 percent, the pro rata gain recognition guidance in paragraph 22 of Opinion 29 should be applied by the receiver of boot, and the payer of boot would not recognize a gain. The Task Force acknowledged that the ability to satisfactorily measure fair value is a prerequisite to the use of fair value.

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[1] For real estate transactions, see Issue 10.

Issue 8(b)—In a monetary exchange (required to be accounted for at fair value), whether "full or partial" gain recognition is appropriate if an entity transfers its ownership of a controlled asset, group of assets, or business to another entity in exchange for a noncontrolling ownership interest in the other entity.

20. The Task Force reached a consensus on Issue 8(b) that the gain should be computed in a manner consistent with the consensus reached in Issue 6. The Task Force reached a consensus that application of the consensus on Issue 8(b) is required for exchange transactions committed to after April 19, 2001. A transaction is committed to if the parties to the transaction have signed a binding, written agreement that specifically sets forth the principal provisions of the transaction. If any of the principal provisions are yet to be negotiated, or are subsequently changed, such a preliminary agreement does not qualify as a commitment for purposes of this consensus.

9. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issues 8(a) and 8(b) without modification.

10. Issue 9 and guidance per EITF 01-2:

Issue 9—In the monetary exchange described below, whether the amount of gain recognized should exceed the amount that would be computed pursuant to the guidance for Issue 8(b).

21. An enterprise transfers its ownership of an individual asset (or assets) or its ownership interest in a subsidiary to a newly created entity in exchange for an ownership interest in that entity that will be accounted for by the equity method and monetary consideration. The monetary consideration received exceeds the fair value of the portion of the surrendered asset that has been sold in the exchange. The excess monetary consideration is funded by proceeds from nonrecourse financing within the newly created entity. Subsequent to the transfer, the enterprise does not control the entity. The specifics of the transaction are as follows:

- Company A owns equipment with a book basis of $100 and an appraised value of $400.
- Company B, previously unrelated to Company A, creates a new subsidiary, Company X, and transfers cash of $60 to Company X.
- Company A transfers the equipment to Company X in exchange for shares of Company X stock that represent a 40 percent ownership interest in Company X. Simultaneously, Company X borrows $300 with recourse to only the equipment and pays Company A $360 cash.

22. The Task Force reached a consensus that if the enterprise has no actual or implied commitment, financial or otherwise, to support the operations of the new entity in any manner, a gain of $260 should be recognized. The investor's basis in the new entity should be no less than zero. The gain calculation is illustrated as follows:

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Fair value of interest in equipment sold ($400 × 60%)	$ 240
Less: Cost of interest in equipment sold ($100 × 60%)	(60)
	$ 180
Plus: Additional gain to the extent of the negative investment	80*
Total gain recognized	$ 260

* The additional gain is calculated as follows:

Cost of equipment	$100
Less: Cost of interest in equipment sold	(60)
Remaining cost	40
Less: Cash received in excess of 60% of the equipment's fair value	(120)
Negative investment	$ (80)

23. Task Force members noted that specific facts and circumstances may affect gain recognition and that it would be impractical for the Task Force to consider all possible variations of the basic transaction described above.

24. The SEC Observer emphasized that any gain recognition is heavily dependent on a careful analysis of specific facts and circumstances. Gain recognition would not be appropriate if a significant uncertainty exists regarding realization or the enterprise has an actual or implied commitment to support the operations of the new entity in any manner (see, for example, SAB 81).

11. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issue 9 without modification. The Working Group also noted the following facts are important to this consensus:

- The monetary consideration in the example is considered significant under the consensus of Issue 8(b), and as such, Issue 9 is considered a **monetary exchange**.
- The monetary consideration received by Entity A in the transaction **exceeds the fair value of the portion of the surrendered asset**.
- The excess monetary consideration is funded by proceeds from nonrecourse financing within Company X. The $300 borrowing with recourse described in the example explicitly states **the recourse is only to the equipment and is not related to Entity A**.
- Prior to the transaction, Entity A and Entity B are unrelated parties. In exchange for the equipment, **Entity A receives shares of Company X stock representing a 40 percent ownership interest**.

In the example above, the monetary consideration received exceeds the fair value of the portion of the surrendered asset that has been sold in the exchange. When this occurs, additional gain should be recognized to ensure the basis in the ownership interest is not less than zero.

12. Issue 10 and guidance per EITF 01-2:

Exchanges of Real Estate Involving Monetary Consideration (Paragraph 22 of Opinion 29)

25. Statement 66 indicates that the accounting for exchanges of real estate is covered by Opinion 29 and not by Statement 66. However, as discussed above in Issue 8(a), the Task Force reached a consensus that an exchange of nonmonetary assets that would otherwise be based on recorded amounts under paragraph 21 of Opinion 29 but that involves boot should be considered a monetary (rather than nonmonetary) transaction if the boot is at least 25 percent of the fair value of the exchange. As a result, the Task Force reached a different consensus for exchanges

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of either (a) real estate held for sale in the ordinary course of business for real estate to be sold in the same line of business or (b) real estate not held for sale in the ordinary course of business for similar real estate when the boot is at least 25 percent of the fair value of the exchange. (Those types of exchanges are referred to in Issues 10(a) and 10(b) as exchanges of similar real estate.)

Issue 10(a)—Whether Statement 66 applies to an exchange of similar real estate that is not subject to Opinion 29 because the transaction involves enough boot for the exchange to be considered monetary under the consensus for Issue 8(a).

26. The Task Force reached a consensus that a transaction involving an exchange of similar real estate that is considered a monetary transaction under Issue 8(a) because boot is at least 25 percent of the fair value of the exchange would be allocated between two components: a monetary portion and a nonmonetary portion. [Note: See STATUS section.] The allocation between the monetary and nonmonetary portions of the transaction should be based on their relative fair values at the time of the transaction. A Task Force member noted that Interpretation 43 provides guidance on when an asset is considered real estate.

Issue 10(b)—If applicable, how Statement 66 should be applied.

27. The Task Force reached a consensus that for the receiver of boot, the monetary portion would be accounted for under Statement 66 as the equivalent of a sale of an interest in the underlying real estate, and the nonmonetary portion would be accounted for based on the recorded amount (after reduction, if appropriate, for an indicated impairment in value) of the nonmonetary asset relinquished pursuant to paragraph 21 of Opinion 29. [Note: See STATUS section.] For the payer of boot, the monetary portion would be accounted for as an acquisition of real estate, and the nonmonetary portion would be accounted for pursuant to paragraph 21 of Opinion 29. Following is an example of the application of this consensus:

Assumptions

- Party A transfers real estate with a fair value of $2,000,000 (Party A's net book value of $1,500,000) to Party B and receives $400,000 cash, a $400,000 note from Party B payable to Party A, and real estate with a fair value of $1,200,000 (Party B's net book value of $800,000).

- The initial investment requirement for full accrual profit recognition under Statement 66 is 20 percent.

- The terms of the note from Party B to Party A would satisfy the continuing investment provisions necessary for application of the full accrual method. The interest rate on the note from Party B is a market rate, and the note is considered fully collectible.

- The values of the real estate transferred by both parties are readily determinable and clearly realizable at the exchange date.

- Neither party has any continuing involvement with the real estate transferred to the other.

Computation of Allocation by Both Party A and Party B

Monetary Portion of Transaction:

Total monetary consideration divided by total fair value of exchange	$800,000 ÷ $2,000,000 = 40%

For this example, the monetary portion of the transaction is the exchange of $400,000 cash and a $400,000 note for real estate with a fair value of $800,000 ($2,000,000 x 40%).

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Nonmonetary Portion of Transaction:

Fair value of real estate exchanged divided by total fair value of exchange	$1,200,000 ÷ $2,000,000 = 60%

For this example, the nonmonetary portion of the transaction is the exchange of real estate with a fair value of $1,200,000 for similar real estate with a fair value of $1,200,000 ($2,000,000 x 60%).

Accounting by Party A (the Receiver of Monetary Consideration)

The monetary portion of the transaction qualifies for full accrual profit recognition because the cash down payment of $400,000 and the $400,000 note meet the criteria in paragraphs 9-12 of Statement 66 for a buyer's initial and continuing investment when applied to the monetary portion of the transaction. Accordingly, a gain of $200,000 ($800,000 total monetary consideration less $600,000 [$1,500,000 total net book value x 40%] pro rata portion of net book value) would be recorded at the date of sale.

The nonmonetary portion of the transaction does not qualify for gain recognition because the exchange involves similar real estate. The accounting basis of the new property equals $900,000 ($1,500,000 total net book value of the real estate exchanged less the $600,000 pro rata portion of net book value sold).

Accounting by Party B (the Payer of Monetary Consideration)

The monetary portion of the transaction represents an acquisition of real estate for the monetary consideration paid of $800,000.

The nonmonetary portion of the transaction does not qualify for gain recognition because the exchange involves similar real estate. The accounting basis of the new property equals $1,600,000 ($800,000 net book value of the real estate exchanged plus $800,000 total monetary consideration paid).

13. The STATUS section of EITF 01-2 states the following relative to Issues 10(a) and 10(b):

> 46. Issues 10(a) and 10(b) previously addressed circumstances in which an entity is involved in a real estate exchange that meet the following conditions: (1) the exchange includes boot that is at least 25 percent of the fair value of the exchange and (2) the exchange is either (a) real estate held for sale in the ordinary course of business for real estate to be sold in the same line of business or (b) real estate not held for sale in the ordinary course of business for similar real estate. Statement 153, however, eliminates the fair value measurement exception for nonmonetary exchanges of similar productive assets provided in Opinion 29 and replaces it with an exception from fair value measurement for nonmonetary exchanges that lack commercial substance. Therefore, Issues 10(a) and 10(b) address circumstances in which an entity is involved in a real estate exchange that meets the following conditions: (1) the exchange includes boot that is at least 25 percent of the fair value of the exchange and (2) the exchange meets one of the conditions set forth in paragraph 20 of Opinion 29.

14. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issues 10(a) and 10(b) with the modification to replace references to FAS 66: *Accounting for Sales of Real Estate* with references to *SSAP No. 40R—Real Estate Investments*. In addition, reporting entities should note that as a result of the issuance of FAS 153, Issues 10(a) and 10(b) address circumstances in which an entity is involved in a real estate exchange that meets the following conditions: (1) the exchange includes boot that is at least 25 percent of the fair value of the exchange and (2) the exchange meets one of the conditions set forth in paragraph 20 of Opinion 29.

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15. Issue 11 and guidance per EITF 01-2:

Nonreciprocal Transfers to Owners (Paragraph 23 of Opinion 29)

Spinoffs or Other Distributions of Loans Receivable to Shareholders

28. An enterprise distributes loans receivable to its owners by forming a subsidiary, transferring those loans receivable to the subsidiary, and then distributing the stock of that subsidiary to shareholders of the parent.

Issue 11—Whether the enterprise should report the distribution at book value as a spinoff or at fair value as a dividend-in-kind if the book value of the loans receivable, which may be either the "recorded investment in the receivable" or the "carrying amount of the receivable," is in excess of their fair value, and how the recipient should record the transaction.

29. The Task Force reached a consensus that the distribution should be reported at fair value by the enterprise and the recipient. Task Force members noted that the transaction is not a spinoff because the subsidiary does not constitute a business.[4] Rather, the transaction should be considered a dividend-in-kind. Under paragraph 23 of Opinion 29, dividends-in-kind are nonreciprocal transfers of nonmonetary assets to owners that should be accounted for at fair value if the fair value of the nonmonetary asset distributed is objectively measurable and would be clearly realizable to the distributing entity in an outright sale at or near the time of distribution. On July 5, 1989, subsequent to the date of the consensus, the SEC staff issued SAB 82, which discusses accounting for transfers of nonperforming assets by financial institutions and disclosure of the impact of financial assistance from regulators. In discussing the value at which a transfer of nonperforming assets should be recorded by the transferor financial institution, SAB 82 makes reference to the Task Force consensus on Issue 10, that an enterprise that distributes loans to its owners should report such distribution at fair value.

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[4] Issue 98-3 provides guidance on determining whether an asset group constitutes a business.

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16. The Working Group reached a consensus to adopt the EITF 01-2 guidance with the modification to replace the reference to paragraph 23 of APB Opinion 29 with paragraph 12 of SSAP No. 95, the reference in footnote 4 to EITF Issue 98-3 shall be replaced with INT 00-26: *EITF 98-3: Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business*.

17. Issue 12 and guidance per EITF 01-2:

Accounting for Reorganizations Involving a Non–Pro Rata Split-off of Certain Nonmonetary Assets to Owners

30. Some believe that paragraph 23 of Opinion 29 requires that nonreciprocal transfers of nonmonetary assets to owners on a non-pro rata basis be accounted for at fair value, without regard to the nature of the nonmonetary assets distributed. Others believe that Opinion 29 requires historical cost accounting for corporate liquidations or reorganizations involving the distribution to owners of all or a significant segment of the business, whether in a spinoff, split-off, or split-up and whether or not the distribution is on a pro rata basis.

31. Although Opinion 29 does not define the term split-off, federal income tax law states that a split-off is a transaction in which a parent company exchanges its stock in a subsidiary for parent company stock held by its shareholders. For federal income tax purposes, the exchange of shares need not be pro rata to all shareholders, or even include all shareholders, in order to be considered a tax-free split-off.

Issue 12—Whether a non-pro rata split-off of all or a significant segment of a business in a corporate plan of reorganization should be accounted for at historical cost or at fair value.

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32. The Task Force reached a consensus that a non-pro rata split-off of a segment of a business in a corporate plan of reorganization should be accounted for at fair value. The Task Force also reached a consensus that a split-off of a targeted business, distributed on a pro rata basis to the holders of the related targeted stock, should be accounted for at historical cost. The Task Force observed that if the targeted stock was created in contemplation of the subsequent split-off, the two steps (creation of the targeted stock and the split-off) cannot be separated and should be viewed as one transaction with the split-off being accounted for at fair value.

18. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issue 12 with the modification to replace references to paragraph 23 of APB Opinion 29 with paragraph 12 of SSAP No. 95.

INT 06-13 Status

19. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 07-01: Application of the Scientific (Constant Yield) Method in Situations of Reverse Amortization

INT 07-01 Dates Discussed

March 10, 2007; June 2, 2007

INT 07-01 References

Current:
SSAP No. 26R—Bonds
SSAP No. 43R—Loan-Backed and Structured Securities

Superseded:
SSAP No. 98—Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43—Loan-Backed and Structured Securities

INT 07-01 Issue

1. SSAP No. 26R and SSAP No. 43R both reference the use of the scientific or constant yield method of amortization of a premium or a discount. *SSAP No. 26R—Bonds* provides the following (bolding added for emphasis):

> **Amortized Cost**
>
> 9. **Amortization of bond premium or discount shall be calculated using the scientific (constant yield) interest method taking into consideration specified interest and principal provisions over the life of the bond.** Bonds containing call provisions (where the issue can be called away from the reporting entity at the issuer's discretion) shall be amortized to the call or maturity value/date which produces the lowest asset value (yield to worst).

SSAP No. 43R—Loan-Backed and Structured Securities provides the following (bolding added for emphasis):

> **Amortization**
>
> 8. **Amortization of premium or discount shall be calculated using the scientific (constant yield) interest method** and shall be recorded as an adjustment to investment income. The interest method results in a constant effective yield equal to the prevailing rate at the time of purchase or at the time of subsequent adjustments to book value. The amortization period shall reflect estimates of the period over which repayment of principal of the loan-backed securities is expected to occur, not the stated maturity period.
>
> **Collection of All Contractual Cashflows is Probable**
>
> 12. The following guidance applies to loan-backed and structured securities for which it is probable that the investor will be able to collect all contractually required payments receivable. (Paragraphs 17-19 provide guidance for securities in which collection of all contractual cash flows is not probable and paragraphs 20-24 provide guidance for beneficial interests.) Prepayments are a significant variable element in the cash flow of loan-backed securities because they affect the yield and determine the expected maturity against which the yield is evaluated. Falling interest rates generate faster prepayment of the mortgages underlying the security, shortening its duration. This causes the reporting entity to reinvest assets sooner than expected at potentially

less advantageous rates. This is called prepayment risk. Extension risk is created by rising interest rates which slow repayment and can significantly lengthen the duration of the security. Differences in cash flows can also result from other changes in the cash flows from the underlying assets. If assets are delinquent or otherwise not generating cash flow, which should be reflected in the cash flow analysis through diminishing security cash flows, even if assets have not been liquidated and gain/losses have not been booked.

13. Changes in currently estimated cash flows, including the effect of prepayment assumptions, on loan-backed securities shall be reviewed periodically, at least quarterly. The prepayment rates of the underlying loans shall be used to determine prepayment assumptions. Prepayment assumptions shall be applied consistently across portfolios to all securities backed by similar collateral (similar with respect to coupon, issuer, and age of collateral). Reporting entities shall use consistent assumptions across portfolios for similar collateral within controlled affiliated groups. Since each reporting entity may have a unique method for determining the prepayment assumptions, it is impractical to set standard assumptions for the industry. Relevant sources and rationale used to determine each prepayment assumption shall be documented by the reporting entity.

14. Loan-backed securities shall be revalued using the currently estimated cash flows, including new prepayment assumptions, using either the prospective or retrospective adjustment methodologies, consistently applied by type of securities. However, if at any time during the holding period, the reporting entity determines it is no longer probable that they will collect all contractual cashflows, the reporting entity shall apply the accounting requirements in paragraphs 17-19.

15. The prospective approach recognizes, through the recalculation of the **effective yield** to be applied to future periods, the effects of all cash flows whose amounts differ from those estimated earlier and the effects and changes in projected cash flows. Under the prospective method, the recalculated effective yield will equate the carrying amount of the investment to the present value of the anticipated future cash flows. The recalculated yield is then used to accrue income on the investment balance for subsequent accounting periods. There are no accounting changes in the current period unless the security is determined to be other than temporarily impaired.

16. The retrospective methodology changes both the yield and the asset balance so that expected future cash flows produce a return on the investment equal to the return now expected over the life of the investment as measured from the date of acquisition. Under the retrospective method, the recalculated **effective yield** will equate the present value of the actual and anticipated cash flows with the original cost of the investment. The current balance is then increased or decreased to the amount that would have resulted had the revised yield been applied since inception, and investment income is correspondingly decreased or increased.

2. The following identifies three situations where, using a constant yield methodology for determining amortization or accretion, changes in amortized value move in the opposite direction of what is expected. That is, if a security is purchased at a premium, the constant yield methodology will, in certain cases, cause the amortized value to move to a discount during the life of the security. Conversely, if the security were purchased at a discount, the constant yield methodology will, in certain cases, cause the amortized value to move to a premium during the life of the security.

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Accounting Issues:

3. The fundamental accounting questions are

Issue 1: When applying the constant yield method to loan-backed or structured securities, can amortized value be interpreted to represent the discounted cash flows?

Issue 2: Should a security purchased at a premium be allowed to move to a discount, or should a discount be allowed to move to a premium, if this occurs as a result of applying the scientific (constant yield) interest method."

Issue 3: On the subject of Parity (described in example 3), is it appropriate under statutory accounting guideline to "assume away" day delay and subsequently eliminate amortizing to a value less than par? If so, should a payment date assumption or a record date assumption be used?

4. Following are practical situations where a security purchased at a premium will have increases in amortized value, and where a security purchased at a discount will have decreases in amortized value. The question is should the scientific (constant yield) method be interpreted to allow these securities to be amortized as illustrated below.

Example 1

5. This first example examines a stepped coupon bond purchased at a discount. At time of acquisition the future interest rate adjustments are known, and so are taken into account in the yield calculation. This example illustrates how a (theoretical) stepped coupon bond, without a call schedule, could result in the amortized value changing from a discount to a premium.

Description: FEDERAL HOME LN MTG CORP MTN
Maturity: 03-18-2019
Int Type: Stepped Coupon not callable
03/18/2004 4.000%
03/18/2007 6.000%
03/18/2013 8.000%
Purchase Date: 3/18/2004
Purchase Price: 97.125
Based on this information, the effective annual yield at acquisition is: 6.3246%

6. The following illustrates the semiannual amortization schedule determined at time of acquisition. The amortized values represent the sum of the discounted future cash flows at each payment date. Based on the purchase price and cash flow assumptions, the semiannual yield is 3.1623%.

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Pay Date	Par Value	Interest Rate Annual	Interest Payment	Total Payment	Income	Accr Disc	Amort Value
3/18/2004	1,000,000.00			(971,250.00)			971,250.00
9/18/2004	1,000,000.00	4.0000%	20,000.00	20,000.00	30,713.97	10,713.97	981,963.97
3/18/2005	**1,000,000.00**	**4.0000%**	**20,000.00**	**20,000.00**	**31,052.78**	**11,052.78**	**993,016.75**
9/18/2005	**1,000,000.00**	**4.0000%**	**20,000.00**	**20,000.00**	**31,402.30**	**11,402.30**	**1,004,419.05**
3/18/2006	1,000,000.00	4.0000%	20,000.00	20,000.00	31,762.88	11,762.88	1,016,181.92
9/18/2006	1,000,000.00	4.0000%	20,000.00	20,000.00	32,134.86	12,134.86	1,028,316.78
3/18/2007	1,000,000.00	4.0000%	20,000.00	20,000.00	32,518.60	12,518.60	1,040,835.38
9/18/2007	1,000,000.00	6.0000%	30,000.00	30,000.00	32,914.48	2,914.48	1,043,749.86
3/18/2008	1,000,000.00	6.0000%	30,000.00	30,000.00	33,006.64	3,006.64	1,046,756.50
9/18/2008	1,000,000.00	6.0000%	30,000.00	30,000.00	33,101.72	3,101.72	1,049,858.22
3/18/2009	1,000,000.00	6.0000%	30,000.00	30,000.00	33,199.81	3,199.81	1,053,058.02
9/18/2009	1,000,000.00	6.0000%	30,000.00	30,000.00	33,300.99	3,300.99	1,056,359.02
3/18/2010	1,000,000.00	6.0000%	30,000.00	30,000.00	33,405.38	3,405.38	1,059,764.40
9/18/2010	1,000,000.00	6.0000%	30,000.00	30,000.00	33,513.07	3,513.07	1,063,277.47
3/18/2011	1,000,000.00	6.0000%	30,000.00	30,000.00	33,624.17	3,624.17	1,066,901.64
9/18/2011	1,000,000.00	6.0000%	30,000.00	30,000.00	33,738.77	3,738.77	1,070,640.41
3/18/2012	1,000,000.00	6.0000%	30,000.00	30,000.00	33,857.00	3,857.00	1,074,497.41
9/18/2012	1,000,000.00	6.0000%	30,000.00	30,000.00	33,978.98	3,978.98	1,078,476.39
3/18/2013	1,000,000.00	6.0000%	30,000.00	30,000.00	34,104.80	4,104.80	1,082,581.19
9/18/2013	1,000,000.00	8.0000%	40,000.00	40,000.00	34,234.61	(5,765.39)	1,076,815.80
3/18/2014	1,000,000.00	8.0000%	40,000.00	40,000.00	34,052.29	(5,947.71)	1,070,868.09
9/18/2014	1,000,000.00	8.0000%	40,000.00	40,000.00	33,864.20	(6,135.80)	1,064,732.30
3/18/2015	1,000,000.00	8.0000%	40,000.00	40,000.00	33,670.17	(6,329.83)	1,058,402.47
9/18/2015	1,000,000.00	8.0000%	40,000.00	40,000.00	33,470.00	(6,530.00)	1,051,872.47
3/18/2016	1,000,000.00	8.0000%	40,000.00	40,000.00	33,263.50	(6,736.50)	1,045,135.97
9/18/2016	1,000,000.00	8.0000%	40,000.00	40,000.00	33,050.47	(6,949.53)	1,038,186.45
3/18/2017	1,000,000.00	8.0000%	40,000.00	40,000.00	32,830.71	(7,169.29)	1,031,017.16
9/18/2017	1,000,000.00	8.0000%	40,000.00	40,000.00	32,603.99	(7,396.01)	1,023,621.15
3/18/2018	1,000,000.00	8.0000%	40,000.00	40,000.00	32,370.11	(7,629.89)	1,015,991.26
9/18/2018	1,000,000.00	8.0000%	40,000.00	40,000.00	32,128.83	(7,871.17)	1,008,120.08
3/18/2019	1,000,000.00	8.0000%	40,000.00	1,040,000.00	31,879.92	(8,120.08)	1,000,000.00
Subtotal						28,750.00	

7. As can be seen from this schedule, the amortized value quickly changes from a discount situation to a premium situation. The question is should the accretion of the discount end when the discount is fully amortized, i.e. when Amortized Value = Par Value. In the above, this would occur somewhere between 3/18/05 and 9/18/05. Or, is it proper to report the amortized value as the sum of the discounted cash flows at a given point in time using the effective yield at acquisition? (Note: A prospective method is not applicable for this situation since the cash flows are known at time of acquisition, and those assumptions will not change over time.)

Example 2

8. The second situation explores a variable rate security using the Retrospective Method of Amortization. This example exemplifies the issue identified as "**Drift**." As variable interest rates are not known in advance, adjustments to yields must be made whenever a new interest rate becomes effective. Using the retrospective method, the effective yield is calculated based upon the purchase price, and the actual received and the projected future cash flows. For simplicity's sake, a bond with a single principal payment at maturity is used, but similar results would occur if the security were any type of variable rate instrument.

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9. The situation presented below shows the cash flow assumptions at purchase when there is only one known interest rate. Immediately following, are the effects of using a retrospective adjustment, once the second interest rate is known and applied.

Original Purchase Assumptions:	
Par value:	1,000,000.00
Price:	98.000
Cost:	980,000.00
Acq Date:	01/022006
Maturity Date:	12/15/2009
Interest rate:	2.000%
Pays:	Quarterly
Effective Annual Yield:	2.53326%
Qrtrly Yield:	.63332%

Pay Date	Par Value	Int Rate	Int Recvd	Prin Recd	Total Cash	Income	Accretion Discount	Amortized Value
1/2/2006	1,000,000	2.00%	(944.44)		(980,944.44)			980,000.00
3/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	5,034.16	978.60	980,978.60
6/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,212.69	1,212.69	982,191.29
9/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,220.37	1,220.37	983,411.67
12/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,228.10	1,228.10	984,639.77
3/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,235.88	1,235.88	985,875.65
6/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,243.71	1,243.71	987,119.36
9/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,251.58	1,251.58	988,370.94
12/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,259.51	1,259.51	989,630.45
3/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,267.49	1,267.49	990,897.94
6/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,275.51	1,275.51	992,173.45
9/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,283.59	1,283.59	993,457.04
12/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,291.72	1,291.72	994,748.76
3/15/2009	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,299.90	1,299.90	996,048.66
6/15/2009	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,308.13	1,308.13	997,356.80
9/15/2009	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,316.42	1,316.42	998,673.22
12/15/2009	1,000,000	2.00%	5,000.00	1,000,000.00	1,000,000.00	6,324.76	1,326.78	-

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10. Based on the purchase assumptions, the amortization schedule for this security is normal. The accretion of discount is a smooth curve, and the amortized value approaches par value at maturity. As previously indicated, the following shows the interest rate adjusted for the accrual period ending 3/15/08. The original purchase assumptions are as stated above. The interest payments from 3/15/06 through 12/15/07 are paid based on the 2.000% annual interest rate effective from issue date (12/15/05) through 12/14/07. For accrual period beginning 12/15/07, however, the interest rate adjusts to 3.500%. Using a retrospective methodology, the following amortization schedule results:

Pay Date	Par Value	Int Rate	Int Recvd	Prin Recd	Total Cash	Income	Accretion Discount	Amortized Value
1/2/2006	1,000,000	2.00%	(944.44)		(980,944.44)			980,000.00
3/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,510.55	2,455.00	982,455.00
6/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,046.82	3,046.82	985,501.81
9/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,071.77	3,071.77	988,573.58
12/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,096.93	3,096.93	991,670.51
3/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,122.30	3,122.30	994,792.81
6/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,147.87	3,147.87	997,940.67
9/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,173.65	3,173.65	1,001,114.33
12/15/2007	1,000,000	**2.00%**	**5,000.00**	**0.00**	**5,000.00**	**8,199.64**	**3,199.64**	**1,004,313.97**
3/15/2008	1,000,000	**3.50%**	**8,750.00**	**0.00**	**8,750.00**	**8,225.85**	**(524.15)**	**1,003,789.82**
6/15/2008	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,221.56	(528.44)	1,003,261.38
9/15/2008	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,217.23	(532.77)	1,002,728.61
12/15/2008	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,212.87	(537.13)	1,002,191.48
3/15/2009	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,208.47	(541.53)	1,001,649.94
6/15/2009	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,204.03	(545.97)	1,001,103.98
9/15/2009	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,199.56	(550.44)	1,000,553.54
12/15/2009	1,000,000	3.50%	8,750.00	1,000,000.00	1,008,750.00	8,195.05	(553.54)	-

11. From this, it is apparent that the amortized value quickly breaks out of the cost / par range and becomes a premium situation. The book value for the periods prior to 12/15/07 would have been reported at the original amortized values as determined in the prior spreadsheet. On the 12/31/07 annual statement there would be a retrospective catch-up adjustment.

12. Because of the variability of cash flows, recalculating a yield based on the retrospective method and applying that yield to calculate an amortized value can cause a security to bust out of the cost / par range, and the amortization (accretion) to move in the "wrong direction." For variable rate, interest only, and principal only asset backed securities, the additional complication caused by day delay would also come into play.

Example 3

13. The third example represents a mortgage backed security purchased at a slight premium. This situation illustrates what is described as **"Parity."** American Banker Online describes parity as "The parity price at which the yield of a mortgage-backed bond equals its net coupon rate. Securities with parity amortize to a value less than 100.

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14. Parity occurs because the accrual date, usually the last day of the month, is many days prior to the payment date, typically 15, or 25 days for a mortgage backed security, and up to 45, or 55 days (or longer) for a collateralized mortgage obligation. The following is a simplified example using a mortgage backed security. The assumption is that the security is purchased at a slight premium (price = 100.1000). Because of day delay, however, the parity price is not 100, but is approximately 99.90.

CUSIP: 123456-AB-1 (Made up)
Description: Sample Mortgage Backed Security
Final payment date: 01/15/2006
Int Rate: 5.50%
Day Delay: 44
CPR: 6%

Purchase Date:	2/15/2004
Purchase Price:	100.1000
Par Purchased:	1,000,000.00
Annual Yield (SIA)	5.16841%
Periodic (monthly) Yield	0.43070%
Interest Rate	5.500%

	Prin Red	Principal	Book	Total Incm	Int Incm	Amort	Amort Fctr
2/15/2004		1,000,000.00	1,001,000.00	-	(2,138.89)	-	1.00100
3/15/2004	46,066.11	953,933.89	954,767.44	4,311.32	4,477.77	(166.45)	1.00087
4/15/2004	45,822.29	908,111.60	908,790.15	4,112.19	4,267.19	(155.00)	1.00075
5/15/2004	45,579.72	862,531.88	863,066.88	3,914.17	4,057.72	(143.56)	1.00062
6/15/2004	45,338.40	817,193.48	817,596.34	3,717.24	3,849.37	(132.13)	1.00049
7/15/2004	45,098.32	772,095.16	772,377.29	3,521.39	3,642.12	(120.73)	1.00037
8/15/2004	44,859.48	727,235.68	727,408.48	3,326.64	3,435.97	(109.33)	1.00024
9/15/2004	44,621.87	682,613.81	682,688.66	3,132.95	3,230.91	(97.95)	1.00011
10/15/2004	44,385.48	638,228.33	638,216.60	2,940.35	3,026.93	(86.58)	0.99998
11/15/2004	44,150.31	594,078.02	593,991.06	2,748.80	2,824.04	(75.23)	0.99985
12/15/2004	43,916.35	550,161.67	550,010.81	2,558.32	2,622.22	(63.89)	0.99973
1/15/2005	43,683.59	506,478.08	506,274.66	2,368.90	2,421.47	(52.57)	0.99960
2/15/2005	43,452.03	463,026.05	462,781.38	2,180.53	2,221.78	(41.25)	0.99947
3/15/2005	43,221.66	419,804.39	419,529.77	1,993.20	2,023.15	(29.95)	0.99935
4/15/2005	42,992.48	376,811.91	376,518.63	1,806.92	1,825.58	(18.66)	0.99922
5/15/2005	**42,764.48**	**334,047.43**	**333,746.76**	**1,621.67**	**1,629.05**	**(7.38)**	**0.99910**
6/15/2005	**42,537.66**	**291,509.77**	**291,212.98**	**1,437.45**	**1,433.57**	**3.88**	**0.99898**
7/15/2005	42,312.00	249,197.77	248,916.12	1,254.26	1,239.12	15.14	0.99887
8/15/2005	42,087.50	207,110.27	206,855.00	1,072.08	1,045.71	26.38	0.99877
9/15/2005	41,864.16	165,246.11	165,028.45	890.93	853.32	37.61	0.99868
10/15/2005	41,641.97	123,604.14	123,435.31	710.78	661.95	48.83	0.99863
11/15/2005	41,420.92	82,183.22	82,074.43	531.64	471.60	60.04	0.99868
12/15/2005	41,201.01	40,982.21	40,944.66	353.50	282.25	71.24	0.99908
1/15/2006	40,982.21	-	-	176.35	93.92	37.55	*

* The last amortization calculation is an adjustment to bring book value to 0.

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15. By looking at the amortization factors, which represent amortized value / remaining principal, it is evident that the security quickly goes from a premium situation to a discount situation between 5/15/2005 and 6/15/2005. Due to Parity, the security does not amortize to a value of 100, but to a slight discount.

16. In addressing the issue of parity for REMICs, the tax code allows for accruing interest and calculating Original Issue Discount (OID) on a payment date to payment date basis, thereby eliminating the discrepancy between the accrual periods and the payment dates. Another method of eliminating parity would be to use the accrual end date (record date) plus one as the assumed payment date. Both methods sync up the accrual period and the payment date, essentially eliminating day delay.

17. Is it appropriate under statutory accounting guideline to "assume away" day delay and subsequently eliminate amortizing to a value less than par? If so, should a payment date assumption or a record date assumption be used?

INT 07-01 Discussion

18. The Working Group came to the following consensuses:

Issue 1: When applying the constant yield method to loan-backed or structured securities, can amortized value be interpreted to represent the discounted cash flows?

19. The Working Group noted that in the case of loan-backed or asset-backed securities; the unamortized balance of an issue at any point in time will represent the present value of all future cash flows discounted to the present using the constant yield.

Issue 2: Should a security purchased at a premium be allowed to move to a discount, or should a discount be allowed to move to a premium, if this occurs as a result of applying the scientific (constant yield) interest method."

20. It has been noted that certain anomalies will exist with certain types of bonds, loan-backed and structured securities when applying the constant yield method. These anomalies can cause a premium to move to a discount, or a discount to move to a premium.

21. Some think that the value should be frozen once this occurs. However, both SSAP No. 26R and SSAP No. 43R are clear that the scientific (constant yield) interest method is required to be used when accreting/amortizing the discount/premium on a bond, loan-backed or structured security.

22. The Working Group noted that recording a discount or a premium and accreting/amortizing to par is consistent with a held to maturity approach that results in no gain or loss at maturity. Although it could be argued that freezing a discount or premium, or stopping at par at a particular point in time, would achieve the same result, this approach appears to ignore the fundamentals of the issue that have led to the anomalies. The Working Group noted that ignoring the facts of the issue in order to prevent the original premium or original discount from reversing is inappropriate, and that the above examples demonstrate that fact. Therefore, a security purchased at a premium is allowed to move to a discount, and that a discount is allowed to move to a premium, if this occurs as a result of applying a constant yield method.

Issue 3: On the subject of Parity (described in example 3), is it appropriate under statutory accounting guideline to "assume away" day delay and subsequently eliminate amortizing to a value less than par? If so, should a payment date assumption or a record date assumption be used?

23. It has been noted for mortgage backed securities; interest is often "earned" as of the end of the month but not paid until a later date. This delay known as the "day delay" is often 10-25 days depending on the contract. The yields as provided by "Bloomberg," are Security Industry Association (SIA)

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compliant yields, which do not "assume away 'day delay'", but produce amortization to a value of less than 100, as seen in the example. After discussion, the Working Group determined that the difference between amortizing to the earned record date or to the payment date for the securities described in issue 3 is typically immaterial. Therefore, the Working Group determined to continue to allow flexibility in amortization for the day delay.

24. The user of this interpretation should also note that amortization continues to apply the effective yield method in the above situations provided that doing so does not conflict with other statutory requirements in the SSAPs. For example, yield to worst is still a continuing requirement and other SVO requirements are still in effect, etc.

INT 07-01 Status

25. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 08-05: EITF 02-11: Accounting for Reverse Spinoffs

INT 08-05 Dates Discussed

March 29, 2008; May 31, 2008

INT 08-05 References

Current:
SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items
SSAP No. 95—Nonmonetary Transactions

INT 08-05 Issue

1. *EITF 02-11: Accounting for Reverse Spinoffs* (EITF 02-11) was issued in September 2002 to address whether to account for spinoffs as reverse spinoffs based on the substance, instead of the legal form, of such transactions. In a reverse spinoff, the legal spinnee should be treated as though it were the spinnor for accounting purposes. *(In spinoff transactions, the 'spinnor' is the entity transferring assets, whereas the term 'spinnee' refers to the new entity.)*

2. As noted within EITF 02-11:

> 1. An entity may desire to reorganize its operations in response to its business needs. For example, an entity (the "spinnor") may transfer assets into a new legal spun-off entity (the "spinnee") and distribute the shares of the spinnee to its shareholders, without the surrender by the shareholders of any stock of the spinnor. Such a transaction is commonly referred to as a "spinoff." Consider the following example:
>
> > Big Company owns and operates a mall and a retail store that occupies the anchor store position in that mall. The mall and the store are managed by two separate divisions. The shareholders of Big Company would like to split Big Company into two companies so that each can focus on its own operations. To achieve this, Big Company transfers the mall's assets and operations into a newly created subsidiary, Mall Company, and distributes the shares of Mall Company to its shareholders on a pro rata basis in a spinoff.
>
> 2. A spinoff allows an entity to be reorganized in a manner that allows it to meet the needs of its owners. However, there may be other benefits as well. If the spinoff qualifies as a nontaxable reorganization, the distribution results in no taxable gain being recognized by either the spinnor or its shareholders. Additionally, if the spinnee is subsequently sold by the shareholders, the double taxation that would have occurred if a company sold its subsidiary directly and distributed the proceeds to its shareholders is avoided.
>
> 3. The accounting guidance for spinoffs is provided in Opinion 29. Although the basic principle underlying Opinion 29 is that the accounting for nonmonetary transactions should be based on the fair values of the assets (or services) involved, it provides a modification to that basic principle for nonreciprocal transfers to owners (such as spinoffs). Opinion 29, paragraph 23 (as amended by Statement 144), states:
>
> > Accounting for the distribution of nonmonetary assets to owners of an enterprise in a spin-off or other form of reorganization or liquidation or in a plan that is in substance the rescission of a prior business combination should be based on the recorded amount (after reduction, if appropriate, for an indicated impairment of value) of the nonmonetary assets distributed. A prorata distribution to owners of an enterprise of shares of a subsidiary or other investee company that has been or is being consolidated or that has been or is being accounted for under the equity method is to be considered to be

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equivalent to a spin-off. Other nonreciprocal transfers of nonmonetary assets to owners should be accounted for at fair value if the fair value of the nonmonetary asset distributed is objectively measurable and would be clearly realizable to the distributing entity in an outright sale at or near the time of the distribution.

4. Accordingly, under Opinion 29, an entity's distribution of the shares of a wholly owned or consolidated subsidiary to its shareholders should be recorded based on the carrying value of the subsidiary. Regardless of whether the spun-off operations will be sold immediately after the spinoff, the transaction should not be accounted for as a sale of the accounting spinnee followed by a distribution of the proceeds.

5. In certain cases, the spinoff of a subsidiary to its shareholders is such that the legal form of the transaction does not match its substance. That is, in certain circumstances, the spinnee will be the continuing entity. The issue is whether to account for a spinoff as a reverse spinoff based on the substance instead of the legal form of the transaction. In a reverse spinoff, the legal spinnee should be treated as though it were the spinnor for accounting purposes (accounting spinnor).

6. Consider the following example:

Snack Food Company owns two subsidiaries—Ice Cream Subsidiary and Snack Subsidiary. Ice Cream Subsidiary is significantly larger and more profitable than Snack Subsidiary. The shareholders of Snack Food Company would like to continue the ice cream operations and dispose of the snack food operations. To facilitate this, Snack Food Company distributes the shares of Ice Cream Subsidiary to the shareholders thereby creating Ice Cream Company. The shareholders are then able to dispose of the operations of Snack Food Company (now solely comprising Snack Subsidiary operations) by selling the shares directly to a third party and, at the same time, retain ownership of the Ice Cream Company.

Accounting for the above transaction based upon its legal form would present Snack Food Company as the spinnor with Ice Cream Company as the spinnee. However, in substance, Snack Food Company has disposed of Snack Subsidiary and continued its ice cream operations. The legal form of the spinoff may have been driven primarily by tax planning strategies. Accounting for the transaction based on its substance depicts Ice Cream Company as the accounting spinnor and Snack Food Company as the accounting spinnee.

3. Per EITF 02-11, paragraph 5, the issue is whether to account for a spinoff as a reverse spinoff based on the substance instead of the legal form of the transaction. In a reverse spinoff, the legal spinnee should be treated as though it were the spinnor for accounting purposes (accounting spinnor).

4. The FASB Emerging Issues Task Force reached the following consensus in paragraphs 7-8 of EITF 02-11:

7. The Task Force reached a consensus that reverse spinoff accounting is appropriate when treatment of the legal spinnee as the accounting spinnor results in the most accurate depiction of the substance of the transaction for shareholders and other users of the financial statements. The Task Force observed that the determination of whether reverse spinoff accounting is appropriate is a matter of judgment that depends on an evaluation of all relevant facts and circumstances.

8. The Task Force reached a consensus that in determining whether reverse spinoff accounting is appropriate, a presumption should exist that a spinoff should be accounted for based on its legal form, in other words, that the legal spinnor is also the accounting spinnor. However, that presumption may be overcome. An evaluation of the following indicators should be considered in that regard. Nevertheless, no one indicator should be considered presumptive or determinative.

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5. The FASB Emerging Issues Task Force identified the following indicators that a spinoff should be accounted for as a reverse spinoff in paragraph 8 of EITF 02-11:

- **The size of the legal spinnor and the legal spinnee**—All else being equal, in a reverse spinoff, the accounting spinnor (legal spinnee) is larger than the accounting spinnee (legal spinnor). The determination of which entity is larger is based on a comparison of the assets, revenues, and earnings of the two entities. There are no established "bright lines" that should be used to determine which entity is the larger of the two.

- **The fair value of the legal spinnor and the legal spinnee**—All else being equal, in a reverse spinoff, the fair value of the accounting spinnor (legal spinnee) is greater than that of the accounting spinnee (legal spinnor).

- **Senior management**—All else being equal, in a reverse spinoff, the accounting spinnor (legal spinnee) retains the senior management of the formerly combined entity. Senior management generally consists of the chairman of the board, chief executive officer, chief operating officer, chief financial officer, and those divisional heads reporting directly to them, or the executive committee if one exists.

- **Length of time to be held**—All else being equal, in a reverse spinoff, the accounting spinnor (legal spinnee) is held for a longer period than the accounting spinnee (legal spinnor). A proposed or approved plan of sale for one of the separate entities concurrent with the spinoff may identify that entity as the accounting spinnee.

INT 08-05 Discussion

6. The EITF consensus is that reverse spinoff accounting is appropriate when treatment of a legal spinnee as the accounting spinnor results in the most accurate depiction of the substance of the transaction for shareholders and other users of the financial statements. The Task Force observed that the determination of whether reverse spinoff accounting is appropriate is a matter of judgment that depends on an evaluation of all relevant facts and circumstances.

7. The Task Force consensus indicated that a presumption should exist that a spinoff should be accounted for based on its legal form (legal spinnor is the accounting spinnor); however that presumption can be overcome based on an evaluation of indicators that may suggest when a reverse spinoff exists (legal spinnee would be accounting spinnor).

8. In various instances within the statutory accounting guidelines, guidance is incorporated to promote accounting in accordance with the substance of transactions instead of their legal form. The Working Group reached a consensus to adopt EITF 02-11, indicating that reverse spinoff accounting is appropriate when treatment of a legal spinnee as the accounting spinnor results in the most accurate depiction of the substance of the transaction. In situations in which reverse spinoff accounting is judged to be most appropriate, this will result with the carrying value of the spinnee, instead of the spinnor, being utilized in determining the spinoff distribution to shareholders.

9. The following examples have been incorporated from EITF 02-11 to illustrate situations in which a spinoff should be accounted for in accordance with the legal form or as a reverse spinoff:

> Example 1 - Retail Company, a retail store chain, has a wholly owned restaurant subsidiary. The retail and restaurant operations are operated independently with a small executive management team overseeing both. Since the two have unrelated operations, the shareholders believe that the two operations should be separated by way of a spinoff. They believe that this will allow those separate companies to pursue opportunities in their respective industries and maximize their individual value. In order to accomplish the spinoff, Retail Company creates a new legal entity, Restaurant Company, into which the assets and operations of the restaurant subsidiary are

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transferred. The shares of Restaurant Company are then distributed to the shareholders of Retail Company on a pro rata basis.

The executive management team of Retail Company will be divided between the two entities. A comparison of the two companies is presented below:

(In 000s)	Assets	Revenues	Net Income	Fair Value
Retail	$500	$410	$150	$675
Restaurant	$100	$ 75	$21	$170

Evaluation: Based on an analysis of the indicators in this example, the spinoff should be accounted for in accordance with its legal form. That is, the transaction should not be accounted for as a reverse spinoff. Retail Company should be designated as the accounting spinnor based on the first two indicators listed below.

- Retail Company has substantially larger operations than Restaurant Company.
- The fair value of Retail Company is greater than Restaurant Company.
- The management team is allocated between the two operations.
- There are no planned or likely disposals of either Retail Company or Restaurant Company.

The designation of Retail Company as the accounting spinnor will provide the most accurate depiction of the transaction to shareholders and other users of the financial statements because, in substance, Retail Company has spun off its Restaurant Company into a separate company.

Example 2 - Retail Company, a retail store chain, has a wholly owned restaurant subsidiary. The retail and restaurant operations are operated independently, with a small executive management team overseeing both. While the restaurant subsidiary has grown rapidly, the retail operations have deteriorated steadily due to increased competition. The shareholders believe that the two operations should be separated by way of a spinoff. Management intends to dispose of the retail operations. In order to accomplish the spinoff, Retail Company creates a new legal entity, Restaurant Company, into which the assets and operations of the restaurant subsidiary are transferred. The shares of Restaurant Company are then distributed to the shareholders of Retail Company on a pro rata basis.

The executive management team of the combined entity will be assigned primarily to Restaurant Company, as the intent is to dispose of Retail Company (now solely comprising the retail operations). A comparison of certain statistics of the two companies is presented below:

(In 000s)	Assets	Revenues	Net Income	Fair Value
Retail	$300	$210	$ 35	$375
Restaurant	$600	$450	$150	$700

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Evaluation: Based on an analysis of the indicators in this example, the spinoff should be accounted for as a reverse spinoff. Restaurant Company, although the legal spinnee, should be designated as the accounting spinnor based on the following:

- Restaurant Company has substantially larger operations than Retail Company.
- The fair value of Restaurant Company is greater than that of Retail Company.
- The management team is primarily assigned to Restaurant Company.
- Management intends to dispose of Retail Company upon finalizing the spinoff.

The designation of Restaurant Company as the accounting spinnor will provide the most accurate depiction of the transaction to shareholders and other users of the financial statements, as, in substance, Retail Company has disposed of its retail operations and continued its restaurant operations.

INT 08-05 Status

10. No further discussion is planned.

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 15-01: ACA Risk Corridors Collectibility

INT 15-01 Dates Discussed

October 19, 2015; November 5, 2015

INT 15-01 References

Current:
SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act

INT 15-01 Issue

1. The federal Affordable Care Act (ACA) includes three types of risk sharing programs known as risk adjustment, reinsurance and risk corridors. The risk corridors program is a temporary program that is effective for benefit years beginning in 2014 through 2016 and applies to Qualified Health Plans (QHPs) in the individual and small group markets whether sold on or outside of an exchange.

2. The risk corridors program creates a mechanism for sharing risk for allowable costs between the federal government and QHP issuers – collecting charges from the issuer if the issuer's QHP premiums exceed claims costs of QHP enrollees by a certain amount, and making payments to the issuer if the issuer's premiums fall short by a certain amount, subject to certain adjustments for taxes, administrative expenses, and other costs and payments. The risk corridors program is intended to protect against inaccurate rate setting by limiting the extent of QHP issuer losses and gains. In the event that risk corridors program collections are not sufficient to cover all the required distributions, the ACA allows the use of other sources of federal funding for the required distributions, subject to the availability of appropriations.

3. On April 11, 2014, the U.S. Department of Health and Human Services (HHS) issued a bulletin titled ''Risk Corridors and Budget Neutrality," which described how it intended to administer risk corridors over the three-year life of the program. HHS stated that if risk corridors collections for a particular year are insufficient to make full risk corridors payments for that year, risk corridors payments for the year will be reduced pro rata to the extent of any shortfall. The HHS noted that lacking other appropriations or sources of funding, subsequent year program collections would first be applied to the unpaid program balances of preceding years. In December 2014, federal funds were not appropriated for the federal costs of the risk-sharing program.

4. On October 1, 2015, HHS announced proration results for 2014 risk corridors payments. Based on current data from QHP issuers' risk corridors submissions, issuers will pay $362 million in risk corridors charges, and have submitted for $2.87 billion in risk corridors payments for 2014. As of October 1, 2015, assuming full collections of risk corridors charges, this will result in a proration rate of 12.6 percent. HHS will begin collection of risk corridors charges in November 2015, and will begin remitting risk corridors payments to issuers starting December 2015. The announcement noted that the risk corridor payment and charge amounts reflected in the October 1, 2015, bulletin do not reflect any payment or charge adjustments due to resubmissions after September 15, 2015, or the effect of subsequent appeals.

5. There was diversity in practice regarding the accrual of 2014 risk corridors receivables for the first two quarters of 2015. Some entities did not accrue material amounts for the risk corridors receivables or did not accrue any amount due to the lack of federal government appropriations, and pursuant to the requirement in *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*, which requires that preparers be conservative and diligent in developing their estimates. Other entities appear to have accrued the full amount of funds estimated to be received under the risk corridors program. For some entities the

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accrued receivables represent a material amount of surplus and uncollectibility or delayed collectibility represents a solvency concern.

6. At a minimum, impairment analysis and/or updated estimates are required under SSAP No. 107 for the 2014 risk corridors receivables. In determining the amount to be impaired, one issue identified is that 2015 and 2016 collections may not be sufficient to cover the full 2014 program requests.

7. The accounting issues are:

Issue 1: **Determining the Amount of Impairment –** The 2015 and 2016 program collections may not be sufficient to fund the shortfall of 2014 program requests. Therefore, the accounting issue identified is how to determine the required impairment amount.

Issue 2: **Nonadmittance** – The accounting questions regarding nonadmission have been focused on the amounts in excess of the confirmed proration payment of 12.6%, of which there is a reasonable and probable expectation that the 2015 and 2016 program collections will cover some portion of the 2014 benefit year shortfall.

An accounting issue identified is whether nonadmittance is required or permitted to be applied to the 2014 program benefits in excess of the 12.6% prorated amount for which reporting entities have a reasonable and probable expectation of future collection. Even if an entity has a reasonable and probable expectation of payment of the amount in excess of the confirmed proration of 12.6%, extended delays in payment are expected.

Issue 3: **Timing of Impairment or Nonadmittance Recognition** – The HHS notice of the 12.6% proration amount was provided on October 1, 2015; however, prior to October 1, there were other indicators that the risk corridors program would have 2014 benefit shortfalls (in April and December of 2014 as detailed above and other public reports). Doubts about program collectibility of receivables and problems with estimations are among the reasons many entities did not accrue risk corridors receivables or only accrued immaterial amounts. The accounting issue identified is whether impairment recognition is required to be reflected in the September 30, 2015, financial statements.

Issue 4: **Accrual of 2015 and 2016 Receivables** – Shall the accrual of receivables for the benefit years 2015 and 2016 continue to be estimated?

INT 15-01 Discussion

8. For Issue 1, impairment analysis and/or updated estimates for the 2014 risk corridors receivables are required under SSAP No. 107.

9. The Working Group determined that impairment is indicated if an entity accrued as of the reporting date under the 2014 Risk Corridors program more than they have a reasonable expectation of receiving. SSAP No. 107, paragraph 59.e. (quoted below), requires evaluation of the collectibility of all amounts receivable from the risk corridors program for each reporting period, and if in accordance with SSAP No. 5R it is probable that risk corridors receivables are uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

> 59. Risk corridors assessments meet the definition of liabilities as set forth in SSAP No. 5R. Risk corridors receivables due to the reporting entity meet the definition of an asset and are admissible to the extent that they meet all of the criteria in this statement.
>
> a. Assumptions used in estimating retrospective premium adjustments shall be consistent with the assumptions made in recording other assets and liabilities necessary to reflect the underwriting results of the reporting entity such as claim and loss reserves (including IBNR) and contingent commissions. Contingent

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commissions and other related expenses shall be adjusted in the same period the additional or return retrospective premiums are recorded.

b. The additions or reductions to premium revenue resulting from the risk corridors program are recognized over the contractual period of coverage, to the extent that such additions or reductions are reasonably estimable. Reporting entities shall be aware of the significant uncertainties involved in preparing estimates and be both diligent and conservative in their estimations. Risk corridors payables and receivables shall be estimated based on experience to date. The method used to estimate the payables and receivables shall be reasonable and consistent between reporting periods. In exercising the judgment required to prepare reasonable estimates for the financial reporting of risk corridors program payables and receivables, the statutory accounting concept of conservatism shall be followed. In addition, reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity's estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. In addition, the estimates shall be consistent with other financial statement assertions and the pricing scenarios used by the reporting entity.

c. The risk corridors receivables are from a federal governmental program. Amounts over 90 days due shall not cause the receivable to be treated as a nonadmitted asset based solely on aging.

d. Provided that the risk corridors receivables due the reporting entity are determined in a manner that is consistent with the requirements of this statement, the receivables are admitted assets until determination of impairment or payment denial is received from the governmental entity or government-sponsored entity administering the program. Upon notification that payments to be paid to the reporting entity will be less than the recorded receivables, any amount in excess of the confirmed amount shall be written off and charged to income, except for amounts that are under appeal. Any receivable for risk adjustment amounts under appeal shall be reflected as a nonadmitted asset.

e. Evaluation of the collectibility of all amounts receivable from the risk corridors program shall be made for each reporting period. If, in accordance with SSAP No. 5R, it is probable that the risk corridors receivables are uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. If it is reasonably possible, that a portion of the balance determined in accordance with this paragraph is not anticipated to be collected and is therefore not written off, the disclosure requirements outlined in SSAP No. 5R shall be followed.

f. Reporting shall be consistent with SSAP No. 66—Retrospectively Rated Contracts, paragraph 9 guidance on reporting for retrospective premium.

10. Current facts and circumstances must be taken into account when determining impairment. In accordance with SSAP No. 107, paragraph 59.e., any uncollectible receivable shall be written off and charged to income in the period the determination is made. The Working Group noted that the following are some, but not an all-inclusive list of the relevant factors to consider in determining the amount of impairment to include:

a. Amounts in excess of the proration amount of 12.6% must be evaluated for impairment.

b. Judgment is involved in the determination of the impairment amount.

c. Information used in determination of impairment shall be based on the most current and reliable information available.

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d. Other known or probable changes in program collections or funding must also be evaluated, including the possibility of fewer contributors or lesser collections due to insolvencies.

e. The intent and ability of the reporting entity to remain in business for a period of time sufficient to allow for recovery of risk corridors receivables.

11. The Working Group noted that the impaired amount would be based on the facts and circumstances and is required to be evaluated at each reporting period by management.

12. For Issue 2, SSAP No. 107 addresses nonadmittance in paragraph 59.c., noting that, "Amounts over 90 days due shall not cause the receivable to be treated as a nonadmitted asset based solely on aging." However, SSAP No. 107 does not preclude nonadmittance for other reasons. In addition, SSAP No. 4 provides that:

> "The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third party interests should not be recognized on the balance sheet, and are, therefore, considered nonadmitted."

13. The lack of appropriations, documented program shortfalls and known extended payment delays are indicative that some of the program receivables are not available to meet policyholder obligations when due, and therefore, evaluation for possible nonadmittance under SSAP No. 4 in addition to impairment evaluation is appropriate.

14. The Working Group discussed that nonadmission was appropriate for amounts that have a reasonable and probable expectation of recovery which are not currently available to pay claims. In this case, 2014 amounts in excess of the 12.6% proration amount which have not been written off for impairment, and have a reasonable expectation of delayed recovery shall be nonadmitted. The Working Group discussed that amounts in excess of the proration amount which are nonadmitted, shall remain nonadmitted until additional proration amounts are confirmed by HHS or other information of a sufficient nature supports that collectibility is probable and reasonable. Consistent with SSAP No. 107, paragraph 59, the statutory accounting concept of conservatism shall be followed when estimating amounts; reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity's estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. Consistent with Issue 4, below, estimates shall not assume the availability of federal funds unless such federal funds are appropriated by Congress for the federal costs of the risk sharing program.

15. Such admitted amounts should also have a reasonably short time horizon to ensure that amounts will be available to pay policyholder claims. Some regulators and reporting entities may also take the position that it is probable that risk corridors receivables accrued during the 2014 plan year are uncollectible in excess of 12.6% proration, and therefore, any amounts in excess of proration would be fully written off. If this were the case, the 12.6% prorated balance would be admitted unless extended payment delays or other information cause a reevaluation of admissibility.

16. For Issue 3, the October 1 notification from HHS provided evidence of the estimated amount of proration for the underfunded program. The underfunded program was a condition that existed at the date of the September 30, 2015, balance sheet. Therefore, in accordance with *SSAP No. 9—Subsequent Events*, paragraph 11 (quoted below) this would be a Type I subsequent event that would be reflected in the financial statements for the third quarter. Type I events include estimates inherent in the process of preparing financial statements.

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11. The following are examples of Type I recognized subsequent events:

a. If the events that gave rise to litigation had taken place before the balance sheet date and that litigation is settled, after the balance sheet date but before the financial statements are issued or are available to be issued, for an amount different from the liability recorded in the accounts, then the settlement amount should be considered in estimating the amount of liability recognized in the financial statements at the balance sheet date.

b. Subsequent events affecting the realization of assets, such as receivables and inventories or the settlement of estimated liabilities, should be recognized in the financial statements when those events represent the culmination of conditions that existed over a relatively long period of time. For example, a loss on an uncollectible trade account receivable as a result of a customer's deteriorating financial condition leading to bankruptcy after the balance sheet date but before the financial statements are issued or are available to be issued ordinarily will be indicative of conditions existing at the balance sheet date. Thus, the effects of the customer's bankruptcy filing shall be considered in determining the amount of uncollectible trade accounts receivable recognized in the financial statements at the balance sheet date.

17. For Issue 4, the Working Group determined that risk corridors receivables for the 2015 and 2016 benefit years estimated in accordance with SSAP No. 107, paragraphs 59.b. and 59.e. are nonadmitted 1) until such time that the prior benefit year is paid in full and 2) until additional proration amounts are confirmed by HHS or other information of a sufficient nature supports that collectibility is probable and reasonable. Consistent with SSAP No. 107, paragraph 59, the statutory accounting concept of conservatism shall be followed when estimating amounts; reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity’s estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. Estimates shall not assume the availability of federal funds unless such federal funds are appropriated by Congress for the federal costs of the risk corridors program.

INT 15-01 Status

18. No further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 18-03: Additional Elements Under the Tax Cuts and Jobs Act

INT 18-03 Dates Discussed

May 14, 2018; August 4, 2018

INT 18-03 References

Current:
SSAP No. 101—Income Taxes

INT 18-03 Issue

1. This interpretation has been issued to provide statutory accounting and reporting guidance for the following items under the federal Tax Cuts and Jobs Act (TCJA) as additional guidance to *SSAP No. 101—Income Taxes*:

   a. Repatriation Transition Tax (RTT)

   b. Alternative Minimum Tax (AMT) Credit

   c. Global Intangible Low-Taxed Income (GILTI)

Issue 1 – Repatriation Transition Tax

2. The Repatriation Transition Tax (RTT) is a one-time transition tax on untaxed foreign earnings of foreign subsidiaries of U.S. companies. Under section 965 of the Internal Revenue Code (IRC), these earnings are deemed to be repatriated. Under the IRC guidance, foreign earnings held in the form of cash and cash equivalents are taxed at a 15.5% rate, and the remaining earnings are taxed at an 8% rate.

   a. The RTT is calculated in the 2017 and, in some cases, the 2018 tax return. It is not a temporary tax item and does not reverse in subsequent years.

   b. The RTT is an amount owed under the revised tax law, and is not impacted by future taxable income.

   c. Although the full amount of the calculated RTT is owed, companies can elect to pay the liability over eight years under a set IRC schedule. If electing to make installment payments, the future RTT payments are due regardless whether a company has future taxable income or losses.

Issue 2 – Alternative Minimum Tax Credit

3. The Alternative Minimum Tax (AMT) credit is, pursuant to the provisions of the TCJA, a tax refund of AMT amounts paid in prior periods. The AMT credit can be recovered through an offset to regular taxes or received as a refund.

   a. A reporting entity could realize all of its AMT receivable in the 2018 tax year if it is used to reduce its regular tax obligation. (It could also be used fully in 2019-2021 in this manner.)

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b. If the AMT credit carryforward is not used to reduce regular taxes, it can be recovered as a refund (50%) to the extent not so used in tax years 2018 through 2020, with a 100% refund in 2021 to the extent not used to reduce 2021 regular tax liability.

c. If the AMT credit will be received as a refund (and not as an offset to tax liability), it may be subject to U.S. federal administrative sequestration requirements, which could reduce the amount paid by the federal government. (In 2017, the sequestration percentage was 6.6%, but this percentage varies yearly.)

d. U.S. GAAP guidance permits reporting the AMT credit as a current-year recoverable or as a deferred tax asset (DTA).

Issue 3 - Global Intangible Low-Taxed Income Tax - Description

4. The Global Intangible Low-Taxed Income (GILTI) tax is a new tax under the TCJA and is calculated each year on a portion of a controlled foreign corporation's active income.

a. GILTI is included in 2018 and subsequent year tax returns. An amount owed for GILTI in any tax year is not a temporary tax item and does not reverse in subsequent years. GILTI is a current income tax.

b. Assessments of changes in the basis differences in foreign entities could result in calculations of deferred tax items related to GILTI. The issue is whether existing basis differences will result in GILTI when they reverse. Although these deferred items may be theoretically correct, such calculations are expected to be very complex and require aggregate assessments that consider all companies within a consolidated tax group.

c. In January 2018, the *Financial Accounting Standards Board* (FASB) *Staff Q&A Topic 740, No. 5 Accounting for Global Intangible Low Taxed Income* identified that reporting entities may make an election to recognize deferred items under GILTI. (The recognition of the deferred items does not impact current tax recognition for GILTI, but whether basis differences for foreign controlled entities shall result in deferred tax assets or deferred tax liabilities.) The FASB Staff Q&A Topic 740, No. 5 also identified that FASB staff will be monitoring how entities that pay tax on GILTI are accounting for and disclosing these deferred effects over the next few quarters. The FASB staff will provide a subsequent update so the FASB can consider whether accounting and disclosure improvements are needed for U.S. GAAP.

INT 18-03 Discussion

5. The Statutory Accounting Principles (E) Working Group consensuses for accounting and reporting for the noted items are included below.

Issue 1 – Repatriation Transition Tax:

6. The Repatriation Transition Tax (RTT) is a current-year tax item captured in SSAP No. 101, paragraph 3. The amount payable shall be recognized as a current-year expense with a liability recognized as "current federal and foreign income taxes" and not as a deferred tax liability (DTL), regardless if an entity elects to make installment payments of the amount owed or pays the amount in full.

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Disclosure

7. Reporting entities that are subject to the RTT shall include the following in a narrative disclosure as part of the income tax disclosures in Note 9:

a. RTT owed under the TCJA.

b. Schedule of payments made and expected future payments to satisfy the RTT liability. This disclosure shall explicitly identify whether the insurance entity has remitted full payment of the RTT, or whether the reporting entity is electing to pay the liability under the permitted installments. If the reporting entity fully remitted the RTT, disclosure of the RTT and the remitted payment is only required in the year-end 2018 financial statements. Reporting entities electing to make installment payments shall include the disclosure beginning in the year-end 2018 financial statements and continuing through the year-end statutory financial statements for the year in which the last installment payment was remitted.

Issue 2 – Alternative Minimum Tax Credit:

8. The Alternative Minimum Tax (AMT) credit qualifies as a current income tax recoverable pursuant to paragraph 9 of SSAP No. 101. Although qualifying as a current-year recoverable, some companies may elect to report the AMT credit as a DTA. Although the AMT refund qualifies as a current income tax recoverable, in order to mirror provisions permitted under U.S. GAAP, reporting entities may elect to report the AMT credit as either a current-year recoverable or as a DTA. If reported as a DTA, it would be subject to the statutory accounting admittance limitations for DTAs. If the AMT credit accounted for as a DTA exceeds statutory admittance provisions, it would be nonadmitted under SSAP No. 101.

Disclosure

9. Reporting entities with an AMT credit shall include the following narrative disclosure as part of the income tax disclosures in Note 9:

a. Identification of whether the AMT credit was recognized as a current-year recoverable or DTA.

b. The balance of the AMT credit carryforward as of the beginning of the year; the amount of the AMT credit recovered during the year; other current-year adjustments to the AMT credit carryforward; the balance of the AMT credit carryforward at the end of the year; the amount, if any, by which the ending balance has been reduced for sequestration; and the amount, if any, by which the reporting entity has elected to nonadmit. (This disclosure intends to capture any nonadmittance of the AMT credit by the reporting entity prior to application of the DTA admittance limitations reflected in SSAP No. 101.)

(These disclosures shall be made on an accrual basis beginning in the 2018 year-end statutory financial statements and continuing through the year-end statutory reporting period in which the AMT credit is fully utilized/received.)

Issue 3 – Global Intangible Low-Taxed Income Tax:

10. Under statutory accounting, reporting entities shall not recognize deferred GILTI tax for basis differences in foreign entities. GILTI tax from the current-year tax return is treated as a current-year tax item captured in SSAP No. 101, paragraph 3. The amount payable shall be recognized as a current-year expense with a liability recognized as a current federal and foreign income tax.

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11. As an exception to this general rule, reporting entities are permitted to recognize deferred tax items for basis differences expected to reverse as GILTI in future years if they have recognized deferred tax items for basis differences expected to reverse as GILTI under U.S. GAAP. However, a reporting entity that has recognized deferred tax items for GILTI under U.S. GAAP may follow the statutory accounting general rule (no recognition of deferred tax items). Reporting entities that recognize deferred tax items for GILTI shall explicitly disclose this item in Note 9, beginning with the 2018 year-end statutory financial statements.

INT 18-03 Status

12. Any accounting change required by INT 18-03 shall, if not otherwise covered by *INT 18-01: Updated Tax Estimates Under the Tax Cuts and Jobs Act*, be recognized as a change in accounting estimate, pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors.*

13. The consensuses adopted in this interpretation provide information regarding the RTT, AMT credit and GILTI under the federal Tax Cuts and Jobs Act, and the statutory accounting assessment for reporting and disclosure for each of these items.

14. No further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 19-02: Freddie Mac Single Security Initiative

INT 19-02 Dates Discussed

February 6, 2019; April 6, 2019

INT 19-02 References

Current:
SSAP No. 26R—Bonds
SSAP No. 43R—Loan-Backed and Structured Securities

INT 19-02 Issue

1. This interpretation has been issued to provide a limited-scope exception to the exchange and conversion guidance in *SSAP No. 26R—Bonds* as well as prescribe guidance in *SSAP No. 43R—Loan-Backed and Structured Securities* (SSAP No. 43R) for instruments converted in accordance with the Freddie Mac Single Security Initiative. Under this initiative, reporting entities will be permitted to exchange "45-day securities" for "55-day securities" without any material change to the securities, or to the loans that back the securities. (With the exchange, there would be a 10-day delay in payment cycle.)

2. Information on the Freddie Mac Single Security Initiative (Freddie Mac Gold PC Exchange). Information is also available via the noted link: *http://www.freddiemac.com/mbs/exchange/faqs.html*.

a. Freddie Mac will offer holders of 45-day, TBA-eligible and non-TBA-eligible Gold PCs and Giants the option to exchange their eligible 45-day securities for 55-day Freddie Mac securities and float compensation. For the TBA-eligible security exchanges, the 55-day corresponding security will be a Uniform Mortgage-Backed Security (UMBS™) or Supers, while for non-TBA eligible exchanges, the corresponding security will be a 55-day Freddie Mac MBS or Giant MBS.

b. Most elements of the new 55-day security received upon exchange will exactly match those of the PC or Giant being exchanged – most fundamentally, the cash flows of the 55-day security will ultimately be backed by the same loans as the original PC or Giant. Each new 55-day security will mostly have the same characteristics as the corresponding PC such as unpaid principal balance, pool factor, and weighted average coupon. The 55-day security will have a new CUSIP, prefix, pool number, and issuance date.

c. Freddie Mac is offering the exchange to promote liquidity in the 55-day TBA-eligible market. The exchange of non-TBA eligible securities for 55-day Freddie Mac MBS will help provide greater consistency across Freddie Mac's fixed-rate securities population. After the Single Security Initiative's implementation, all new issue Freddie Mac Single Family fixed-rate securities will have a 55-day payment delay.

d. Exchanges will be initiated at the option of the investor and will not be mandatory. The exchange offer is expected to open in May 2019, the month prior to the Single Security Initiative go-live. The Dealer-facilitated path will stay open for the foreseeable future, while the Direct-to-Freddie Mac exchange path is expected to stay open for 3-5 years.

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e. Investors will receive a one-time payment that will be the approximate fair value compensation for the 10 days' delay of the bond's payment, or float compensation. For the Direct-to-Freddie Mac exchange path, this compensation will be paid through a one-time cash payment. For the Dealer-facilitated path, it is anticipated that the dealer will likely net the float compensation payment from the buy-back price of the 55-day security. Freddie Mac will treat the float compensation payment as a tax-free adjustment to the security basis. As such, for those investors that execute their exchange through the Direct-to-Freddie Mac path, Freddie Mac does not intend to report the payment as taxable income to the investor or to the IRS. However, Freddie Mac is not dictating to investors how they must treat the payment. Some investors may conclude, after consulting with their tax advisors, that the float compensation is taxable income when received**.**

INT 19-02 Discussion

3. The Working Group reached a consensus to incorporate a limited-scope exception to *SSAP No. 26R—Bonds* and prescribe guidance for SSAP No. 43R specific to securities exchanged as part of the Freddie Mac Single Security Initiative. This limited-scope exception requires continuation of the amortized cost basis of the security surrendered to the new security received in the exchange. This is an exception to the guidance in SSAP No. 26R that requires fair value of the surrendered security to become the cost basis for the received security, unless the fair value of the security received is more clearly evident. Although there is not explicit guidance for exchanges in SSAP No. 43R, an entity referring to other statutory accounting standards for application, (such as *SSAP No. 95—Nonmonetary Transactions)* would infer a fair value measurement, rather than a continuation of the amortized cost basis.

4. By continuing the amortized cost basis, the reporting entity shall not recognize any gains or losses (from comparison of fair value to the amortized cost basis) as a result of the exchange. This is considered appropriate as most of the elements of the security held after the exchange will exactly match the security surrendered, including unpaid principal balance, pool factors and weighted average coupon. Furthermore, the cash flows of the new securities will be ultimately backed by the same loans as the original security.

5. This interpretation also permits reporting entities to adjust the security's basis (decrease) for the float compensation received. This treatment agrees to how Freddie Mac will treat the compensation payment. This treatment was determined by Freddie Mac after receiving confirmation from the Securities Exchange Commission (SEC) that the SEC does not object to the treatment of the exchange as a minor modification of an existing security. Freddie Mac has also identified that it does not intend to report the float compensation as taxable income to the investor or the IRS, but has identified that the holders of the securities must rely on their own tax and accounting advisors in determining the best course of action.

INT 18-03 Status

6. The consensus adopted in this interpretation shall remain applicable as long as securities are exchanged under the Freddie Mac Single Security Initiative. This interpretation is only applicable for the specific exchange program reviewed and shall not be inferred to other security exchanges.

7. No further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 20-01: ASUs 2020-04, ~~&~~ 2021-01 & 2022-06 - Reference Rate Reform

INT 20-01 Dates Discussed

March 26, 2020; April 15, 2020; May 20, 2021, March 22, 2023, August 13, 2023

INT 20-01 References

Current:
SSAP No. 15—Debt and Holding Company Obligations
SSAP No. 22R—Leases
SSAP No. 86—Derivatives

This INT applies to all SSAPs with contracts within scope of ASU 2020-04, which allows for modifications due to reference rate reform and provides for the optional expedient to be accounted for as a continuation of the existing contract.

INT 20-01 Issue

1. This interpretation has been issued to provide statutory accounting and reporting guidance for the adoption with modification of *ASU 2020-04 – Reference Rate Reform (Topic 848), Facilitation of the Effects of Reference Rate Reform on Financial Reporting*, ~~and~~ *ASU 2021-01, Reference Rate Reform (Topic 848), Scope*, and *ASU 2022-06, Reference Rate Reform (Topic 848), Deferral of the Sunset Date of Topic 848* for applicable statutory accounting principles. The Financial Accounting Standards Board (FASB) issued ~~both~~ ASU 2020-04, ~~and~~ ASU 2021-01, and ASU 2022-06 to provide optional, transitional and expedient guidance as a result of reference rate reform.

2. Reference rate reform typically refers to the transition away from referencing the London Interbank Offered Rate (LIBOR), and other interbank offered rates (IBORs), and moving toward alternative reference rates that are more *observable* or transaction based. In July 2017, the governing body responsible for regulating LIBOR announced it will no longer require banks to continue LIBOR submissions after 2021 – likely sunsetting both the use and publication of LIBOR. An important note is that while LIBOR is the primary interbank offering rate, other similar rates are potentially affected by reference rate reform.

3. With a significant number of financial contracts solely referencing IBORs, their discontinuance will require organizations to reevaluate and modify any contract that does not contain a substitute reference rate. A large *volume* of contracts and other arrangements, such as debt agreements, lease agreements, and derivative instruments, will likely need to be modified to replace all references of interbank offering rates that are expected to be discontinued. While operational, logistical, and legal challenges exist due to the sheer volume of contracts that will require modification, accounting challenges were presented as contract modifications typically require an evaluation to determine whether the modifications result in the establishment of a new contract or the continuation of an existing contract. As is often the case, a change to the critical terms (including reference rate modifications) typically requires remeasurement of the contract, or in the case of a hedging relationship, a dedesignation of the transaction.

4. The overall guidance in ASU 2020-04 is that a qualifying modification (as a result of reference rate reform) should not be considered an event that requires contract remeasurement at the modification date or reassessment of a previous accounting determination. FASB concluded that as reference rate changes are a market-*wide* initiative, one that is required primarily due to the discontinuance of LIBOR, it is outside the control of an entity and is the sole reason compelling an entity to make modifications to contracts or hedging strategies. As such, FASB determined that the traditional financial reporting requirements of discontinuing

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such contracts and treating the modified contract as an entirely new contract or hedging relationship would, 1) not provide decision-useful information to financial statement users, and 2) require a reporting entity to incur significant costs in the financial statement preparation and potentially reflect an adverse financial statement impact, one of which may not accurately reflect the intent or economics of a modification to a contract or hedging transaction.

5. Guidance in ASU 2020-04 allows a method to ensure that the financial reporting results would continue to reflect the intended continuation of contracts and hedging relationships during the period of the market-wide transition to alternative reference rates – thus, generally not requiring remeasurement or dedesignation if certain criteria are met.

6. Guidance in ASU 2021-01 expanded the scope of ASU 2020-04 by permitting the optional, transitional, expedient guidance to also include derivative contracts that undergo a similar transition but do not specifically reference a rate that is expected to be discontinued. While these contract modifications do not reference LIBOR (or another reference rate expected to be discontinued), the changes are the direct result of reference rate reform and were deemed to be eligible for similar exception treatment. ASU 2021-01 allows for modifications in interest rates indexes used for margining, discounting or contract price alignment, as a result of reference rate reform initiatives (commonly referred to as a "discounting transition") to be accounted for as a continuation of the existing contract and hedge accounting. On August 13, 2023, the Working Group added the guidance in ASU 2022-06 which only acts to defer the sunset date of Topic 848 from December 31, 2022, to December 31, 2024, after which entities will no longer be permitted to apply the relief from the prior ASUs.

7. The optional, expedient and exceptions guidance provided by the amendments in ASU 2020-04, ~~and~~ ASU 2010-01, and ASU 2022-04 are applicable for all entities. However, they are only effective as of March 12, 2020, through December 31, ~~2022~~2024. This is because the amendments are intended to provide relief related to the accounting requirements in generally accepted accounting principles (GAAP) due to the effects of the market-wide transition away from IBORs. The relief provided by the amendments is temporary in its application in alignment with the expected market transition period. However, the FASB will monitor the market-wide IBOR transition to determine whether future developments warrant any changes, including changes to the end date of the application of the amendments in this ASU. If such an update occurs, the Working Group may also consider similar action. It is not expected that the Working Group will take action prior to or in the absence of a FASB amendment.

8. The accounting issues are:

a. Issue 1: Should a reporting entity interpret the guidance in ASU 2020-04 as broadly accepted for statutory accounting?

b. Issue 2: Should the optional, expedient and exception guidance in ASU 2020-04 apply to debt and other service agreements addressed in SSAP No. 15?

c. Issue 3: Should the optional, expedient and exception guidance in ASU 2020-04 apply to lease transactions addressed in SSAP No. 22R?

d. Issue 4: Should the optional, expedient and exception guidance in ASU 2020-04 apply to derivative transactions addressed in SSAP No. 86?

e. Issue 5: Should the optional, expedient and exception guidance in ASU 2021-01 apply to derivative transactions addressed in SSAP No. 86?

INT 20-01 Discussion

9. For Issue 1, the Working Group came to the consensus that ASU 2020-04 shall be adopted, to include the same scope of applicable contracts or transactions for statutory accounting with the only modification related to a concept not utilized by statutory accounting, as noted below. The Working Group

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agreed the amendments provide appropriate temporary guidance that alleviate the following concerns due to reference rate reform:

a. Simplifies accounting analyses under current GAAP and statutory accounting principles (SAP) for contract modifications.

   i. All contracts within scope of ASU 2020-04, which allows for modifications due to reference rate reform and provides for the optional expedient to be accounted for as a continuation of the existing contract.

b. Allows hedging relationships to continue without dedesignation upon a change in certain critical terms.

c. Allows a change in the designated benchmark interest rate to a different eligible benchmark interest rate in a fair value hedging relationship.

d. Suspends the assessment of certain qualifying conditions for fair value hedging relationships for which the shortcut method for assuming perfect hedge effectiveness is applied.

e. Simplifies or temporarily suspends the assessment of hedge effectiveness for cash flow hedging relationships.

f. The only SAP modification to this ASU is related to the option to sell debt currently classified held-to-maturity. This concept is not employed by statutory accounting and thus is not applicable.

10. For Issue 2, the Working Group came to the consensus that debt and service agreement modifications, as a result of reference rate reform, should not typically rise to the level of requiring a reversal and rebooking of the liability, as SSAP No. 15 states such liabilities should only be derecognized if extinguished. A reference rate modification should not generally require de-recognition and re-recognition under statutory accounting. Nonetheless, for clarity and consistency with ASU 2020-04, the Working Group came to the consensus that should an eligible contract be affected by reference rate reform, then the temporary guidance in ASU 2020-04 shall apply.

11. For Issue 3, the Working Group came to the consensus that lease modifications, solely caused by reference rate reform and ones eligible for optional expedience, likely do not rise to the level of a modification requiring re-recognition as a new lease under statutory accounting. SSAP No. 22R, paragraph 17 states only modifications in which grant the lessee additional rights shall be accounted for as a new lease. These *changes* are outside the scope allowed for optional expedience in ASU 2020-04. Nonetheless, for clarity and consistency with ASU 2020-04, the Working Group came to a consensus that if an eligible lease affected by reference rate reform, then the temporary guidance in ASU 2020-04 shall apply.

12. For Issue 4, the Working Group came to the consensus that ASU 2020-04 shall be applied to derivative transactions as the following considerations provided in the ASU are appropriate for statutory accounting:

a. For any hedging relationship, upon a change to the critical terms of the hedging relationship, allow a reporting entity to continue hedge accounting rather than dedesignate the hedging relationship.

b. For any hedging relationship, upon a change to the terms of the designated hedging instrument, allow an entity to change its systematic and rational method used to recognize the excluded component into earnings and adjust the fair value of the excluded component through earnings.

c. For fair value hedges, allow a reporting entity to change the designated hedged benchmark interest rate and continue fair value hedge accounting.

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d. For cash flow hedges, adjust the guidance for assessment of hedge effectiveness to allow an entity to continue to apply cash flow hedge accounting.

13. For Issue 5, the Working Group came to a consensus on May 20, 2021, that ASU 2021-01 shall be applied to derivative transactions for statutory accounting. Accordingly, derivative instruments that are modified to change the reference rate used for margining, discounting, or contract price alignment that is a result of reference rate reform (regardless of whether the reference rate that is expected to be discontinued) are eligible for the exception guidance afforded in ASU 2020-04 in that such a modification is not considered a change in the critical terms that would require dedesignation of the hedging relationship. In addition, for all derivatives (those qualifying for hedge accounting, those that do not qualify for hedge accounting and replication (synthetic asset) transactions (RSAT)), a reporting entity may account for and report modifications (that are within the scope of INT 20-01) as a continuation of the existing contract even when the legal form of the modification is a termination of the original contract and its replacement with a new reference rate reform contract. This includes in-scope modifications of centrally cleared swap contracts whether they are automatically transitioned at a cessation date or voluntarily executed prior to cessation.

14. Additionally, for GAAP purposes, if an entity has not adopted the amendments in *ASU 2017-12, Derivatives and Hedging*, it is precluded from being able to utilize certain expedients for hedge accounting. For statutory accounting purposes, only the hedge documentation requirements were adopted from ASU 2017-12, while the remainder of the items are pending statutory accounting review. The Working Group concluded that all allowed expedient methods are permitted as elections for all reporting entities under statutory *accounting*. However, if a reporting entity is a U.S. GAAP filer, the reporting entity may only make elections under ASU 2017-12 if such elections were also made for their U.S. GAAP financials.

INT 20-01 Status

15. ~~No f~~Further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 20-06: Participation in the 2020 TALF Program

INT 20-06 Dates Discussed

May 5, 2020; May 20, 2020

INT 20-06 References

SSAP No. 64—Offsetting and Netting of Liabilities
SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
INT 01-31: Assets Pledged as Collateral

INT 20-06 Issue

1. The Federal Reserve reestablished the Term Asset-Backed Securities Loan Facility (TALF) on March 23, 2020, to support the flow of credit to consumers and businesses. The TALF program will enable the issuance of asset-backed securities (ABS) backed by student loans, auto loans, credit card loans, loans guaranteed by the Small Business Administration (SBA), and certain other assets.

2. Under the TALF program, the Federal Reserve will lend on a non-recourse basis to holders of certain AAA-rated ABS backed by newly and recently originated consumer and small business loans. The Federal Reserve will lend an amount equal to the market value of the ABS less a haircut and will be secured at all times by the ABS. Treasury, using the Exchange Stabilization Fund (ESF), will also make an equity investment in the special purpose vehicle (SPV) established by the Federal Reserve for this facility.

3. The TALF is established by the Federal Reserve under the authority of Section 13(3) of the Federal Reserve Act, with approval of the Treasury Secretary.

4. Per review of public data available from the prior 2009 TALF program, there were a limited number of insurance reporting entities that were the actual borrower (entity that directly received the loan) under the TALF program. Rather, in most instances, insurance reporting entities were a material investor to the actual borrower. Per the TALF data, a material investor reflects the entity or individual with 10 percent or greater beneficial ownership interest in any class of securities of a borrower. Such ownership interest may be a direct, intermediate or ultimate interest. Due to the different methods of participating in the TALF program, this interpretation focuses on both reporting entity borrowers and reporting entity investors.

5. For reporting entity borrowers (entity that directly received the loan), the accounting issues addressed in this interpretation include:

   a. How the loan received, and collateral provided shall be reported within the statutory financial statements.

   b. Whether the pledged assets shall be reported as admitted assets as the collateral pledged to the TALF program is not permitted to be substituted.

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6. For reporting entities that are not the direct borrowers, but represent investors to the direct borrower, the accounting issues addressed in this interpretation include:

a. How the reporting entity shall report their investment to a TALF borrower.

b. Whether the reporting entity investor is permitted to pledge assets under the TALF program, and retain admittance, when the reporting entity is not the direct borrower under the TALF program.

7. The April 9, 2020, term sheet for the 2020 TALF program:

https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200409a1.pdf

Term Asset-Backed Securities Loan Facility

Effective April 9, 2020
(The Board of Governors of the Federal Reserve System ("Board") and Secretary of the Treasury may make adjustments to the terms and conditions described in this term sheet. Any changes will be announced on the Board's website.)

Facility:
The TALF is a credit facility authorized under section 13(3) of the Federal Reserve Act intended to help meet the credit needs of consumers and businesses by facilitating the issuance of asset-backed securities ("ABS") and improving the market conditions for ABS more generally.

The TALF will serve as a funding backstop to facilitate the issuance of eligible ABS on or after March 23, 2020. Under the TALF, the Federal Reserve Bank of New York ("Reserve Bank") will commit to lend to a special purpose vehicle ("SPV") on a recourse basis. The Department of the Treasury will make an equity investment of $10 billion in the SPV, as described below.

The TALF SPV initially will make up to $100 billion of loans available. The loans will have a term of three years; will be nonrecourse to the borrower; and will be fully secured by eligible ABS.

Eligible Borrowers:
All U.S. companies that own eligible collateral and maintain an account relationship with a primary dealer are eligible to borrow under the TALF. For the purpose of this document, a U.S. company is defined as a business that is created or organized in the United States or under the laws of the United States and that has significant operations in and a majority of its employees based in the United States.

Eligible Collateral:
Eligible collateral includes U.S. dollar denominated cash (that is, not synthetic) ABS that have a credit rating in the highest long-term or, in the case of non-mortgage backed ABS, the highest short-term investment-grade rating category from at least two eligible nationally recognized statistical rating organizations ("NRSROs") and do not have a credit rating below the highest investment-grade rating category from an eligible NRSRO. All or substantially all of the credit exposures underlying eligible ABS must have been originated by a U.S. company, and the issuer of eligible collateral must be a U.S. company. With the exception of commercial mortgage-backed securities ("CMBS"), eligible ABS must be issued on or after March 23, 2020. CMBS issued on or after March 23, 2020, will not be eligible. For CMBS, the underlying credit exposures must be to real property located in the United States or one of its territories. Eligible collateral must be ABS where the underlying credit exposures are one of the following:

1) Auto loans and leases;
2) Student loans;
3) Credit card receivables (both consumer and corporate);
4) Equipment loans and leases;
5) Floorplan loans;

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6) Insurance premium finance loans;
7) Certain small business loans that are guaranteed by the Small Business Administration;
8) Leveraged loans; or
9) Commercial mortgages.

Eligible collateral will not include ABS that bear interest payments that step up or step down to predetermined levels on specific dates. In addition, the underlying credit exposures of eligible collateral must not include exposures that are themselves cash ABS or synthetic ABS.

To be eligible collateral, all or substantially all of the underlying credit exposures must be newly issued, except for legacy CMBS.

The feasibility of adding other asset classes to the facility or expanding the scope of existing asset classes will be considered in the future.

Conflicts of interest: Eligible borrowers and issuers of eligible collateral will be subject to the conflicts of interest requirements of section 4019 of the CARES Act.

Restriction on single-asset single-borrower ("SASB") CMBS and commercial real estate collateralized loan obligations ("CRE CLOs"): SASB CMBS and CRE CLOs will not be eligible collateral.

Restrictions on CLO loan substitution: Only static CLOs will be eligible collateral.

Collateral Valuation: Haircut schedule is below. The haircut schedule is consistent with the haircut scheduled used for the TALF established in 2008.

Pricing: For CLOs, the interest rate will be 150 basis points over the 30-day average secured overnight financing rate ("SOFR"). For SBA Pool Certificates (7(a) loans), the interest rate will be the top of the federal funds target range plus 75 basis points. For SBA Development Company Participation Certificates (504 loans), the interest rate will be 75 basis points over the 3-year fed funds overnight index swap ("OIS") rate. For all other eligible ABS with underlying credit exposures that do not have a government guarantee, the interest rate will be 125 basis points over the 2-year OIS rate for securities with a weighted average life less than two years, or 125 basis points over the 3-year OIS rate for securities with a weighted average life of two years or greater. The pricing for other eligible ABS will be set forth in the detailed terms and conditions. Fees: The SPV will assess an administrative fee equal to 10 basis points of the loan amount on the settlement date for collateral.

Maturity: Each loan provided under this facility will have a maturity of three years.

Investment by the Department of the Treasury: The Department of the Treasury, using the Exchange Stabilization Fund, will make an equity investment of $10 billion in the SPV.

Non-Recourse: Loans made under the TALF are made without recourse to the borrower, provided the requirements of the TALF are met.

Prepayment: Loans made under the TALF will be pre-payable in whole or in part at the option of the borrower, **but substitution of collateral during the term of the loan generally will not be allowed.**

Program Termination: No new credit extensions will be made after September 30, 2020, unless the TALF is extended by the Board of Governors of the Federal Reserve System and the Department of the Treasury.

Other Terms and Conditions: More detailed terms and conditions will be provided at a later date, primarily based off of the terms and conditions used for the 2008 TALF. In addition, the Federal Reserve reserves the right to review and make adjustments to these terms and conditions –

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including size of program, pricing, loan maturity, collateral haircuts, and asset and borrower eligibility requirements – consistent with the policy objectives of the TALF.

INT 20-06 Discussion

For Reporting Entity Borrowers - Insurance Reporting Entity Received the Loan

8. Reporting entity borrowers shall report the cash received under the TALF program with a corresponding liability. The liability shall be captured in scope of *SSAP No. 15—Debt and Holding Company Obligations* and reported as "borrowed money." The disclosures in SSAP No. 15 shall be completed. Once the cash received has been reinvested, the reporting entity shall report the acquired asset in accordance with the applicable statement of statutory accounting principle.

9. Reporting entity borrowers shall report asset-backed securities pledged to the TALF program as restricted assets with the appropriate code in the investment schedules and disclosed in accordance with *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures*, and in General Interrogatory, Part 1: 25.30 – Pledged as Collateral. Assets pledged to the TALF program are subject to the underlying asset risk-based capital charge but are excluded from an additional "restricted asset" risk-based capital charge. (As a carryover from the 2009 TALF Program, existing provisions in the risk-based capital instructions instruct the removal of assets pledged to the TALF program reported as restricted assets in the General Interrogatories.)

10. Reporting entity borrowers are permitted to continue reporting pledged asset-backed securities as admitted assets in the statutory financial statements if the following two conditions are met:

a. Asset qualified as an admitted asset before it was pledged to the TALF program.

b. The reporting entity has not committed an uncured contract default.

11. As the TALF program specifically identifies that substitution of pledged collateral during the term of the loan will generally not be allowed, this interpretation provides an exception to existing statutory accounting requirements. Pursuant to *INT 01-31: Assets Pledged as Collateral*, a pledged asset shall be readily substitutable in order to be admitted in the statutory financial statements. With the exception in this interpretation, assets held by the insurance reporting entity (borrower) that are pledged to the TALF program can be admitted even though they are not generally substitutable.

12. Reporting entity borrowers shall not net the obligation to return the liability and the pledged collateral in the statutory financial statements. The criteria for a valid right of offset in *SSAP No. 64—Offsetting and Netting of Assets and Liabilities* has not been met for these transactions. Specifically, the reporting entity does not have the right to offset the amount owed under the TALF program and the reporting entity does not intend to setoff the amount owed. Although the collateral pledged could be claimed under the TALF program in the event that the insurer reporting entity commits a loan repayment default, the ability to claim pledged collateral does not represent a "right of setoff" with the counterparty.

13. Although the transaction is similar to a repurchase agreement accounted for as a secured borrowing, the TALF transaction is not a repurchase transaction. As such, the provisions and disclosures for repurchase agreements are not applicable.

14. In the event that a reporting entity commits a contract default, and the pledged collateral is retained under the TALF program, the reporting entity shall follow the guidance in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, paragraph 20, in removing the pledged assets and liability from the statutory financial statements.

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For Reporting Entity Investors - Insurance Reporting Entity Does Not Receive the Loan but is an "Investor" to an Entity that was the Direct TALF Borrower

15. Reporting entity investors shall report the investment in the borrower in accordance with the underlying nature of the investment and the relationship with the borrower. The underlying investments will be subject to the reporting and RBC requirements for the applicable SSAP and reporting schedule:

a. If the borrower is a limited liability company (LLC), the investment shall be reported in accordance with *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies.*

b. If the borrower is a private equity fund (e.g., joint venture), the investment shall be reported in accordance with *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies.*

c. If the borrower is an affiliate, the investment shall be reported in accordance with *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities.*

16. Reporting entity investors are not permitted to admit assets pledged to the TALF program if they are not the direct borrower. This is because the return of the assets would be contingent on the action of the actual borrower to the TALF program and not the reporting entity. This provision is consistent with *SSAP No. 4—Assets and Nonadmitted Assets*, footnote 2:

> If assets of an insurance entity are pledged or otherwise restricted by the action of a related party, the assets are not under the exclusive control of the insurance entity and are not available to satisfy policyholder obligations due to these encumbrances or other third-party interests. Thus, pursuant to SSAP No. 4, paragraph 2(c), such assets shall not be recognized as an admitted asset on the balance sheet. Additional guidance for assets pledged as collateral is included in INT 01-31.

INT 20-06 Consensus

17. The Working Group reached a consensus to prescribe statutory accounting guidance for insurance reporting entity involvement in the 2020 TALF Program. Pursuant to this consensus:

a. Reporting entities borrowers who directly receive the TALF loan shall follow guidance in paragraphs 8-14 of this interpretation for the statutory accounting and reporting. As detailed in paragraph 11, this interpretation provides an exception to allow admitted asset reporting for the pledged securities although the TALF program does not permit the pledged assets to be generally substitutable.

b. Reporting entities that do not directly receive the TALF loan, but are investors to borrowers that receive the TALF loan, shall follow the provisions in paragraphs 15-16 for the statutory accounting and reporting.

18. The provisions detailed in this interpretation are applicable for the duration of the 2020 TALF loan program.

INT 20-06 Status

19. No further discussion planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 20-09: Basis Swaps as a Result of the LIBOR Transition

INT 20-09 Dates Discussed

July 15, 2020; July 30, 2020

INT 20-09 References

Current:
SSAP No. 86—Derivatives

INT 20-09 Issue

1. This interpretation is to provide statutory accounting and reporting guidance for "basis swaps." Basis swaps within the scope of this interpretation are defined as compulsory derivatives issued by Central Clearing Parties (CCP), for certain cleared derivatives, issued solely in response to the market-wide transition away from the London Interbank Offered Rate (LIBOR) and toward the Secured Overnight Financing Rate (SOFR).

2. SOFR is a broad measure of the cost of borrowing cash overnight, generally collateralized by Treasury Securities. It represents nearly a risk-free rate that is correlated with other money market rates and is fully transaction based (thus ensuring full transparency), by reflecting a broad measure of overnight U.S. Treasury repurchase transactions. In conjunction with the transition from LIBOR, many alternative reference rates, such as the Effective Federal Funds Rate (EFFR), an interest rate typically utilized by banks representing a charge for overnight loans, used to meet regulatory reserve requirements, are also being transitioned to SOFR. Accordingly, under the general topic referred to as "Reference Rate Reform," contracts which reference or utilize LIBOR or EFFR, are anticipated to be modified to reference SOFR.

3. The Statutory Accounting Principles (E) Working Group previously adopted *INT 20-01: Reference Rate Reform,* which substantially adopted *ASU 2020-04 – Reference Rate Reform* and applies to all SSAPs with contracts within scope of ASU 2020-04. INT 20-01 allows for contract modifications, due to reference rate reform, to be accounted for as a continuation of the existing contract and thus not requiring remeasurement. Among other things, INT 20-01 allows for 1) certain hedging relationships to continue without requiring dedesignation upon a change in certain critical terms (i.e., changing reference rates), and 2) changes in the designated benchmark interest rate to a different eligible benchmark interest rate in a fair value hedging relationship. INT 20-01 recognized that many of these contracts, as part of the discontinuance of LIBOR, will transition to SOFR, an industry recognized preferred benchmark rate.

4. CCPs will make a similar transition, converting open derivative end-of-day valuation calculations from EFFR to SOFR. This transition will occur in two steps, both of which are anticipated to occur on October 16. First, the CCPs will conduct a *standard end-of day valuation* cycle based on EFFR. Then, the CCP will conduct a *special valuation cycle* on those same positions, however utilizing SOFR as the new, ongoing discounting rate. Based on the differences between EFFR and SOFR, the CCP will issue cash adjustments to each account to offset the value adjustments arising from the change in discount rates and additionally will issue mandatory EFFR/SOFR basis swaps, thus restoring the account holder's original risk profile.

5. *SSAP No. 86—Derivatives* addresses the recognition and measurement of derivatives used for hedging, income generation, and replication transactions. Additionally, guidance is provided for derivatives not utilized for one of these broad categories (known as "other derivatives"). Derivatives that are classified

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as "other derivatives" are nonadmitted under SSAP No. 86, whereas derivatives in the other categories are admitted provided they conform to the requirements of the statement.

6. The accounting issues are:

a. Issue 1: How should EFFR/SOFR basis swaps be classified and reported in the statutory financial statements?

b. Issue 2: How should EFFR/SOFR basis swaps be valued in the statutory financial statements?

INT 20-09 Discussion

7. For Issue 1, the Working Group reached a consensus that mandatory basis swaps issued by CCPs, in response to reference rate reform, shall be classified as a derivative used for "hedging." In collaboration with industry representatives, Working Group support staff has confirmed that a significant majority of the derivatives transacted through a CCP meet the definition of a hedging transaction. By using this "used for hedging" classification, instead of an "other derivative" classification, the basis swap derivative received will be admitted under SSAP No. 86.

8. For Issue 2, the Working Group reached a consensus that although the instrument shall be considered a hedging derivative, the instrument shall not be considered or reported as an "effective" hedging derivative (using the "hedge accounting" measurement approach permitted in SSAP No. 86), unless the instrument qualifies, with the required documentation, as a highly effective hedge under SSAP No. 86. Unless the effective hedge requirements are met, the instruments shall be reported on Schedule DB, utilizing the category of "Hedging Other." Pursuant to the guidance in SSAP No. 86, if the basis swap derivative is not an effective hedge, the derivative shall be accounted for at fair value and the changes in fair value shall be recorded as unrealized gains or unrealized losses (referred to as fair value accounting.)

INT 20-09 Status

8. No further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 21-01: Accounting for Cryptocurrencies

INT 21-01 Dates Discussed

March 15, 2021, May 20, 2021

INT 21-01 References

SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments

INT 21-01 Issue

1. This interpretation is to address questions regarding statutory accounting treatment for cryptocurrencies, which are defined as a digital currency in which transactions are verified and records maintained by a decentralized system using cryptography, rather than by a centralized authority. Cryptocurrencies are purchased and exchanged using a limited number of unregulated digital currency exchanges and are not held or offered by major banks.

2. The most valuable cryptocurrency as of February 2021 is Bitcoin, which has been in circulation since 2009, and there are approximately 4,000 different cryptocurrencies available on 200 different cryptocurrency exchanges. Cryptocurrencies have seen significant price volatility and have experienced an extreme increase in value over the past year, with the value of the total outstanding cryptocurrencies nearing $1 trillion as of February 2021. The total market value and increased popularity has led to increased interest in the market by traditional financial institutions and insurance companies.

3. No NAIC Committees or groups have taken any action or established a position on cryptocurrencies. Currently, auditors must rely on guidance provided by the American Institute of Certified Public Accountants through a nonauthoritative practice guide.

4. This Interpretation intends to clarify that directly held cryptocurrencies are nonadmitted assets for statutory accounting.

INT 21-01 Discussion

5. Directly held cryptocurrencies have not been identified in the *Accounting Practices and Procedures Manual* (AP&P Manual) as an admitted asset, and do not meet the definition of any admitted asset that is defined in the AP&P Manual. Accordingly, by default they are a nonadmitted asset per *SSAP No. 4—Assets and Nonadmitted Assets,* paragraph 3*,* as they are not specifically identified in the *Accounting Practices and Procedures Manual* as an admitted asset.

6. Cash is defined in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* as a "medium of exchange that a bank or other similar financial institution will accept for deposit and allow an immediate credit to the depositor's account." Cryptocurrencies are currently not accepted by major banks and do not operate like a traditional currency, and as such do not meet the definition of cash in SSAP No. 2R.

INT 21-01 Consensus

7. The Statutory Accounting Principles (E) Working Group reached a consensus that directly held cryptocurrencies do not meet the definition of an admitted asset and are therefore considered to be a

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nonadmitted asset for statutory accounting. The Working Group intends to rely on this interpretation for statutory accounting and will address cryptocurrencies further once FASB has provided definitive guidance.

INT 21-01 Status

8. No further discussion is planned.

9. The Statutory Accounting Principles (E) Working Group will continue to monitor the evolution of cryptocurrencies and subsequently review this interpretation as appropriate as part of the normal maintenance process.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 22-01: Freddie Mac When-Issued K-Deal (WI Trust) Certificates

INT 22-01 Dates Discussed

April 4, 2022; May 24, 2022

INT 22-01 References

Current:
SSAP No. 43R—Loan-Backed and Structured Securities
SSAP No. 86—Derivatives

INT 22-01 Issue

1. This interpretation is to address questions on the accounting and reporting for Freddie Mac "When-Issued K-Deal (WI Trust) Certificates" (WI Program). Ultimately, the question is whether the structure should be initially captured in scope of *SSAP No. 43R—Loan-Backed and Structured Securities* or as a forward contract in scope of *SSAP No. 86—Derivatives*.

2. The design of the WI Program is summarized as follows:

    a. Investor acquires WI Trust certificates, which are backed by cash held in the WI Trust and pay a fixed coupon amount funded from a Freddie Mac guarantee.

    b. Within 90 days, the trust uses the cash to acquire newly issued K-Deal structured pass-through certificates (SPCs) meeting certain pooling parameters laid out in the respective WI Offering Circular Supplement. K-Deal SPC (s) are Freddie Mac-issued structured pass-through certificates backed by the corresponding class of certificates issued by a separate REMIC trust that holds multifamily fixed-rate mortgage loans. The cash flows from the mortgage loans held by the REMIC trust provide pass-through payments to holders of the K-Deal SPCs.

    c. An investor can choose to continue to hold the WI Trust certificates or exchange dollar-for-dollar their WI-securities into the underlying K-Deal SPCs. In either case, the investor receives a pass-through of cash flows generated by the mortgages held in the REMIC trust and the performance of the K-Deal SPCs is guaranteed by Freddie Mac. If continuing to hold the WI Trust certificates – rather than convert the certificates to K-deal SPCs – the K-Deal SPCs are held by the WI Trust, who in turn passes the cashflows to WI Trust investors. The WI Trust certificates benefit from Freddie Mac payment guarantee which guarantees that any cashflows collected from the K-Deal SPCs will be paid to the WI certificate holders.

3. Additional characteristics on this program include the following:

    a. The WI Trust certificates are public securities and tradeable shortly after pricing.

    b. The WI Trust certificates are backed by a Freddie Mac guarantee from acquisition.

    c. From acquisition of the WI Trust certificates, the investor receives fixed coupon amounts reflective of the investment terms of the K-Deal SPCs.

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d. The WI Trust is obligated to acquire, and Freddie Mac is required to sell, the K-Deal SPCs at the amount stated at the time of initial investment. Meaning, the investor is not at a risk of loss, nor will experience any variation in outcome due to underlying variables that occur from the time of initial investment in the WI Trust until the K-Deal SPCs are acquired. If market forces change the purchase price of the K-Deal SPCs during the 90-days after initial acquisition of the WI Trust certificates, then Freddie Mac is still required to sell the K-Deal certificates at the terms agreed to at original investment. Ultimately, the investor is guaranteed an investment in K-Deal SPCs that reflects the notional value of the WI Trust-certificates and coupon terms at initial acquisition. (For example, if the investor acquired $100 million of WI Trust certificates at acquisition, when the K-Deals are subsequently acquired, the entity will receive $100 million of K-Deal SPCs with the same payment terms regardless of any market impacts.)

e. In the event that Freddie Mac is unable to acquire the K-Deal SPCs within the 90-day period, Freddie Mac is required to return the principal to the investor as well as provide a yield maintenance payment calculated using the full coupon payments that would have been received over the course of the investment.

f. In the event that the investor elects to exchange the WI Trust certificates to the K-Deal SPCs, the investor receives an equivalent principal amount of the K-Deal SPCs of the same class. Although the investment will have a change in CUSIP, any such exchange is not deemed to be a taxable event as described in the respective Offering Circular Supplements for the WI Certificates. As such investors will not recognize a gain or loss on the exchange and investors will be treated as continuing to own the interests that were owned immediately prior to the exchange. Stated differently, any gains or losses on the exchanged WI-Certificates are "rolled into" the investors' new K-Deal Certificate position.

4. The question of whether the structure is a loan-backed or structured security, or a derivative is primarily focused on the initial acquisition and the 90-day (or less) timeframe before the WI Trust acquires K-Deal certificates. The question is whether the initial 90-day acquisition of the WI Trust certificate, prior to the trust's acquisition of the K-Deal certificates, represents a forward contract required to be accounted for under SSAP No. 86. Key excerpts from SSAP No. 86 are as follows:

a. The definition of a derivative instrument from SSAP No. 86, paragraph 4:

> 4. "Derivative instrument" means an agreement, option, instrument or a series or combination thereof:
>
> a. To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or
>
> b. That has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests.

b. The definition of a forward contract from SSAP No. 86, paragraph 5.d.:

> 5.d. "Forwards" are agreements (other than futures) between two parties that commit one party to purchase and the other to sell the instrument or commodity underlying the contract at a specified future date. Forward contracts fix the price, quantity, quality, and date of the purchase and sale. Some forward contracts involve the initial payment of cash and may be settled in cash instead of by physical delivery of the underlying instrument.

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5. This interpretation intends to clarify whether investments in the Freddie Mac WI Program shall be initially captured in scope of SSAP No. 86 or captured in scope of SSAP No. 43R.

INT 21-01 Discussion

6. This interpretation clarifies that investments in the Freddie Mac WI Program shall be captured in scope of SSAP No. 43R from initial acquisition, and not as a derivative forward contract, for the following reasons:

a. The WI Program is fully guaranteed by Freddie Mac and ensures that the investor will receive pass-through certificates, backed my mortgage loans held in trust, that reflect the terms of the investment set at original acquisition. In the event that the K-Deal certificates cannot be acquired, Freddie Mac is guaranteed to provide payment to the investor that reflects the full principal and interest per the original terms of the agreement, which reflects the payments that would have been received overtime if K-Deal certificates had been acquired.

b. The definition of a forward contract in SSAP No. 86 reflects an agreement between two parties that commit one party to purchase and another party to sell the instrument underlying the contract at a specified future date. With the WI Trust Program, the investor does not have a future commitment to acquire securities, as the investor acquires the WI Trust certificate on day one of the transaction and the investor is not required to convert the WI Trust certificates at any time. This WI Trust certificate is not a derivative instrument, as at the time of acquisition, the certificate reflects a tradeable investment in a trust structure backed by cash and a Freddie Mac guarantee of cash flows in accordance with terms established at original acquisition. In addition to having no variation to the investor as a result of an underlying interest, there is no requirement on the investor to take delivery of a different investment. The ability to convert the WI Trust certificate to a K-Deal certificate is strictly an election to the investor and is not a requirement to receive the pass-through cash flows per the terms of the initial investment.

c. The WI Program, and resulting obligation of Freddie Mac, ultimately reflects an investment where the investor receives pass-through cash flows generated from mortgage loans acquired and held in trust. This investment dynamic is within the scope of SSAP No. 43R, paragraphs 2-4:

> 2. Loan-backed securities are defined as securitized assets not included in structured securities, as defined below, for which the payment of interest and/or principal is directly proportional to the payments received by the issuer from the underlying assets, including but not limited to pass-through securities, lease-backed securities, and equipment trust certificates.
>
> 3. Structured securities are defined as loan-backed securities which have been divided into two or more classes for which the payment of interest and/or principal of any class of securities has been allocated in a manner which is not proportional to payments received by the issuer from the underlying assets.
>
> 4. Loan-backed securities are issued by special-purpose corporations or trusts (issuer) established by a sponsoring organization. The assets securing the loan-backed obligation are acquired by the issuer and pledged to an independent trustee until the issuer's obligation has been fully satisfied. The investor only has direct recourse to the issuer's assets, but may have secondary recourse to third parties through insurance or guarantee for repayment of the obligation. As a result, the sponsor and its other affiliates may have no financial obligation under the instrument, although one of those entities may retain the responsibility for servicing

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the underlying assets. Some sponsors do guarantee the performance of the underlying assets.

d. The WI Program, and treatment as a SSAP No. 43R security, is consistent with the current guidance for TBA securities when an insurer intends to take possession of the resulting mortgage-backed security. A TBA security reflects the pre-purchase of mortgage-backed securities prior to the finalization of the security issuance. Pursuant to the annual statement instructions, TBA securities are to be reported on Schedule D-1: Long-Term Bonds unless the structure more closely resembles a derivative. This determination depends on how a company uses the TBA. (For example, if a company intended to assume the mortgage-backed security once issued, the TBA would be captured on Schedule D-1 at initial acquisition. If a reporting entity was to continually trade/roll TBA exposures, this would be more characteristics of a derivative and would be captured on Schedule DB as a derivative.)

INT 22-01 Consensus

5. The Statutory Accounting Principles (E) Working Group reached a consensus that investments in the WI Trust Program shall be captured in scope of SSAP No. 43R from initial acquisition.

6. If a reporting entity elects to convert WI Trust SPC securities into K-Deal SPC securities, the guidance in the Annual Statement Instructions, Schedule D, Part 3 and Part 4 shall be followed. Per that guidance, the transition from a WI Trust to a K-Deal shall not be reported as a disposal or acquisition. As the terms and cost basis of the SPC certificates would be identical, and the change would only reflect a CUSIP number change, a disposal and reacquisition shall not be recorded.

7. Excerpt from Annual Statement Instructions, Schedule D, Part 3 and 4:

This schedule should include a detailed listing of all securities that were purchased/acquired during the current reporting year that are still owned as of the end of the current reporting year (amounts purchased and sold during the current reporting year are reported in detail on Schedule D, Part 5 and only in subtotal in Schedule D, Part 3). This should include all transactions that adjust the cost basis of the securities. Thus, it should not be used for allocations of TBAs to specific pools subsequent to initial recording in Schedule D, Part 3 or other situations such as CUSIP number changes.

INT 22-01 Status

8. No further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 22-02: Third Quarter 2022 through ~~First~~Second Quarter 2023 Reporting of the Inflation Reduction Act - Corporate Alternative Minimum Tax

INT 22-02 Dates Discussed

October 6, 2022; October 24, 2022, November 16, 2022; December 13, 2022; April 12, 2023; May 16, 2023

INT 22-02 References

Current:
SSAP No. 9—Subsequent Events
SSAP No. 101—Income Taxes

INT 22-02 Issue

Key Provisions of the Inflation Reduction Act

1. The Inflation Reduction Act (Act) was enacted on August 16, 2022, and included a new corporate alternative minimum tax (CAMT). The Act and the CAMT go into effect for tax years beginning after 2022. Reporting entities shall refer to the Act and the resulting regulations and other tax guidance to determine application, but a non-authoritative high-level summary based on information at the time of initial INT discussion regarding the CAMT is as follows:

a. The CAMT is 15% of the corporation's "adjusted financial statement income" for the tax year, reduced by corporate alternative minimum foreign tax credit.

b. The CAMT will only apply to "applicable corporations" (determined on an affiliated group basis) with average adjusted financial statement income in excess of $1 billion for the three prior tax years. This threshold is reduced to $100 million in the case of certain foreign-parented corporations. When a corporation becomes subject to the CAMT, it remains an applicable corporation for purposes of the CAMT, even if its average adjusted financial statement income is less than $1 billion, unless an exception applies.

c. A corporation's adjusted financial statement income is the amount of net income or loss the corporation reports on its applicable financial statement. The income is adjusted for various purposes including certain adjustments in the case of consolidated returns or for foreign income.

d. The Act includes references to the tax codes which provides a hierarchy for determining the "applicable financial statement." At a high level, the first choice is U.S. generally accepted accounting principles (GAAP) financial statements; the second choice is international financial reporting standards (IFRS) financial statements. If GAAP and IFRS financial statements are not available, the financial statements filed by the taxpayer with any other regulatory or government body is acceptable. If the taxpayer is part of an affiliated group of corporations filing a consolidated return, the adjustable financial statement income for the group considers the group's applicable financial statement.

e. To determine its U.S. federal income tax liability, an applicable corporation will need to compute taxes under both systems—the regular tax system and the CAMT system. The CAMT is payable to the extent the tentative CAMT exceeds the regular corporate income

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tax. Any CAMT paid is available indefinitely as a credit carryover that could reduce future regular tax in future years if the regular tax liability is in excess of CAMT tax liability.

f. The Act directs the Treasury to issue regulations and other guidance relate to implementing the CAMT, so several issues are pending detailed clarifications including clarifying the definition of an applicable corporation, and providing guidance on the starting point for, and adjustments to, adjusted financial statement income, as well as the handling of separate company tax returns when required under current tax law that are unique to the insurance industry.

Interpretation Issues

2. This interpretation is focused on addressing third quarter 2022 transition accounting and reporting aspects of the new CAMT. While most insurers will not be subject to the CAMT, for those that know that they are subject, and those that could be subject to the CAMT, there are a variety of reporting uncertainties, particularly regarding reporting for third quarter 2022.

3. The CAMT is effective for the tax years on or after 2023.

4. Both statutory accounting principles and U.S. GAAP require the effects of tax changes on deferred taxes, including the valuation allowance (future realizability of existing DTAs) in the period in which the legislation is enacted (third quarter 2022). *SSAP No. 101—Income Taxes,* paragraph 7.e. requires the statutory valuation allowance adjustment as a direct reduction in the gross DTA if, based on the weight of available evidence, it is more likely than not that some or all of the gross DTAs will not be realized. Gross DTA less the statutory valuation allowance results in adjusted gross DTAs. The statutory valuation allowance adjustment is not reported as a separate line in the statutory financial statements (it is an off-balance sheet item that reduces the gross DTAs). The statutory valuation allowance is disclosed.

5. The statutory accounting calculation for admissible DTAs is determined using adjusted gross DTAs (gross DTAs reduced by the valuation allowance). For statutory accounting, admittance of adjusted gross DTAs in SSAP No. 101 depends on a three-component calculation, for which the second step limits admittance of adjusted gross DTAs to those that are expected to be realized in a timeframe that does not exceed three years. The actual number of years permitted depends on specifics for each reporting entity (type and other information about the reporting entity), but the maximum timeframe is three years. The last step admits DTAs which can be offset by DTLs.

6. Guidance in *SSAP No. 9—Subsequent Events* requires consideration of Type I and Type II[1] subsequent events through the date of the statutory financial statements and the date of issuance of the audited financial statements, or the date in which audited financial statements are available to be issued. For subsequent events identified after the statutory financial statements are filed (example, March 1), but before the audited financial statements are issued (example, June 1), reporting entities are generally required by their domestic state to amend their filed statutory financial statements to ensure that the statutory financial statements and the audited financial statements are consistent. Under this guidance, as additional information is made available on the impact of the Act, or information becomes available to update estimates and assessments, under existing statutory accounting guidance in SSAP No. 9, reporting entities would need to identify updated estimates as a Type I subsequent event in the audited financial statements.

[1] A Type I subsequent event relates to an event or transaction that provides additional evidence with respect to conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Under SSAP No. 9, entities shall recognize in the financial statements the effects of all material Type I subsequent events. A Type II subsequent event pertains to events or transactions that provide evidence to conditions that did not exist at the balance sheet date but arose after that date. Type II events are disclosed in the financial statements.

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Issue 1 – Consideration of the Act for Third Quarter 2022 Financial Statements

7. During the period of enactment (third quarter 2022) reporting entities filing statutory financial statements would normally have to consider the applicability of the CAMT and if applicable, determine the impact on the statutory valuation allowance as well as assess DTAs for admissibility (e.g., realization timeframe). These elements will be collectively referred to as "calculations impacted by the Act" or "calculations impacted by the CAMT."

8. This interpretation will address the issue for what reporting entities are required to report or disclose regarding the calculations impacted by the CAMT for September 30, 2022, financial statements.

Issue 2 – Consideration of Subsequent Events for Third Quarter 2022 Financial Statements

9. SSAP No. 9 requires consideration of subsequent events through the date of the statutory financial statements and the date of issuance of the audited financial statements, or the date in which audited financial statements are available to be issued.

10. For reporting entities that materially revise or establish calculations impacted by the CAMT subsequent to September 30, 2022 (including the statutory valuation allowance, the timing of determination of net admitted DTAs, and the determination of the applicability of the CAMT), this interpretation will address the extent a Type I or Type II subsequent event assessment is required for third quarter 2022 financial reporting.

INT 22-02 Discussion

11. The Statutory Accounting Principles (E) Working Group consensuses to the noted issues are included below.

Response: Issue 1 – Consideration of the Act for Third Quarter 2022 Financial Statements

12. Reporting entities that are aware they will be subject to the CAMT would normally reflect the effects of the Act on the calculations impacted by the CAMT if reasonably estimable for third quarter 2022. Because of the timing of the adoption of the Act and the considerable number of unknown variables for September 30, 2022, reporting, the Working Group has determined that a reasonable estimate is not determinable for third quarter 2022 interim financial statements for the calculations impacted by the CAMT.

13. Because reasonable estimates of calculations impacted by the CAMT are not determinable, reporting entities shall not recognize impacts related to CAMT for third quarter 2022 financial statements, but shall make the following disclosures regarding the CAMT and the Act:

a. The Act was enacted during the reporting period on August 16, 2022.

b. A statement regarding whether the reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined if it expects to be liable for CAMT in 2023. For example:

i. The reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined that it does not expect to be liable for CAMT in 2023.

ii. The reporting entity (or the controlled group of corporations of which the reporting entity is a member) has not determined as of the reporting date if it will be liable

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for CAMT in 2023. The third quarter 2022 financial statements do not include an estimated impact of the CAMT because a reasonable estimate cannot be made.

iii. The reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined that it expects to be liable for CAMT in 2023. The third quarter 2022 financial statements do not include an estimated impact of the CAMT, because a reasonable estimate cannot be made.

Response: Issue 2 – Consideration of Subsequent Events for Third Quarter 2022 Financial Statements

14. For third quarter 2022 reporting, CAMT updated estimates or other calculations affected by the Act determined subsequent to third quarter statutory financial statement or filing date shall not be recognized as Type I subsequent events. Meaning, amended financial statements are not required to reflect updated estimates subsequent to the third quarter filing date and prior to the filing the third quarter financial statements. With the disclosure required under Issue 1, additional subsequent event disclosure (such as what would be required for Type II event) is not required.

15. Reporting entities shall be working in good faith to complete the accounting for the changes adopted under the Act.

INT 22-02 Status

16. The consensuses in this interpretation were adopted on October 24, 2022, to provide reporting guidance regarding the calculations impacted by the CAMT and provide limited-scope, limited-time exceptions to the valuation allowance and DTA calculations in response to legislation under SSAP No. 101 as well as Type I subsequent event requirements in SSAP No. 9 for September 30, 2022, statutory reporting. As detailed, the exceptions to SSAP No. 101 and SSAP No. 9 are effective for third quarter 2022.

17. On December 13, 2022, the Working Group adopted a consensus to extend this interpretation for December 31, 2022, and first quarter 2023 statutory financial statements. For application as of year-end 2022 and first quarter 2023:

a. Consistent with paragraphs 12 and 13, the Working Group has concluded that a reasonable estimate is not determinable for December 31, 2022, and March 31, 2023, therefore impacts related to the CAMT in the year-end 2022 and March 31, 2023, financial statements are not required.

~~b. The reporting entity shall include disclosures in paragraph 13 in the year-end 2022 and March 31, 2023, financial statements. In addition, the reporting entity shall disclose the following:~~

~~i. If, based on information regarding the projected adjusted financial statement income for 2023, the entity or the controlled group of corporations of which the reporting entity is a member has determined if it is an "applicable corporation" to determine if CAMT exceeds the regular federal income tax payable. That is, disclose if the reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined if average "adjusted financial statement income" is above the thresholds for 2023 tax year that they expect to be required to perform the CAMT calculations. This disclosure is about being applicable corporation, not if the entity is required to pay.~~

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~~c.~~b. Consistent with paragraph 14, CAMT updated estimates or other calculations affected by the Act determined subsequent to filing the December 31, 2022, and March 31, 2023, financial statements shall not be recognized as Type I subsequent events.

~~d.~~c. For year-end 2022 financial statements, the subsequent event exception is expanded to encompass events that occur prior to the issuance of statutory financial statements as well as events that occur before the date the audited financial statements are issued, or available to be issued. This provision intends to prevent reporting entities from having to amend statutory financial statements from material Type I subsequent events as a result of updated information / estimates received after the reporting date of year-end 2022 statutory financial statements pertaining to the accounting for the enactment of the Act.

18. On May 16, 2023, the Working Group adopted a consensus to extend this interpretation for the second quarter 2023 statutory financial statements. For application to the second quarter 2023 financial statements, reporting entities shall follow the guidance in this interpretation paragraphs 17.a. through 17.c.

~~18.~~19. With the extension, this interpretation will be automatically nullified on ~~June 15~~August 16, 2023.

~~19.~~20. No further discussion is planned.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 23-01: Net Negative (Disallowed) Interest Maintenance Reserve

INT 23-01 Dates Discussed

April 10, 2023, June 28, 2023, August 13, 2023

INT 23-01 References

Current:
SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve
Annual Statement Instructions

INT 23-01 Issue

1. The statutory accounting guidance for interest maintenance reserve (IMR) and the asset valuation reserve (AVR) is within *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*, but the guidance within SSAP No. 7 is very limited. It provides a general description, identifies that IMR/AVR shall be calculated and reported per the guidance in the applicable SSAP, and if not explicit in the SSAP, in accordance with the annual statement instructions. The SSAPs most often simply direct allocation to (or between) IMR and AVR, with the bulk of the guidance residing within the annual statement instructions.

2. As detailed in SSAP No. 7, paragraph 2, the guidance for IMR and AVR applies to life and accident and health insurance companies and focuses on IMR and AVR liability recognition and distinguishing between IMR and AVR:

> 2. Life and accident and health insurance companies shall recognize liabilities for an AVR and an IMR. The AVR is intended to establish a reserve to offset potential credit-related investment losses on all invested asset categories excluding cash, policy loans, premium notes, collateral notes and income receivable. The IMR defers recognition of the realized capital gains and losses resulting from changes in the general level of interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the investments sold. The IMR also applies to certain liability gains/losses related to changes in interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the liability released.

3. The IMR guidance in the annual statement instructions provides information on the net balance. A positive IMR represents net interest rate realized gains and is reported as a liability on a dedicated reporting line. A negative disallowed IMR represents net interest rate realized losses and is reported as a miscellaneous other-than-invested write-in asset in the general account and nonadmitted.

4. IMR balances between the general account and separate accounts are separate and distinct. Meaning, a net negative IMR in the general account only represents activity that occurred in the general account that was allocated to IMR. However, the net positive or negative balance of the general account influences how the net positive or negative balances are reported in separate account statements (and vice versa). (A net negative IMR balance in the general account may not be disallowed if there is a covering net positive IMR in the separate account. Negative IMR that is not disallowed is reported as a contra-liability.) The instructions for reporting the net negative and positive balances are detailed in the annual statement instructions:

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Line 6 – Reserve as of December 31, Current Year

Record any positive or allowable negative balance in the liability line captioned "Interest Maintenance Reserve" on Page 3, Line 9.4 of the General Account Statement and Line 3 of the Separate Accounts Statement. A negative IMR balance may be recorded as a negative liability in either the General Account or the Separate Accounts Statement of a company only to the extent that it is covered or offset by a positive IMR liability in the other statement.

If there is any disallowed negative IMR balance in the General Account Statement, include the change in the disallowed portion in Page 4, Line 41 so that the change will be appropriately charged or credited to the Capital and Surplus Account on Page 4. If there is any disallowed negative IMR balance in the Separate Accounts Statement, determine the change in the disallowed portion (prior year less current year disallowed portions), and make a direct charge or credit to the surplus account for the "Change in Disallowed Interest Maintenance Reserve" in the write-in line, in the Surplus Account on Page 4 of the Separate Accounts Statement. The following information is presented to assist in determining the proper accounting:

General Account IMR Balance	Separate Account IMR Balance	Net IMR Balance
Positive	Positive	Positive (See rule a)
Negative	Negative	Negative (See rule b)
Positive	Negative	Positive (See rule c)
Positive	Negative	Negative (See rule d)
Negative	Positive	Positive (See rule e)
Negative	Positive	Negative (See rule f)

Rules:

a. If both balances are positive, then report each as a liability in its respective statement.

b. If both balances are negative, then no portion of the negative balances is allowable as a negative liability in either statement. Report a zero for the IMR liability in each statement and follow the above instructions for handling disallowed negative IMR balances in each statement.

c. If the general account balance is positive, the separate accounts balance is negative and the combined net balance is positive, then all of the negative IMR balance is allowable as a negative liability in the Separate Accounts Statement.

d. If the general account balance is positive, the separate account balance is negative, and the combined net balance is negative, then the negative amount not covered by the positive amount is not allowable. Report only the allowable portion as a negative liability in the Separate Accounts Statement and follow the above instructions for handling the disallowed portion of negative IMR balances in the Separate Accounts Statement.

e. If the general account balance is negative, the separate account balance is positive, and the combined net balance is positive, then all of the negative IMR balance is allowable as a negative liability in the General Account Statement.

f. If the general account balance is negative, the separate account balance is positive, and the combined net balance is negative, then the negative amount not covered by the positive amount is not allowable. Report only the allowable portion as a negative liability in the General Account Statement and follow the above instructions for handling the disallowed portion of negative IMR balances in the General Account Statement.

5. In October 2022, the ACLI requested the Statutory Accounting Principles (E) Working Group to reassess the guidance for net negative (disallowed) IMR, with a request to consider admittance of those

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amounts. The ACLI noted that the nonadmittance of disallowed negative IMR can have adverse negative ramifications for insurers with two key themes:

a. In general, rising interest rates are favorable to the financial health of the insurance industry and policyholders. However, with negative IMR, there is an inappropriate perception of decreased financial strength through lower surplus and risk-based capital.

b. Negative IMR could impact the rating agency view of the industry or incentivize companies to avoid prudent investment transactions that are necessary to avoid mismatches between assets and liabilities. In either scenario, negative IMR encourages short-term non-economic activity that is not in the best long-term interest of a reporting entity's financial health or its policyholders.

6. In considering the request, the Working Group concluded that, for year-end 2022, there would be no change to statutory accounting guidance and deviations from statutory accounting principles would need to be approved via a permitted or prescribed practice. The Working Group then held company-specific educational sessions in January 2023 to receive detailed information regarding negative IMR and received a subsequent comment letter from the ACLI.

7. During the 2023 Spring National Meeting, the Working Group further discussed the topic of negative IMR and directed NAIC staff to proceed with drafting guidance for a 2023 solution and to begin work towards a long-term solution.

INT 23-01 Discussion

8. This interpretation prescribes limited-time, optional, statutory accounting guidance, as an exception to the existing guidance detailed in SSAP No. 7 and the annual statement instructions that requires nonadmittance of net negative (disallowed) IMR as a short-term solution. Specifically, this interpretation impacts the annual statement instruction rules regarding disallowed negative IMR detailed in rules 'b,' 'd' and 'f' shown in paragraph 4.

9. Reporting entities are permitted to admit net negative (disallowed) IMR with the following restrictions:

a. Reporting entities that qualify pursuant to paragraph 9.b., are permitted to admit net negative (disallowed) IMR up to 10% of the reporting entity's adjusted general account[1] capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for its most recently filed statement with the domiciliary state commissioner. The capital and surplus shall be adjusted to exclude any net positive goodwill, EDP equipment and operating system software, net deferred tax assets and admitted[2] net negative (disallowed) IMR.

b. Reporting entities applying this interpretation are required to have a risk-based capital (RBC) greater than 300% authorized control level (ACL) after an adjustment to total adjusted capital (TAC) that reflects a reduction to remove any net positive goodwill, EDP equipment and operating system software, net deferred tax assets and admitted net negative (disallowed) IMR. Compliance with this adjusted RBC calculation shall be affirmed for all

[1] The general account capital and surplus includes surplus reflected in the separate account; therefore, an aggregation of general account and separate account surplus is not necessary.

[2] As the separate account does not have "admitted" assets, broad reference to "admitted net negative (disallowed) IMR" throughout this interpretation includes what is admitted in the general account and what is recognized as an asset in the separate accounts.

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quarterly and annual financial statements for which net negative (disallowed) IMR is reported as an admitted asset in the general account or recognized as an asset in the separate accounts. Reporting entities shall provide documentation to illustrate compliance with this requirement upon state regulator request. Reporting entities with an adjusted RBC calculation of 300% ACL or lower are not permitted to admit net negative (disallowed) IMR in the general account or recognize IMR assets in the separate accounts.

c. The net negative (disallowed) IMR permitted for admittance shall not include losses from derivatives that were reported at fair value prior to derivative termination[3] unless the reporting entity has historically followed the same process for interest-rate hedging derivatives that were terminated in a gain position. In other words, there is a requirement for documented, historical evidence illustrating that unrealized gains from derivatives reported at fair value were reversed to IMR (as a liability) and amortized as part of IMR. Reporting entities that do not have evidence of this past application are required to remove realized losses from derivatives held at fair value from the net negative (disallowed) IMR balance to determine the amount permitted to be admitted. Reporting entities that begin a new process for the use of hedging derivatives, perhaps with a theoretical process to treat derivative losses and derivative gains similarly, but do not have evidence illustrating the historical treatment of derivative gains through IMR are not permitted to include derivative losses in the net negative (disallowed) IMR permitted to be admitted. This evidence is required separately for the general account, insulated separate account and non-insulated separate account if losses from derivatives previously reported at fair value are currently being allocated to IMR in those accounts.

10. Reporting entities that admit net negative (disallowed) IMR shall follow the following process:

a. All net negative (disallowed) IMR in the general account shall first be admitted until the capital and surplus percentage limit, as detailed in paragraph 9.a., is reached.

b. If all general account net negative (disallowed) IMR has been fully admitted, and the reporting entity is still below the paragraph 9.a. capital and surplus limit, then the reporting entity can report net negative (disallowed) IMR as an asset in the separate accounts. Reporting entities that have both insulated and non-insulated separate accounts shall recognize IMR assets proportionately between the insulated and non-insulated statements until the aggregated amount recognized as an admitted asset in the general account and as an asset in the insulated and non-insulated statements reaches the percentage limit of capital and surplus detailed in paragraph 9.a.

11. Reporting entities that admit net negative (disallowed) IMR in the general account shall report the admittance in the balance sheet as follows:

a. Reporting entities shall report the net negative (disallowed) IMR as an aggregate write-in to miscellaneous other-than-invested assets (line 25) (named as "Admitted Disallowed IMR") on the asset page. The net negative (disallowed) IMR shall be admitted to the extent permitted per paragraph 9.a., with the remaining net negative (disallowed) IMR balance nonadmitted.

b. Reporting entities shall allocate an amount equal to the general account admitted net negative (disallowed) IMR from unassigned funds to an aggregate write-in for special surplus funds (line 34) (named as "Admitted Disallowed IMR"). Although dividends are

[3] Reference to derivative termination throughout this interpretation includes all actions that close out a derivative, including, but not limited to, termination, expiration, settlement, or sale.

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contingent on state specific statutes and laws, the intent of this reporting is to provide transparency and preclude the ability for admitted negative IMR to be reported as funds available to dividend.

12. Reporting entities that record net negative (disallowed) IMR as an asset in the separate account shall report the recognition in the balance sheet as follows:

a. Reporting entities shall report the permitted net negative (disallowed) IMR as an aggregate write-in to miscellaneous other-than-invested assets (line 15) (named as "Recognized Disallowed IMR") on the asset page.

b. Reporting entities shall allocate an amount from surplus equal to the asset recognized as disallowed IMR as an aggregate write-in for special surplus funds (line 19) (named as "Recognized Disallowed IMR) on the liabilities and surplus page.

13. Reporting entities admitting net negative (disallowed) IMR are required to complete the following disclosures in the annual and quarterly financial statements for IMR:

a. Reporting entities that have allocated gains/losses to IMR from derivatives that were reported at fair value prior to the termination of the derivative shall disclose the unamortized balances in IMR from these allocations separately between gains and losses.

b. Reporting entities shall complete a note disclosure that details the following:

i. Net negative (disallowed) IMR in aggregate and allocated between the general account, insulated separate account and non-insulated account,

ii. Amounts of negative IMR admitted in the general account and reported as an asset in the separate account insulated and non-insulated blank,

iii. The calculated adjusted capital and surplus per paragraph 9.a., and

iv. Percentage of adjusted capital and surplus for which the admitted net negative (disallowed) IMR represents (including what is admitted in the general account and what is recognized as an asset in the separate account).

c. Reporting entities shall include a note disclosure that attests to the following statements:

i. Fixed income investments generating IMR losses comply with the reporting entity's documented investment or liability management policies,

ii. IMR losses for fixed income related derivatives are all in accordance with prudent and documented risk management procedures, in accordance with a reporting entity's derivative use plans and reflect symmetry with historical treatment in which unrealized derivative gains were reversed to IMR and amortized in lieu of being recognized as realized gains upon derivative termination.

iii. Any deviation to 13.c.i was either because of a temporary and transitory timing issue or related to a specific event, such as a reinsurance transaction, that mechanically made the cause of IMR losses not reflective of reinvestment activities.

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iv. Asset sales that were generating admitted negative IMR were not compelled by liquidity pressures (e.g., to fund significant cash outflows including, but not limited to excess withdrawals and collateral calls).

INT 23-01 Status

14. The consensuses in this interpretation were adopted on August 13, 2023, to provide limited-time exception guidance to SSAP No. 7 and the annual statement instruction for the reporting of net negative (disallowed) IMR. The provisions within this interpretation are permitted as a short-term solution until December 31, 2025, and will be automatically nullified on January 1, 2026.

15. The effective date of this interpretation may be adjusted (nullified earlier or with an extended effective date timeframe) in response to Statutory Accounting Principles (E) Working Group actions to establish statutory accounting guidance specific to net negative (disallowed) IMR.

16. No further discussion is planned.

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Application Guidance for Admitting / Recognizing Net Negative (Disallowed) IMR

General Account:

1. Net negative IMR in the general account that exceeds net positive IMR in the separate accounts is considered "disallowed" general account IMR. (Determination of the disallowed IMR in the general account shall be compared against the aggregate IMR balance in all separate accounts.)

2. Net negative disallowed IMR in the general account shall be reported as an aggregate write-in for other-than-invested assets as "Admitted Disallowed IMR" on line 25 of the asset page and nonadmitted. The change in nonadmittance shall be reported on line 41 in the summary of operations.

3. To the extent the reporting entity is permitted to admit net negative disallowed IMR pursuant to the provisions in this interpretation, the reporting entity shall admit the disallowed IMR reported on line 25 of the asset page to the extent permitted, with the change in nonadmittance reflected on line 41 in the summary of operations.

4. Reporting entities shall report an amount equal to the general account admitted net negative (disallowed) IMR as an aggregate write-in for special surplus funds (line 34 of the Liabilities, Surplus an Other Funds page) named as "Admitted Disallowed IMR."

5. Reporting entities shall include note disclosures in the quarterly and annual financial statements as required in paragraph 13 of the interpretation.

Separate Account:

6. Net negative IMR in the separate account (aggregated IMR in both insulated and non-insulated separate accounts) that exceeds net positive IMR in the general account is considered "disallowed" separate account IMR. If the aggregate separate account IMR is positive, with a negative IMR in the insulated separate account and positive IMR in non-insulated separate account (or vice versa), then the negative IMR in the insulated separate account is not permitted to be reported as an asset. In those situations, the separate account has an aggregate positive IMR balance.

7. Net negative (disallowed) IMR in the separate account permitted to be recognized as an asset, as the admittance in the general account did not utilize the full percentage of adjusted capital and surplus permitted within this interpretation, shall be proportionately divided between insulated and non-insulated separate accounts if both separate accounts are in a negative position. If the separate account IMR is an aggregate net negative, but only one separate account blank is in a negative position, then only the separate account blank with a net negative position can recognize disallowed IMR as an asset.

8. If negative IMR in the separate account has previously been recognized as a direct charge to surplus, the reporting entity shall recognize an asset as an aggregate write-in for other-than-invested assets as "Recognized Disallowed IMR" on line 15 of the separate account asset page, with an offsetting credit to surplus. This credit to surplus shall reverse the charge previously recognized. This process shall continue in subsequent quarters if additional separate account IMR is permitted as an asset to the extent IMR was previously taken as a direct charge to surplus. Once prior surplus impacts have been fully eliminated, then the entity shall follow the guidance for new net negative (disallowed) IMR as detailed in the following paragraph. If subsequent quarters result with a decline in the permitted IMR asset in the separate account, then the asset shall be credited with an offsetting charge to surplus.

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9. If the reporting entity enters a net negative (disallowed) IMR position (meaning, there has not been a prior charge to surplus for net negative (disallowed) IMR), then the entity shall recognize the asset as an aggregate write-in for other-than-invested assets as "Disallowed IMR" on line 15 of the separate account balance sheet, with an offsetting credit to IMR (line 3 of the liability page) until the IMR liability equals zero. This process shall continue in subsequent quarters if additional net negative IMR is generated from operations and is permitted as an asset under the provisions of this interpretation. If subsequent quarters result with a decline in the permitted IMR asset in the separate account, then the asset shall be credited with an offsetting charge to surplus.

10. Reporting entities shall report an amount equal to the asset recognized reflecting net negative (disallowed) IMR as an aggregate write-in for special surplus funds (line 19) (named as "Recognized Disallowed IMR." This shall be included in each separate account statement (insulated and non-insulated) if net negative disallowed IMR is recognized as an asset in that statement.

11. Reporting entities shall include note disclosures in the quarterly and annual financial statements as required in paragraph 13 of the interpretation.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax

INT 23-03 Dates Discussed
August 13, 2023; September 21, 2023

INT 23-03 References

Current:
SSAP No. 4—Assets and Nonadmitted Assets
SSAP No. 9—Subsequent Events
SSAP No. 101—Income Taxes

INT 23-03 Issue

Key Provisions of the Inflation Reduction Act

1. The Inflation Reduction Act (Act) was enacted on August 16, 2022, and included a new corporate alternative minimum tax (CAMT). The CAMT is effective for tax years beginning after 2022. Reporting entities shall refer to the Act and the resulting regulations and other tax guidance to determine application, but a high-level summary of the CAMT is below.

a. The tentative CAMT is 15% of the corporation's "adjusted financial statement income" for the tax year, reduced by corporate alternative minimum foreign tax credit.

b. The CAMT differs from the previous traditional alternative minimum tax that applied under pre-2018 tax law in that it starts at a financial statement measure (book income) – not an Internal Revenue Code taxable income calculation. Adjusted financial statement income does not include other comprehensive income including unrealized gains and losses on available for sale securities. The determination of whether the CAMT applies is made on a tax-controlled group basis (scope determination), the tentative CAMT is based on the group's adjusted financial statement income (not adjusted regular taxable income), and any tax due (liability determination) is based on a comparison of consolidated tentative CAMT to consolidated regular tax (non-CAMT).

c. The CAMT applies only to corporations (determined on a tax-controlled group basis as defined for federal income tax purposes, this could include standalone unaffiliated entities which meet the specified income thresholds – see paragraph 3) with average annual adjusted financial statement income in excess of $1 billion for three prior taxable years. The threshold is reduced to $100 million in the case of certain foreign-owned corporations. A corporation that meets the applicable threshold is an "applicable corporation." Applicable corporations generally remain applicable corporations for subsequent taxable years unless certain limited exceptions apply. Applicable corporation status means that CAMT must be tentatively determined and compared to regular (non-CAMT) tax liability.

d. A corporation's adjusted financial statement income is the amount of net income or loss the corporation reports on its applicable financial statement. The income is adjusted for various purposes including certain adjustments in the case of consolidated returns or for foreign income.

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e. The Act includes references to the tax code which provides a hierarchy for determining the applicable financial statement. At a high level, the first choice is U.S. generally accepted accounting principles (GAAP) financial statements; the second choice is international financial reporting standards (IFRS) financial statements. If GAAP and IFRS financial statements are not available, the financial statements filed by the taxpayer with any other regulatory or government body are acceptable. If the taxpayer is part of a tax-controlled group of corporations, the group's applicable financial statement is the applicable financial statement for each member of the group.

f. To determine its U.S. federal income tax liability, an applicable corporation will need to compute taxes under both systems – the regular tax system and the CAMT system. The CAMT is payable to the extent the tentative CAMT exceeds the sum of the regular corporate income tax plus base erosion and anti-abuse tax (BEAT) liability.

g. Any CAMT paid is available indefinitely as a credit carryover that would reduce future regular tax in future years when the regular tax liability is in excess of the tentative CAMT liability. That is, the CAMT credit can be used to reduce the regular tax but not below tentative CAMT liability.

h. A foreign tax credit (FTC) may reduce the tentative minimum CAMT. Note that unused FTCs may be carried forward for 5 years. General business credits can generally offset up to 75% of the sum of regular and minimum tax.

2. This interpretation is focused on addressing accounting and reporting aspects of the CAMT. As most reporting entities will not be above the applicable corporation threshold and will not be subject to the CAMT calculation, this guidance has been developed as an interpretation. While most insurers will not be applicable corporations, this interpretation provides comprehensive statutory accounting guidance for all reporting entities with respect to the CAMT. This interpretation incorporates a principles-based approach for purposes of statutory accounting for the CAMT.

3. Although it is likely that most insurers that are applicable corporations will be members of a tax-controlled group of corporations and included in a consolidated federal income tax return with other members of the group, this interpretation applies to all reporting entities subject to the CAMT, whether an unaffiliated corporation[1] that files a separate tax return, a member of a tax-controlled group not included in the common parent company's consolidated tax return that files a separate company tax return or a separate consolidated tax return with other members of the group, or as a member of the common parent's consolidated return group.

4. For reporting entities that are included in a consolidated tax return, the fundamental statutory tax accounting issue for the CAMT is how to reflect in the reporting entity's separate company financial statements a portion of what is essentially an add-on tax for a consolidated tax return group that is based on the group's financial statement income and group tax rate. Even if a member of a tax-controlled group of corporations files its own separate federal income tax return, the tax law does not provide for a separate company scope determination, but rather looks to the tax-controlled group for applicable corporation status and determination of the applicable financial statement.

INT 23-03 Discussion

5. The discussion along with the Statutory Accounting Principles (E) Working Group tentative consensuses are included below.

[1] As used herein, an "unaffiliated" corporation is one that is not a member of a tax-controlled group.

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Categories of Reporting Entities

6. In an annual determination of applicable corporation status, all reporting entities are separated into one of the following categories:

a. Nonapplicable reporting entities

b. Applicable reporting entities

c. Applicable reporting entities with tax allocation agreement (also called tax sharing agreements) exclusions

Nonapplicable Reporting Entities

7. Nonapplicable reporting entities are reporting entities that do not reasonably expect to be an applicable corporation either as a member of a tax-controlled group of corporations[2] or individually as an unaffiliated corporation, for the taxable year that includes the current reporting period. Nonapplicable reporting entities are not required to calculate or recognize a payable for CAMT. If a reporting entity is not subject to pay CAMT, then they will have no CAMT credit carryforward. For nonapplicable reporting entities, further assessment of the CAMT is not required for current or deferred tax computations, and the remaining accounting components of the interpretation do not apply. Applicable disclosures are required.

8. A reporting entity that was an applicable corporation for the preceding taxable year shall reasonably expect to be an applicable corporation for the current taxable year, unless one of the tax law exceptions to continued applicable corporation status applies.

Applicable Reporting Entities

9. Applicable reporting entities are reporting entities that reasonably expect to be applicable corporations for the taxable year that includes the current reporting period, either individually as an unaffiliated corporation or as a member of a tax-controlled group of corporations[3]. Applicable reporting entities are required to consider CAMT in current and deferred tax computations in the manner set forth in this interpretation.

10. Because CAMT is not payable by an applicable corporation unless it is in excess of regular tax liability, the CAMT calculations for applicable reporting entities within this interpretation may or may not result in different current and deferred income taxes than if the CAMT was not taken into account. (Applicable reporting entities with tax allocation agreement exclusions that meet the requirements of paragraph 11 of this interpretation shall follow the guidance in paragraph 12 of this interpretation.)

Applicable Reporting Entities with Tax Allocation Agreement Exclusions

11. Applicable reporting entities with tax allocation agreement exclusions are reporting entities that qualify as an applicable corporation as a member of a tax-controlled group of corporations pursuant to

[2] A reporting entity that is a member of a tax-controlled group that does not reasonably expect to be applicable corporation on a group basis is not required to make a separate company determination as the CAMT is determined on a group basis.

[3] Determination of applicable reporting entity within a tax-controlled group is subject to the tax law. A reporting entity within a tax-controlled group is captured with the group's applicable corporation status regardless of if they were excluded from the consolidated tax return and filed their own separate return. For example, if the reporting entity is a life insurance company and i) the group has not made a "life-nonlife" consolidated return election, or ii) the reporting entity has been recently acquired and is excluded from the life-nonlife consolidated return for a period of 5 years.

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paragraphs 9 and 10 of this interpretation, and is a party to a tax allocation agreement that is in effect for the reporting period that has all of the following terms:

a. The reporting entity is excluded from charges for any portion of the group's CAMT, and

b. The reporting entity is not allocated any portion of the group's CAMT credit carryover.

12. Reporting entities with tax allocation agreement exclusions which qualify under paragraph 11 of this interpretation, are not required to calculate, or recognize CAMT in their current or deferred tax computations. Even with the tax allocation agreement exclusions, the general current tax liability guidance pursuant to *SSAP No. 101—Income Taxes*, paragraph 3 continues to apply. This guidance requires the reporting entity to recognize the amount the reporting entity has paid or is payable, which includes any additional amount the reporting entity expects to pay on behalf of its co-obligors.

Accounting for Applicable Reporting Entities

Impact of Tax Allocation Agreements

13. This interpretation is based on the principle that the statutory accounting for the CAMT for reporting entities included in a consolidated tax return should be matched to the CAMT charges reasonably estimated to be paid by the reporting entity and the corresponding CAMT credits reasonably estimated to be received by the reporting entity. For such reporting entities, this interpretation applies the provisions of the intercompany tax allocation agreement[4] (also referred to as a tax sharing agreement) that governs allocation of consolidated taxes to individual members of the group.

14. SSAP No. 101, paragraph 16 provides that in the case of a reporting entity that files a consolidated income tax return with one or more affiliates, income tax transactions between the affiliated parties shall be recognized if such transactions are economic transactions as defined in *SSAP No. 25—Affiliates and Other Related Parties*; are pursuant to a written tax allocation agreement; and income taxes incurred are accounted for in a manner consistent with the principles of FAS 109 the predecessor of what is now ASC 740, as modified by SSAP No. 101.

15. For a reporting entity that is included in a consolidated tax return and is subject to a qualifying tax allocation agreement which is consistent with paragraphs 16 and 17 of SSAP No. 101, the amount of CAMT payable (expense) or CAMT credit carryforward is recognized in accordance with the tax allocation agreement.

Recognition of CAMT Payable

16. Reporting entities that are applicable corporations, excluding those having qualifying tax allocation agreement exclusions per paragraph 11 of this interpretation, are required to take CAMT payable into account in the calculation of current income tax expense pursuant to SSAP No. 101. Reporting entities shall accrue the CAMT owed, reflecting the amount owed as a separate return filer or in accordance with the amount allocated through the consolidated tax return group's tax sharing agreement pursuant to paragraph 15 of this INT.

[4] SSAP No. 101, paragraphs 16 and 17 provide requirements for tax allocation agreement recognition. Tax allocation agreements are also subject to internal revenue service requirements and are subject to domiciliary regulator review under the Insurance Holding Company System Regulatory Act (Model #440), which also requires that the terms of intercompany agreements be fair and reasonable. In assessing fair and reasonable, state insurance regulators are encouraged to assess the terms of the TSA for allocations to the insurance reporting entity for both CAMT payables and CAMT credit carryforwards.

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17. Consistent with SSAP No. 101, paragraph 8, changes in deferred tax assets (DTAs) and deferred tax liabilities (DTLs), including changes attributable to changes in tax rates and changes in tax status, if any, shall be recognized as a separate component of gains and losses in unassigned funds (surplus) as "change in net deferred income tax," excluding any change reflected in unrealized capital gains.

18. Paragraph 8.3 of SSAP No. 101 Exhibit A – Implementation Questions and Answers (Q&A) is not applicable to reporting entities subject to CAMT through a tax-controlled group structure. This exclusion is provided due to the consolidated nature of the CAMT calculation. Any theoretical separate entity calculation of the CAMT liability may be unrelated to the actual consolidated tax return computations and to the tax allocation agreement allocation of liability.

Recognition of CAMT Credit Deferred Tax Asset

19. Reporting entities shall recognize a corresponding DTA which represents the non-expiring tax credit carryforward equal and offsetting to the current CAMT accrued. The CAMT credit can be used to reduce regular tax in future years when the regular tax liability is in excess of the tentative CAMT liability as permitted under the tax law. The CAMT credit carryforward is a type of deferred tax asset.

Impact of CAMT to the Statutory Valuation Allowance

20. *SSAP No. 101—Income Taxes*, paragraph 7.e. requires the statutory valuation allowance adjustment as a direct reduction in the gross DTA if, based on the weight of available evidence, it is more likely than not that some or all of the gross DTAs will not be realized. Gross DTA less the statutory valuation allowance results in adjusted gross DTAs. The statutory valuation allowance adjustment is not reported as a separate line in the statutory financial statements (it is an off-balance sheet item that reduces the gross DTAs). The statutory valuation allowance is disclosed.

21. The determination of a statutory valuation allowance[5] for CAMT credit deferred tax assets depends on whether the reporting entity is part of a consolidated tax return group or a separate tax return filer:

a. Consolidated Tax Return Group: A reporting entity that is an applicable entity and a member of consolidated tax return group shall utilize the statutory valuation assessment for the CAMT credit deferred tax assets completed at the consolidated tax return group level. A reporting entity is not required to adjust the group statutory valuation allowance for CAMT credit deferred tax assets. Rather, the group determined statutory valuation allowance and the resulting credit deferred tax asset deemed to be more likely than not to be realized, is permitted to be allocated (consistent with tax allocation agreement) to the reporting entity and reflected as an CAMT credit adjusted gross DTA. The reporting entity shall continue to have a separate statutory valuation allowance calculation for non-CAMT deferred tax assets as required under SSAP No. 101. The combination of the CAMT credit adjusted gross deferred tax asset (as received from the group) and the adjusted gross deferred tax assets from non-CAMT deferred tax assets shall equal the total adjusted gross deferred tax assets reviewed for admittance within the scope of this interpretation.

b. Separate Tax Return Filer: A reporting entity that is an applicable entity and files a separate tax return, is required to complete a statutory valuation allowance for all deferred tax assets, including CAMT credit deferred tax assets, in determining their total adjusted gross DTAs. (The CAMT credit deferred tax assets can be assessed separately from non-

[5] Although reporting entities may conclude that the non-expiring CAMT DTA more likely than not will ultimately be realized, reporting entities will not be able to utilize the tax credit until the reporting entity if a separate tax return filer, or the tax consolidated group of corporations if the reporting entity is a member of such group , are no longer CAMT payors and have sufficient tax liability that permits the group the ability to use the CAMT credits.

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CAMT deferred tax assets in determining whether the deferred tax asset is more likely than not to be realized.) The total adjusted gross deferred tax assets are then reviewed for admittance within the scope of this interpretation.

22. A reporting entity is allowed an accounting policy election to either consider or disregard CAMT when evaluating the need for a valuation allowance for its non CAMT deferred tax assets.[6] The accounting policy election applies for valuation allowance purposes only – that is, in the determination of adjusted gross deferred tax assets other than the CAMT credit deferred tax assets. This accounting policy election cannot be used to avoid a valuation allowance analysis for CAMT credit DTAs. The accounting policy election must be disclosed in the notes to the financial statements and applied consistently in subsequent reporting periods.

Admissibility

Admittance - Implications of Group Tax Assessment (Related Parties)

23. For reporting entities that are applicable corporations as they are a member of a tax-controlled group of corporations, the reporting entity may be subject to the CAMT, or be hindered from utilizing the CAMT credit, through the actions of their consolidated tax return group related parties. (As noted in footnote 5, although a reporting entity may have earned an non-expiring tax credit through payment of CAMT, the reporting entity is not eligible to utilize that tax credit until the consolidated tax return group has sufficient tax liability that allows the members of the group to utilize their tax credit. This means that on a group basis they are no longer CAMT payors.) *SSAP No. 4—Assets and Nonadmitted Assets* requires assets that are restricted by the action of a related party to be nonadmitted assets.

> SSAP No. 4, Footnote 2: If assets of an insurance entity are pledged **or otherwise restricted by the action of a related party, the assets are not under the exclusive control of the insurance entity and are not available to satisfy policyholder obligations due to these encumbrances or other third-party interests. Thus, pursuant to paragraph 2, such assets shall not be recognized as an admitted asset on the balance sheet.** Additional guidance for assets pledged as collateral is included in INT 01-31.

24. A key focus of this interpretation is the admittance of the CAMT deferred tax assets (credits). However, it is recognized that under the existing statutory accounting guidance in SSAP No. 4 a reporting entity recognizing CAMT credit deferred tax assets would not be permitted to admit those deferred tax assets if as part of a consolidated tax return group the ability to receive those CAMT credits is explicitly linked to the actions of other entities within the group. If the group on a collective basis does not incur enough tax to allow utilization of the tax credits, then the reporting entity cannot use the tax credits, regardless of the income or tax paid by the reporting entity. This aspect is not impacted by the tax sharing agreement. Although the tax sharing agreement may specify how the CAMT credits will be allocated among the group, such tax credits allocated to the reporting entity can only be realized when the group qualifies for the credit.

25. For the CAMT credit adjusted gross deferred tax assets allocated to the reporting entity to be eligible to be admitted, this interpretation provides an exception to the guidance in SSAP No. 4, footnote 2, recognizing that the impact to ultimately utilize the allocated tax credits is dependent on the actions of the other parties within the group.

[6] SSAP No. 101, FAS 109 and ASC 740 do not specifically address whether future years' CAMT should be anticipated in a valuation allowance assessment for non-CAMT DTAs. Accordingly, an accounting policy election is allowed for GAAP purposes as to whether to consider or disregard CAMT when evaluating the need for a valuation allowance for non-CAMT DTAs.

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Admittance – Adjusted Gross DTAs

26. The guidance in SSAP No. 101 allows admittance of adjusted gross DTAs (gross DTAs reduced by the statutory valuation allowance) pursuant to a three-component calculation, for which the second step limits admittance of adjusted gross DTAs to those that are expected to be realized in a timeframe that does not exceed three years. The actual number of years to realization permitted depends on specifics for each reporting entity (type and other information about the reporting entity), but the maximum timeframe is three years. The last step (SSAP No. 101, paragraph 11.c.) admits DTAs which can be offset by DTLs.

27. Due to the following aspects regarding the CAMT credits, specific admittance guidance for the CAMT credit DTAs has been established:

a. The CAMT credit is a tax credit DTA that does not expire. As long as the reporting entity is a CAMT payor or is part of a tax-consolidated group that is a CAMT payor, the reporting entity cannot utilize the tax credit.

b. The ability to utilize the CAMT credit is contingent on the actions and tax paying behaviors of the consolidated tax return group. Although the reporting entity may be paying sufficient tax above the CAMT threshold, if other parties within the group do not act in a similar manner, putting the group below the CAMT threshold, then the CAMT credit cannot be utilized by the reporting entity.

28. With these noted limitations in utilization of the earned tax credits, reporting entities are only permitted to admit CAMT credits if the reporting entity tax projections (if a separate tax return filer) or projections of the tax-consolidated group (if a member of such group) indicate that the CAMT credit will be realizable within the stated timeframes using the applicable SSAP No. 101, paragraph 11 realization table thresholds[7]. This means that the tax projections will have sufficient tax liability that permits utilization of the CAMT credits. For example, a reporting entity with greater than 300% ExDTA ACL RBC can only admit CAMT credits that are expected to be realized (consistent with the tax allocation agreement) in three years. Reporting entities that have ExDTA ACL RBC between 200-300% can only admit CAMT credits that are expected to be realized in one year. If a reporting entity cannot project (either on its own if a separate return filer or at the group if a consolidated tax return group member) sufficient tax liability that allows them to utilize the CAMT credit within the applicable realizable timeframes for admittance, then the portion of CAMT credits that cannot be utilized are required to be nonadmitted under SSAP No. 101, paragraph 11.b.

29. CAMT credits included in the SSAP No. 101, paragraphs 11 and 11.b. calculation as they are expected to be realized within the applicable 1 or 3 year permitted timeframes shall then be combined with non-CAMT adjusted gross deferred tax assets and admitted to the extent that the total DTAs admitted under paragraph 11.b. do not exceed the capital and surplus percentage limit for the company type. All references to SSAP No. 101, paragraph 11.b. include the modifications in this Interpretation.

30. Reporting entities shall use the Realization Threshold Limitations Tables in SSAP No. 101, paragraph 11.b. as applicable to the entity for determination of the admissibility of the CAMT credits. The percentage limitations of capital and surplus of and the projected realization periods continue to apply to admitted adjusted gross DTAs, including the adjusted gross DTA for any CAMT credit DTA.

31. A reporting entity which meets or exceeds the top line of the applicable of the Realization Threshold Limitation Table (Ex. 3 years and 15%) is **not required** to take the CAMT into account in calculating the

[7] The examples in this paragraph reference Ex-DTA ACL RBC, however, SSAP No. 101, paragraph 11.b. also includes realization threshold tables which apply to non-RBC filers.

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"with and without[8]" tax liability for purposes of determining the amount expected to be realized under SSAP No. 101, paragraph 11.b. for non-CAMT DTAs. Specifically, the reporting entity's "with and without" regular tax liability is not reduced by CAMT, if any, reasonably expected to be incurred during the SSAP No. 101, paragraph 11.b. applicable period. In the case of a reporting entity included in a consolidated federal income tax return, the amount expected to be incurred refers to the portion of the consolidated CAMT, if any, reasonably expected to be allocable to the reporting entity pursuant to the group's tax allocation agreement. However, any admitted CAMT credits in this step must be realizable within the applicable time period specified in the applicable Realization Threshold Limitation Table (Ex, top line - 3 years), determined consistent with the tax allocation agreement. The post-valuation allowance adjusted gross DTA for any CAMT credit DTA is admitted following the guidance in SSAP No. 101, paragraph 11.b.i. as modified by this Interpretation. The 15% limitation of capital and surplus which is provided in SSAP No. 101, paragraph 11.b.ii. continues to apply to admitted adjusted gross DTAs, including the adjusted gross DTA for any CAMT credit DTA.

32. A reporting entity which meets the second line of the applicable Realization Threshold Limitation Table (Ex. 1 year and 10%), the amount expected to be realized under SSAP No. 101, paragraph 11.b.i. within the applicable period determined under paragraph 11.b. **is based** on the reporting entity's "with and without" regular tax liability reduced by CAMT, if any, reasonably expected to be incurred during the paragraph 11.b. applicable period. In the case of a reporting entity included in a consolidated federal income tax return, the amount expected to be realized is reduced by the portion of the consolidated CAMT, if any, reasonably expected to be allocable to the reporting entity pursuant to the group's tax allocation agreement. CAMT credit utilization during the applicable period is recognized based on the same principles, – that is, as an admitted DTA. The purpose of these computations is to account for CAMT in deferred taxes in the same manner as CAMT would be reflected in current taxes.

33. A reporting entity which meets or is below the third line of the applicable Realization Threshold Limitation Table (Ex. 0 years and 0%), is not permitted to admit either CAMT credit DTAs or non-CAMT DTAs under SSAP No. 101, paragraph 11.b.

34. The adjusted gross DTA for any CAMT credit carryforward which does not qualify for admission under SSAP No. 101, paragraph 11.b. is permitted to be recognized as an offset against DTLs in accordance with SSAP No. 101, paragraph 11.c. The reporting entity shall admit the remaining amount of adjusted gross DTAs, after application of paragraphs 11.a. and 11.b. that can be offset against existing gross DTLs. The reporting entity shall consider the character (i.e., ordinary versus capital) of the DTAs and DTLs such that offsetting would be permitted in the tax return under existing enacted federal income tax laws and regulations.

Admittance - Projections

35. Projections of CAMT liability, if any, (and CAMT credit utilization) during the applicable period involve forward-looking data, groupings, of assets and liabilities, estimates and other adjustments for both the reporting entity and the group of which it is a member. The manner in which this is done shall be conducted in a reasonable and consistent manner. A reporting entity shall retain internal documentation to support these computations and the methodologies so employed. Modifications to the estimation methodology are permitted should events or circumstances change from a previous period – such as a change in materiality or administrative costs associated with the computations, or system changes that affect the level of detail available. Entities that make such modifications should be prepared to rationalize the

[8] "With and without" is further described in SSAP No. 101.

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changes. Disclosure of material modifications, and the general reason for such, should be made in the notes to the financial statements.[9]

Admittance - Tax Planning Strategies

36. SSAP No. 101 provides that tax-planning strategies are required to be considered in the valuation allowance analysis and may be considered in determining the admission of DTAs under SSAP No. 101, paragraph 11. For reporting entities that are part of a consolidated tax return group, tax planning strategies impacting the CAMT are determined at a group level, as long as the tax planning strategies at the group level do not conflict with tax planning strategies at the reporting level and vice versa. For reporting entities that are separate tax return filers, a reporting entity must consider tax-planning strategies in making the valuation allowance analysis required under this interpretation.

Transition Guidance

37. Even though the CAMT was enacted in 2022 and generally became effective January 1, 2023, the requirements for statutory tax accounting for the CAMT have effectively been deferred by INT 22-02. This paragraph provides the applicable transition rules for year-end 2023 statutory accounting for requests for a timely-filed tax allocation agreement amendment or a new tax allocation agreement for the 2023 taxable year.

a. Because the CAMT was newly enacted effective for 2023, tax allocation agreements in effect for periods prior to the 2023 taxable year include no explicit provisions relating to the CAMT. Thus, applicable reporting entities (with and without tax allocation agreement exclusions) may need to amend tax allocation agreements to deal with the CAMT effective for the entire 2023 taxable year. A reporting entity would file a request for amendment to a tax allocation agreement or a new tax allocation agreement on Form D – Prior Notice of a Transaction as required under the *Insurance Holding Company System Regulatory Act* (Model #440) and the related regulation, (Model #450) with its applicable domiciliary regulator(s) and commercial domiciliary regulator(s).

b. Time is of the essence in both requesting and approving tax allocation agreement amendments or a new tax allocation agreement relating to the CAMT for the 2023 taxable year to be applicable to the 2023 reporting period. Accordingly, if, a reporting entity files the applicable Form D request(s) for tax allocation agreement amendment or a new tax allocation agreement prior to the end of 2023 to address the CAMT for 2023 and subsequent taxable years, and the domiciliary regulator has confirmed in writing that they have no objections to using the new tax allocation agreement amendment or new tax allocation agreement, while under review. The reporting entity shall be allowed to account for the tax allocation agreement as applicable for the entire 2023 reporting period.

c. If the final approved tax allocation agreement differs in its treatment of the CAMT allocation from the tax allocation agreement originally requested on the Form D, the difference shall be recorded as follows:

    i. If Form D approval occurs subsequent to the balance sheet date, but before the issuance of the statutory financial statements and before the date the audited financial statements are issued, or available to be issued, such approval shall be considered a Type I subsequent event within the meaning of *SSAP No. 9—Subsequent Events*.

[9] See paragraph 2.9 of the *SSAP No. 101 Q&A* for similar requirements in the context of grouping of assets and liabilities for measurement.

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ii. If the Form D approval occurs after the period which defines a subsequent event in SSAP No. 9, the difference created by such approval shall be recognized and disclosed in the period in which the approval is given.

d. The transition guidance in paragraph 37 does not apply to a reporting entity that does not file a Form D request for a CAMT-related tax allocation agreement amendment or a new tax allocation agreement prior to the end of 2023.

38. Consistent with *SSAP No. 3—Accounting Changes and Corrections of Errors,* paragraph 4, initial application of this interpretation shall not be considered a change in accounting principle, but instead application of a new principle for the first time.

Disclosures

39. The reporting entity shall disclose whether it is a nonapplicable reporting entity; an applicable reporting entity with tax allocation agreement exclusions or an applicable reporting entity.

40. Additionally, the following disclosures shall be made in the notes to the financial statements of applicable reporting entities (which do not have tax allocation agreement exclusions in accordance with paragraph 11 of this interpretation):

a. If the reporting entity has made an accounting policy election to either consider or disregard CAMT when evaluating the need for a valuation allowance for its non-CAMT DTAs described in paragraph 22 of this interpretation.

b. Any disclosure of material modifications to the methodology used to project CAMT as required by paragraph 35 of this interpretation.

41. Relevant disclosures required by SSAP No. 101 also apply to, including but not limited to, the following:

a. The disclosure of the statutory valuation allowance as required by SSAP No. 101, paragraph 21.

b. The disclosure of tax planning strategies is required by SSAP No. 101. In the disclosure required by SSAP No. 101, paragraph 28.b., a statement as to whether the reporting entity may be charged with a portion of CAMT incurred by the consolidated group (or credited with a portion of the consolidated group's CAMT credit utilization).

c. Inclusion of CAMT credit DTAs, if any, in the disclosure required by SSAP No. 101, paragraph 26.a. regarding the origination dates and expiration of tax credit carry forwards.

d. The impact of CAMT planning strategies, if any, in the disclosure required by SSAP No. 101, paragraph 22.f.

INT 23-03 Status

42. The consensuses in this interpretation are effective beginning with year-end 2023 financial statements and periods thereafter.

43. No further discussion is planned.

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Examples

Basic Facts Used in All Examples

44. The reporting entity is a member of a tax-affiliated group of corporations that files consolidated federal income tax returns which reasonably expects to be an applicable corporation for 20X3.

a. Reporting entity also has $200x of non-CAMT adjusted gross DTAs (i.e., has already reduced by any required valuation allowance of $40x). Of this $200x of which $150x reverses over the 3-year applicable period 20X4-20X6 and is expected to be realized.

b. At the end of 20X3, reporting entity has a $50x CAMT credit DTA (pursuant to the consolidated group's tax allocation agreement, reporting entity was allocated a portion of the group's expected 20X3 current CAMT expense, which reporting entity included in its 20X3 current tax expense).

c. The consolidated group of which the reporting entity is a member establishes a $20x valuation allowance against its $50x CAMT credit DTA, resulting in a CAMT adjusted gross DTA of $30x that is more likely than not to be realized.

d. The reporting entity makes an accounting policy election to disregard CAMT when evaluating the need for a valuation allowance for its non-CAMT DTAs.

e. Reporting entity’s capital and surplus for purposes of calculating the limitation under SSAP No. 101, paragraph 11.b. ii. is $2,000. Therefore, the 15% of surplus limitation is $300 (based on the top line of the applicable SSAP No. 101 paragraph 11.b. realization threshold limitation table), the 10% limitation is $200 (based on the second line of the applicable SSAP No. 101 paragraph 11.b. realization threshold limitation table).

f. For the purposes of these examples any DTA admittance under SSAP No. 101, paragraphs 11.a. and 11.c. is ignored.

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Example 1 – Applicable reporting entity meets or exceeds the top line of the relevant SSAP No. 101, paragraph 11.b. Realization Threshold Limitation table (Ex. 3 years, 15%).

45. The basic facts above apply with the following additional information:

a. For 20x3, the reporting entity exceeds the first line of the applicable realization threshold limitation in SSAP No. 101, paragraph 11.b. for use of a 3-year applicable period and the limitation of capital and surplus is 15%. Pursuant to paragraph 31 of this interpretation, the reporting entity would not have to take the CAMT into account in calculating the "with and without" tax liability for purposes of determining the amount expected to be realized under SSAP No. 101, paragraph 11.b.i.

b. The consolidated tax return group has assessed and determined that the CAMT credit DTA amounts after the valuation allowance of $30x is expected to be utilized in 20x4and 20x5but $15x of CAMT would be incurred in 20x6.

46. The reporting entity admits the $30x adjusted gross DTA for its portion of the allocated CAMT credit DTA expected to be utilized within three years and admits the $150x non-CAMT adjusted gross DTA after valuation allowance than can be utilized within three years. Therefore, the admitted non-CAMT DTA and admitted CAMT credit DTA would total $180x ($150 +$30 =$180).

47. Although the consolidated group is expecting to incur CAMT during the 3-year period, the reporting entity does not reduce its non-CAMT admitted DTAs by the $15x the CAMT expected to be allocated under the tax allocation agreement to the reporting entity during the three years (pursuant to paragraph 31 of this Interpretation). Note that if the consolidated tax return group had assessed and determined that only a portion of the CAMT credit DTA after the valuation allowance was expected to be utilized in 20x4 20x5 and 20x6 then the reporting would only admit its allocation (per its tax allocation agreement) of the amount of CAMT credit DTA that will be utilized by the consolidated group during the 3 years.

48. The $180 is less than the $300 15% of surplus limitation in paragraph 11.b.ii., so it is not a limiting factor. (However, if reporting entity's 15% of surplus limitation under paragraph 11.b.ii. was $175x, the reporting entity's admitted adjusted gross DTA would be further reduced to $175).

	DTA	Valuation Allowance	Not Recoverable Within 3 Years	DTA Admitted Standalone	Impact of Consol. DTA	Admitted DTA under 11bi	15% surplus limitation under 11bii	Nonadmitted DTAs
DTAs	240	-40	-50	150		150		50
CAMT credit DTA	50	-20	0		30	30		
totals	**290**	**-60**	**-50**	**150**	**30**	**180**	**300**	**50**

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Example 2 – Applicable entity, that meets level 2 on the relevant SSAP No. 101, paragraph 11.b. Realization Threshold Limitation table (Ex.-1 year 10%).

49. The basic facts above apply with the following additional information:

a. For 20x3, the reporting entity meets the second line of the applicable realization threshold limitation in SSAP No. 101, paragraph 11.b. for use of a 1-year applicable period and the limitation of capital and surplus is 10%. Pursuant to paragraph 32 of this interpretation, the reporting entity would have to also apply the with and without calculation of the determination of the impact of the CAMT on the realization of DTAs.

b. The consolidated group of which the reporting entity is a member expects to incur CAMT in 20x4, of which $10 is expected to be allocated under the tax allocation agreement to reporting entity. The reporting entity reduces its $150x of non-CAMT admitted adjusted gross DTAs by its $10x share of the consolidated CAMT expected to be incurred in 20x4.

50. The reporting entities admitted DTA would be $140x. The result is an adjusted gross non-CAMT DTA of $150x, minus the $10 impact of the consolidated CAMT (with and without) equals 140 admitted DTA.

51. The resulting $140x of DTA admitted under paragraph 11.b.i., which is less than the $200x paragraph is less than the $200 10% of surplus limitation in paragraph 11.b.ii., so it is not a limiting factor.

	DTA	Valuation Allowance	Not Recoverable Within 1 Year	DTA Admitted Standalone	Impact of Consol. DTA and VA	Admitted DTA under 11bi	10% surplus limitation under 11bii	Nonadmitted DTAs
DTAs	240	-40	-50	150	-10	140		60
CAMT credit DTA	50	-20	-30				-	30
totals	**290**	**-60**	**-80**	**150**	**-10**	**140**	**200**	**90**

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Example 3 – Applicable entity with qualifying tax allocation agreement exclusions.

52. The basic facts situation applies.

a. Similar to Example 1, the reporting entity meets the exceeds the first line of the applicable realization threshold limitation in SSAP No. 101, paragraph 11.b. for use of a 3-year applicable period and the limitation of capital and surplus is 15%.

b. The reporting entity is excluded pursuant to the tax allocation agreement from any allocation of CAMT or CAMT credit utilization in a qualifying tax allocation agreement as described in paragraph 11 of this interpretation.

53. Accordingly, the reporting entity for 20x3, would be excluded from the CAMT calculations, and the reporting entity's admitted adjusted gross DTA would be $150x. which is the amount after the valuation allowance of $40 and the $50 reduction for the amount not recoverable within 3 years.

54. The $150 is less than the $300 15% of surplus limitation in paragraph 11.b.ii., so it is not a limiting factor.

	DTA	Valuation Allowance	Not Recoverable Within 3 Years	DTA Admitted Standalone	Impact of Consol. DTA and VA	Admitted DTA under 11bi	15% surplus limitation under 11bii	Nonadmitted DTAs
DTAs	240	-40	-50	150		150		50
CAMT credit DTA	0						-	-
totals	**240**	**-40**	**-50**	**150**		**150**	**300**	**50**

Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 23-04: Scottish Re Life Reinsurance Liquidation Questions

INT 23-04 Dates Discussed
October 23, 2023; October 24, 2023; December 1, 2023; January 10, 2024

INT 23-04 References

Current:
SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance

INT 23-04 Issue

Background

1. Liquidations of U.S. licensed reinsurers are uncommon. Due to a 2023 liquidation order of a U.S.-based life reinsurer, life industry cedents have requested an interpretation to address the accounting and reporting for reinsurance receivables from the reinsurer's estate. This interpretation is intended to be applied generically; however, the following circumstances are relevant to the accounting issues identified.

a. The recent liquidation order was for Scottish Re, a U.S. life reinsurance entity, which was in regulatory supervision for several years.

b. The life reinsurer was not assuming new business but was receiving ongoing premium on yearly renewable contracts.

c. The 2023 liquidation order cancelled reinsurance contracts on a cut-off basis, effective September 30, 2023.

d. Settlement from the reinsurer's estate is expected to exceed one year.

e. Settlement from the reinsurer's estate to the ceding entities is expected to be less than 100%. That is, cedents are expected to receive a portion of what they are owed.

f. Some ceding insurers established trusts to hold assets backing the reserves under the reinsurance agreements.

Interpretation Discussion

2. This interpretation is applicable only to the accounting and reporting of reinsurance recoverables from Scottish Re, a U.S.-based life reinsurer in liquidation. The Statutory Accounting Principles (E) Working Group consensuses to the noted issues are included below.

Issue 1 – Commutation or Recapture of a Life Reinsurance Contract

3. If a liquidation order cancels a life reinsurance contract on a cut-off basis, should the life reinsurance commutation guidance in S*tatement of Statutory Accounting Principle*s (*SSAP) No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* be used as the primary accounting guidance for the commutation?

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4. Yes. SSAP No. 61R, paragraph 58, provides the primary guidance for a life reinsurance commutation. The guidance provides that:

> **Recaptures and Commutations**
>
> 58. A recapture or a commutation of a reinsurance agreement is a transaction which results in the complete and final settlement and discharge of all present and future obligations between the parties arising out of the agreement or a portion of the agreement. Commuted and recaptured balances shall be accounted for by writing them off through the accounts, exhibits and schedules in which they were originally recorded. The assumed reserves and reserve credits taken are eliminated by the reinsurer and ceding entity, respectively. The reinsurer and ceding entity must also make any required IMR liability adjustment changes. Any net gain or loss is reported in the summary of operations.

Issue 2 – Impairment of Reinsurance Recoverables

5. The reinsurer that was previously in regulatory supervision and is now in liquidation was known to have financial difficulties and many ceding entities have either established valuation allowances and/or written off reinsurance recoverables as impairment losses. Questions have been received in response to the diversity in practice on whether the ceding entities were reporting impairment losses or were reporting a valuation allowance on all categories of their expected reinsurance recoverables from the reinsurer which is now in liquidation.

6. Do reporting entities have the choice of setting up a valuation allowance or applying the impairment guidance in SSAP No. 61R to the reinsurance recoverables from the life reinsurer in liquidation?

7. No. Reporting entities do not have a choice of a valuation allowance or applying impairment analysis. SSAP No. 61R, paragraph 42, requires impairment analysis of uncollectible reinsurance amounts in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Asset.* The guidance requires that impaired amounts shall be written off through a charge to the Statement of Operations utilizing the same accounts which established the reinsurance recoverables. SSAP No. 5R and SSAP No. 61R do not permit a valuation allowance.

8. The liquidation order of a reinsurer should prompt an impairment analysis of all amounts recoverable from the reinsurer with a write-off of amounts not expected to be recovered.

9. The impairment analysis shall be updated at every reporting date.

Issue 3 – Reporting of Reinsurance Recoverables

10. The liquidation order results in a commutation and recapture of business for the ceding entity. A liquidation will determine the reinsurer's estate assets, then determine payments based on liquidation priority. This will result in a delay in settlement from the estate of the reinsurer. As previously detailed, the amounts paid by the estate shall be impaired to the amount expected to be received by the ceding entities.

11. Where shall the ceding entity report the remaining receivables for the reinsurer's estate?

12. In accordance with the recapture and commutation guidance in SSAP No. 61R, paragraph 58 (quoted above), the ceding entity shall remove balances through the schedules and exhibits originally reported. No reserve credit or contra-liabilities shall be reported. The reinsurance reserve credits shall be removed. Gains or losses are reported in the summary of operations.

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13. Based on preliminary information received, it is expected that there will be an amount receivable for paid claims incurred before the reinsurance contract cancellation. This amount shall be reported on the asset page line 16.1 - Amounts Recoverable from Reinsurers.

14. Amounts recoverable from the reinsurer's estate for claims incurred before the reinsurance contract cancellation and unpaid as of the reporting date shall be reported on the asset page line 16.3 - Other Amounts Receivable Under Reinsurance Contracts.

15. If the ceding entity owes amounts to the reinsurer's estate, the amounts shall be reported as a liability on line 9.3 - Other Amounts Payable on Reinsurance.

16. After impairing the recoverables, any other amount expected to be recovered from the reinsurer's estate shall be reported on line 25 Aggregate Write-ins for Other Than Invested Assets.

Issue 4 – Admissibility of Reinsurance Recoverables

17. As noted above, quarterly impairment analysis of collectability is required. After evaluating for impairment, if there are remaining receivables from the reinsurer's estate, do those assets qualify as admitted reinsurance recoverable assets?

18. Reinsurance recoverables from Scottish Re in liquidation are admitted as follows:

a. The reinsurance recoverable amount from Scottish Re from paid claims incurred prior to the reinsurance contract cancellation which are reported on the asset page line 16.1 - Amounts Recoverable from Reinsurers which are not in dispute are admitted after impairment review.

b. To the extent reinsurance amounts recoverable are secured by assets in an Appendix A-785 - Credit for Reinsurance compliant trust, such recoverable amounts may be admitted to the extent the that the amounts are not in dispute and that the collateral in an Appendix A-785 compliant trust is sufficient.

19. Other reinsurance recoverables, which are not identified as admitted assets in paragraph 18 are nonadmitted until received. This includes amounts either in dispute or not secured by collateral in a trust that is compliant with Appendix A-785.

Issue 5 – Disclosures

20. Do the relevant disclosures in SSAP No. 61R and other relevant SSAPs apply to a commuted life reinsurance contract which has not been fully settled due to a liquidation?

21. Yes. The relevant disclosures in SSAP No. 61R and other relevant SSAPs continue to apply to a life reinsurance contract which is commuted and recaptured due to a liquidation. These disclosures include but are not limited to the disclosures regarding commutation, uncollectible reinsurance and anything else that is required.

22. Disclosure in the reinsurance notes to the financial statements shall include additional information necessary to obtain an understanding of the impact of Scottish Re reinsurance counterparties in liquidation, including but not limited to, reinsurance payable liabilities, reinsurance recoverables by paid claims and other amounts, information regarding the status of any collateral and its fair value. Where applicable, reporting entities should disclose any individual components (e.g., unreimbursed claims or provisions for future losses) of recoverable amounts that are presented in the aggregate on the financial statements. The

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disclosure shall include measurement, impairment and collectability of any reinsurance recoverables including timing of expected payments and nonadmitted amounts.

INT 23-04 Summary

23. Although readers should refer to the detailed guidance above, a summary of the key provisions is as follows:

a. Issue 1 – Commutation or Recapture of a Life Reinsurance Contract: Follow SSAP No. 61R, paragraph 58, as it provides primary recapture and commutation guidance.

b. Issue 2 – Impairment of Reinsurance Recoverables: SSAP No. 61R paragraph 42, requires impairment of uncollectible reinsurance in accordance with SSAP No. 5R.

c. Issue 3 – Reporting of Reinsurance Recoverables: Follow the recapture and commutation guidance in SSAP No. 61R, then analyze for impairment. Report reinsurance payables separate from reinsurance recoverables. Amounts related to paid and unpaid claims incurred prior to reinsurance contract cancellation are reported on asset page line 16.1 - Amounts Recoverable from Reinsurers and asset page line 16.3 - Other Amounts Receivable Under Reinsurance Contracts, respectively. Any remaining reinsurance recoverables from the reinsurance counterparty after impairment assessment shall be reported on the asset page line 25 Aggregate Write-ins for Other than Invested Assets.

d. Issue 4 – Admissibility of Reinsurance Recoverables: Admit amounts related to claims incurred prior to contract cancellation which have been paid by the reporting entity as of the reporting date (reported on asset page line 16.1 - Amounts Recoverable from Reinsurers) which are not in dispute after impairment review. Admit reinsurance recoverables which are not in dispute, and which are secured by collateral in an A-785 compliant trust. Nonadmit all amounts recoverable from a life reinsurer in liquidation which are either in dispute or which are not secured by collateral in a trust compliant with Appendix A-785.

e. Issue 5 – Disclosures: Follow existing applicable disclosures and provide additional information sufficient to understand the nature and impact of a reinsurance counterparty in liquidation as described in paragraph 22.

INT 23-04 Status

24. The consensuses in this interpretation were adopted on January 10, 2024, with an effective date of reporting periods on or after December 31, 2023.

25. No further discussion is planned.

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NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Accounting Practices and Procedures Manual

As of March 2024

VOLUME II

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APPENDIX D – GAAP CROSS-REFERENCE TO SAP

APPENDIX E – STATUTORY ISSUE PAPERS

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Appendix C
Actuarial Guidelines

Introduction

The NAIC Life Actuarial (A) Task Force and the Health Actuarial (B) Task Force, formerly known as the Life and Health Actuarial Task Force, have been asked on many occasions to assist a particular state insurance department in interpreting a statute dealing with an actuarial topic relative to an unusual policy form or situation not contemplated at the time of original drafting of a particular statute. The Life Actuarial (A) Task Force and the Health Actuarial (B) Task Force, in developing an interpretation or guideline, must often consider the intent of the statute, the reasons for initially adopting the statute and the current situation. The Life Actuarial (A) Task Force and the Health Actuarial (B) Task Force feel that for those situations which are sufficiently common to all states, that the publishing of actuarial guidelines on these topics would be beneficial to the regulatory officials in each state and would promote uniformity in regulation which is beneficial to everyone. To this end, the Life Actuarial (A) Task Force and the Health Actuarial (B) Task Force have developed certain actuarial guidelines and will continue to do so as the need arises. The guidelines are not intended to be viewed as statutory revisions but merely a guide to be used in applying a statute to a specific circumstance.

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
I (AG 1)	Interpretation of The Standard Valuation Law With Respect to the Valuation of Policies Whose Valuation Net Premiums Exceed the Actual Gross Premium Collected	December 1978	Standard Valuation Law	No
II (AG 2)	Reserve Requirements With Respect to Interest Rate Guidelines on Active Life Funds Held Relative to Group Annuity Contracts	December 1978	Standard Valuation Law	No
III (AG 3)	Interpretation of Minimum Cash Surrender Benefit Under Standard Nonforfeiture Law For Individual Deferred Annuities	December 1978	Standard Nonforfeiture Law for Individual Deferred Annuities	No
IV (AG 4)	Actuarial Interpretation Regarding Minimum Reserves For Certain Forms of Term Life Insurance	December 1984	Standard Valuation Law	Yes
V (AG 5)	Interpretation Regarding Acceptable Approximations For Continuous Functions	December 1979	Standard Valuation and Nonforfeiture Laws	No
VI (AG 6)	Interpretation Regarding Use of Single Life or Joint Life Mortality Tables 20 June 1983	December 1979	Standard Valuation and Standard Nonforfeiture Law for Life Insurance	Yes
VII (AG 7)	Interpretation Regarding Calculation of Equivalent Level Amounts	December 1979	Standard Valuation and Nonforfeiture Laws	No
VIII (AG 8)	The Valuation of Individual Single Premium Deferred Annuities	December 1980	Standard Valuation Law	No
IX (AG 9)	Form Classification of Individual Single Premium Immediate Annuities For Application of the Valuation and Nonforfeiture Laws	June 1981	Standard Valuation Law and Standard Nonforfeiture Law for Individual Deferred Annuities	No
IX-A (AG 9-A)	Use of Substandard Annuity Mortality Tables In Valuing Impaired Lives Under Structured Settlements	June 1989	Standard Valuation Law	No

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
IX-B (AG 9-B)	Clarification of Methods Under Standard Valuation Law For Individual Single Premium Immediate Annuities, Any Deferred Payments Associated Therewith, Some Deferred Annuities, and Structured Settlements Contracts	December 1988	Standard Valuation Law	No
IX-C (AG 9-C)	Use of Substandard Annuity Mortality Tables in Valuing Impaired Lives Under Individual Single Premium Immediate Annuities	March 2001	Standard Valuation Law	No
X (AG 10)	Guideline For Interpretation of NAIC Standard Nonforfeiture Law For Individual Deferred Annuities	December 1981	Standard Nonforfeiture Law for Individual Deferred Annuities	No
XI (AG 11)	Effect of an Early Election By an Insurance Company of an Operative Date Under Section 5-C of the Standard Nonforfeiture Law For Life Insurance	December 1982	Standard Nonforfeiture Law for Life Insurance	No
XII (AG 12)	Interpretation Regarding Valuation and Nonforfeiture Interest Rates	June 1983 Withdrawn March 1993	Standard Valuation Law and Standard Nonforfeiture Law for Life Insurance	No
XIII (AG 13)	Guideline Concerning the Commissioners' Annuity Reserve Valuation Method	March 1985	Standard Valuation Law	No
XIV (AG 14)	Surveillance Procedure For Review of the Actuarial Opinion For Life and Health Insurers	December 1985	Instructions for Financial Examiners	No
XV (AG 15)	Illustrations Guideline For Variable Life Insurance Model Regulation	June 1986	Variable Life Insurance Model Regulation	No
XVI (AG 16)	Calculation of CRVM Reserves On Select Mortality and/or Split Interest	December 1986	Standard Valuation Law	No
XVII (AG 17)	Calculation of CRVM Reserves When Death Benefits Are Not Level	December 1986	Standard Nonforfeiture Law for Life Insurance	No

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
XVIII (AG 18)	Calculation of CRVM Reserves On Semi-Continuous, Fully Continuous or Discounted Continuous Basis	December 1986	Standard Valuation Law	No
XIX (AG 19)	1980 CSO Mortality Table With Ten-Year Select Mortality Factors	December 1986	NAIC Procedure for Permitting Same Minimum Nonforfeiture Standards for Men and Women Insured Under 1980 CSO and 1980 CET Mortality Tables Model Regulation	No
XX (AG 20)	Joint Life Functions For 1980 CSO Mortality Table	December 1986	Standard Valuation Law	No
XXI (AG 21)	Calculation of CRVM Reserves When (B) Is Greater Than (A) and Some Rules For Determination of (A)	June 1987	Standard Valuation Law	No
XXII (AG 22)	Interpretation Regarding Nonforfeiture Values For Policies With Indeterminate Premiums	June 1987	Standard Nonforfeiture Law for Life Insurance	No
XXIII (AG 23)	Guideline Concerning Variable Life Insurance Separate Account Investments	June 1987	Variable Life Insurance Model Regulation	No
XXIV (AG 24)	Guidelines For Variable Life Nonforfeiture Values	June 1987	Standard Nonforfeiture Law For Life Insurance and Variable Life Insurance Model Regulation	No
XXV (AG 25)	Calculation of Minimum Reserves and Minimum Nonforfeiture Values For Policies With Guaranteed Increasing Death Benefits Based On an Index	October 2010	Standard Valuation Law	Yes
XXVI (AG 26)	Election of Operative Dates Under Standard Valuation Law and Standard Nonforfeiture Law—June 3, 1989	December 1989	Standard Valuation Law Standard Nonforfeiture Law	No
XXVII (AG 27)	Accelerated Benefits	June 1991	Standard Valuation Law Standard Nonforfeiture Law	No

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
XXVIII (AG 28)	Statutory Claim Reserves For Group Long-Term Disability Contracts With A Survivor Income Benefit Provision	December 1991	Standard Valuation Law Minimum Reserve Standards for Individual and Group Health Insurance Contracts	No
XXIX (AG 29)	Guideline Concerning Reserves of Companies in Rehabilitation	December 1992	Standard Valuation Law	No
XXX (AG 30)	Guideline for the Application of Plan Type to Guaranteed Interest Contracts (GICs) With Benefit Responsive Payment Provisions Used to Fund Employee Benefit Plans	December 1992	Standard Valuation Law	No
XXXI (AG 31)	Valuation Issues vs. Policy Form Approval	December 1992	Standard Valuation Law	No
XXXII (AG 32)	Reserve for Immediate Payment of Claims	December 1993	Standard Valuation Law	No
XXXIII (AG 33)	Determining CARVM Reserves For Annuity Contracts With Elective Benefits	November 2015	Standard Valuation Law	Yes
XXXIV (AG 34)	Variable Annuity Minimum Guaranteed Death Benefit Reserves	December 2003 Repealed December 2009	Standard Valuation Law	Yes
XXXV (AG 35)	The Application of the Commissioners Annuity Reserve Method to Equity Indexed Annuities	December 1998	Standard Valuation Law	No
XXXVI (AG 36)	The Application of the Commissioners Reserve Valuation Method to Equity Indexed Life Insurance Policies	June 2000	Standard Valuation Law	No
XXXVII (AG 37)	Variable Life Insurance Reserves For Guaranteed Minimum Death Benefits	October 2001	Standard Valuation Law	No
XXXVIII (AG 38)	The Application of the Valuation of Life Insurance Policies Model Regulation	August 2017	The Valuation of Life Insurance Policies Model Regulation	Yes

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
XXXIX (AG 39)	Reserves For Variable Annuities With Guaranteed Living Benefits	September 2008 Sunset December 2009	Standard Valuation Law	Yes
XL (AG 40)	Guideline For Valuation Rate of Interest For Funding Agreements and Gurauranteed Interest Contracts (GICs) With Bail-Out Provisions	September 2003	Standard Valuation Law	No
XLI (AG 41)	Projection of Guaranteed Nonforfeiture Benefits Under CARVM	June 2006	Standard Valuation Law and Standard Nonforfeiture Law for Individual Deferred Annuities	No
XLII (AG 42)	The Application of the Model Regulation Permitting the Recognition of Preferred Mortality Tables For Use In Determining Minimum Reserve Liabilities	December 2018	Model Regulation Permitting the Recognition of Preferred Mortality Tables for Use in Determining Minimum Reserve Liabilities	Yes
XLIII (AG 43) *Applies for Valuations Prior to 1/1/2020*	CARVM For Variable Annuities	March 2010	Standard Valuation Law	Yes
XLIII (AG 43) *Applies for Valuations on or after 1/1/2020 with early adoption in 2019*	CARVM For Variable Annuities	August 2019	Standard Valuation Law	Yes
XLIV (AG 44)	Group Term Life Waiver of Premium Disabled Life Reserves	December 2022	Standard Valuation Law	Yes
XLV (AG 45)	The Application of the Standard Nonforfeiture Law For Life Insurance to Certain Policies Having Intermediate Cash Benefits	December 2008	Standard Nonforfeiture Law	No

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
XLVI (AG 46)	Interpretation of the Calculation of the Segment Length With Respect to the Life Insurance Policies Model Regulation Upon a Change in the Valuation Mortality Rates Subsequent to Issue	September 2009	The Valuation of Life Insurance Policies Model Regulation	No
XLVII (AG 47)	The Application of Company Experience in the Calculation of Claim Reserves Under the 2012 Group Long-Term Disability Valuation Table	December 2016	The Health Insurance Reserves Model Regulation	Yes
XLVIII (AG 48)	Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation (Model #830)	August 2017	The Valuation of Life Insurance Policies Model Regulation	Yes
XLIX (AG 49)	The Application of the Life Illustrations Model Regulation to Policies with Index-Based Interest	December 2020	The Life Insurance Illustrations Model Regulation	Yes
XLIX-A (AG 49-A)	The Application of the Life Illustrations Model Regulation to Policies with Index-Based Interest Sold (On or After December 14, 2020)	March 2023	Life Insurance Illustrations Model Regulation	Yes
L (AG 50)	2013 Individual Disability Income Valuation Table Actuarial Guideline	August 2016	The Health Insurance Reserves Model Regulation (Model #10)	No
LI (AG 51)	The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves	August 2017	Asset Adequacy Analysis Required by the NAIC Valuation Manual (VM-30)	No
LII (AG 52)	Variable Annuity Early Adoption	December 2019	Variable Annuity Framework Requirements for 2020 Valuation Manual (VM-21)	No
LIII (AG 53)	Application of the Valuation Manual for Testing the Adequacy of Life Insurer Reserves	August 2022	VM-30, Actuarial Opinion and Memorandum Requirements	No

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Guideline No.	Title	Date Adopted By NAIC	Interpretation of	Revision of Earlier Guideline
LIV (AG 54)	Nonforfeiture Requirements for Index-Linked Variable Annuity Products	March 2023	NAIC Model 805, *Standard Nonforfeiture Law for Individual Deferred Annuities*	No

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Actuarial Guideline I

INTERPRETATION OF THE STANDARD VALUATION LAW WITH RESPECT TO THE VALUATION OF POLICIES WHOSE VALUATION NET PREMIUMS EXCEED THE ACTUAL GROSS PREMIUM COLLECTED

1. The purpose of this guideline (items 2 and 3 below) is to clarify the intent of the Standard Valuation Law.

2. The method of valuation promulgated by the model legislation adopted by the NAIC in December 1976 for the valuation of life insurance policies whose valuation net premiums exceeds the actual gross premiums collected is a change in method of reserve calculation and not a change in reserve standards.

3. For policies so valued the maximum permissible valuation interest rate and the applicable mortality basis specified is that in effect at the date of issue of such policies.

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Actuarial Guideline II

RESERVE REQUIREMENTS WITH RESPECT TO INTEREST RATE GUIDELINES ON ACTIVE LIFE FUNDS HELD RELATIVE TO GROUP ANNUITY CONTRACTS

As part of the determination of the aggregate minimum group annuity reserves, a computation must be made of minimum reserves for deposit administration group annuity funds with interest rate guarantees including all such funds pertaining to possible purchase of group annuities whether such funds are held in a separate account or in a general account, whether shown as premiums, advance premiums, auxiliary funds, etc. and whether the liability is shown in Exhibit 8 or elsewhere. In making such computations, the procedure and minimum standards described below shall be applicable for the December 31 calendar year "y" valuation giving recognition to the dates deposits were made. Where appropriate and with the approval of the commissioner, recognition may be given to the extent and time of application of active life funds to purchase annuities, expense assessments against the funds, and excess of purchase price over minimum reserves. In no event shall the reserve be less than the transfer value, if any, of the fund. Approximate methods and averages may be employed with the approval of the commissioner.

To the extent that the application of these valuation procedures and standards would require a company to establish aggregate minimum reserves for group annuities and related funds in excess of reserves which it would not otherwise hold if these valuation procedures and standards did not apply, such company shall set up additional reserve liability shown in its general account or in a separate account, whether shown in Exhibit 8 or elsewhere.

The valuation procedures and standards specified in this guideline shall not be applicable to the extent that the valuation procedures and standards relating to reserves for deposit administration group annuity funds with interest rate guarantees (i.e., group annuity and guaranteed interest contracts) in the amendments to the Standard Valuation Law adopted by the National Association of Insurance Commissioners in December 1980, or in later NAIC amendments, have become applicable in a jurisdiction.

For funds receive:

(1) Prior to calendar year 1976, follow the procedure used at that time.

(2) In calendar year 1976 or later, follow the minimum standards described below:

(a) Contracts having no guaranteed interest rates in excess of 6% on future contributions to be received more than one year subsequent to the valuation date.

The minimum reserve shall be equal to the sum of the minimum reserves for funds attributable to contributions received in each calendar year.

Where V_y = Minimum reserve for funds attributable to contributes received in calendar year y.

$V_y = [C_y \times (1 + i_{gy})^n]/(1 + i_{py})^n$

C_y = Portion of guaranteed fund attributable to contributions received in calendar year y

i_{gy} = Interest rate guaranteed under the contract with respect to funds attributable to contributions received in calendar year y.

i_{py} = Lowest of:

(1) The net new money rate credited by the company on group annuity funds attributable to contributions received in calendar year y less .005; or

(2) i_{gy}; or

(3) i_{my}; where

(i) i_{my} = for calendar years y + 1 through y + 10, the values shown in the table of values of i_{my} distributed each year by the Central Office of the National Association of Insurance Commissioners;

(ii) i_{my} = for calendar years y + 11 and later, .060.

n = Number of guarantee years, and fractions thereof, remaining as of the December 31 valuation.

(b) Contracts having guaranteed interest rates in excess of 6% on future contributions to be received more than one year subsequent to the valuation date.

The same procedures as set forth under (a) above shall be used except that the deduction under (1) of i_{py} shall be .01 instead of .005 and i_{my} for calendar years y + 1 through y + 10 shall be reduced by .005.

Table of Values of i_{my}

(Effective for the December 31, 1977 Valuation)

Calendar Year y in Which Contributions Were Received	Value of i_{my} for Calendar Years y + 1 Through y + 10
1976	.089
1977	.087
1978	.081
1979	.084
1980	.100
1981	.124
1982	.145

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Actuarial Guideline III

INTERPRETATION OF MINIMUM CASH SURRENDER BENEFIT UNDER STANDARD NONFORFEITURE LAW FOR INDIVIDUAL DEFERRED ANNUITIES

Section 6 of the model bill as written does not require that cash surrender benefits to be paid; but where they are paid, it requires that such cash surrender benefits grade into maturity value using an interest rate not more than one percent higher than the rate specified in the contract for accumulating net considerations. While this method will be suited for contracts having a sales load at issue, it may create a problem for contracts having surrender charges for cash surrender.

For contracts providing cash surrender values, the cash surrender value at maturity shall be at least equal to the minimum nonforfeiture amount at maturity as defined in Section 4. For purposes of calculating cash surrender values prior to maturity, the term “maturity value” in the Standard Nonforfeiture Law for Individual Deferred Annuities shall mean the cash surrender value at maturity.

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Actuarial Guideline IV

ACTUARIAL INTERPRETATION REGARDING MINIMUM RESERVES FOR CERTAIN FORMS OF TERM LIFE INSURANCE

Scope

This interpretation recommended by the NAIC Technical Task Force to Review Valuation and Nonforfeiture Value Regulation deals only with term life insurance without cash values which the owner has the unilateral right to maintain in force until its stated expiry date, subject only to the payment of required premiums which vary (generally increasing on a per $1000 basis) during the term of the policy and under which premium rates are guaranteed to the stated final expiry. This interpretation applies only to such term plans valued on the 1958 CSO Mortality Table for the current term period.

Ten-year renewable term, five-year renewable term and one-year renewable term to a stated age with generally increasing premiums are titles commonly given to such policies, but this interpretation concerns itself with the actual coverage provided and is not controlled by the name given the coverage.

Background Information

Historically, reserves on one-year renewable term policies have consisted of a basic reserve for the current term period of one-half the cost of insurance for the current term period, plus a deficiency reserve, if any. The application of the Commissioners Reserve Valuation Method to determine basic reserves and deficiency reserves for such policies is subject to varying interpretations as noted in Walter O. Menge's paper, "Commissioners Reserve Valuation Method" written at the time of construction of the Standard Valuation Law.

> ...the adaptation of the commissioners reserve valuation method to fit policies for which the gross premium varies from year to year becomes a problem of generalization which, from a purely theoretical viewpoint, has an infinite number of possible solutions, some of which are practical and others of which are impractical.[1]

and

> For these reasons, it seems desirable not to formulate at this time any fixed rules for the valuation of these unusual types of policies and riders. The second paragraph of Section 4 of the Standard Valuation Law does not define the method of valuation of such contracts but requires that the method used, whatever it may be, must be consistent with that employed for uniform premium policies providing uniform insurance benefits, thus leaving open the possibility of a choice of several consistent methods.[2]

Acceptable Approaches

Two approaches to "consistent" reserves are suggested. The unitary policy approach considers such policies as variable premium policies up to the mandatory expiry date. Under this approach the valuation net premiums are a uniform percentage of gross premiums with the percentage fixed at issue date. If appropriate deficiency reserves are held, this approach has great appeal. However, it is susceptible to manipulation and illogical results. Reserves according to this approach should be acceptable only if the company can demonstrate that actual reserves, including deficiency reserves, for all renewable term business valued using this approach are of the same general magnitude as would occur using an approved method as defined below.

The other approach is to hold policy reserves for only the current period of years (not necessarily equal to the renewal period) during which the required premium per $1000 remains level, including deficiency reserves if appropriate. Additional reserves are established where net premiums, calculated on a basis

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which reflects current mortality, exceed gross premiums for future periods of level premiums. Although not speaking directly to valuation problems in this instance, the Hooker Committee report said:

> The question was raised whether a policy providing term insurance for several years, automatically followed by permanent insurance, should be considered as two separate policies for the purpose of the Act. In the Committee's opinion, the respective portions may be treated separately if the portion providing permanent insurance takes the Company's regular rate at the then attained age. The rated age provision in the law appears to cover this point. However, the Committee draws a distinction between policies providing purely term insurance followed by permanent insurance at the company's published rate at the attained age of conversion, and the policies providing for an initial premium such that the increased premium at a subsequent duration differs from that for a new policy at the attained age. The latter case obviously constitutes a single policy to which the formula should be applied at the outset.[3]

The second sentence of the above quotation lends support to the approach of separating successive periods of level premiums.

Under this interpretation, an approved method is any method which produces reserves greater than or equal to the sum of policy reserves, including deficiency reserves, for the current period of level premiums calculated on the basis of the applicable mortality and interest standards and reserve method specified in the Standard Valuation Law plus additional reserves calculated according to the following applied uniformly to all such policies.

> The present value of the excess of test premiums for future periods of level premiums for which gross premiums are guaranteed over the respective gross premiums, such test premiums and present values being calculated on the Commissioners' 1980 Standard Ordinary Mortality Table with Ten-Year Select Mortality Factors and 4 1/2 percent interest. For each plan of insurance with separate rates for smokers and nonsmokers an insurer may substitute the 1980 CSO Smoker and Nonsmoker Mortality Tables with Ten-Year Select Mortality Factors for the Commissioners' 1980 Standard Ordinary Mortality Table with Ten-Year Select Mortality Factors.

In case a future gross premium exceeds the test premium, the excess shall be considered zero and not a negative amount. This is in accordance with the principle of anticipating no future profits but providing for all future losses.

Reinsured Business

If reinsurance is assumed under an agreement in which the reinsurer reserves the right to raise premiums to a level at least as great as the net valuation premiums, the reinsurer is not required to establish deficiency reserves or additional reserves, and the ceding company is not permitted to take credit for such reserves on the portion of the business which is required.

If a reinsurance agreement guarantees future reinsurance premiums, the reinsurer should establish deficiency reserves and additional reserves as required by this interpretation for the period for which reinsurance premiums are guaranteed, and the ceding company may take credit for such reserves against its deficiency and additional reserves on the portion of the business which is reinsured to the extent permitted by law.

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Adequacy of Reserves

Although the above alternative is acceptable as meeting the intent of the Standard Valuation Law, this does not in any way relieve the certifying actuary of the insurance company from exercising his own best judgment with respect to the appropriate reserves. In particular, the actuary should consider term contracts of this nature when he states his opinion that aggregate reserves "make a good and sufficient provision for all unmatured obligations of the company guaranteed under the terms of its policies" and "include provision for all actuarial reserves and related statement items which ought to be established."[4]

References

1. The Record, American Institute of Actuaries, Vol. XXXV, 1946, p. 270.

2. Ibid., p. 300.

3. 1947 NAIC Proceedings, 257.

4. Instructions for Completing NAIC Life and Health Annual Statement Blank, 1976, p. 1.

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Actuarial Guideline V

INTERPRETATION REGARDING ACCEPTABLE APPROXIMATIONS FOR CONTINUOUS FUNCTIONS

Text

For reserves and values using continuous functions:

(a) $\overline{D}_x = \int_0^1 D_{x+t}\,dt$

By assuming that D_{x+t} is linear for $0<t<1$

$\overline{D}_x = (D_x + D_{x+1})/2.$

By assuming that the deaths in the year of age x to x+1 are uniformly distributed over that year of age,

$\overline{D}_x = [(\delta-d)/\delta^2]D_x+[(i-\delta)/\delta^2]D_{x+1}$

where: $d = iv = i/(1+i)$

δ = force of interest

i = interest rate

(b) $\overline{C}_x = \int_0^1 D_{x+t}\,\mu_{x+t}\,dt$

By assuming that deaths in the year of age x to x+1 are uniformly distributed over that year of age,

$\overline{C}_x = (i/\delta)C_x.$

By assuming that the total deaths are concentrated at the middle of the year of age,

$\overline{C}_x = (1+i)^{1/2}C_x$ or $(1+i/2)C_x.$

Background Material

The actuarial mathematics used in calculating net premiums, reserves, and nonforfeiture values for life insurance policies was first developed using two basic assumptions. These basic assumptions are: (1) that all death benefits are payable at the end of the policy year of death and (2) that all gross premiums due under the policy are payable annually at the beginning of the policy year. Actuarial values which are calculated under these two basic assumptions are described as being calculated using curtate functions. For any specific mortality table and interest rate, all the necessary actuarial values are uniquely defined for a policy using curtate functions.

The Standard Valuation Law and the Standard Nonforfeiture Law define minimum reserves and minimum nonforfeiture values, respectively, for life insurance policies using curtate functions. These two model laws originated in the early 1940s when almost all insurance companies were using the two basic assumptions inherent in the curtate functions. However, the wording of the model laws does not prohibit

insurance companies from using other assumptions if the resulting reserves and nonforfeiture values will always be at least as large as the minimum amounts defined in these laws.

Nowadays, many insurance companies do prefer to use alternative assumptions in computing the reserves and nonforfeiture values for their life insurance policies. These companies consider the alternative assumptions more appropriate for their policies. These alternative assumptions are: (1) that all death benefits are payable immediately upon death and (2) that all gross premiums due under the policy are payable continuously throughout the policy year.

Actuarial values which are calculated under both of the alternative assumptions, pertaining to death benefits and gross premiums, are described as being calculated using continuous functions. However, the underlying mathematics for continuous functions involves two integrals, representing the actuarial functions C_x and D_x, which must be approximated. In the past, there has been some disagreement among actuaries as to which approximations for the two integrals are the most suitable. Because of the use of different approximations for these two integrals, actuaries have obtained different numerical amounts for the necessary actuarial values using continuous functions even though these actuaries were working with the same mortality table and interest rate.

Some insurance companies prefer to calculate their reserves and nonforfeiture values assuming: (1) that death benefits are payable immediately upon death and (2) that all gross premiums due under the policy are payable annually at the beginning of the policy year. Thus, these companies are using the alternative assumption pertaining to death benefits and the basic assumption pertaining to gross premiums. The underlying mathematics for the combination of these two assumptions involves the integral C_x, which must be approximated. Thus, the use of these two assumptions together gives rise to essentially the same problem as using continuous functions.

Actuarial Guideline VI

INTERPRETATION REGARDING USE OF SINGLE LIFE OR JOINT LIFE MORTALITY TABLES 20 JUNE 1983

The Standard Valuation Law and the Standard Nonforfeiture Law for Life Insurance apply to policies which provide joint life insurance benefits as well as to policies which provide single life insurance benefits. References in these laws to plans such as "nineteen-year premium whole life" or "a whole life policy...with uniform premiums for the whole of life" are to be interpreted as references to such plans based on the same life status(es) as the policy for which minimum reserves or nonforfeiture benefits are being determined. For example, if the net level annual premium on the nineteen-year premium whole life plan is needed to calculate the minimum reserve for a policy which insures two lives and pays a death benefit at the first death, the premium is to be that for a policy which insures two lives and pays a benefit at the first death. The same principle would apply to a policy which insures only one life, or a policy which pays a benefit at the first death of more than two lives. The principle also applies to a policy that pays a benefit on the death of t-th life of n lives (t is greater than 1 but less than or equal to n).

Background Material

The great majority of life insurance policies provide single life insurance benefits. These policies identify one specific individual as the named insured. A death benefit under the basic policy is payable if this named insured dies while the policy is in force. Usually, there are no further gross premiums due on and after the death of this named insured. The basic policy may provide endowment benefits which are conditional on the survival of this named insured. The policy does not contain any provisions whereby the amount of the death benefits, endowment benefits or gross premiums are affected by the survival or nonsurvival of any other persons besides the insured, except possibly in the settlement option provisions or in the provisions of an attached term insurance rider which requires an extra premium.

In contrast to policies which provide single life insurance benefits, policies which provide joint life insurance benefits depend on the survival or nonsurvival of two or more named insureds. Until quite recently, virtually all policies which provided joint life insurance benefits were written on the whole life insurance plan. Such policies paid the face amount as a death benefit on the death of the first of the named insureds to die, provided that the policy was then in full force. No further gross premiums were due after the death, and the policy terminated upon payment of the death benefit.

Recently, there has been increasing interest in plans providing joint life insurance benefits, and insurance companies have developed a variety of new life insurance plans. For example, some policies provide for payment of a death benefit only on the death of the last to die of the named insureds.

The Standard Valuation Law and the Standard Nonforfeiture Law clearly apply to policies which provide joint life insurance benefits as well as to policies which provide single life insurance benefits. Both of these model laws define an "expense allowance" which is added to the present value of the future guaranteed insurance benefits under the policy, and which affects the modified premiums used for computing minimum reserves and the adjusted premiums used for computing minimum nonforfeiture values. A different amount of "expense allowance" is defined for nonforfeiture values than that defined for reserves, but the principle is much the same.

Insurance companies are allowed to select "expense allowances" for use in computing their reserves and nonforfeiture values up to the level of the "expense allowances" defined in these model laws. A higher "expense allowance" would produce reserves or nonforfeiture values which are less than the minimum defined in the model laws, and therefore state insurance departments cannot permit companies to use a higher amount as an "expense allowance."

The wording of these model laws is generally clear and precise in defining the "expense allowances" which are permitted for policies which provide single life benefits. However, the proper level of the

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"expense allowances" for policies providing joint life insurance benefits is not so clear. The "expense allowance" defined in the Standard Valuation Law depends on the modified net premium for a policy on the 20-payment whole life insurance plan, and the "expense allowance" defined in the Standard Nonforfeiture Law depends on the adjusted premium for a policy on the ordinary life plan.

Actuaries have had different opinions as to how to apply the joint life insurance mortality tables in order to obtain the modified net premium and the adjusted premium required by model laws, so as to calculate the "expense allowances" which are appropriate under those laws. The question has become increasingly important with the development of the new plans providing joint life insurance benefits.

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Actuarial Guideline VII

INTERPRETATION REGARDING CALCULATION OF EQUIVALENT LEVEL AMOUNTS

Text

Pure endowments will not be considered in the determination of equivalent level amounts for valuation and nonforfeiture purposes.

Background Material

The "Background Material" section relating to the previous actuarial guideline went into some detail concerning the "expense allowances" defined in the Standard Valuation Law and the Standard Nonforfeiture Law. See Actuarial Guideline VI, "Interpretation Regarding Use of Joint Life Insurance Tables."

This Actuarial Guideline VII is also concerned with the level of these "expense allowances" defined in these model laws. The most common plans of life insurance provide a level face amount as the death benefit, during the period the policy is in full force. These plans do not provide for any benefit which is payable as a pure endowment. (A pure endowment benefit pays a specified amount of pure endowment to the policyholder if the insured is still alive on the specified maturity date and if the policy is still in full force on this maturity date.) However, policies which provide for a death benefit which varies with the duration and policies which provide one or more endowment benefits can be legally written in most states.

The Standard Valuation Law and the Standard Nonforfeiture Law do apply to such policies with varying death benefits or pure endowment benefits. In fact, the wording of the model laws shows that considerable thought was given to the treatment of these kinds of policies. In the case of both model laws, the present value of future guaranteed benefits under the policy clearly includes both the death benefits and the "expense allowances" defined under these model laws.

The Standard Nonforfeiture Law includes a paragraph which reads as follows:

> In the case of a policy providing an amount of insurance varying with duration of the policy, the equivalent uniform amount thereof for the purpose of this Section shall be deemed to be the uniform amount of insurance provided by an otherwise similar policy, containing the same endowment benefit or benefits, if any, issued at the same age and for the same term, the amount of which does not vary with duration and the benefits under which have the same present value at the date of issue as the benefits under the policy; provided, however, that in the case of a policy providing a varying amount of insurance issued on the life of a child under age ten, the equivalent uniform amount may be computed as though the amount of insurance provided by the policy prior to the attainment of age ten were the amount provided by such policy at age ten.

While the wording of the above paragraph is rather complex, the meaning seems to be actuarially precise. The paragraph defines an "equivalent uniform amount" which affects the "expense allowance" defined in the law. The phrase "containing the same endowment benefit or benefits, if any" effectively means that pure endowment benefits are to be ignored in computing this "equivalent uniform amount." This "equivalent uniform amount" or "equivalent level amount" becomes a sort of weighted average of the death benefits provided by the policy, an average which is not affected in any way by the pure endowment benefits which may be provided by the policy.

The Standard Valuation Law is not nearly so clear on this point. It contains wording as follows:

> Reserves according to the Commissioners Reserve Valuation Method for (1) life insurance policies providing for a varying amount of insurance----shall be calculated by a method consistent with the principles of the preceding paragraph-----.

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(Note that the quoted wording refers back to the preceding paragraph in the Standard Valuation Law. It does not intend to refer to the paragraph quoted from the Standard Nonforfeiture Law.)

Most actuaries have interpreted the Standard Valuation Law so as to use an "equivalent level amount" which is not affected by any pure endowments included in the policy. They would then use this "equivalent level amount" to calculate the "expense allowance" defined in the model law. This "equivalent level amount" is also a weighted average of the death benefits provided by the policy, in the same fashion as the "equivalent uniform amount" used in applying the Standard Nonforfeiture Law. Some insurance companies use the same "equivalent level amount," for the purpose of the Standard Valuation Law, as the "equivalent uniform amount" defined in the Standard Nonforfeiture Law. Other companies use a very similar calculation to obtain a special "equivalent level amount," for the purpose of the Standard Valuation Law, based only on the death benefits provided on and after the first policy anniversary.

Some actuaries have felt that the wording of the Standard Valuation Law permits an alternate calculation of the "equivalent level amount" which would be affected by pure endowment benefits. Such an "equivalent level amount" would be used to calculate an "expense allowance" under the Standard Valuation Law, even though the "equivalent level amount" no longer has the character of a weighted average of the death benefits provided by the policy.

The inclusion of the pure endowment benefits in the calculation of the "equivalent level amount" would affect the level of the "expense allowance" defined in the Standard Valuation Law, and therefore, it would affect the level of the minimum reserves required by the policy. Typically, the denominator of the fraction used in calculating the "equivalent level amount" would remain the same, but the numerator of this fraction would be increased because of this inclusion. Thus, the "equivalent level amount" itself and the resulting "expense allowance" defined in the Standard Valuation Law would also be increased with the inclusion. The end result of the inclusion would be lower minimum reserves at every duration.

If the amounts and maturity dates of the new pure endowment benefits were carefully selected, a considerable degree of reduction in the reserve factors would probably be possible.

This actuarial guideline would expressly prohibit including the pure endowment benefits in determining the "equivalent level amount" for either valuation or nonforfeiture purposes. As explained under "Background," the need for this actuarial guideline arises primarily for valuation purposes under the Standard Valuation Law. The wording of the Standard Nonforfeiture Law is sufficiently precise that this actuarial guideline is virtually a truism for the purpose of calculating nonforfeiture values.

The purpose of this actuarial guideline is to assist state insurance departments and insurance company actuaries by identifying a method of calculating "equivalent uniform amounts" and "expense allowances" which is not considered proper and which will not be accepted.

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Actuarial Guideline VIII

THE VALUATION OF INDIVIDUAL SINGLE PREMIUM DEFERRED ANNUITIES

Text

With respect to those states which have enacted the 1976 amendments to the Standard Valuation Law; individual single premium deferred annuity reserves shall at least equal the greatest of any of the discounted values of all guaranteed future benefits including cash surrender values available after the date of valuation, such benefits discounted to the valuation date at the maximum permissible statutory interest rate. This method applies to all individual single premium deferred annuities which are subject to the provisions of the Standard Valuation Law in those states which have enacted the 1976 amendments. For those states which have not yet enacted the 1976 amendments this interpretation is a method of valuing individual single premium deferred annuities.

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Actuarial Guideline IX

FORM CLASSIFICATION OF INDIVIDUAL SINGLE PREMIUM IMMEDIATE ANNUITIES FOR APPLICATION OF THE VALUATION AND NONFORFEITURE LAWS

Text

Solely for the purposes of the applicable Valuation and Nonforfeiture Laws, an individual single premium annuity shall be considered to be immediate, as opposed to deferred, provided:

1. The first annuity payment is due not more than thirteen months from the annuity issue date;

2. succeeding payments under the annuity, after the initial payment, are due at regular intervals no less frequently than annually;

3. in the case of a fixed benefit annuity, the total guaranteed payments due in any contract year are not greater than 115% of the total guaranteed payments due in the immediately preceding contract year. In the case of variable annuities and indexed annuities, the same characteristic would be required for the underlying pattern of payments, before adjustments which are made solely because of the performance of the separate account associated with a variable annuity or the changes in the associated index. (This characteristic is not intended to prevent or reduce any lawful nonguaranteed payments under the annuity which are in the nature of dividends or excess interest credits.)

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Actuarial Guideline IX–A

USE OF SUBSTANDARD ANNUITY MORTALITY TABLES IN VALUING IMPAIRED LIVES UNDER STRUCTURED SETTLEMENTS

Text

The Standard Valuation Law permits modifications of annuity mortality tables. Solely for the purpose of valuing:

1. Periodic benefits arising from settlements of various forms of claims pertaining to court settlements or out of court settlements from tort actions, such as arising from accidents or medical malpractice;

2. Settlements involving similar action such as workers' compensation; or

3. Settlements of long term disability claims where a temporary or life annuity has been used in lieu of continuing disability payments.

A substandard annuity mortality table may be used where the annuitant (or measuring life) is the injured party and there are relevant hospital records, treating physicians' reports, and/or independent medical evaluations from those medical doctors that are or have been involved in the care of the injured party, that have been used during the underwriting process and have been retained in the underwriting file of the company as proof of the individual's impaired health and shortened longevity.

In such case the insurer may modify the statutory annuity mortality table or tables cited in Section 3a of the Standard Valuation Law or in any regulation promulgated pursuant to such section so as to reflect the longevity based on a medical doctor's written evaluation or records as indicated above. The table may be modified by a percentage of standard mortality or by a specified number of extra deaths or by a combination thereof, provided that the mortality table so adjusted produces reserves that are at least as great as the minimum reserves indicated below. The percentage extra mortality or the specified number of extra deaths may vary by duration. A rated up age with the standard annuity table which is approximately equivalent to the actual age on the substandard annuity table may be used only if the procedure is modified to produce reserves that at each duration are at least as great as the minimum reserves indicated below.

The fact that a company has held minimum reserves as herein described shall in no way relieve the actuary from considering whether such reserves are adequate.

Minimum Reserves

The minimum reserves for applicable annuity contracts are the reserves obtained by making a constant addition to the mortality rate of the otherwise applicable valuation mortality table such that the expectation of life on the adjusted valuation table is greater than or equal to the average of the expectations of life indicated by or obtained from information given by the company's medical directors or underwriters during the underwriting and pricing process. The constant addition to the mortality table herein described shall be made as of the issue date and, once determined, held constant for the period of time that the contract remains in force. The addition of a constant to the valuation mortality rate produces a gradually declining percentage extra mortality such that reserves will grade into standard reserves at the end of the standard valuation mortality table thereby making the reserve more conservative (closer to standard) each year that the annuitant or measuring life lives.

For annuitants (measuring lives) other than the injured person in such settlements, the actual age and a standard annuity mortality table specified in Section 3A of the Standard Valuation Law or in any subsequent regulation promulgated thereto or any modification of such table which produces reserves at

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least as high as those that would be produced under the standard table based on the actual age must be used.

For contracts not included in one of the three categories described in the first paragraph of the Guideline, standard reserves at the actual age shall be held.

Where an insurer uses a modified table with higher mortality rates or a rated age with an unmodified table for impaired lives under structured settlements, such insurer shall maintain records of actual to expected mortality to monitor the appropriateness of the substandard mortality.

Background

Structured settlements take their name from the fact that the settlements, which arise from tort action, including workers' compensation claims, are frequently structured to fit the circumstances of the injured party and/or the injured party's dependents. The injured party and/or dependents are apt to be much younger than normal retirement age such that the payments may well stretch out for 30, 40, and 50 years or more. Some payments are certain; others are contingent upon the measuring life being alive at the time of payment.

The volume of structured settlement business has boomed in recent years. Periodic and deferred payments have been encouraged and even mandated in some states as a means of controlling costs under malpractice claims and ensuring that the monies would be available in future years and not squandered as could happen with lump sum payments. Periodic and deferred payments may be a result of settlement of automobile claims, other accidents involving tort action, as well as workers' compensation claims and medical malpractice claims, where the individual(s) upon which the tort or other action was based may well be substandard.

At the time of the adoption of the NAIC 1980 revisions of the Standard Valuation Law (SVL), structured settlement business was relatively minor, and how to treat such business was not explicitly covered in the SVL.

The SVL allows for modification of the standard annuity mortality table specified in the minimum valuation standard. Any modification had traditionally been such as to result in higher reserves. If lower reserves were produced, it could render the minimum meaningless.

In case of structured settlements, the injured party may be highly substandard. If an insurance company had to set up reserves on a standard table, or on a basis that grades into standard mortality too rapidly, it could result in either an excessive price for the payments or it could result in such a level of surplus strain to the insurer. If the price reflects the actual expected mortality, that the coverage might not be offered at all. To encourage settlements involving periodic payments, it is recommended that, in the limited area involving the injured party, the table may be modified so as to reflect the expected mortality based on the relevant medical records, reports and/or evaluations described earlier.

Since this is an area with little experience, it is required that an insurer monitor the experience in order to be able to justify its choice of adjusted mortality assumption.

It is recognized that at issue the vast bulk of the liability normally pertains to payments that are certain and not contingent upon survival, since the vast majority of substandard contracts contain a certain period and most of the benefits either fall within that certain period or are guaranteed to be paid. It is also noted that the interest discount factor in the early durations is far more important than the mortality element. The selection of the interest discount factor is the subject of Guideline IX-B.

Because experience and methodology are still emerging for substandard annuities, it is expected that this whole subject will be reviewed again in the not too distant future, both as it applies to whether the criteria

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herein established for settlement annuities are too conservative and also whether or how it might be acceptable to apply similar standards to substandard non-settlement annuities.

Effective Date

Where the requirements of this Guideline produce higher reserves than those calculated by an insurer, such insurer may continue its present procedures for the 1989 year end valuation, but must comply with this Guideline for 1990 and later issues for the 1990 and later valuations and for all of its business by the 1993 year end valuation.

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Actuarial Guideline IX–B

CLARIFICATION OF METHODS UNDER STANDARD VALUATION LAW FOR INDIVIDUAL SINGLE PREMIUM IMMEDIATE ANNUITIES, ANY DEFERRED PAYMENTS ASSOCIATED THEREWITH, SOME DEFERRED ANNUITIES, AND STRUCTURED SETTLEMENTS CONTRACTS

Text

1. Solely for the purpose of applying the Standard Valuation Law, an annuity shall be considered as a series of payments not less frequently than annually over five years or more wherein the payments in any one contract or calendar year (at the option of the insurer) do not exceed 115% of the payments in the immediately preceding contract or calendar year. An immediate annuity is an annuity wherein the first payment begins in thirteen months or less from issue and a deferred annuity is an annuity wherein the first payment begins more than thirteen months after issue. A series of payments over less than five years otherwise qualifying as an annuity shall be considered equivalent to a lump sum. Any payments in a year in excess of 115% of the prior year's payments may be considered as a lump sum or equivalent thereto or may be considered as part of a new annuity depending on the circumstances. Some contracts may consist of combinations of annuities and of lump sums.

2. Where the deferred income payments are guaranteed and there are no cash settlement options, the reserve shall be based on the present value of the income payments based on an appropriate annuity mortality table and the valuation rate of interest in accordance with the Standard Valuation Law based on the issue year method and a guarantee duration equal to the number of years from the date of issue to the date the first payment begins.

3. At the time benefit payments begin, whether under single premium immediate annuity contracts, supplementary contracts providing for annuity payments or deferred annuity contracts (with the first payment deferred more than thirteen months), the insurer may use the valuation interest rate for the calendar year in which (a) the deferred contract was issued or (b) the consideration was received or (c) the payments begin, but must apply such procedure elected in a consistent manner

4. Individual structured settlements vary considerably in payment pattern and duration. These contracts may provide for both level and/or increasing periodic payment schedules, as well as lump sum benefit payments. In valuing individual structured settlements, a split of all or a portion of the lump sum payments from the annuity payments may be appropriate. Such splits should be at the discretion of the valuation actuary. However, splits not in accordance with (5)(a) or (5)(b) and with (6)(a) below would require valuation in accordance with procedure (6)(b) or (6)(c) below.

5. For a block of single premium immediate annuities, deferred annuities without cash settlement options, structured settlement business with the annuity portion having no cash settlement options, or other contracts having some portion with periodic payments without cash settlement options, issued in a given calendar year, the calendar year valuation interest rate appropriate for single premium immediate annuities where the first payment begins in thirteen months or less after issue and for Plan Type A contracts without cash settlement options based on the date to first payment where the first payment begins more than thirteen months after issue may be used provided:

    a. The guaranteed payment under each contract in the block due in any contract or calendar year (at the option of the insurer) after the first is not greater than 115% of the guaranteed payment due in the immediately preceding contract or calendar year, and once payments

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begin such payments are not less frequent than annually and are payable over five years or more; or

b. The total guaranteed payments under all contracts combined included in the block due in any calendar year after the first are not greater than 110% of the total guaranteed payments due in the immediately preceding calendar year but only contracts having payments not less frequent than annually for at least five years shall be included.

The year to year comparison of benefits may be made before or after considering the effect of mortality or any certain period, but the actuary should be prepared to indicate which method is used.

6. If a block of immediate annuities, deferred annuities without cash settlement options, structured settlement contracts with the annuity portion having no cash settlement options, or other contracts having some portion with periodic payments without cash settlement options fails the test described in (5) above, then one of the following procedures must be used:

a. The block must be divided into components so that the contracts/payments satisfying the tests are included in one or more components and those not satisfying the tests are included in another component or other components. The Plan Type A valuation interest rate or rates may be used for the component or components which satisfies the test. The Plan Type A guarantee duration is the number of years from the date of issue or date of purchase to the date that the first annuity payment is due. The maximum valuation interest rate for any payment included in a component which does not satisfy the test shall be determined using the guarantee duration of the lump sum payment including installments over less than five years and on the assumption that the payment is made under a contract of Plan Type A. The Plan Type A guarantee duration of a lump sum payment is the number of years from the date of issue or date of purchase to the date that payment or the first installment payment is due. Year of issue valuation interest factors must be used. The actuary should be prepared to describe the components and justify the choice of valuation interest rate or rates for the component or components of the block which, if included, would cause the block to fail the test.

b. The reserves for each contract for each valuation year shall be the greater of the "level interest rate reserves" and of the "graded interest rate reserves." Graded interest rate reserve factors for each separate year of issue for all future payments of such year of issue, whether periodic or lump sum payments, shall be graded in a manner that produces reserves at least as great as the method described in the balance of this paragraph.

(i) Step one, calculate the present value of future benefits at issue for each contract using the appropriate level Plan Type A interest rate for contracts without cash settlement options for the guarantee duration corresponding to the number of years from the date of issue or date of purchase to the date that the first payment is due. Call this value PV (0), and call reserves at successive durations using the appropriate (level) Plan Type A interest rate "level interest rate reserves."

(ii) Step two, solve for "X percent" such that the present value of future benefits at issue for each contract is equal to PV (0) (calculated in Step one), using "X percent" as the valuation interest rate for the first twenty contract years after issue and thereafter the Type A interest rate for contracts without cash settlement options for guarantee durations of more than twenty years. However, "X percent" shall not be greater than 115% of the appropriate Type A interest rate in step one; where such limit is effective, the present value at issue will be greater than PV (0).

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(iii) For each valuation year calculate "graded interest rate reserves" based on the assumption that the valuation interest rate during the first twenty contract years is "X percent" as calculated in step two and thereafter is the Plan Type A interest rate for contracts without cash settlement options for guarantee durations of more than twenty years.

(iv) In lieu of the individual contract valuation above, a group valuation may be made as for example on the assumption that all contracts issued during a given year are issued as a single contract on July 1, and once X% is determined for such year, it need not be redetermined; or

c. Any other method producing reserves at least as great as (a) or (b) and specifically approved by the Commissioner.

7. Where the requirements of this guideline produce higher reserves than those calculated by an insurer in good faith based on a more liberal interpretation, such insurer may continue its present procedures for the 1989 year end valuation but must comply with this guideline for 1990 and later issues for the 1990 and later year end valuations and for all its inforce, subject to the 1980 amendments to the NAIC Model Standard Valuation Law, by the 1993 year-end valuation.

8. The examiner should request that the insurer demonstrate that the assets are sufficient for the liabilities by cash flow projections of the supporting assets and the liabilities under various interest scenarios, in particular for declining interest rates.

9. The examiner should note that date of acquisition and the yields of the supporting assets and compare such with the date of issue of the structured settlements and the valuation interest rates. If such differ, the examiner may request a new valuation using the date of acquisition of the majority of the supporting assets as the date of issue of remaining payments. This is especially important where, for example, an insurer during 1986 exchanged high yielding assets originally acquired in 1982 for low yielding assets acquired in 1986. Also, many of the high yielding assets may have been called during 1986. Also, due to the long-term nature, often as many as 30, 40, and 50 years, the increasing nature of the payments and the lump sum payments, the value of future payments with a single fixed interest rate may actually increase after issue. The result is that there is a large reinvestment risk and large liabilities may exist after all the original supporting investments have matured and new investments acquired.

10. The procedures above are interim procedures pending a reconstitution of the valuation laws.

Background

Current Actuarial Guideline IX provides guidance for determining what is an immediate annuity but it does not advise how contracts failing to meet the test should be treated for valuation purposes. Three examples of failing contracts are: (1) annual payments increasing 120% each year, (2) level payments payable biannually, (3) level annual payments with extra lump sum payments equal to four times a regular annual payment payable every five years. These examples are not practical examples for annuity payments beginning at normal retirement ages such as 60, 65 or 70 under individual or group retirement programs, but combinations of irregular payments and increasing regular payments are practical under structured settlements.

At the time of the adoption of the NAIC 1980 revisions of the Standard Valuation Law, structured settlement business was relatively minor, and how to treat such business was not explicitly covered in the SVL. The volume of structured settlement business has boomed in recent years. Periodic and deferred payout was encouraged and even mandated in some states as a means of controlling costs under malpractice claims and ensuring that the monies would be available in future years and not squandered as

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could happen with lump sum payments. Periodic and deferred payments may result in settlement on automobile claims, other accidents involving tort action as well as medical malpractice claims and workers' compensation claims such that the individuals may well be substandard.

Where payments are contingent on the individual being alive, under a related guideline, substandard annuity mortality tables may be recognized for valuation based on a written evaluation of the injured individual's longevity by a medical doctor. For all other annuitants, substandard annuity mortality tables should not be recognized as such is contrary to the establishment of minimum reserves for such annuitants. However, the vast bulk of reserves for structured settlements is based on certain payments, such that the valuation interest rate is by far the more important factor. This guideline covers valuation procedures and valuation interest rates leaving application of substandard annuity mortality table to Guideline IX-A.

Structured settlements take their name from the fact that the settlements are frequently structured to fit the circumstances of the injured party and/or the injured party's dependents. The injured party and/or dependents are apt to be much younger than normal retirement age such that the payments may well stretch out for 30, 40, and 50 years or more. Lump sum payments may be scheduled to coincide with particular events such as college for dependent children.

The 1980 changes in the SVL initiated a set of valuation interest factors for each year of issue so as to roughly have the factor correspond to the investment rates at the time at which monies are received and invested. In 1980 the emphasis in the dynamic valuation interest rate was on the valuation interest rates for group guaranteed interest contracts (GIC). Group GIC's generally have had a guaranteed interest period of 5-10 years with a lump sum available at the end of the period. Any renewal of an interest guarantee and period is generally considered as a new issue for valuation purposes, whether the year of issue or the change in fund method is used.

Most retirement annuities under individual or group programs had level or slightly increasing payments with payments beginning at age 60, 65 or 70, such that for annuities in course of payments, there should be little reinvestment risk and reserves should decrease.

There is a large reinvestment risk in case of structured settlements. There is also a risk that the original assets may be called or exchanged for lower yielding assets.

Guideline IX-B would split up the contract and treat that portion of the payments meeting the test as an annuity and any excess payments separately for purposes of determining the appropriate valuation interest factors based on the duration to first payment of such excess. The guideline also offers a new dual interest procedure as an alternative to splitting the payments.

The guideline recognizes that the use of the statutory formulae with the rates determined based on the date of purchase may be inappropriate where the assets have been exchanged or acquired in later years. It is suggested that the examiner may wish to adjust the issue year for selection of the valuation interest factors so as to make them consistent with the date of investment.

It is recognized that these procedures for determining statutory formulae reserves are only temporary while the Special Committee on Valuation is developing a new statutory formula to go along with a valuation of liabilities based on the supporting assets and the actuary's best judgment to account for reasonable deviations.

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Actuarial Guideline IX–C

USE OF SUBSTANDARD ANNUITY MORTALITY TABLES IN VALUING IMPAIRED LIVES UNDER INDIVIDUAL SINGLE PREMIUM IMMEDIATE ANNUITIES

The NAIC model Standard Valuation Law, Section 4a, A(2), permits modifications of annuity mortality tables approved by the commissioner. In states which have adopted this or similar Standard Valuation Law language, this guideline provides for modifications of annuity mortality tables solely for the purpose of valuing:

> Individual single premium immediate annuities not covered by Guideline IX-A, but for which medical records indicate the expectation of life has been reduced and for which the premium charged reflects such reduction,

A substandard annuity mortality table may be used where the annuitant (or measuring life) has relevant hospital records, treating physicians' reports, and/or independent medical evaluations from those medical doctors that have been used during the underwriting process and have been retained in the underwriting file of the company as proof of the individual's impaired health and shortened longevity. The medical assessment must support at least a 25% reduction in the expectation of life (based on either the current valuation table or the company's pricing table, consistently applied) compared to a normally healthy individual at the same age and gender.

In such case the insurer may modify the statutory annuity mortality table or tables cited in Section 3a of the Standard Valuation Law or in any regulation promulgated pursuant to such section so as to reflect the longevity based on a medical doctor's written evaluation or records as indicated above. The table may be modified by a percentage of standard mortality or by a specified number of extra deaths or by a combination thereof, provided that the mortality table so adjusted produces reserves that are at least as great as the minimum reserves indicated below. The percentage extra mortality or the specified number of extra deaths may vary by duration. A rated up age with the standard annuity table which is approximately equivalent to the actual age on the substandard annuity table may be used only if the procedure is modified to produce reserves that at each duration are at least as great as the minimum reserves indicated below.

The fact that a company has held minimum reserves as herein described shall in no way relieve the actuary from considering whether such reserves are adequate.

Minimum Reserves

The minimum reserves for applicable annuity contracts are the reserves obtained by making a constant addition to the mortality rate of the otherwise applicable valuation mortality table. The amount of the constant addition is determined as follows:

1) Calculate the present value of future benefits at issue for each contract using a rated up age, the applicable valuation mortality table, and the appropriate level Plan Type A interest rate for contracts without cash settlement options. The rated up age must produce an expectation of life under this valuation mortality table whose percent reduction from the actual age expectation of life under this table is not greater than the percent reduction in the expectation of life, supported by the medical assessment above, which qualified the contract to utilize the mortality adjustments provided by this actuarial guideline.

2) Solve for the constant addition to the true age mortality rates such that the present value of future benefits at issue is equal to or greater than the present value obtained in 1). The base mortality table and the valuation interest rate shall be the same as used in 1).

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The constant addition to the mortality table herein described shall be made as of the issue date and, once determined, held constant for the period of time that the contract remains in force. The addition of a constant to the valuation mortality rate produces a gradually declining percentage extra mortality such that reserves will grade into standard reserves at the end of the standard valuation mortality table thereby making the reserve more conservative (closer to standard) each year that the annuitant or measuring life lives.

Where an insurer uses a modified table with higher mortality rates or a rated age with an unmodified table for impaired lives under individual single premium immediate annuities, such insurer shall maintain records of actual to expected mortality to monitor the appropriateness of the substandard mortality. The appointed actuary must comment on the appropriateness of the substandard mortality and report any material deviations. Such comments and report should be provided in the actuarial memorandum which supports the annual actuarial opinion.

Background

Guideline IX-A provides a methodology to allow less than a standard reserve to be held at issue for certain kinds of pay-out annuities and for grading the reserve toward standard reserves over the remaining lifetime of the annuitant using the "constant extra death" method (CED). The longer the annuitant lives, the closer reserves get to standard reserves.

Guideline IX-A says, "Because experience and methodology are still emerging for substandard annuities, it is expected that this whole subject will be reviewed again in the not too distant future, both as it applies to whether the criteria herein established for settlement annuities are too conservative and also whether or how it might be acceptable to apply similar standards to substandard non-settlement annuities".

It has now been almost 11 years since Guideline IX-A was adopted and it appears the industry has done a responsible job of underwriting and valuing substandard annuities covered by Guideline IX-A. Structured settlement mortality studies done by the Society of Actuaries bear this out. (See the 1995-1996 Reports of the Society of Actuaries, starting on page 395.)

Guideline IX-A has been successful in allowing structured settlements to be priced fairly and has benefited injured parties and society in general. There is no evidence that there has been any strain to insurance companies from under reserving due to Guideline IX-A.

For some time, a number of companies have had a significant and increasing opportunity to provide immediate annuities at less than a standard price to a growing number of potential clients not covered by Guideline IX-A. However, the potential price reductions that the industry can give consumers, perhaps 15% to 25% of the single premium on some cases, depending on the benefit stream desired, are greatly reduced because of the current requirement to hold standard reserves. The initial statutory strain (loss) on highly substandard cases can easily exceed 50% or 100% of the single premium, which requires a significantly increased price to the customer over what could be charged if less than standard reserves were permitted. With Guideline IX-A type reserves, the strain might be reduced to something closer to 10%.

The population is aging and the need for fairly priced single premium immediate annuity benefits is substantially increasing. Forcing companies to hold standard reserves results in many people being overcharged (for the extra cost of capital associated with the higher reserve) at a time in their life when they may have the greatest need.

Since this is an area with little experience, it is required that an insurer monitor the experience in order to be able to justify its choice of an adjusted mortality assumption. It is recognized that the initial liability pertains to a large extent to payments that are certain and not contingent upon survival. This is because the majority of non-settlement substandard contracts contain a certain period and most of the benefits fall

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within that certain period. It is also noted that the interest discount factor in the early durations is far more important than the mortality element. The selection of the interest discount factor is the subject of Guideline IX-B.

Because the standard annuity valuation table is an aggregate table, there is some concern that carving out the substandard lives may cause the table to be inadequate for the remaining lives. As a result, it is recommended that an individual life have a significant impairment before use of a substandard valuation table is allowed. For this purpose, significant has been defined as a medical condition that reduces the expectation of life of the individual by at least 25% compared to a normal, healthy life. The reasoning is that not very many lives that are significantly substandard (i.e. greater than a 25% reduction in the expectation of life) are contained in the underlying mortality of individual non-settlement annuity mortality tables. Thus, treating them separately will not diminish the adequacy of the standard table. For convenience, either the applicable individual annuity valuation table or the company's pricing table can be used to measure the change in the expectation of life.

A public policy issue was discussed wherein this actuarial guideline could be viewed as rewarding unhealthy behavior. However, this actuarial guideline would benefit others who were simply unfortunate to be in an impaired condition. It was noted that it would be difficult or impossible to carve out those with intentionally unhealthy behavior. Ultimately it was believed that this actuarial guideline provides for reasonable public policy to facilitate lower single premiums for substandard annuitants.

Effective Date

This Guideline will be effective for contracts issued on or after January 1, 2001.

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Actuarial Guideline X

GUIDELINE FOR INTERPRETATION OF NAIC STANDARD NONFORFEITURE LAW FOR INDIVIDUAL DEFERRED ANNUITIES

Text

For contracts which provide cash surrender benefits, the NAIC Model Law prescribes a basis for determination of minimum cash surrender benefits. That law does not require that a company grant additional amounts in excess of the amounts guaranteed in the contract, either in the form of excess interest credits or otherwise. When such additional amounts have been credited to the contract, the question of how the Model Law applies to such amounts must be considered.

Under one interpretation the portion of the maturity values which would arise from such amounts may be discounted to the date of surrender at an interest rate 1% higher than the rate specified in the contract for accumulating such amounts. This interpretation would permit a surrender charge against such amounts on the same basis as the surrender charge which may be applied to the contractually guaranteed portion of the interest credited to the contract.

Under another interpretation such amounts could not be treated as providing a portion of the maturity value and, therefore, would be included in the phrase "any additional amounts credited by the company to the contract." This interpretation would require that the cash surrender value be increased by 100% of the accrued value of such amounts.

By providing for a surrender charge to be made in determining the minimum cash surrender value, the Model Law enables a company to provide for recovery of all or part of any (1) excess first year expenses not yet recovered, and (2) potential investment losses at surrender. The reason for permitting surrender charges to be made against accumulated amounts of contractually guaranteed interest are equally valid reasons for permitting surrender charges against any non-guaranteed interest credited. If such surrender charges were not permitted, companies offering such contracts may be discouraged from crediting as much additional interest as they might if the additional interest were to contribute to the minimum cash surrender value in the same manner as do the interest amounts derived from the rates guaranteed in the contract.

In view of the above considerations, the following guidelines are recommended:

I. Treatment of Amounts of Excess Interest Credited to Deferred Annuity Contracts

The NAIC Standard Nonforfeiture Law for Individual Deferred Annuities shall be interpreted to permit the portion of the maturity value which would arise from the amounts of interest credited in excess of the minimum rates guaranteed in the contract to be discounted to the date of surrender at an interest rate 1% higher than the rate specified in the contract for accumulating such amounts, provided such excess interest is declared prior to the period for which it is to be effective, and provided such excess interest accrues over the effective period. Amounts of excess interest treated in accordance with the above interpretation shall not be included by the phrase "additional amounts credited by the company to the contract" in Section 6 of the Model Law.

II. Treatment of Dividends Credited to Deferred Annuity Contracts

No single rule can be given for the treatment of dividends credited to deferred annuity contracts. The contractual wording of the applicable dividend option must be taken into account together with the appropriate provisions of the NAIC Standard Nonforfeiture Law for Individual Deferred Annuities.

If the dividend option in effect provides that dividends be left on deposit at interest, without any further qualification, then the cash surrender value should be increased by the full accumulated amount. In this

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case, the phrase “increased by any additional amounts credited by the company to the contract” applies and no surrender charge may be made.

In other cases, the dividends may be added, directly or indirectly, to the contractual value and made subject to the surrender charge provision. This would be the case when dividends are applied to purchase additional paid-up benefits or applied as premiums.

Contracts may contain other provisions or variations of these provisions. In such cases, the terms of the contract and the provision of the NAIC Standard Nonforfeiture Law for Individual Deferred Annuities should be taken into account.

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Actuarial Guideline XI

EFFECT OF AN EARLY ELECTION BY AN INSURANCE COMPANY OF AN OPERATIVE DATE UNDER SECTION 5-C OF THE STANDARD NONFORFEITURE LAW FOR LIFE INSURANCE

Section 5-C of the Standard Nonforfeiture Law for Life Insurance May be Made Operational for One or More Plans at a Time Provided That:

A. Sales are discontinued in this state on all like plans using rates and values generated by past requirements;

B. Sales are discontinued in all other states which have enacted the new legislation on all like plans using rates and values generated by past standards, provided the state of sale has allowed changes to 1980 requirements on a plan-by-plan basis;

C. Once the new law has been made operational for one plan, the new law shall be operational for all subsequent new plans of the same generic form to be marketed in this state unless the insurer can demonstrate to the Commissioner's satisfaction the need to continue the prior set of requirements;

"Like plans," as mentioned in Sections A and B, refers to plans with the same benefits, including cash values, and with the same premium paying period and pattern of premiums;

"Generic form," as mentioned in Section C, refers to generic groups, such as ordinary vs. group, term vs. permanent, flexible cash value vs. fixed cash value, separate account vs. fixed account.

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Actuarial Guideline XII

INTERPRETATION REGARDING VALUATION AND NONFORFEITURE INTEREST RATES

Actuarial Guideline XII was withdrawn on March 7, 1993.

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Actuarial Guideline XIII

GUIDELINE CONCERNING THE COMMISSIONERS' ANNUITY RESERVE VALUATION METHOD

Preamble

At its December 1976 meeting, the NAIC adopted the Commissioners' Annuity Reserve Valuation Method (CARVM) and incorporated it in its Model Standard Valuation Law. CARVM is now included in the laws of nearly all of the states. Differences in interpretation of CARVM have developed in practice, particularly on whether and under what conditions surrender charges may be taken into account in determining CARVM reserves. This guideline is intended to clarify which surrender charge factors may be taken into account and which are to be disregarded under CARVM.

Reserves according to CARVM depend in part upon the present values of "future guaranteed benefits, including guaranteed nonforfeiture benefits." It has always been recognized that this phrase, as used in the NAIC Model Standard Valuation Law, includes cash surrender values based on contractual guarantees after reduction for any contractual surrender charges available to the insurer. This is illustrated in the Proceedings. See *Proceedings of the National Association of Insurance Commissioners*, Vol. 1 (1977), 538-45.

Guideline

The phrase, "future guaranteed benefits, including guaranteed nonforfeiture benefits," as used in CARVM include the cash surrender values based on contractual guarantees after reduction for any surrender charges available under the contract.

In recent years, annuity contracts with contingent surrender charges have become more prevalent. For example, a contract may provide the option to surrender without surrender charge if the rate at which interest is credited falls below a specified rate, referred to in this guideline as the "bail-out" rate. Contingent surrender charges may not be available upon cash surrender at future contract anniversaries, and it is not consistent with the conservative nature of CARVM to reduce the value of future guaranteed benefits on account of such contingent surrender charges.

The value of future guaranteed benefits under CARVM may not be reduced by contingent surrender charges which may not be available upon cash surrender.

There may be some contracts with contingent surrender charges with bail-out rates which are so low that it would not be contrary to the conservative intent of CARVM to treat such surrender charges as available. The calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty years, which is used in the Standard Valuation Law in connection with the definition of guaranteed duration for most annuities and guaranteed interest contracts, provides an appropriate measure for this purpose. Whether or not such surrender charges should be treated as available should be determined as of December 31, 1984 for contracts in force at the date and as of the date of issue for contracts subsequently issued.

For contracts issued on and after January 1, 1985, contingent surrender charges with bail-out rates less than or equal to the calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty years issued in the same year may be treated as available. For contracts issued prior to January 1, 1985, contingent surrender charges with bail-out rates less than or equal to 6.00% (the calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty years issued in 1984) may be treated as available.

There are some contracts with contingent surrender charges with bail-out rates which are a function of an external index whose future values are not known. Judgment is required to determine whether or not such

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surrender charges may be treated as available. Comparison to the calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty years may be useful.

For contracts with contingent surrender charges with bail-out rates which are a function of an external index, a judgment as to the availability of the surrender charges may be made by comparing historical values of the function with corresponding values of the calendar year statutory valuation interest rate for life insurance with guarantee duration in excess of twenty years. If the values of the function have generally been less than or equal to the valuation rates, then the surrender charges may be treated as available.

For the purpose of this guideline, in the case of a variable annuity that offers the policyholder a choice of multiple investment options, a surrender charge that may be waived for all the accounts of the contract by reference to one or more of the accounts will be treated as a contingent surrender charge that may not be available upon cash surrender with respect to the entire contract. If no surrender charge is imposed on transfers among the accounts, and the surrender charge may be waived for one account, provided the formula for the availability of the waiver is set at the date of issuance, then the surrender charge will be treated as a contingent surrender charge that may not be available upon cash surrender with respect to the entire contract.

Since this guideline is intended to apply to all contracts in force that are subject to CARVM, its application may work an undue hardship on some insurers who have, on the basis of a good faith interpretation of CARVM, held reserves less than required by this guideline. In cases of severe hardship, state insurance commissioners may wish to permit insurers to conform on a gradual basis.

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Actuarial Guideline XIV

SURVEILLANCE PROCEDURE FOR REVIEW OF THE ACTUARIAL OPINION FOR LIFE AND HEALTH INSURERS

To assist regulators in their responsibility for surveillance of life and health insurers, the NAIC adopts the following interim procedure for use of the Actuarial Opinion to be used until such time as model legislation and/or regulations are adopted and become effective.

1. The regulator should accept Actuarial Opinions only from qualified actuaries. The educational and experience standards established by the American Academy of Actuaries for this purpose offers evidence that an individual is so qualified.

2. The regulator should determine if an opinion is qualified in any respect, or omits items from the outline provided in the Instructions to the Blank. If so, a follow up with the actuary rendering the opinion as to the nature of the qualification or omission is appropriate if the opinion does not provide a satisfactory explanation.

3. The regulator should examine the circumstances where the actuary rendering the opinion differs from the prior actuary, and ascertain the reasons for the change. In some cases the regulator may wish to discuss the change with the current and prior actuaries.

4. The regulator should, if desired, obtain for reviews, documentation supporting the Actuarial Opinion. Except in matters of professional discipline, the regulator's use of these documents should be considered within the department's guidelines for confidential information.

5. The regulator may require that the actuary furnish an Actuarial Report supporting the Actuarial Opinion. The report should conform to the standards of the American Academy of Actuaries with respect to Actuarial Reports (Opinion 3 to the Guides to Professional Conduct). It should document the methodology and approach to assumptions used in making the opinions and, additionally, provide specific details in reference to items in 6 through 10 below if such details are required by the regulator.

6. In the Actuarial Report, the actuary providing the opinion should refer to the NAIC Insurance Regulatory Information System (IRIS) ratios, point out ratio values outside the prior year's range of usual values, and provide explanations for those which are significant.

7. In the Actuarial Report, the actuary providing the opinion should make specific reference to the extent to which the good and sufficient analysis considered all the unmatured obligations of the company, in aggregate, guaranteed under the terms of its policies. (Note: To the extent that the insurer declares guarantees more favorable than those in the policy, such declared guarantees shall be used in the calculation of all the unmatured obligations.)

8. In the Actuarial Report, the actuary providing the opinion should make specific reference as to whether the good and sufficient analysis, with respect to annuities and other products with benefits (guaranteed or non-guaranteed) sensitive to interest rates, considered future insurance and investment cash flows as they would emerge under a reasonable range of future interest rate scenarios, and, if so, what those considerations were.

9. In the Actuarial Report, the actuary providing the opinion should make specific reference as to whether the good and sufficient analysis considered the inter-relationships of assumptions with respect to guaranteed benefit payments, future expenses, policyowner dividends, and post-issue premium or benefit adjustments, especially among persistency, mortality, morbidity, inflation, and interest rates, and, if so, what those consideration were.

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10. In the Actuarial Report, the actuary providing the opinion should document the extent to which the opinion is influenced by a continuing business assumption, and, if the impact is material, comment on the company's plan of operations with regard to this assumption as it affects assumed expenses and interest rates, and future reserve requirements.

11. A review of the documentation obtained in (4) above, undertaken or sponsored by the regulator, should:

    a. Be done by a qualified reviewer;

    b. Emphasize an examination of the appropriateness of the actuary's work process, methodology, and approach to assumptions.

12. If at any time during the review, the regulator requires more information deemed to be material to the development of the opinion, the company would be expected to comply with requests for such information.

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Actuarial Guideline XV

ILLUSTRATIONS GUIDELINE FOR VARIABLE LIFE INSURANCE MODEL REGULATION

Any sales illustration shown or furnished in connection with the sale of variable life insurance must conform with the following requirements except that these requirements only apply to the variable portion of contracts with fixed and variable funding options. Item 9 specifically pertains to variable life insurance contracts offering both fixed and variable funding options.

1. The hypothetical interest rates used to illustrate accumulated policy values must be an annual effective gross rate after brokerage expenses and prior to any deduction for taxes, expenses and contract charges.

2. If illustrations of accumulated policy values are shown then for the highest interest rate used, one illustration must be based solely upon guarantees contained in the policy contract being illustrated. (For example, if the illustration includes the effect of mortality charges and administrative charges which are below the guaranteed maximums for such charges, an illustration must be prepared which involves the effect of the maximum charges.)

3. Except for illustrations contained in the prospectus, the pattern of premium payments used in an illustration should be the initial pattern requested by the proposed policyholder at inception or upon changes in face amount requested by the policyholder.

4. If the illustrated policy contract provides for a variety of investment options, the illustration may either use an asset charge which is reasonably representative or use the asset charge of a particular option. The illustration should clearly identify the asset charge and either label it "hypothetical" or identify the fund.

5. The illustration must disclose the transaction charges which will be levied against the contract because of transactions requested in accordance with rights and privileges specified in the policy contract. Any charge for the exercise of a right or privilege upon which the illustration is based must be reflected in the illustrated values. The nature of any other such charges must be disclosed in a clear statement accompanying such illustrations. (For example, a charge to switch from one investment option or death benefit option to another.)

6. A clear statement must be made following the Table of Illustrated Accumulated Policy Values that use of hypothetical investment results does not in any way represent actual results or suggest that such results will be achieved and must indicate that the policy values which actually arise will differ from those shown whenever the actual investment results differ from the hypothetical rates illustrated. Assumptions upon which illustrations are based must be clearly disclosed.

7. Any sales illustration to a prospective policyholder must reflect the policy being presented accurately. Misleading statements or captions or other misrepresentations are prohibited.

8. The requested sales illustration must be printed clearly and legibly on hard paper copy. An illustration displayed on a computer screen may be used in addition to, but not as a substitute for, hard paper copy.

9. In connection with variable life insurance contracts offering both fixed and variable funding options:

    a. An illustration of the variable funding option must comply with these guidelines;

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b. If an illustration of the fixed funding option is shown, accumulated policy values must be shown on the basis of guaranteed rates. One or more additional rates may also be shown but such rates may not exceed current rates;

c. A summary illustration may be given in which results from comparable illustrated and hypothetical interest rates are combined. Such summary must cross-reference to the accompanying separate illustrations of the fixed and variable funding options.

10. Nothing herein shall prohibit the distribution to the prospective policyholder of illustrations in addition to those required by Article VII of the NAIC Model Variable Life Insurance Regulation provided that, except for Item 3 which shall only apply to required illustrations under Article VII, such additional illustrations comply with the standards set forth herein.

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Actuarial Guideline XVI

CALCULATION OF CRVM RESERVES ON SELECT MORTALITY AND/OR SPLIT INTEREST

Text

When CRVM reserves are being calculated, it is necessary to determine the value of ${}_{19}P_{x+1}$. The Standard Valuation Law permits the use of Select Mortality Factors with the 1980 CSO Table. While the maximum valuation interest rate for any policy is level for all durations, the law permits the use of other interest rates as long as the resulting reserves are not less than those according to the minimum standard. Thus, it is possible to calculate reserves by the CRVM method using split interest rates, i.e., interest rates that are not the same at all durations.

When either Select Mortality Factors or split interest are involved, the "net level annual premium on the nineteen-year premium whole life plan" is the renewal net level premium for a 20-payment life valued on the full preliminary term basis. That is ${}_{19}P_{[x]+1}$ should be used instead of, for example, ${}_{19}P_{[x+1]}$.

Background Information

The Report of the Society of Actuaries Committee on Specifications for Monetary Values - 1980 CSO Tables recommended this approach. This Report was accepted by the Board of Governors of the Society and forwarded to the NAIC early in 1984. This approach is logical because it is consistent with the calculation of the "net level annual premium equal to the present value, at the date of issue, of such benefits provided for after the first policy year, divided by the present value, at the date of issue, of an annuity of one per annum payable on the first and each subsequent anniversary of such policy on which a premium falls due....." (See Section 4 of the Standard Valuation Law, emphasis added.)

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Actuarial Guideline XVII

CALCULATION OF CRVM RESERVES WHEN DEATH BENEFITS ARE NOT LEVEL

Text

In the definition of the Commissioners' Reserve Valuation Method, the Standard Valuation Law (Section 4) refers to the "net level annual premium on the nineteen-year premium whole life plan for insurance of the same amount...." The law does not define "the same amount" for cases when death benefits are not level. For policies issued after the operative date of Section 5-c of the Standard Nonforfeiture Law for Life Insurance (Section 5-c provides for the use of the 1980 CSO Table, among other things) "the same amount" is to be taken as the renewal nine-year arithmetic average, i.e., the arithmetic average of the death benefit at the beginning of each of policy years 2 through 10, inclusive.

Background Information

The Report of the Society of Actuaries Committee recommended this approach. Walter O. Menge in his paper Commissioners Reserve Valuation Method, RAIA XXXV (see p 277ff, especially p 283), defined an "equivalent level renewal amount" which has been accepted and still is the appropriate function for policies issued before the operative date of Section 5-c of the Standard Nonforfeiture Law for Life Insurance. The Society Committee indicated that the strongest factor that weighed in its conclusion was the effect on reserves for such plans as jumping juvenile. Menge noted the similarity between his definition of "equivalent level renewal amount" and the definition of "equivalent uniform amount" in Section 5 of the Standard Nonforfeiture Law for Life Insurance. In the same way, the function prescribed above is consistent with the "average amount of insurance" in Section 5-c of the Standard Nonforfeiture Law for Life Insurance. A principal reason for the change in the Standard Nonforfeiture Law was to simplify calculations, and this guideline will also have that result.

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Actuarial Guideline XVIII

CALCULATION OF CRVM RESERVES ON SEMI-CONTINUOUS, FULLY CONTINUOUS OR DISCOUNTED CONTINUOUS BASIS

Text

The Standard Valuation Law uses the "excess of (a) over (b)" in the definition of the modified net premiums in Section 4. If reserves are calculated on a basis other than curtate, i.e., using semi-continuous, fully continuous or discounted continuous functions, the excess of (a) over (b) may be calculated using the same basis (semi-continuous, etc.).

Background Information

The Report of the Society of Actuaries Committee recommended this approach. The excess of (a) over (b) is sometimes referred to as the initial expense allowance. Basing this expense allowance on curtate functions is conservative as this results in the smallest amount of expense allowance. Also, the expense allowance is the same regardless of which type of functions are used. On the other hand, the use of curtate functions when the basic calculation is based on other functions can result in complications in calculation. The difference in the resulting reserves does not justify the additional complication.

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Actuarial Guideline XIX

1980 CSO MORTALITY TABLE WITH TEN-YEAR SELECT MORTALITY FACTORS

Text

The Standard Valuation Law and the Standard Nonforfeiture Law for Life Insurance make reference to the Commissioners' 1980 Standard Ordinary Mortality Table with Ten-Year Select Mortality Factors. The Ten-Year Select Mortality Factors referred to are those developed by the Society of Actuaries Special Committee to Recommend New Mortality tables for Valuation (see Report on p. 617ff and table of Ten-Year Select Mortality Factors on p. 669 of TSA XXXIII).

The NAIC model regulation regarding mortality tables independent of sex refers to certain specific tables which are blends of the male and female mortality rates of the 1980 CSO Table and specifies that these tables may be used with or without Ten-Year Select Mortality Factors. The Ten-Year Select Mortality Factors to be used with these blended tables are to be determined by use of the formula in the letter from Robert J. Johansen to Ted Becker reproduced on p. 457 of NAIC Proceedings 1984 Vol. I.

Background Information

The published report of a committee of the Society of Actuaries contains two sets of alternative select mortality factors. While that committee recommended that the alternative factors not be adopted, their publication has caused some confusion.

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Actuarial Guideline XX

JOINT LIFE FUNCTIONS FOR 1980 CSO MORTALITY TABLE

Text

The tables of uniform seniority and the "Ultimate 1xx Tables" in Appendix 5 of the Report of the Society of Actuaries Committee on Specifications for Monetary Values - 1980 CSO Tables are acceptable for use in calculating reserves or nonforfeiture values for joint life policies on the 1980 CSO basis. These tables from Appendix 5 of the report are reproduced on the following pages of this Actuarial Guideline. These tables are numbered A5-1, A5-6 and A5-7 to coincide with the page numbers of those tables in Appendix 5 of the Society Committee report. (These are the only tables considered necessary for the purpose of this guideline.)

Other methods of calculating joint life functions may also be acceptable. In particular, it is acceptable to calculate "exact" joint life functions using published 1980 CSO mortality rates for the actual ages and genders of the lives to be insured.

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1980 CSO and 1980 CET TABLES

A5-1

Tables showing the deduction to be made from the age of the older of two lives in order to obtain the equivalent equal ages. The equivalent equal ages are then used to enter tablesof functions derived from tables based on one male and one female of the same age.

MALE/MALE

Difference in Ages	Deduct from Older Age
0-1 Years	-2
2-3	-1
4-6	0
7-9	1
10-13	2
14-19	3
20-32	4
33-55	5
56 & Over	6

FEMALE/FEMALE

Difference in Ages	Deduct from Older Age
0-1 Years	3
2-3	4
4-6	5
7-9	6
10-13	7
14-20	8
21-48	9
49-70	8
71 & Over	7

OLDER MALE/YOUNGER FEMALE

Difference in Ages	Deduct from Older Age
0-1 Years	0
2-4	1
5-8	2
9-14	3
15-27	4
28-54	5
55 & Over	6

OLDER FEMALE/YOUNGER MALE

Difference in Ages	Deduct from Older Age
0 Years	0
1-2	1
3-4	2
5-6	3
7-8	4
9-11	5
12-14	6
15-18	7
19-25	8
26-47	9
48-70	8
71 & Over	7

It is not appropriate to apply values from the FEMALE/FEMALE column so that a negative joint equal age results. In such situations equivalent equal age zero should be used.

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1980 CSO AND 1980 CET TABLES

ULTIMATE 1_{XX} TABLES

A5-6

MALE/FEMALE - JOINT EQUAL AGES

Age	1980 CSO ANB	1980 CET ANB	Age	1980 CSO ANB	1980 CET ANB
0	60,560,928	16,765,573,343	50	50,059,381	12,731,016,815
1	60,133,368	16,611,833,035	51	49,476,690	12,538,651,151
2	60,016,709	16,554,688,329	52	48,854,768	12,334,020,364
3	59,908,679	16,500,057,858	53	48,189,855	12,115,954,884
4	59,802,641	16,446,102,669	54	47,476,163	11,882,965,072
5	59,699,780	16,393,146,218	55	46,711,322	11,634,492,272
6	59,600,678	16,341,343,876	56	45,894,341	11,370,389,297
7	59,505,913	16,290,849,123	57	45,025,102	11,090,791,424
8	59,415,464	16,241,650,759	58	44,105,689	10,796,774,543
9	59,328,717	16,193,575,473	59	43,138,010	10,489,174,436
10	59,243,877	16,146,128,297	60	42,120,816	10,168,205,698
11	59,160,343	16,099,143,064	61	41,050,947	9,833,163,320
12	59,073,969	16,051,489,601	62	39,922,456	9,482,414,384
13	58,981,223	16,002,211,528	63	38,727,178	9,114,117,409
14	58,878,596	15,950,364,363	64	37,455,765	8,726,038,290
15	58,763,783	15,895,335,606	65	36,104,361	8,317,746,958
16	58,635,678	15,836,840,771	66	34,673,184	7,890,297,942
17	58,494,366	15,774,918,724	67	33,168,368	7,446,389,780
18	58,341,111	15,709,926,059	68	31,598,177	6,989,702,695
19	58,180,090	15,643,001,774	69	29,974,031	6,524,328,290
20	58,012,531	15,574,485,426	70	28,301,780	6,052,945,571
21	57,841,394	15,505,178,968	71	26,582,447	5,577,062,990
22	57,669,027	15,435,715,764	72	24,815,246	5,097,324,032
23	57,497,173	15,366,563,757	73	22,997,777	4,614,505,500
24	57,326,406	15,297,875,217	74	21,131,047	4,130,490,018
25	57,156,720	15,229,646,694	75	19,226,083	3,649,618,370
26	56,989,251	15,162,179,359	76	17,303,859	3,178,781,104
27	56,822,842	15,095,162,526	77	15,392,302	2,726,027,311
28	56,656,351	15,028,290,956	78	13,522,753	2,299,540,338
29	56,488,648	14,961,264,778	79	11,725,985	1,906,364,931
30	56,318,617	14,893,789,474	80	10,025,717	1,551,018,508
31	56,145,156	14,825,724,856	81	8,438,546	1,235,758,486
32	55,966,614	14,756,488,721	82	6,977,243	961,383,029

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ULTIMATE 1_{XX} TABLES (CONT'D)

Age	1980 CSO ANB	1980 CET ANB	Age	1980 CSO ANB	1980 CET ANB
33	55,783,044	14,686,100,270	83	5,651,637	727,555,449
34	55,592,824	14,614,138,379	84	4,470,897	533,319,971
35	55,393,802	14,540,044,697	85	3,444,826	377,233,215
36	55,185,521	14,463,709,462	86	2,579,176	256,609,122
37	54,964,779	14,384,303,697	87	1,872,714	167,383,564
38	54,728,980	14,301,162,422	88	1,316,256	104,405,498
39	54,476,679	14,213,496,296	89	893,896	62,098,302
40	54,204,296	14,119,829,355	90	585,350	35,106,033
41	53,909,967	14,019,719,765	91	368,642	18,789,100
42	53,590,820	13,911,767,923	92	222,531	9,470,646
43	53,246,767	13,795,743,779	93	128,118	4,461,337
44	52,876,702	13,671,168,213	94	69,801	1,940,503
45	52,480,127	13,537,874,323	95	35,420	760,483
46	52,055,563	13,395,455,885	96	16,202	255,127
47	51,602,680	13,243,953,279	97	6,225	65,264
48	51,120,195	13,083,039,247	98	1,699	9,381
49	50,606,437	12,912,305,585	99	200	200

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ULTIMATE 1_{XX} TABLES

A5-7

MALE/FEMALE - JOINT EQUAL AGES

Age	1980 CSO ALB	1980 CET ALB	Age	1980 CSO ALB	1980 CET ALB
0	60,347,148	16,688,703,189	50	49,768,036	12,634,833,983
1	60,075,038	16,583,260,682	51	49,165,729	12,436,335,758
2	59,962,694	16,527,373,094	52	48,522,312	12,224,987,624
3	59,855,660	16,473,080,264	53	47,833,009	11,999,459,978
4	59,751,210	16,419,624,444	54	47,093,742	11,758,728,672
5	59,650,229	16,367,245,047	55	46,302,832	11,502,440,784
6	59,553,296	16,316,096,500	56	45,459,722	11,230,590,360
7	59,460,688	16,266,249,941	57	44,565,396	10,943,782,984
8	59,372,090	16,217,613,116	58	43,621,850	10,642,974,490
9	59,286,297	16,169,851,885	59	42,629,413	10,328,690,067
10	59,202,110	16,122,635,680	60	41,585,882	10,000,684,509
11	59,117,156	16,075,316,332	61	40,486,702	9,657,788,852
12	59,027,596	16,026,850,564	62	39,324,817	9,298,265,896
13	58,929,910	15,976,287,946	63	38,091,472	8,920,077,850
14	58,821,190	15,922,849,984	64	36,780,063	8,521,892,624
15	58,699,730	15,866,088,188	65	35,388,772	8,104,022,450
16	58,565,022	15,805,879,748	66	33,920,776	7,668,343,861
17	58,417,738	15,742,422,392	67	32,383,272	7,218,046,238
18	58,260,600	15,676,463,916	68	30,786,104	6,757,015,492
19	58,096,310	15,608,743,600	69	29,137,906	6,288,636,930
20	57,926,962	15,539,832,196	70	27,442,114	5,815,004,280
21	57,755,210	15,470,447,365	71	25,698,846	5,337,193,511
22	57,583,100	15,401,139,760	72	23,906,512	4,855,914,766
23	57,411,790	15,332,219,487	73	22,064,412	4,372,497,759
24	57,241,563	15,263,760,956	74	20,178,565	3,890,054,194
25	57,072,986	15,195,913,026	75	18,264,971	3,414,199,737
26	56,906,046	15,128,670,942	76	16,348,080	2,952,404,208
27	56,739,596	15,061,726,741	77	14,457,528	2,512,783,824
28	56,572,500	14,994,777,867	78	12,624,369	2,102,952,634
29	56,403,632	14,927,527,126	79	10,875,851	1,728,691,720
30	56,231,886	14,859,757,165	80	9,232,132	1,393,388,497
31	56,055,885	14,791,106,788	81	7,707,894	1,098,570,758
32	55,874,829	14,721,294,496	82	6,314,440	844,469,239
33	55,687,934	14,650,119,324	83	5,061,267	630,437,710
34	55,493,313	14,577,091,538	84	3,957,862	455,276,593

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ULTIMATE 1_{XX} TABLES (CONT'D)

Age	1980 CSO ALB	1980 CET ALB	Age	1980 CSO ALB	1980 CET ALB
35	55,289,662	14,501,877,080	85	3,012,001	316,921,168
36	55,075,150	14,424,006,580	86	2,225,945	211,996,343
37	54,846,880	14,342,733,060	87	1,594,485	135,894,531
38	54,602,830	14,257,329,359	88	1,105,076	83,251,900
39	54,340,488	14,166,662,826	89	739,623	48,602,168
40	54,057,132	14,069,774,560	90	476,996	26,947,566
41	53,750,394	13,965,743,844	91	295,586	14,129,873
42	53,418,794	13,853,755,851	92	175,324	6,965,992
43	53,061,734	13,733,455,996	93	98,960	3,200,920
44	52,678,414	13,604,521,268	94	52,610	1,350,493
45	52,267,845	13,466,665,104	95	25,811	507,805
46	51,829,122	13,319,704,582	96	11,214	160,196
47	51,361,438	13,163,496,263	97	3,962	37,322
48	50,863,316	12,997,672,416	98	950	4,790
49	50,332,909	12,821,661,200	99	100	100

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Actuarial Guideline XXI

CALCULATION OF CRVM RESERVES WHEN (B) IS GREATER THAN (A) AND SOME RULES FOR DETERMINATION OF (A)

Text

The Standard Valuation Law used the "excess of (a) over (b)" in the definition of the modified net premiums in Sec. 4. If the excess of (a) over (b) is negative, and the policy is issued on or after January 1, 1987, the excess is to be taken as zero.

The Standard Valuation Law defines (a) as a net level premium, subject to a maximum. The net level premiums for the policy are a uniform percentage of the respective gross premiums such that the present value at issue of the net level premiums payable on and after the first anniversary is equal to the present value at issue of the benefits provided for by the policy after the first anniversary. The net level premium used in determining (a) is the net level premium payable on the first anniversary. The maximum for (a) is the net level premium on the 19-year premium whole life plan for a policy with level premiums issued at an age one year higher than the age at issue of the policy.

The value of (a) is to be calculated as defined in the Standard Valuation Law, even if the resulting reserves are not equal to reserves according to the full preliminary term method.

Background Information

The Report of the Society of Actuaries Committee on Specifications for Monetary Values—1980 CSO Tables recommended that a negative excess of (a) over (b) be taken as zero. Walter O. Menge in his paper Commissioners Reserve Valuation Method, RAIA XXXV (see pp. 260 and 261) pointed out the illogic of a negative excess of (a) over (b). A negative excess, if used, would result in CRVM reserves that are greater than net level premium reserves. This principle has been recognized since Menge wrote his paper, but some actuaries are not aware of the paper.

Defining the net level premiums as being a uniform percentage of the respective gross premiums is consistent with the definition in Menge's paper. Since the denominator of (a) is the present value of an annuity commencing on the first anniversary, the logical value for (a) is the net level premium (as defined) payable on the first anniversary.

In his paper, Menge indicates that CRVM reserves are equal to full preliminary term reserves unless the value of (a) is the maximum defined in the Standard Valuation Law, or unless the excess of (a) over (b) is negative. Menge does not appear to have considered the case where the gross premium for the first policy year does not equal the gross premium for the second policy year. For such policies a literal application of the Standard Valuation Law does not result in full preliminary term reserves.

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Actuarial Guideline XXII

INTERPRETATION REGARDING NONFORFEITURE VALUES FOR POLICIES WITH INDETERMINATE PREMIUMS

Text

Indeterminate premium policies provide that premiums after issue will be determined by the insurer based on then current assumptions as to future experience. The policies also provide a schedule of maximum premiums which the premiums actually charged will not exceed.

The minimum nonforfeiture values for an indeterminate premium policy are the greater of those assuming that the gross premiums for the policy are (i) those according to the schedule of gross premiums based on current assumptions at issue and illustrated to prospective policyholders, or (ii) those according to the schedule of maximum gross premiums included in the policy:

Background Information

Indeterminate premium policies are a fairly recent development in life insurance. They can serve a legitimate function by enabling a nonparticipating policy to include a safety margin that need not be called upon unless it is needed. Indeterminate premiums are sometimes used to avoid deficiency reserve requirements. In general, regulators have not objected to this.

Section 6 of the Standard Nonforfeiture Law for Life Insurance refers to "any plan of life insurance which provides for future premium determination, the amounts of which are to be determined by the insurance company based on then estimates of future experience...." This is a direct reference to the types of life insurance policies commonly known as indeterminate premium plans (see "Detailed Analysis of Recommended Changes in the Standard Valuation Law and the Standard Nonforfeiture Law for Life Insurance; NAIC Proceedings - 1981 Vol. II, p. 831). The Standard Nonforfeiture Law for Life Insurance provides that minimum nonforfeiture values for such policies are to be computed by a method consistent with the principles of the Law as determined by regulations promulgated by the commissioner.

Section 5 and Section 5-c of the Standard Nonforfeiture Law for Life Insurance each provide that "the adjusted premiums for any policy shall be calculated on an annual basis and shall be....(a) uniform percentage of the respective premiums specified in the policy for each policy year..." Indeterminate premium policies provide for two amounts of premiums for each year: the actual premium to be charged and the maximum amount of the actual premium. This raises the question of which premium is to be used in setting adjusted premiums as a uniform percentage of the gross premiums.

The maximum premiums have the advantage that they are known at the time the policy is issued. However, use of maximum premiums to determine minimum values can lead to manipulation. A level premium whole life policy has a readily determined set of minimum values in accordance with the Standard Nonforfeiture Law for Life Insurance. If the policy has indeterminate premiums and the premiums illustrated to the customer (with proper disclosure of their indeterminate nature) are level for life, there should be no change in the minimum values. If the minimum values were determined by reference to the maximum premiums and not to the schedule of premiums on the current assumptions, introduction of maximum premiums that increase by duration would result in lower minimum values.

This guideline was written with policies other than universal life insurance in mind. However, it is possible to design a fixed premium universal life insurance policy to which this guideline would be applicable.

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Actuarial Guideline XXIII

GUIDELINE CONCERNING VARIABLE LIFE INSURANCE SEPARATE ACCOUNT INVESTMENTS

A variable life insurance separate account shall be deemed to have sufficient net investment income and readily marketable assets to meet anticipated obligations under policies funded by the account, as required by [statutory reference for state], if, and only if, it can be demonstrated to the satisfaction of the Commissioner that the sum of the market value of readily marketable assets in the account at the date of valuation, plus the anticipated net investment income for the calendar year following the date of valuation exceeds by at least 15% the anticipated death benefits, surrenders, withdrawals and other such obligations payable from current account values during the same period. For the purposes of this demonstration, readily marketable assets means cash or those investments which have readily ascertainable market value and which can be marketed before the close of the next business day; net investment income excludes capital gains or losses; and the value of the anticipated death benefits, surrenders, withdrawals and other such obligations payable during the calendar year following the date of the valuation shall not be estimated at less than 10% of the market value of the account assets at the date of valuation.

If a variable life insurance separate account is divided into separate series, portfolios or other investment subdivisions, each series, portfolio or investment subdivision shall comply with this subsection.

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Actuarial Guideline XXIV

GUIDELINES FOR VARIABLE LIFE NONFORFEITURE VALUES

Minimum cash surrender values for variable life insurance policies shall be determined separately for the basic policy and any benefits and riders for which premiums are paid separately. The methods pertain to a basic policy and any benefits and riders for which premiums are not paid separately.

Minimum cash surrender values for variable life polices may be determined using option B (Retrospective Method), C (Prospective Method), or D (Maximum Charge Method).

A. Definitions

(1) "Valuation Rate" as used in this guideline means the higher of the Assumed Investment Rate (AIR) or guaranteed interest rate included in the policy, if any, otherwise the highest valuation interest rate allowed under the Standard Nonforfeiture Law.

(2) "Net Cash Surrender Value" means the maximum amount payable to the policyowner upon surrender.

(3) "Cash Surrender Value" means the Net Cash Surrender Value plus any amounts outstanding as policy loans.

(4) "Policy Value" means the amount to which separately identified interest credits and or investment return and mortality, expense, or other charges are made under a variable life insurance policy.

(5) "Accumulation Rate" means the net investment return and/or any interest credits applied towards the policy value.

B. Retrospective Method

The minimum cash surrender value (before adjustment for indebtedness and dividend credits) available on a valuation date shall be equal to the value using the Accumulation Rate through that date of the premiums paid minus the accumulation through that date of (i) the benefit charges, (ii) the averaged administrative expense charges for the first policy year and any insurance-increase years, (iii) actual administrative expense charges for other years, (iv) initial and additional acquisition expense charges not exceeding the initial or additional expense allowances, respectively, (v) any service charges actually made (excluding charges for cash surrender or election of a paid-up nonforfeiture benefit) and (vi) any deductions made for partial withdrawals; all accumulations being at the Accumulation Rate at which changes in policy values have been made unconditionally to the policy (or has been made conditionally, but for which the conditions have since been met), and minus any unamortized unused initial and additional expense allowance.

Accumulation for the premiums and for all charges referred to in items (i)-(vi) above shall be based on the Accumulation Rate for the applicable account(s) from and to such dates as are consistent with the manner in which such Accumulation Rate is credited in determining the policy value.

The benefit charges shall include the charges made for mortality and any charges made for riders or supplementary benefits for which premiums are not paid separately. If benefit charges are substantially level by duration and develop low or no cash values, then the Commissioner shall have the right to require higher cash values unless the insurer provides adequate justification that the cash values are appropriate in relation to the policy's other characteristics.

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The administrative expense charges shall include charges per premium payment, charges per dollar of premium paid, periodic charges per thousand dollars of insurance, periodic per policy charges, and any other charges permitted by the policy to be imposed without regard to the policyowner's request for services. The averaged administrative expense charges for any year shall be those which would have been imposed in the year if the charge rate or rates for each transaction or period within the year had been equal to the arithmetic average of the corresponding charge rates which the policy states will be imposed in policy years through twenty in determining the policy value.

The initial acquisition expense charges shall be the excess of the expense charges, other than service charges, actually made in the first policy year over the averaged administrative expense charges for that year. Additional acquisition expense charges shall be the excess of the expense charges, other than service charges, actually made in an insurance-increase year over the averaged administrative expense charges for that year. An insurance-increase year shall be the year beginning on the date of increase in the amount of insurance by policyowner request (or by the terms of the policy).

Service charges shall include charges permitted by the policy to be imposed as a result of a policyowner's request for a service by the insurer (such as the furnishing of future benefit illustrations) or of special transactions.

The initial expense allowance shall be the allowance provided by Items (ii), (iii), (iv) of Section 5, or by Items (ii) and (iii) of Section 5c(1), as applicable, of the Standard Nonforfeiture Law for Life Insurance, as amended in 1980, for a fixed premium, fixed benefit endowment policy with a face amount equal to the initial face amount of the variable life insurance policy, with level premiums paid annually until the highest attained age at which a premium may be paid under the variable life insurance policy, and maturing on the latest date permitted under the policy, if any, otherwise at the highest age in the valuation mortality table. The unused initial expense allowance shall be the excess, if any, of the initial expense allowance over the initial acquisition expense charges as defined above.

If the amount of insurance is subsequently increased upon request of the policyowner (or by the terms of the policy), an additional expense allowance and an unused additional expense allowance shall be determined on a basis consistent with the above and with Section 5c(5) of the Standard Nonforfeiture Law for Life Insurance, as amended in 1980, using the face amount and the latest maturity date permitted at that time under the policy.

The unamortized unused initial expense allowance during the policy year beginning on the policy anniversary at age x + t (where "x" is the issue age) shall be the unused initial expense allowance multiplied by $\ddot{a}_{x+t}/\ddot{a}_x$ where $\ddot{a}_{x+t}$ and $\ddot{a}_x$ are present value of an annuity of one per year payable on policy anniversaries beginning at ages x + t and x, respectively, and continuing until the highest attained age at which a premium may be paid under the policy, both on the morality guaranteed in the policy and the Valuation Rate for the policy. An unamortized unused additional expense allowance shall be the unused additional expense allowance multiplied by a similar ratio of annuities, with $\ddot{a}_x$ replaced by an annuity beginning on the date as of which the additional expense allowance was determined.

(Note: The drafters chose a whole life initial expense allowance for several reasons. Variable life insurance is generally considered a permanent life insurance plan and most companies encourage a premium level which will provide lifetime insurance protection. Every variable life insurance policy of which the drafters are aware has a "net level premium" that could be computed which would guarantee permanent protection using some suitable interest assumption. As a result, it is expected that most variable life insurance policies will be sold as permanent plans.

Traditional whole life insurance, which is accorded a permanent plan expense allowance by the Standard Nonforfeiture Law (SNFL), is much more flexible than is often realized. Premiums may be stopped with term coverage resulting, policy loans can result in "stop and go" premiums, or a vanishing premium arrangement can be effected, all without the permanent plan expense allowance being affected. The SNFL

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does not require cash values for many forms of term insurance. All other permanent plans develop an expense allowance greater than that for whole life insurance under the SNFL.

The alternative of basing the initial expense allowance on a policyowner's "planned premium" was considered but rejected as artificial and subject to substantial manipulation by agents and/or insurers.)

C. Prospective Method

The minimum cash surrender value (before adjustment for indebtedness and dividend credits) available on a date as of which interest is credited to the policy shall be equal to [(1) - (2) - (3) - (4)] where:

(1) is the present value of all future benefits;

(2) is the present value of future adjusted premiums. The adjusted premiums are calculated as described in Sections 5 and 5a or in Section 5c(1), as applicable, of the Standard Nonforfeiture Law for Life Insurance, as amended in 1980. If Section 5c(1) is applicable, the nonforfeiture net level premium is equal to the quantity PVFB/$\ddot{a}_x$, where PVFB is the present value of all benefits at issue assuming future premiums are paid by the policyowner and all guarantees contained in the policy or declared by the insurer, and using the Valuation Rate.

$\ddot{a}_x$ is the present value of an annuity of one per year payable on policy anniversaries beginning at age x and continuing until the highest attained age at which a premium may be paid under the policy.

(3) is the present value of any quantities analogous to the nonforfeiture net level premium which arise because of guarantees declared by the insurer after the issue date of the policy. $\ddot{a}_x$ shall be replaced by an annuity beginning on the date as of which the declaration became effective and payable until the end of the period covered by the declaration.

(4) is the sum of any quantities analogous to (2) which arise because of structural changes in the policy.

(Note: Structural changes are those changes which are separate from the automatic workings of the policy. Such changes usually would be initiated by the policyowner and include changes in the guaranteed benefits, changes in latest maturity date, or changes in allowable premium payment period.)

Future benefits are determined by (1) projecting the policy value, taking into account future premiums, if any, and using the guaranteed interest rate, if any; otherwise, the lesser of the AIR, if any, or the highest state approved nonforfeiture interest rate, and using the mortality, expense deductions, etc. contained in the policy or declared by the insurer; and (2) taking into account any benefits guaranteed in the policy or by declaration which do not depend on the policy value.

All present values shall be determined using (i) an interest rate (or rates) specified by the Standard Nonforfeiture Law for Life Insurance, as amended in 1980, for policies issued in the same year and (ii) the mortality rates specified by the Standard Nonforfeiture Law for Life Insurance, as amended in 1980, for policies issued in the same year or contained in such other table as may be approved by the Commissioner for this purpose.

(Note: The types of quantities included in (3) are increased current interest rate credits guaranteed for a future period, decreased current mortality rate charges guaranteed for a future period, or decreased current expense charges guaranteed for a future period.)

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D. Maximum Charge Method

(1) Definitions: Wherever used in this Section, the terms have the respective meanings set forth or indicated in this paragraph.

(a) Policy Value is equal to gross premiums paid (excluding separate identified premiums for riders or supplementary benefits which are not credited to policy value) plus net investment income (which may be positive or negative and may vary based on policy loans) less the following as specified in the policy: (i) administrative charges (which may be taken in part from premiums and in part from policy value), (ii) acquisition and other charges, (iii) deferred acquisition and other charges, (iv) benefit charges, (v) service charges, (vi) partial withdrawals, and (vii) partial surrender charges.

(b) Benefit Charges made to the Policy Value are mortality charges made for life insurance on the insured person or persons and any charge made for riders and supplementary benefits.

(c) Service Charges made to the Policy Value are charges for transactional costs such as partial withdrawals, reallocations of policy values and benefit illustrations. Transactional charges shall not be assessed unless specifically permitted by law or regulation for transactions made under mandatory policy provisions.

(d) Administrative Charges is a per policy charge made regularly to the Policy Value (or deducted from premiums on scheduled premium policies) for the cost of administration. This charge may not exceed $5.00 per month in 1986. In subsequent years the limit for any new or in force policy shall be the product of $5.00 and the ratio (not to exceed 2.00) of (1) the Consumer Price Index (for all urban households) for the September preceding the year for which the determination is being made to (2) the Consumer Price Index for September 1986. The Commissioner may allow a higher charge upon an insurer demonstrating a justification.

(e) Acquisition and Other Charges are deducted from gross premiums before they are credited to Policy Value and/or made to the Policy Value. They may be expressed as a percentage of premium or a dollar amount per $1,000 of insurance or a dollar amount per premium payment or a per policy charge (other than the Administrative Charge). They do not include charges made as a reduction in investment return. These charges may vary by premium size, policy size and by policy year.

(f) Excess First Year Acquisition and Other Charges shall be the maximum excess of (A) over (B) based on the assumption that any premium (other than a single premium) payable in the first policy year is also payable during the entire premium paying period. (A) is the Acquisition and Other Charge made in the first policy year and (B) is the arithmetic average of the corresponding charges which the policy states would be made in policy years two through twenty.

(g) Excess Acquisition and Other Charges for a Face Amount Increase shall be the maximum excess of (A) over (B) based on the assumption that the net level whole life annual premium for the increase (as defined in (j) below) applies throughout the remaining premium paying period. (A) is the Acquisition and Other Charge for the increase, and (B) is the arithmetic average of the

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corresponding charges which the policy states would be made in the nineteen policy years following the increase.

(h) Net Investment Return is the actual amount credited to Policy Value net of investment expenses and/or other charges made as a reduction in investment return.

(i) The net level whole life annual premium at issue is based on the assumption of level insurance and level annual premium for life, the mortality table rate used to calculate the maximum mortality charges and an interest rate based on the higher of 4% or that specified in the policy.

(j) The net level whole life annual premium for an increase in the face amount of insurance shall be determined as of the date of the increases as though such increase were a separate policy under (i) above. Only increases in the face amount requested by the policyowner and increases in the face amount pursuant to the terms of the policy (e.g. an option to purchase or a cost of living increase) shall give rise to such a premium and the associated Excess Acquisition and Other Charges for a Face Amount Increase. Increases for this purpose shall not include increases in face amount resulting from a change in the death benefit option or changes in death benefit pursuant to policy terms that do not affect the face amount. Increases for this purpose shall be reduced by the amounts of any earlier decrease by reason of a partial withdrawal, but not a decrease resulting from a change in the death benefit option.

(k) Surrender Charge is a deferred charge made to the Policy Value in the event of a full or partial surrender of the policy, reduction in the face amount of insurance or premium, or a lapse.

(l) Cash Surrender Value is the Policy Value less any Surrender Charge, before reduction for outstanding loans or other amounts due under the policy.

(m) Deferred Acquisition and Other Charges are Acquisition and Other Charges deducted from the Policy Value after the first policy year.

(2) Cash Surrender Values determined in accordance with this subparagraph shall meet minimum requirements.

(a) If Acquisition and Other Charges do not exceed the sum of:

(1) 90% of premiums received up to the net level whole life annual premium at issue (regardless of when received).

(2) 10% of all other premiums received.

(3) 90% of the net level whole life annual premium for increases in the face amount of insurance as defined in 1(j).

(4) $10 per $1,000 of initial face amount in the first policy year.

(5) $1 per $1,000 of face amount in subsequent policy years.

(6) $10 per $1,000 of any increase in the face amount of insurance other than an increase resulting from a change in the death benefit option. Increases

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up to the amount of earlier decreases are included here but not in (3) above.

(7) $200 per policy in the first year.

(b) A surrender charge may be established provided that the initial surrender charge together with the actual Acquisition and Other Charges made in the first policy year (and on premiums up to the net level whole life annual premium if received after the first year) do not exceed the sum of (1), (2) in the first year, (4) and (7) in (a) above. Additional surrender charges may be established after issue in connection with an increase in face amount provided that any such additional surrender charge and any Acquisition and Other Charges made in connection with such increase do not exceed the sum of (3) and (6) in (a) above.

(c) A Deferred Acquisition and Other Charge may be charged against the Policy Value in any policy year after the first, such that the total of all such charges imposed to date plus the surrender charge for that year does not exceed the maximum initial surrender charge. The Deferred Acquisition and Other Charges in any one year may not exceed the maximum allowable surrender charge for that year. Similar Deferred Acquisition and Other Charges may be imposed with respect to an increase in face amount.

(d) The maximum allowable surrender charge for any year shall be the maximum initial surrender charge multiplied by $\ddot{a}_{x+t}/\ddot{a}_{x}$, where "x" is the issue age and "t" is the number of years since issue. Similar maximums shall be determined with respect to any additional surrender charges, with x and t based on the date of increase.

(Note: The minimum cash value methods B, C, or D are not intended to prohibit the current practice of allowing the imposition of additional surrender charges defined as follows. In the case of combination general account and separate account variable life products, additions or amounts derived from more favorable interest, mortality, and expense than those guaranteed in the policy on the general account fund and credited within 12 months prior to surrender may be subject to forfeiture upon surrender.)

E. Minimum Paid-Up Nonforfeiture Benefits

If a variable life insurance policy provides for the optional election of a paid-up nonforfeiture benefit, it shall be such that its present value shall be at least equal to the cash surrender value provided by the policy on the effective date of the election. The present value shall be based on mortality and interest standards at least as favorable to the policyowner as (1) the mortality and interest basis, if any, specified in the policy for determining the policy value, or (2) the mortality and interest standards permitted for paid-up nonforfeiture benefits by the Standard Nonforfeiture Law for Life Insurance, as amended in 1980. In lieu of the paid-up nonforfeiture benefit, the insurer may substitute, upon proper request not later than sixty days after the due date of the premium in default, an actuarially equivalent alternative paid-up nonforfeiture benefit which provides a greater amount or longer period of death benefits, or, if applicable, a greater amount or earlier payment of endowment benefits.

(Note: It is possible that policies will have secondary guarantees. Such guarantees should be taken into consideration when computing minimum paid-up nonforfeiture benefits.)

Ever since the adoption of the original Standard Nonforfeiture Law (SNFL) in 1942, provision has been made for nonforfeiture calculations on the basis of substandard mortality. (See Sections 5.5a. and 5c, Paragraph 8(e) of SNFL.)

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While this provision has been used infrequently in the past, it is anticipated the substandard mortality will be more frequently utilized in variable life insurance, given its flexible nature, to reflect the mortality classification assigned to the policy by the insurer.

A charge may be made at the surrender of the policy provided that the result after the deduction of the charge is not less than the minimum cash surrender value required by this guideline.

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Actuarial Guideline XXV

CALCULATION OF MINIMUM RESERVES AND MINIMUM NONFORFEITURE VALUES FOR POLICIES WITH GUARANTEED INCREASING DEATH BENEFITS BASED ON AN INDEX

A. Valuation - Text

For a policy where premiums are fixed in amount at issue which provides for whole life insurance with the amount of death benefit adjusted periodically with the Consumer Price Index or another cost of living index, the value of the minimum reserve at any time shall be based on the maximum valuation interest rate for the year of issue and an acceptable mortality table for life insurance statutory reserves and based on the death benefit and premium pattern adjusted as provided in the policy by reasonable annual increases based on the index. The present value of future benefits component shall be further adjusted each year by the ratio of the then current amount of death benefit to the initially projected amount of death benefit. If the policy provides for future premiums and such premiums are also adjusted periodically with the Consumer Price Index or another cost of living index, the present value of future premiums component shall likewise be further adjusted each year by the ratio of the then current amount of death benefit to the initially projected amount of death benefit. The assumption as to what is a reasonable annual increase in death benefits based on the index must not be less than the maximum valuation interest rate for the year of issue less:

1. 2.0% If the annual increase is limited to an annual and non-cumulative maximum of 0% through 5.0%

2. 1.5% If the annual increase is limited to an annual and cumulative maximum of 0% through 5.0%.

3. 1.5% If the annual increase is limited to an annual and non-cumulative maximum of 5.01% through 10.0%.

4. 1.25% If the annual increase is limited to an annual and cumulative maximum of 5.01% through 10.0%.

5. 1.0% For all other plans.

The term “annual and non-cumulative maximum” refers to a maximum where each annual increase is limited to the lower of the maximum or the increase in the index without carry forward of excess index increases.

The term “annual and cumulative maximum” refers to a maximum where each annual increase is limited to the lower of the maximum or the increase in the index with carry forward of excess index increases.

In no event shall the assumption as to an annual increase based on the index be less than 1.0%.

This guideline for valuation shall be effective immediately for policies issued on or after January 1, 1991.

B. Nonforfeiture – Text

The threshold amount shall be $10,000 until December 31, 2009. For years beginning after December 31, 2009, the threshold amount for a calendar year shall be the product of $10,000 and the ratio of 1) the index for June of the prior year to 2) 136.0 (the index as of June 30, 1991), rounded to the nearest $25. If this calculation would result in an increase in the threshold amount of less than $500, the unadjusted

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threshold amount from the prior year shall continue in effect for the next calendar year. In no calendar year shall the increase in threshold amount exceed 5% of the prior calendar year threshold amount.

The index used to determine the threshold amount for years beginning after December 31, 2009, shall be the Consumer Price Index for All Urban Consumers (CPI-U) as of June 30 of that year. If this index is no longer available, another index which, in the actuary's opinion, reflects the change in general consumer prices for the year should be substituted.

I. FOR POLICIES WHERE ANY DEATH BENEFIT FOR ANY POLICY YEAR WOULD EXCEED THE THRESHOLD AMOUNT EVEN IN ABSENCE OF ANY ANNUAL INCREASES BASED ON THE INDEX

For a policy where premiums are fixed in amount at issue which provides for whole life insurance with the amount of death benefit adjusted periodically with the Consumer Price Index or another cost of living index, the value of the minimum nonforfeiture benefit at any time shall be based on the maximum nonforfeiture interest rate for the year of issue and an acceptable mortality table for life insurance nonforfeiture and based on the death benefit and premium pattern adjusted as provided in the policy by reasonable annual increases based on the index. The present value of future benefits component shall be further adjusted each year by the ratio of the then current amount of death benefit to the initially projected amount of death benefit. If the policy provides for future premiums and such premiums are also adjusted periodically with the Consumer Price Index or another cost of living index, the present value of future premiums component shall likewise be further adjusted each year by the ratio of the then current amount of death benefit to the initially projected amount of death benefit. The assumption as to what is a reasonable annual increase in death benefits based on the index must not be less than the maximum valuation interest rate for the year of issue less:

1. 2.0% If the annual increase is limited to an annual and non-cumulative maximum of 0% through 5.0%.

2. 1.5% If the annual increase is limited to an annual and cumulative maximum of 0% through 5.0%.

3. 1.5% If the annual increase is limited to an annual and non-cumulative maximum of 5.01% through 10.0%.

4. 1.25% If the annual increase is limited to an annual and cumulative maximum of 5.01% through 10.0%.

5. 1.0% For all other plans.

The term "annual and non-cumulative maximum" refers to a maximum where each annual increase is limited to the lower of the maximum or the increase in the index without carry forward of excess index increases.

The term "annual and cumulative maximum" refers to a maximum where each annual increase is limited to the lower of the maximum or the increase in the index with carry forward of excess index increases.

In no event shall the assumption as to an annual increase based on the index be less than 1.0%.

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II. FOR POLICIES WHERE ANY DEATH BENEFIT FOR ANY POLICY YEAR WOULD NOT EXCEED THE THRESHOLD AMOUNT IN ABSENCE OF ANY ANNUAL INCREASES BASED ON THE INDEX

For a policy where premiums are fixed in amount at issue which provides for whole life insurance with the amount of death benefit adjusted periodically with the Consumer Price Index or another cost of living index, the unadjusted value of the minimum nonforfeiture benefit at any time shall be based on a level death benefit, an acceptable mortality table for life insurance nonforfeiture and a nonforfeiture interest rate equal to the greater of (a) and (b):

(a) The nonforfeiture interest rate defined in Section 3 of VM-02, Minimum Nonforfeiture Mortality and Interest, less:

1. 0bp If the annual increase based on the index is limited to a maximum of 0% through 5.0%.

2. 25bp If the annual increase based on the index is limited to a maximum of 5.01% through 10.0%.

3. 50bp For all other plans.

(b) The Applicable Accumulation Test Minimum Rate in the Cash Value Accumulation Test under IRS Section 7702 *(Life Insurance Contract Defined)* of the U.S. Internal Revenue Code.

The present value of future benefits component shall be further adjusted each year by the ratio of the then current amount of death benefit to the initially projected amount of death benefit. If the policy provides for future premiums and such premiums are also adjusted periodically with the Consumer Price Index or another cost of living index, the present value of future premiums component shall likewise be further adjusted each year by the ratio of the then current amount of death benefit to the initially projected amount of death benefit.

For purposes of this guideline multiple policies on a single life shall be aggregated and only those policies aggregating not more than $10,000 (or the threshold amount[1] after December 31, 2009), shall be considered under B.II.

This guideline for nonforfeiture shall be effective immediately for policies issued on or after January 1, 1991.

BACKGROUND

A number of companies are marketing individual life insurance policies with guaranteed increasing death benefits tied in to a consumer price index or another cost of living index and are for low initial amounts of insurance sold through funeral directors to provide for burial expenses. Some of the policies provide for graded death benefits such as the return of premium with or without interest for the early policy years or for a fixed scheduled increase in death benefits prior to the operation of the index. In some cases there is a maximum on the increase for any year. The vast majority of such policies are single premium policies but some are annual premium policies (generally limited payment). The annual premium may or may not be subject to adjustment with the index.

Since the changes in the index are not known at issue, but from past experience, increases within a given range can be expected with a high probability, it is necessary to assume some increases and then to

[1] In 2010, the actuarial guideline was modified to substitute a threshold amount for 10,000, such threshold being increased by the change in the CPI-U, the CPI for All Urban Consumers.

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continually adjust the present value of future benefits component and, if appropriate, the present value of future premiums component in the reserve and nonforfeiture calculation.

Theoretically the same assumed increases in the death benefits should be used for both valuation and nonforfeiture. This guideline so provides for policies where the amount of death benefit in any given policy year would exceed $10,000 (or the threshold amount[1] after December 31, 2009), even if there were no increases based on the index. For practical purposes this may mean that such policies are not marketable for higher amounts as it is most likely that such policies will not qualify under the IRS Section 7702. The cash value accumulation test to qualify thereunder requires a minimum interest rate and an assumed level amount of death benefits.

In the case of policies for an initial amount of insurance of $5,000 or less, the IRS rules provide an exception to the prohibition of assuming increasing death benefits. However, since many of the policies for very low amounts of initial face amount of insurance would require relatively high expenses if underwritten, many of the policies are issued with simplified underwriting or on a guaranteed issue basis with lower amounts of death benefits in the early policy years, some of the resulting annual increases are such as would disqualify many of the policies for the exception. Therefore it is recommended that policies for low amounts of insurance be allowed to qualify under the cash value accumulation test by permitting the nonforfeiture values to be based on a level death benefit and an interest rate not less than the Applicable Accumulation Test Minimum Rate in the Cash Value Accumulation Test under IRS Section 7702 and requiring such values to be updated as increases based on the index take place. The amount in this guideline is set at $10,000 (or the threshold amount[1] after December 31, 2009), to allow for future adjustments and for different patterns of benefits for low amounts.

For single premium policies, the value of nonforfeiture benefits based on a level death benefit and a net assumed nonforfeiture interest rate equal to the maximum nonforfeiture interest rate less an assumed increase based on the index and such factors then adjusted by the projected increases will approximate factors based on assumed increases and the maximum nonforfeiture interest rate. The procedure of assuming a level death benefit and a net assumed rate of not less than the Applicable Accumulation Test Minimum Rate in the Cash Value Accumulation Test under IRS Section 7702 for policies of low amounts of insurance is apt to produce lower cash values than the procedure for large amounts of insurance. Such lower values can be justified based upon the fact that the highly specialized market is prearranged funeral expenses for very small amounts of insurance per policy.

To emphasize the qualification with the IRS rules for the very low amounts of insurance, the nonforfeiture guideline for small amount policies is stated in terms of the net rate, a level death benefit and continual adjustment.

For solvency purposes, reserves should be conservative. The same rules apply for reserve regardless of the size of the policy. That is, lower reserves are not permitted for policies with very low amounts of insurance per policy.

Paragraph 5c(3) of the Model Standard Nonforfeiture Law states that unscheduled changes do not need to be taken into account until the time of the change. The changes guaranteed according to an index are a hybrid, i.e. the changes are scheduled but the amount of the change is not known until the index is determined. Thus the changes must be recognized at issue. This guideline is a hybrid with increases assumed at issue either explicitly or implicitly but with further adjustments made at the time the increase based on the index is determined.

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Actuarial Guideline XXVI

ELECTION OF OPERATIVE DATES UNDER STANDARD VALUATION LAW AND STANDARD NONFORFEITURE LAW

June 3, 1989

Preamble

The model Standard Nonforfeiture Law for Life Insurance contains Section 5-C, which defines new mortality and interest rate components to be used as the minimum standard for nonforfeiture values for life insurance policies. The Commissioners 1980 Standard Ordinary Table, or that table with Ten-Year Select Factors, is identified in Section 5-C as the applicable mortality table component for ordinary life insurance policies (although there is a provision for other alternate mortality tables to be permitted by regulation). Section 5-C also incorporates "dynamic" interest rates, as the applicable interest rate component. In addition, Section 5-C contains a new and different formula to be used in computing the adjusted premiums that define minimum nonforfeiture values.

Section 5-C contains a mandatory operative date, but there is also language permitting companies to elect an early operative date under certain conditions.

The model Standard Valuation law contains a cross reference to operative date for Section 5-C of the Standard Nonforfeiture Law for Life Insurance. After such operative date, there are mortality and interest rate components defined for use as the minimum standard for computing reserves. The Commissioners 1980 Standard Ordinary Table, or that table with Ten-Year Select Factors, is identified as the applicable mortality table component for ordinary life insurance policies (although there is a provision for other alternate mortality tables to be permitted by regulation). "Dynamic" interest rates determine the applicable interest rate component, but a lower maximum interest rate is defined for reserves than for nonforfeiture values.

Generally, the applicable mortality rates are lower and the applicable interest rates higher after the operative date. Thus, the reserves defined under the minimum standard would be lower for policies issued on or after the operative date.

Text

Under no circumstances can an insurance company elect an operative date for the purpose of Section 5-C of the Standard Nonforfeiture Law for Life Insurance, if such operative date would be in a calendar year prior to the calendar year in which that company furnished written notice of election of an operative date under that law.

Background Material

The purpose of this actuarial guideline is to ensure consistency and provide guidance in the election of this operative date.

Historically, insurance companies have been allowed to elect early operative dates so as to pass along the benefits of improved mortality rates and current interest rates to policyholders who purchase new life insurance policies. These new policies would typically have lower nonforfeiture values and would require lower reserves, and net premiums would be lower also. The expectation is that the lower net premiums might allow the company to reconsider its gross premium rates for these new policies issued after the operative date, and in many cases to lower the new gross premium rates.

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A second reason for allowing the election of an early operative date would be to allow insurance companies and state insurance departments more time to prepare and review new life insurance policies, which are to be introduced into them marketplace. If every life insurance policy had to be changed over on the same mandatory operative date, it would be a great burden on the resources of all the parties involved.

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Actuarial Guideline XXVII

ACCELERATED BENEFITS

PURPOSE

This guideline is designed to cover the actuarial aspects of accelerated benefits. Three general categories of accelerated benefits are covered:

I) non-discounted acceleration of benefits

II) actuarially discounted acceleration of benefits

III) interest accrual approach to financing acceleration of benefits

In addition, there is a separate section to cover the special considerations for a policy lien approach, which is Section IV.

General considerations which apply to any method of determining accelerated benefits are given in Section V.

I. NON-DISCOUNTED ACCELERATION OF BENEFITS

A. Description

The type of plans considered in this subsection are those which provide for a defined event triggering one time acceleration of some or all of the death benefit of the base contract or rider, in such a way that every dollar of acceleration has a non-discounted matching reduction in the amount payable on death. These plans have been available in four forms, via

1. A contract integrating the acceleration feature with other, more traditional, features;

2. A rider attached to a regular contract at time of issue, to provide acceleration;

3. A rider, as in (2), but which may be attached to inforce contracts of the same company; or

4. A policy acting similar to the rider in (3) above, but for which the acceleration is applicable to inforce contract of other companies.

B. Reserves

1. Reserving Approach

Payment of benefits earlier than death itself is an early payment rather than a different payment. The basic reserve structure and requirements for regular life insurance need not be disturbed. Therefore, the CRVM methodology is acceptable, as is any other reserving methodology allowable for life insurance when determining the reserves needed for policies with an accelerated benefit or when determining the reserves for the accelerated benefit by itself.

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2. General Consideration

A reserve formula should consider all relevant factors.

Approximations to develop a single decrement table which utilize all relevant factors except for voluntary termination rates are acceptable for policies and riders subject to this subsection provided it can be demonstrated that the approximations used produce essentially similar reserves, conservative reserves, or immaterial reserves. The calculations should take into account the reduction in life insurance benefits due to prior acceleration. However, in no event shall the reserves for the accelerated benefit and the life insurance benefit when taken together be less than the reserves for the life insurance benefit assuming no acceleration feature prior to payment of any accelerated benefits.

In the development and calculation of reserves for policies and riders subject to this subsection, due regard shall be given to the applicable policy provisions, marketing methods, administrative procedures and all other considerations which have an impact on projected claims costs, including, but not limited to the following:

a. Definition of acceleration events,

b. Premium waiver provision,

c. Marketing method,

d. Underwriting procedures,

e. Delay in eligibility for benefit,

f. Maximum benefit,

g. Optional nature of benefit, and/or

h. Guaranteed insurability options.

II. ACTUARIALLY DISCOUNTED ACCELERATION OF BENEFIT

A. Description

The products that are allowable under this type of approach generally provide for an acceleration of the death benefit payable under a life insurance policy, with an appropriate actuarial adjustment in the amount of money paid to the policyholder that represents the amount of money foregone by the Company by paying out the death benefit early. These products have no additional premium payable. This product can be made available at issue of the contract or after issue of the contract. It can either be a separate rider or part of the integrated policy. The interest rate or interest rate methodology used for discounting must be specified in the contract or rider or in the actuarial memorandum.

B. Reserves

The application of standard valuation law and CRVM reserves is appropriate for these policies. No additional reserves need be held as long as the actuary is convinced that the method used to discount the death benefit reflects sound actuarial principles.

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If the actuary is convinced that the discounting procedure does not appropriately reflect these conditions, he or she should determine a reserve such that reserves are adequate for the life insurance benefits based on aggregates. There is nothing in this benefit design that changes that equation.

III. INTEREST ACCRUAL APPROACH TO FINANCING ACCELERATION OF BENEFITS

A. Description

Under this approach, the insurer accrues an interest charge on the accelerated benefit to account for lost investment income from the date of acceleration to the date of death. The interest may be accrued until death or may be required to be paid in cash periodically, or may be offset against the policy's remaining death benefit.

1. Alternative methods of including an interest accrual option:

   a. A benefit of this type may be provided either as an integral part of a life insurance policy or as a rider to a life insurance policy.

   b. If offered as a rider to a life insurance policy, such rider may be attached to either a new policy or to an existing policy.

2. Alternative Benefit Designs using this option: The rider or policy form should specify whether interest accruing on prior accelerated benefit payment needs to be paid in cash or whether additional accelerated benefit payments will be made to cover such interest accruals as they become due. Either approach is equally acceptable.

B. Interest Accrual Rate

1. The rider or policy form or the actuarial memorandum should specify the method used to determine the rate(s) of interest to be charged.

2. The specification of the method should be clear and unambiguous.

3. The method used for determining the interest rate should be included in the Actuarial memorandum.

C. Reserves

1. Prior to the occurrence of an event qualifying the policy for accelerated benefits, minimum statutory reserves for policies containing interest accrual provisions are the same as for policies with identical death benefits that do not contain interest accrued lien provisions, provided that the method of determining the interest rate to be charged, as specified in the rider or policy provisions or actuarial memorandum, results in an interest rate at least equal to the valuation interest rate applicable to the policy. If such is not the case, an extra reserve may be necessary on such policies, if it is determined that the aggregate reserves are not good and sufficient.

2. Following the occurrence of a qualifying event, accrued interest is an asset of the company for statutory reporting purposes. However, the valuation actuary should make certain that reserves in the aggregate are adequate to assure that such aggregate accrued interest is provided for. This will assure that such accrued interest assets can be held as admitted assets. The insurer's valuation actuary may

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voluntarily increase the statutory reserve liability on each such policy in order to eliminate the need to non-admit a portion of the accrued interest policy lien or policy loan.

IV. BENEFIT PAYMENT LIENS

This section deals specifically with benefit payment liens and their effect on future policy premiums and benefits.

A. The presence of a lien against the policy does not require a pro-rata reduction in the policy premiums or other values.

B. Amount of lien computed as of the date of death may be deducted from the death benefit.

C. Access to non-forfeiture benefits upon surrender or through future policy loans may be restricted to any excess of the cash surrender value over the sum of any outstanding loans and the lien.

D. If the lien approach is used and RPU is available as a non-forfeiture benefit, the amount of RPU may be calculated as if no lien existed and the lien may continue to apply, provided that the lien continues to satisfy any percentage and dollar maximums and minimums specified in the contract. Alternatively, RPU may be made unavailable while the lien exists, provided an ETI benefit is available. Alternatively, the excess, if any, of the cash surrender value over the sum of outstanding loans and the lien may be applied in calculating the amount of the RPU, provided an ETI benefit is available. If the choice of methods is not left as an option to be the policyholder, the rider or policy form should specify which method will apply.

E. If the lien approach is used an ETI is available as a non-forfeiture benefit, the period of ETI may be calculated as if no lien existed and the lien may continue to apply, provided that the lien continues to satisfy any percentage and dollar maximums and minimums specified in the contract.

F. If the lien approach is used, any accelerated death benefit payment may first be applied toward repaying the portion of any outstanding policy loans which causes the sum of the accelerated death benefit and policy loans to exceed the cash value. Alternatively, outstanding policy loans may be retained and the lien that would otherwise be allowed may be reduced by any outstanding policy loans at the time of acceleration. If the choice of methods is not left as an option to the policyholder, the rider or policy form should specify which method will apply.

G. The rider or policy form accelerated benefit lien provisions may specify that the existence of a benefit lien will not prevent termination of the policy in accordance with the regular policy termination provisions.

H. If a policy terminates while subject to a lien, the insurer shall extinguish the lien without further recourse to the policyholder unless the policy or rider clearly indicates otherwise. In the event that the policy is reinstated, the lien may also be reinstated with interest accrued as if the policy had never terminated.

I. The policyholder should have the option of paying all or part of any premium or accrued interest that would be capitalized under the terms of the rider or policy provisions in cash, as well as the option of repaying all or part of any lien in cash, in order to prevent the lien from causing the policy to terminate.

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V. GENERAL CONSIDERATIONS

The items below should be considered, where applicable, for all types of accelerated benefits:

A. The rider or policy form should specify whether any premium becoming due after the initial accelerated benefit payment is established needs to be paid in cash or whether additional accelerated benefit payment will be made to cover such premiums as they become due. Either approach is equally acceptable.

B. The rider or policy form may specify any percentage and dollar minimum and maximum payments that may be accelerated. Any dollar or percentage minimums or maximums is equally acceptable. If no maximum is specified, it will be assumed to be 100% of the death benefit.

C. The accelerated benefit may include a reasonable expense charge for administrative expenses and risks assumed by the company. If the available amount of the initial accelerated benefit is less than the maximum allowed, the rider or policy form should specify how such initial amount will be determined.

D. The rider or policy form should specify the actions required, if any, to prevent policy termination if premium or interest expected to be capitalized would result in a total accelerated benefit payment exceeding the percentage or dollar maximum amount specified in the rider or policy form. Any such excess may be required to be paid in cash within an appropriate grace period in order to prevent policy termination. The rider or policy form may also specify that future premiums or interest becoming due must be paid in cash. If not specifically addressed, the rider or policy should remain inforce and be administered with no change from the premium or interest requirement that existed immediately prior to the time at which the maximum was reached and the accelerated benefit would not be increased beyond the maximum specified in the rider or policy form.

E. The rider or policy form may specify whether the accelerated benefit provision would apply to the original base insurance policy death benefit or the current insurance policy death benefit. If not specifically addressed, the rider or policy form should be administered as if maximums are automatically increased, but not automatically decreased.

F. The rider or policy form may specify that an accelerated benefit is not available unless established prior to the policyholder's election of or lapse to ETI or RPU. If not specifically addressed, the rider or policy forms should be administered to provide an accelerated benefit after election of or lapse to ETI or RPU.

G. The rider or policy form may specify that an accelerated benefit is not available if the policy has an irrevocable beneficiary or is assigned when accelerated benefits are initially claimed. Alternatively, the irrevocable beneficiary or assignee must provide a signed acknowledgement of concurrence for payout. The rider or policy form may specify that the policy may not be assigned (except to the insurer) after an accelerated benefit has been paid.

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Actuarial Guideline XXVIII

STATUTORY CLAIM RESERVES FOR GROUP LONG-TERM DISABILITY CONTRACTS WITH A SURVIVOR INCOME BENEFIT PROVISION

Background

Many of the major writers of group long-term disability income insurance have included survivor benefits in such contracts. Provisions related to the survivor benefit include minimum disability periods, benefit amounts defined in terms of a number of months of disability benefits and a specified percentage of the monthly disability benefit.

This benefit is sometimes overlooked in the valuation process or ignored as being trivial in amount.

Drafting Note: Please see the 1990 “Proceedings,” Vol. 2, Pages 995-999, and the 1991 “Proceedings,” Vol. 1B, Pages 1321-1328.

Text

Claim reserves for survivor income benefits contained in group long-term disability contracts must be established based on the design of the survivor income benefit including the minimum period of disability before the spouse of a disabled person becomes eligible for a survivor income benefit and the amount of the benefit. A suitable approximation to the sum of the reserves for the basic disability benefit and the reserve for the survivor income benefit can be calculated by computing the reserve for the basic disability at an interest rate less than the maximum valuation interest rate.

Before any approximation can be accepted, rigorous testing of the approximation to the combined reserves for both the basic disability claim and the survivor income benefit must be performed. Tests indicated that basic disability reserves and survivor income benefit based on a 12-month disability requirement and a maximum survivor income benefit duration of 24 months with a survivor income benefit of .667 of the disability income with all reserves based on a valuation interest rate of 5.5% can be adequately approximated by basic disability reserves alone but calculated at a 3.5% valuation interest rate.

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Actuarial Guideline XXIX

GUIDELINE CONCERNING RESERVES OF COMPANIES IN REHABILITATION

Preamble

The life insurance and annuity contracts of life insurance companies can be restructured by court order in rehabilitation proceedings. The contract restructuring may take the form of reduction in account values and/or guaranteed interest crediting premiums. Typically, the court order imposes restrictions on surrender of the contract while the company is in rehabilitation. These restrictions can include bans on surrenders while a rehabilitation plan is being developed and temporary limitations on the cash that can be obtained upon surrender. These restrictions are intended to prevent *en masse* surrenders while the company faces liquidity problems.

Several issues have arisen as to the interpretation of the Standard Valuation Law in these circumstances. The issues relate to the interpretation of the Commissioners' Reserve Valuation Method (CRVM) and the Commissioners' Annuity Reserve Valuation Method (CRVM), the determination of the guaranteed nonforfeiture benefits provided in the restructured contract and identification of the issue date of the contract after restructuring.

The Standard Valuation Law does not specifically address minimum reserve requirements after a contract has been restructured by court order. The minimum reserve requirements should be interpreted in the context of court-ordered contract restructuring to result in the most appropriate reserves under the particular circumstances. In general, this should be left to the regulators to determine.

Guideline

The phrase "future guaranteed benefits, including guaranteed nonforfeiture benefits," as used in CARVM, includes the cash surrender values based on contractual guarantees after reduction for any surrender charges available under the contract. In general, the value of future guaranteed benefits under CARVM may not be reduced by contingent surrender charges which may not be available upon cash surrender. See *Guideline Covering the Commissioners' Annuity Reserve Valuation Method (CARVM) (1985).*

Whether or not a court-imposed temporary restriction on the availability of cash on surrender is taken into account under CARVM depends upon whether the rehabilitation plan specifies that the restriction is a reduction in the guaranteed nonforfeiture benefits in the restructured contracts. If the rehabilitation plan imposes a distinct temporary charge to ensure liquidity as opposed to changing common surrender charges that are historically used to determining nonforfeiture benefits, the temporary charges will not reduce guaranteed nonforfeiture benefits for purposes of CARVM.

A similar rule applies for purposes of reporting those reserves on life insurance contracts entitled "For surrender values in excess of reserves otherwise required."

For life insurance contracts, CRVM does not dictate that a particular method must be applied after a contract has been restructured. In the case of policies providing for a varying amount of insurance or requiring the payment of varying premiums, reserves are calculated by a method consistent with CRVM applicable to policies providing for a uniform amount of insurance and requiring the payment of uniform premiums.

A method consistent with CRVM adopted for purposes of a rehabilitation program should consider the valuation bases and expense allowance prior to restructuring as well as after restructuring. Depending upon the types of changes to the restructured contract, it may or may not be appropriate to take into account the guaranteed benefits and premium structure prior to restructuring.

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The issue date for purposes of determining the applicable mortality tables and interest rates also depends on the circumstances. For example, it may be appropriate to treat annuity contracts as newly issued so that reserves are required to be recomputed using more current discount rates. However, in the same rehabilitation plan it may be inappropriate to treat a restructured level premium whole life contract as newly issued. Accordingly, whether a contract is treated as having a new issue date after contract restructuring depends upon the terms of the rehabilitation plan and the restructured contracts. In general, contracts are not treated as newly issued unless the rehabilitation plan or state filing for the restructured contracts so provides.

Similarly, the appropriate CRVM expense allowance will depend upon the terms and the intent of the restructuring and rehabilitation plan. Depending upon the types of changes to the restructured contract, it may be appropriate to carry forward an unamortized expense allowance based on original policy date. In other cases, a new unamortized expense allowance would be calculated as of the restructure date. In general, a new unamortized expense allowance is not calculated unless the rehabilitation plan or the state filing for the restructured contract so provides.

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Actuarial Guideline XXX

GUIDELINE FOR THE APPLICATION OF PLAN TYPE TO GUARANTEED INTEREST CONTRACTS (GICS) WITH BENEFIT RESPONSIVE PAYMENT PROVISIONS USED TO FUND EMPLOYEE BENEFIT PLANS

Background Material

Guaranteed Interest Contracts (GICs) that are used to fund employee benefit plans often times contain a provision that allows individual participants to voluntarily move funds on a book value basis to other investment opportunities. These contracts also allow for the withdrawal of funds on a book value basis to provide employee benefits such as a death benefit to a surviving beneficiary, disability benefits and benefits paid upon bona fide termination of employment. In the situations described above, the individual participant is to be distinguished from the policyholder. Typical contractual language is as follows:

1. Withdrawal for Redirection of Investments - Subject to the provisions of Subsection____above, the contract owner shall direct the withdrawal and transfer to the contract owner of the pro rata amounts from the accumulation accounts for the purpose of redirecting an employee investment to an equity fund in accordance with the provision of the Plan.

2. Withdrawal for Plan Benefit Payments - Subject to the provisions of Subsection____above, the contract owner shall direct the withdrawal and transfer to the contract owner of the pro rata amounts from the accumulation account due to distribution made to participants (or to their beneficiaries, in case of the participant's death) under the Plan.

Both examples of contractual language make reference to the "provisions of the Plan." Plan provisions reduce the disintermediation (C-3) risk, from the insurance company standpoint, associated with GICs. For example, plan provisions may restrict the opportunity for the 401 (k) plan participant to move funds from the GIC option to a competing "guarantee of principal" option within the plan.

The Standard Valuation Law utilizes a concept known as Plan Type to distinguish between different levels of voluntary withdrawal rights by policyholders. Voluntary withdrawal rights are contractual policyholder rights which may be exercised at the option of the policyholder and do not include such items as scheduled contractual payouts or payouts upon termination. The greater the level of voluntary withdrawal right afforded to the policyholder, the more conservative is the resulting valuation interest rate. Plan Types are designated in the Standard Valuation Law as with Plan Type A, Plan Type B or Plan Type C and are defined as follows:

1. Plan Type A is a plan under which the policyholder may not withdraw funds, or may withdraw funds at any time but only (a) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, (b) without such an adjustment but in installments over five years or more, or (c) as an immediate life annuity.

2. Plan Type B is a plan under which the policyholder may not withdraw funds before expiration of the interest rate guarantee, or may withdraw funds before such expiration but only (a) with an adjustment to reflect changes in interest rate or assets values since receipt of the funds by the insurance company, or (b) without such an adjustment but in installments over five years or more. At the end of the interest rate guarantee, funds may be withdrawn without such adjustment in a single sum or installments over less than five years.

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3. Plan Type C is a plan under which the policyholder may withdraw funds before expiration of the interest rate guarantee in a single sum or installments over less than five years either (a) without adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (b) subject only to a fixed surrender charge stipulated in the contract as a percentage of the funds.

Text

For purposes of the application of the Standard Valuation Law to Guaranteed Interest Contracts (GICs) with benefit responsive provisions, the withdrawal of funds at book value for the purpose of redirecting or withdrawing an employee investment shall be considered a withdrawal by the policyholder unless the underlying plan or GIC contain written provisions which are designed to reduce the C-3 risk to the insurance company. As an example, a provision which meets this criteria would include both the following:

1. No direct transfer to competing funds, whether such funds are alternate funds of the insurance company or not. This provision prohibits direct transfer of funds from the GIC option to a competing plan option that offers either a guarantee of principal or to an option in which the risk of loss of principal is small such as a money market fund or short-term bond fund. Any transfer to such an option must first go through an non-competing plan option and reside there for at least 90 days or three months.

   and

2. For GICs that fund plan investment options where interest is allocated to plan participants based on how much of their account balance is in each particular interest rate "cell," participants are not allowed to redirect any of the balance they have in a GIC funding a particular cell to a competing fund until the GIC's maturity date.

In addition, the valuation actuary must be satisfied that the GIC provisions designed to reduce the C-3 risk are administered by the insurer in the designed manner.

This requirement may be fulfilled by obtaining from the appropriate insurance company officer a certificate of intent regarding the insurance company administration of the provisions.

In addition, the valuation actuary must periodically review the actual experience under the contract to verify the appropriateness of the Plan Type assumption with reference to this Guideline.

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Actuarial Guideline XXXI

VALUATION ISSUES VS. POLICY FORM APPROVAL

Background

Occasionally, the NAIC Life and Health Actuarial Task Force addresses valuation (reserve) issues related to a policy form or benefit design that has not been accepted or approved by a particular state. The development of reserving methods or providing guidance concerning reserve questions for such policy forms is necessary because the annual statement filed in each state, including states for which a particular policy form has not been approved for use, must reflect appropriate reserve for all policy forms and associated benefits.

Text

The adoption of an Actuarial Guideline by the NAIC Life and Health Actuarial Task Force dealing with a reserve issue associated with a particular policy form or benefit does not represent an endorsement for the approval of the particular policy form or benefit.

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Actuarial Guideline XXXII

RESERVE FOR IMMEDIATE PAYMENT OF CLAIMS

Background Material

Section 5 Reserve Valuation Method—Life Insurance and Endowment Benefits of the NAIC Standard Valuation Law refers to an annual premium in defining the commissioners reserve valuation method. However, it has been general practice to hold an additional reserve where fractional premiums are paid and any fractional premium not yet due in the policy year of death is waived and to hold a further additional reserve for the refund of any premium paid beyond the end of the month in the policy year of death. These additional reserves are called for in the Miscellaneous Section of Exhibit 8 of the annual statement. These additional reserves are generally included in the basic reserves where an insurer uses an assumption of continuous payment of premiums.

Although Section 7 of the NAIC Standard Nonforfeiture Law for Life Insurance explicitly permits in calculating nonforfeiture "the assumption that any death benefit is payable at the end of the policy year of death," there is no similar explicit permission to use such assumption in the NAIC Standard Valuation Law. The annual statement instructions are silent on any adjustment. A long time ago some life insurance policies provided that claims would be paid at the end of the policy year of death. However, for many years many policies have provided that claims will be paid immediately upon satisfactory proof of death. In fact, some states require that interest shall accrue from date of death.

Many insurers have held a reserve for immediate payment of claims either by an adjustment to curtate reserves or by including provision therefore in the basic reserves calculated on a continuous payment of claims basis.

Text

RESERVES FOR IMMEDIATE PAYMENT OF CLAIMS

I. Reserves based on either fully continuous functions or on semi-continuous functions where the death portion reflects approximately one half of one year's valuation rate of interest are considered as making appropriate provision for immediate payment of claims.

II. Where the basic reserves are based on curtate functions with no provision for immediate payment of claims:

1. For any policy where the contract calls for payment of death claims at the end of the policy year in which death occurs, no adjustment to curtate reserves need be made.

2. For any policy where the contract calls for payment of death claims immediately upon receipt of due proof of death of the insured, the death portion of curtate reserves shall be increased by one third of one year's valuation rate of interest. (Approximations may be used to split the total curtate reserves into death portion and the pure endowment portion.)

3. For any policy where the contract provides for payment of interest on the death proceeds from date of death to date of payment, the death portion of curtate reserves shall be increased by one half of one year's valuation rate of interest. (Approximations may be used to split the total curtate into the death portion.)

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III. Where an insurer pays interest on death proceeds at an earlier point than as required by contract, it is appropriate that the statutory formula reflect such practice.

IV. Where the actual formula reserves are more conservative than minimum statutory formula reserves, an insurer using curtate functions without provision for immediate payment of claims must demonstrate compliance with minimum statutory formula reserves adjusted in accordance with II above.

V. This guideline shall apply to all new life insurance policies issued beginning January 1 following the date the guideline is adopted.

VI. The guideline shall be applicable to policies issued prior to the date the guideline is adopted with any additional reserve graded in as follows for the years following the date the guideline is adopted:

1. First year 20%

2. Second year 40%

3. Third year 60%

4. Fourth year 80%

5. Fifth and later years 100%

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Actuarial Guideline XXXIII

DETERMINING CARVM RESERVES FOR ANNUITY CONTRACTS WITH ELECTIVE BENEFITS

Background Information

1. Introduction

The Standard Valuation Law (SVL) defines the methods and assumptions which are to be used in determining minimum statutory formula reserves. This law establishes the standards for annuity contracts (which therefore includes any annuity riders or endorsements, and any or all components of which, such as premiums, benefits, contract charges, primary or secondary accumulation values or other components, either relating to annuity benefits provided by the contract or providing separate annuity benefits) and includes the criteria for the interest and mortality assumptions to be used in determining minimum formula contract reserves. The 1980 revisions to the SVL provide for the maximum statutory formula reserve interest rate to be determined through a dynamic formula in order to incorporate changes in economic conditions, liquidity needs and the risks inherent in certain types of contracts.

The SVL defined methodology for annuity contracts, the commissioners annuity reserve valuation method (CARVM), requires that reserves be the greatest of the respective excesses of the present values, at the date of valuation, of the future guaranteed benefits, including guaranteed nonforfeiture benefits, provided for by such contracts at the end of each respective contract year, over the present value, at the date of valuation, of any future valuation considerations derived from future gross considerations, required by the terms of such contracts, that become payable prior to the end of such respective contract year. Such reserves are established to adequately fund all guaranteed contract obligations, including those obligations which are optional to the contract owner and which may not have yet been elected.

Industry practices and methods of reserving under CARVM for annuity contracts with multiple benefit streams have not been found to be consistent. These range from a low reserve equal to the cash surrender value to a reserve representing the greatest actuarial present value of the future benefit streams under all potential annuity or other nonforfeiture benefit election options using a conservative rate of interest.

The major purpose of this Actuarial Guideline is to provide clarification and consistency in applying CARVM to annuities with multiple benefit streams. Some of the areas requiring clarification include: the valuation of annuitization benefits; the application of incidence rates in CARVM; the application of the integrated benefit stream approach in CARVM; how to determine valuation interest rates and mortality tables for multiple benefit streams; and certain practical considerations regarding multiple benefit streams.

2. Annuitization Benefits

Varying forms of contracts provide that the cash value available to the contract owner is less than the amount available to purchase an annuitization option under the terms of the contract.

For purposes of this Actuarial Guideline, “accumulation fund” is defined as the policy value which is used to purchase an annuity option under the terms of the contract.

Frequently there are significant discontinuities in the reserves, both upward and downward, at the time a settlement option is elected, between the reserve held immediately prior to the settlement as

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compared to the reserve required for the greatest actuarial present value of the annuitization option elected.

One of the most significant reasons for discontinuities in the reserve patterns at the time of election is the difference in the SPIA valuation rate available at the time of election as compared to the valuation rate used based on the date of issue of the original SPDA contract. Another significant reason is the difference between the guaranteed purchase rate contained in the contract and used for reserve development as compared to the rate actually used to purchase the annuity option at the time of election.

3. Application of Incidence Rates in CARVM

Since CARVM was adopted, there has been an increase in the types of benefits offered under certain annuity contracts, including enhanced death benefits, nursing home benefits, and various partial withdrawal provisions, including some dependent on values other than those used to determine cash values and which may allow for benefits to continue past the point where the cash value is zero. For some of these benefit types, the SVL is not explicit as to whether incidence tables prescribed under the SVL may be used to determine such benefits, versus requiring consideration of all contract owner options available under the contract, and choosing the set of incidence rates which produce the greatest present value.

4. Integrated Benefit Stream Approach

CARVM requires that reserves be based on the greatest present value of all potential future guaranteed benefits. For annuity contracts offering more than one type of potential benefit stream, the SVL is not explicit regarding whether or how blends of more than one type of benefit must be considered under CARVM.

Under the integrated benefit stream approach, any potential benefit stream must be considered, including blends reflecting the interaction of more than one type of benefit. Such potential benefit streams include all types of benefits for which the greatest present value concept is required. Additionally, adjustments must be made to all such potential benefit streams to reflect those benefit types for which prescribed incidence tables are required (e.g., death benefits).

For example, consider an annuity contract offering surrender, annuitization and death benefits. Potential benefit streams that would be considered include surrender streams, annuitization streams, and streams reflecting blends of surrender and annuitization benefits. All such streams would also be adjusted to reflect death benefits and to discount all benefits for survivorship (based on the mortality table prescribed in the SVL).

5. Valuation Interest Rates

For annuities offering more than one type of benefit, the SVL is not explicit as to how valuation interest rates should be determined. The SVL is also not explicit as to how valuation interest rates should be determined for certain types of benefits offered under annuity contracts, such as death and nursing home benefits.

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Purpose

The purpose of this Actuarial Guideline is to codify the basic interpretation of CARVM and does not constitute a change of method or basis from any previously used method, by clarifying the assumptions and methodologies which will comply with the intent of the SVL. This Actuarial Guideline shall apply to all annuity contracts subject to CARVM, where any elective benefits (as defined below) are available to the contract owner under the terms of the contract. However, life or health insurance riders attached to an annuity contract, where all components of the rider (e.g., premiums, benefits, contract charges, accumulation values and other components) are separate and distinct from the components of the annuity contract, should be treated as a separate life or health insurance contract not subject to this Actuarial Guideline. While this Actuarial Guideline applies to all annuity contracts subject to CARVM, in the event an actuarial guideline or regulation dealing with reserves is developed for a specific annuity product design, the product specific actuarial guideline or regulation will take precedence over the Actuarial Guideline.

Definitions

1. Elective and Non-Elective Benefits in CARVM

   For purposes of determining reserves under CARVM, each benefit available under the annuity contract must be placed into one of the two categories defined as follows:

   Non-Elective Benefits: Benefits that are payable to contract owners or beneficiaries only after the occurrence of a contingent or scheduled event independent of a contract owner's election of an option specified in the contract, including (but not limited to) death benefits, accidental death benefits, disability benefits, nursing home benefits, and benefits payable under either a deferred or immediate annuity contract (with or without life contingencies), where no benefit options are available under the terms of the contract.

   Elective Benefits: Benefits that do not fall under the non-elective benefits category (i.e., benefit options that may be freely elected under the terms of the contract). Elective benefits include (but are not limited to) full surrenders, partial withdrawals, and full and partial annuitizations.

   In some cases it may not be clear whether some benefits are elective or non-elective. The presence of certain types of non-elective benefits may affect other non-elective benefits and/or elective benefits. The Valuation Actuary should use judgment in making these determinations by considering factors such as the degree to which contract owner actions would be influenced by the availability of each benefit in the contract.

2. Elective and Non-Elective Incidence Rates in CARVM

   For non-elective benefits, incidence rates from tables prescribed by the SVL should be applied to determine the payment of non-elective benefits and to discount, for survivorship, all benefit payments included in an Integrated Benefit Stream, as defined below. If no incidence tables are prescribed by the SVL, then company or industry experience (with margins for conservatism) may be used, as appropriate. Annuity mortality tables prescribed by the SVL should be used to determine all mortality based benefits under the contract (including, but not limited to, annuitizations and death benefits) and to discount other types of benefit payments for survivorship.

   Actuarial judgment should be used as to the appropriateness of applying any non-elective incidence rates other than mortality. For non-elective waiver-of-surrender-charge benefits other than mortality-based benefits and for similar non-elective benefits, incidence rates greater than zero are not to be applied at any time in the projection after the earlier of: (a) the end of the surrender charge period

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applicable immediately after the first premium is paid; and (b) when the projected cash value has been depleted.

For elective benefits, incidence rates should not be based on tables reflecting past company experience, industry experience or other expectations. Instead, every potential guaranteed elective benefit stream required to be reserved by CARVM must be considered in the determination of integrated benefit streams as defined below. This is accomplished by considering trial sets of guaranteed elective benefit incidence rates, either through numerical testing or analytical means, to determine which trial set produces the "greatest present value" as described in Text paragraph 1 below. Theoretically, this means that all possible elective benefit incidence rates between 0% and 100% should be considered. However, in practice, such a greatest present value will typically occur by assuming an incidence rate of either 0% or 100%.

3. Integrated Benefit Stream

An integrated benefit stream is one potential blend of guaranteed elective and non-elective benefits available under the contract, determined as the combination of A and B, where:

A equals one potential stream of one or more types of guaranteed elective benefits available under the terms of the contract, based upon a chosen set of elective benefit incidence rates; and

B equals the stream of all guaranteed non-elective benefits provided under the terms of the contract, recognizing the guaranteed elective benefit stream under consideration in A above, and the non-elective incidence rates defined in 2. above.

Both A and B above should be discounted for survivorship, based on the non-elective incidence rates defined in 2. above.

Text

1. Greatest Present Value

All guaranteed benefits potentially available under the terms of the contract must be considered in the valuation process and analysis and the ultimate policy reserve held must be sufficient to fund the greatest present value of all potential integrated benefit streams, reflecting all guaranteed elective and non-elective benefits available to the contract owner. Each integrated benefit stream available under the contract must be individually valued and the ultimate reserve established must be the greatest of the present values of these values, based on valuation interest rate(s) as defined in Section 3 below.

2. Examples of Integrated Benefit Streams That Must Be Considered

A. Cash Value Streams

One mandatory set of integrated benefit streams for a deferred annuity with cash settlement values which must always be considered is any possible blend of future guaranteed partial withdrawals and full surrenders available under the contract, as specified in the SVL, accumulated at the guaranteed credited interest rate(s) and discounted at the valuation rate(s) of interest defined in section 3 below, with appropriate recognition of all guaranteed non-elective benefits available under the contract.

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B. Annuitization Streams

A second mandatory set of integrated benefit streams that must be considered is any possible blend of future guaranteed full or partial annuitization elections, as specified in the SVL, available to the contract owner at each election date required by CARVM, with appropriate recognition of all guaranteed non-elective benefits available under the terms of the contract. In determining the integrated benefit streams to value the annuitization option, the guaranteed purchase rates contained in the contract, as well as any other contract provisions, excluding any current purchase rates which may be applicable, are applied to the accumulation fund.

C. Other Elective Benefit Streams

In addition to the cash value and annuitization streams described above, all other possible guaranteed elective benefits available under the contract, including blends of more than one type of guaranteed elective benefit, must be considered in a manner consistent with the mandatory cash value and annuitization streams, with appropriate recognition of all guaranteed non-elective benefits available under the contract.

3. Determination of Valuation Interest Rates

Section 4b of the SVL determines valuation rates for an annuity contract based on the following Parameters:

A. The basis of valuation (issue year or change in fund);

B. Whether or not the annuity provides for cash settlement options;

C. Whether interest is guaranteed on premiums received more than 12 months following issue (or the valuation date for change in fund basis);

D. The guarantee duration; and

E. The Plan Type.

Parameters A, B and C above should be determined at a contract level. Additional requirements regarding the change in fund basis of valuation are set forth in Section 5 below. Parameters D and E should be determined at a benefit level, as set forth in Section 4 below.

Under a contract level determination, parameters are set based on the characteristics of the contract as a whole. Under a benefit level determination, parameters are set based on the characteristics of each benefit, resulting in potentially different valuation rates for each benefit type comprising the integrated benefit stream.

4. Determination of Guarantee Duration and Plan Type

Guarantee duration and Plan Type are based upon the specific characteristics of each individual benefit type that comprise the integrated benefit stream, as follows:

A. For portions of the integrated benefit stream attributable to full surrender and partial withdrawal benefits, the Plan Type should be based upon the withdrawal characteristics of the benefit, as stated in the contract. This may result in a Plan Type A, B or C under the 1980 amendments of the SVL. The guarantee duration is the number of years for which interest rates are guaranteed in

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excess of the calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty (20) years.

B. For portions of the integrated benefit stream attributable to full and partial annuitization benefits, the determination of the valuation interest rate involves the use of the appropriate Plan Type and weighting factor as determined by the SVL, with the guarantee duration as the number of years from the original date of issue or date of purchase, to the date the annuitization is assumed to commence. If the underlying assumption is that the contract owner may withdraw funds only as an immediate life annuity or as installments over 5 years or more, this will generally result in a Plan Type A, under the 1980 amendments of the SVL, with the valuation interest rate changing as different assumed annuitization dates determine guarantee durations which will fall into different guarantee duration bands under the SVL. An assumed annuitization option which has a non-life contingent payout period of less than five (5) years shall be considered a Plan Type C, with the valuation interest rate changing as different assumed annuitization dates determine guarantee durations which will fall into different guarantee duration bands under the SVL.

C. For portions of the integrated benefit stream attributable to non-elective benefits, since the underlying assumption is that no withdrawal is permitted, Plan Type A should generally be used, with a guarantee duration determined as the number of years from issue or purchase to the date non-elective benefits may first be paid. In most cases, the guarantee duration should be less than five years, since non-elective benefit coverage usually begins immediately after issue, with benefits payable commencing in the first contract year.

For benefit types incorporating multiple payments, paragraphs 4(A), 4(B), and 4(C) above should be applied to each separate payment according to the withdrawal, annuitization, or non-elective benefit characteristics of the contract and payment provisions at the time each payment is to be made. If a portion of the integrated benefit stream is part of an immediate life annuity or a series of installments over five (5) years or more, but can be changed directly or indirectly by exercise of contract owner withdrawal options, then it would be inappropriate to apply paragraph 4(B) to that portion of the integrated benefit stream, since the contractholder may withdraw funds other than as a life annuity or in installments of five (5) years or more.

For example, a Guaranteed Lifetime Income Benefit (GLIB) is a guarantee to the owner of a fixed deferred annuity contract, whether traditional or indexed to an external referent such as an equity index, that the owner can have a defined income for life in an amount determined by formula, while the owner retains traditional rights (such as withdrawal) to the other values provided by the underlying deferred annuity and while such values continue to exist. Income benefits are typically deducted from one or more of the annuity's defined values to the extent such values remain positive. Once the GLIB is elected, the contract owner may have rights to stop and restart the income benefit and may also request full or partial surrender of any remaining annuity value, though doing so may negatively impact or eliminate subsequent guaranteed income benefits. Thus, applying 4(A) and 4(B) above, the GLIB benefit stream is seen to be composed of two portions to determine the Plan Type and guarantee duration, as follows:

The first portion consists of the series of defined payments to the extent that the payments, or any fraction thereof, are withdrawals that reduce or deplete the annuity's defined values. Applying paragraph 4(A) to this portion would result in Plan Type A, Plan Type B, or Plan Type C, by following the definitions of such contained within the Standard Valuation Law and reflecting the specific contract provisions, especially with regard to withdrawal. Paragraph 4(A) would also apply to any residual withdrawals that can be made following election of the GLIB benefit.

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The second portion is a life annuity without option to take or receive additional amounts under the contract, and consists of the payments not included in the above portion. Applying paragraph 4(B), Plan Type A would generally apply to this segment with the guarantee duration determined using the period from contract issue to commencement of payments in this second portion.

5. Change in Fund Basis

As indicated by section 4b.C.(1)(c)(vi) of the SVL, a company may elect to value annuity contracts with cash settlement options on either an issue year basis or on a change in fund basis. Annuity contracts with no cash settlement options must be valued on an issue year basis. The issue year basis or change in fund basis should be determined for the contract as a whole, and thus must be consistently applied to all portions of all integrated benefit streams available under the annuity contract. The election of issue year or change in fund basis must be made at the issuance of the contract and must not change during the term of the contract without the prior written approval of the commissioner.

6. Purchase Rates

Contracts may provide, as contractual guarantees, the use of preferential purchase rates to those listed in the contract. As an example, a contract may provide that the company will offer, at the time of annuitization, the rates offered to new purchasers of immediate annuities if such rates will provide a higher annuity benefit than would result from the contractually guaranteed rates provided in the contract. This creates a contract guarantee which must be valued under CARVM. Ignoring this benefit in determining reserves will produce reserves less than the statutory formula reserves required under CARVM. Valuation of this benefit, however, is complicated by the fact that the company does not currently know what the exact rate will be at the time of the settlement election. In order to determine conservative statutory formula reserves, if use of future unknown rates are guaranteed, the company shall establish reserves not less than the contract's accumulation fund value, on the valuation date, reduced by an "expense allowance" not to exceed 7% of such fund. This section does not require the calculation of a reserve for the annuitization of business based upon current purchase rates pursuant to the "annuitization streams" described in Paragraph 2.B. above.

Likewise for contracts which provide for additional amounts during the payout period over those guaranteed at the commencement of the annuity payments, the reserve during the deferred period shall not be less than the contract's accumulation fund reduced by an expense allowance not to exceed 7% of such fund.

7. Practical Considerations

The major purpose of this Actuarial Guideline is to provide clarification and consistency in applying CARVM to annuities with multiple benefit streams. However, in practice there may be other acceptable methods of applying CARVM which are substantially consistent with the methods described in this Actuarial Guideline. Such methods may also be used, with prior regulatory approval.

Additionally, in applying this Actuarial Guideline there may theoretically be an infinite number of contract owner options that are possible under the contract. However, it may not be practical, possible or even appropriate to test every conceivable combination of potential integrated benefit streams theoretically available under the contract. This Actuarial Guideline requires that the actuary consider, not necessarily test, all potential integrated benefit streams to determine to what extent each contract owner option has a material impact on the reserve**.** In practice, the actuary may be able to eliminate some potential integrated benefit streams by analytical methods. The actuary may also be able to demonstrate the reserve adequacy of certain approximations. For example, in certain situations it may

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be shown that a CARVM reserve ignoring non-elective benefits, plus an "add-on" reserve for non-elective benefits, is a reasonable approximation for the theoretically correct CARVM reserve.

Effective Date

This guideline shall be effective on December 31, 1998, affecting all contracts issued on or after January 1, 1981. A company may request a grade-in period for contracts issued prior to December 31, 1998 from the domiciliary commissioner upon satisfactory demonstration that the method and level of current reserves held for such contracts are adequate in the aggregate. This phase-in will require establishment of no less than 33 1/3% of the additional reserves resulting from the application of this guideline on December 31, 1998, no less than 66 2/3% on December 31, 1999, and 100% by December 31, 2000.

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Actuarial Guideline XXXIV

VARIABLE ANNUITY MINIMUM GUARANTEED DEATH BENEFIT RESERVES

Actuarial Guideline XXXIV was repealed December 30, 2009, and was replaced by *Actuarial Guideline XVIII—CARVM for Variable Annuities*, effective December 31, 2009.

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Actuarial Guideline XXXV

THE APPLICATION OF THE COMMISSIONERS ANNUITY RESERVE METHOD TO EQUITY INDEXED ANNUITIES

Background

The purpose of this Actuarial Guideline is to interpret the standards for the valuation of reserves for equity indexed annuities. This Guideline codifies the interpretation of the Commissioners Annuity Reserve Valuation Method (CARVM) by clarifying the computational methodologies which will comply with the intent of the Standard Valuation Law (SVL).

Equity indexed deferred annuity products provide policyholders with a minimum guaranteed interest accumulation rate on a portion of all premium payments and a portion of the growth, if any, of an equity based index such as the S&P 500. While there is no "typical" equity indexed product, there are design features that are common to most products. Some of these features are a participation rate guaranteed for one or more years, a cap on the portion of the index growth that is credited to policyholders, and a policy term which defines a time period for which current guarantees are applicable.

Equity indexed immediate annuity products provide policyholders with a minimum guaranteed annuitization rate and an opportunity to receive larger periodic payments based on the growth, if any, in an equity index. The product design may include features such as a participation rate, cap or term.

While contract parameters such as participation rate and cap are guaranteed for a period of time, growth of the underlying index is not. Index growth may be positive or negative. This combination of guaranteed parameters and unknown equity index growth makes the application of CARVM to these products problematic.

CARVM defines minimum statutory reserves as "the greatest of the respective excesses of the present value, at the date of valuation, of the future guaranteed benefits, including guaranteed nonforfeiture benefits, … over the present value, at the date of valuation, of any future valuation considerations derived from future gross considerations, required by the terms of such contract, that become payable prior to the end of such respective contract year. The future guaranteed benefits shall be determined by using the mortality table, if any, and the interest rate, or rates, specified in such contracts for determining guaranteed benefits."

In order that all insurers issuing equity indexed annuity products establish reserves for statutory reporting purposes that are consistent with CARVM minimum statutory formula reserves requirements, this actuarial guideline identifies a computational method that is deemed to be consistent with CARVM in situations when specific operational criteria called "Hedged as Required" criteria are met. In addition, two computational methods are defined that are deemed to be consistent with CARVM in the event the "Hedged as Required" criteria are not met.

Two forms of the "Hedged as Required" criteria are provided. The "basic" criteria are applicable when an insurer uses long dated options to hedge the equity risk embedded in an equity indexed annuity. The second set of criteria is applicable when an insurer uses an option replication strategy.

Scope

This Actuarial Guideline applies to all equity indexed annuity contracts, regardless of the date of issue, that are subject to CARVM.

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Computational Methods

Computational methods deemed to be consistent with CARVM can be classified into two groups, Type 1 methods and Type 2 methods. The following computational method is considered a Type 1 method: the Enhanced Discounted Intrinsic Method (EDIM). Type 1 computational methods are deemed to be consistent with CARVM if the applicable "Hedged as Required" are met. The following methods are considered Type 2 methods: the Commissioners Annuity Reserve Method with Updated Market Values (CARVM with UMV) and the Market Value Reserve Method (MVRM). Also, an adaptation of the MVRM, known as the Black-Scholes Projection Method (BSPM), is recognized. For a complete description of these methods, please consult Attachment 1.

General Requirements on the Use of Certain Computational Methods

The MVRM and EDIM computational methods are both based on a future value. In the case of MVRM, a projected index is determined. The projected index is then used to determine end of term and interim benefit amounts. CARVM is applied to these benefit amounts. In the case of EDIM, the end of term guaranteed value (a future value) is used to determine an interest rate for calculating terminal reserves for the guaranteed benefits after the initial terminal reserve. Determination of the "term" is an essential component of both computational methods.

The EDIM, MVRM and the BSPM adaptation of the MVRM computational methods are considered acceptable interpretations of CARVM under the following conditions:

1. The policy form design features a single dominant benefit which is the most likely benefit to be provided under the policy form with the determination of the single dominant benefit based on a consideration of product features such as the pattern of guaranteed participation rates, surrender charges, vesting rates, spread deductions, and marketing/advertising material.

2. The point in time associated with the single dominant benefit most likely to be provided under the contract is used as the terminal point of the current term for purposes of applying the computational method and complying with the "Hedged as Required" criteria, if applicable.

3. The appointed actuary has demonstrated to the satisfaction of the regulatory officials in each state in which the insurer is required to submit a statutory financial statement, prior to the use of the MVRM or EDIM computational methods, that the requirements above have been met.

Variations from the MVRM and EDIM as described in Attachment 1, are not acceptable interpretations of CARVM. The BSPM is considered an acceptable adaptation of the MVRM.

Type 1 Methods

A Type 1 computational method is deemed to be consistent with CARVM if an insurer using the method complies with the applicable "Hedged as Required" criteria (Attachment 2) and provides a certification as to compliance with the criteria. The certification must be signed by the appointed actuary. The certification shall be provided with each annual and quarterly statutory financial statement filed with the appropriate insurance regulatory official in each state in which the insurer does business.

For purposes of determining compliance with the "equivalence of characteristics" requirement in the "Hedged as Required" criteria, the current term of an equity indexed deferred annuity policy will be determined based on the requirements in the section captioned "General Requirements on Use of Certain Computational Methods." For purposes of applying a Type 1 computational method, the time horizon for

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present value calculations should be based on the current term of the policy based on the requirements in the section captioned "General Requirements on Use of Certain Computational Methods."

The Enhanced Discounted Intrinsic Method (EDIM) requires an initial reserve amount that is determined by methods that are not specifically included in the EDIM. For purposes of compliance with statutory minimum formula reserve requirements, the initial reserve under EDIM must be set at least equal to the initial reserve produced by either CARVM with UMV, or the MVRM with assumptions used to compute any necessary option market values reasonable as of the date of issue of the policy. The insurer must provide a certification (Attachment 3) as to the reasonableness of the assumptions.

Type 2 Methods

The use of Type 2 method is not conditioned upon the requirement to meet the "Hedged as Required" criteria. However, an insurer using a Type 2 method must provide a certification (Attachment 4) signed by the appointed actuary with each annual and quarterly statutory financial statement filed with the appropriate insurance regulatory official in each state in which the insurer does business. This certification deals with the assumptions underlying the option market values included in the calculation of reserves using a Type 2 method and the consistency in assumptions between these option market values and the statement value of any options owned by the insurer to support the equity indexed annuity business being valued.

For purposes of applying the MVRM and the BSPM recognized adaptation computational methods, the time horizon for present value calculations should be based on the requirements in the section captioned "General Requirements on Use of Certain Computational Methods."

Required Change in Method

In the event an insurer that is using a Type 1 computational method for a block of business fails to meet the applicable "Hedged as Required" criteria, the required actuarial certification must disclose this fact. If the reason for failing the "Hedged as Required" criteria is not corrected within one quarterly financial reporting of the initial disclosure of the failure in the actuarial certification, the insurer must use a Type 2 computational method for determining minimum statutory formula reserves for this block of business.

If at a later date, the insurer can demonstrate to the satisfaction of its domiciliary commissioner that it is meeting the applicable "Hedged as Required" criteria, the insurer may, with the approval of the domiciliary commissioner, resume using a Type 1 computational method. In addition, the insurer must notify the appropriate regulatory official in each state in which the insurer does business subject to the change in computational method.

Optional Change in Method

An insurer using either a Type 1 or Type 2 computational method for a block of business, may with the approval of its domiciliary commissioner and after notifying the appropriate regulatory official in all the other states in which the insurer writes this block of business, use a computational method of the other type. If the change in computational methods involves a change from a Type 2 computational method to a Type 1 computational method, the request to the domiciliary commissioner for approval of the change in method must be accompanied with a demonstration of compliance with the applicable "Hedged as Required" criteria.

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Plan Type

The use of either a Type 1 computational method or a Type 2 computational method requires a determination of Plan Type for purposes of determining the maximum valuation interest rate. Design features unique to equity indexed annuities, such as an equity enhanced surrender values, vesting schedules, or participation rate, should not used to determine the Plan Type of a policy form. Only those design features specifically identified in Section 4b. Paragraph C of the NAIC Model SVL may be used to assign a Plan Type to a policy form.

The definition of Plan Type A and Plan Type B in the NAIC Model SVL includes the phrase "with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company..." The reference to "change in ... asset values" does not include changes in policy values due to changes in the equity index underlying the policy form.

Other Regulatory Requirements

The guidance provided in this Actuarial Guideline concerning statutory minimum formula reserves for equity indexed annuity products supersedes the valuation guidance in Sections 5 and 6 of the NAIC Interest-Indexed Annuity Contracts Model Regulation.

Asset Adequacy Testing of Reserves

To the extent required by law, regulation, or regulatory requirements, reserves established for equity indexed annuity policies must be tested for adequacy using appropriate methods and assumptions.

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ATTACHMENT 1
Description of Computational Methods

CARVM-UMV

Step 1: For each duration and each benefit at which an index-based benefit is available, determine the market value of the appropriate call option. The appropriate call option is one that exactly hedges the floor of the benefit at that point in time. This means that the payoff of the call option should exactly equal the difference between the specific benefit available at that point in time (reflecting all relevant contract features) and the guaranteed floor of that benefit. The market value should be determined using an appropriate option pricing technique, such as Black-Scholes or a stochastic scenario method.

Step 2: The market value of all of the call options are projected forward at the appropriate valuation interest rate to the point in time at which the call option would expire. The valuation interest rate should be consistent with the requirements of any applicable Actuarial Guidelines or regulations, such as Actuarial Guideline XXXIII or Actuarial Guideline IX-B.

Step 3: The future guaranteed benefits for each benefit at each time point are determined by adding the guaranteed floors of the benefit to the amounts determined in Step 2.

Step 4: Now a CARVM calculation can be performed. The CARVM calculation should be in accordance with Actuarial Guideline XXXIII and any other applicable regulations or Actuarial Guidelines.

MVRM

Step 1: Calculate the projected index value at the end of the "term" which would produce a benefit at the end of the "term" equal to the sum of (1) the contract guarantee at that time, and (2) the current market value of the call option(s) which would fully hedge the index-based benefit, accumulated at the appropriate valuation interest rate. This calculation should be performed assuming equal annual percentage increases in the index. The call options used are those with maturity dates coterminous with the setting of participation rates, spread, or any other method of determining index-based benefits. The valuation interest rate used to accumulate the call options should be consistent with the requirements of any applicable Actuarial Guidelines or regulations, such as Actuarial Guideline XXXIII or Actuarial Guideline IX-B. Note that the "term" referred to above should be consistent with the "term" described in this Actuarial Guideline.

Step 2: From the current level of the index and the projected level of the index at the end of the term, calculate an implied compound constant growth rate of the index from the valuation date to the end of the term. Use this implied growth rate to project the level of the index at intermediate anniversaries.

Step 3: All annuity benefits can now be determined from the index levels.

Step 4: Now a CARVM calculation can be performed. The CARVM calculation should be in accordance with Actuarial Guideline XXXIII and any other applicable regulations or Actuarial Guidelines.

MVRM Using Black-Scholes Projection Method

This is an adaptation of the basic MVRM approach to accommodate products for which the participation rate, spread, or any other benefit determination method is redetermined during the term (particularly annually).

Step 1: Calculate the cost of a full hedging call option as a percentage of the account value for the period that the benefit determination is guaranteed, accumulate the percentage to the end of that period at the risk-free interest rate, and use the accumulated percentage cost as the projected growth rate of the account value during the period. Perform the same type of calculation for each successive period within the term,

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giving recognition to the benefit guarantees, forward interest rates, forward index volatility, and index dividend levels.

Step 2: Determine the index level which would provide the projected account level on each anniversary on the basis of the participation rate, spread, or other benefit determination method used.

Step 3: All annuity benefits can now be determined from the index levels.

Step 4: Now a CARVM calculation can be performed. The CARVM calculation should be in accordance with Actuarial Guideline XXXIII and any other applicable regulations or Actuarial Guidelines.

EDIM

Step 1: The Fixed Component at issue is the formula reserve produced by either CARVM-UMV or MVRM. The Fixed Component at the end of the term is the floor of the benefit actually being hedged.

Step 2: The intermediate values of the Fixed Component are found by solving for an interest rate that would accumulate the initial value to the ending value. For example, assume you purchase options assuming that 90% of policyholders will surrender at maturity, and that 10% of policyholders will annuitize at maturity. The Fixed Component is the sum of (1) 90% of the Fixed Component that grows to the floor of the surrender benefit; and (2) 10% of the Fixed Component that grows to the floor of the annuitization benefit.

Step 3: The Equity Component is equal to the discounted intrinsic value of the options. The discounted intrinsic value of the options is found by taking the intrinsic value at the valuation date, and discounting at the valuation rate for the number of years from the valuation date to the end of the term. The valuation interest rate used to discount the intrinsic value of the call options should be consistent with the requirements of any applicable Actuarial Guidelines or regulations, such as Actuarial Guideline XXXIII or Actuarial Guideline IX-B.

Step 4: The reserve is the sum of a Fixed Component and an Equity Component.

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ATTACHMENT 2
Hedged as Required Criteria

In order to use a Type 1 computational method, the appointed actuary needs to certify quarterly that it meets either the "Basic" or "Option Replication" criteria.

Basic

1. Required equivalence of characteristics between the option contracts held and the options imbedded in the products with respect to specific contract features such as: Index, averaging features, option type, strike price, term, etc.

2. The amount of hedge purchased, at or near the contract issuance, must be greater than or equal to a Specified Percentage of the product's account value, at contract issuance. The Specified Percentage varies by the length of the option guarantee (some annual ratchet products may have a term of several years, but the participation rates are only guaranteed for one year, so the "term" for this purpose is 1 year), and allows the company to assume no more than 3% per year of elective benefit decrements, unless the Commissioner agrees to a higher limit. For example, for a five-year point-to-point product, the Specified Percentage would be: SP% = (1 - .03) ^ 5 = 86%.

3. The Company must have a specific plan for hedging risks associated with interim death benefits, early surrenders, etc.

4. The Company must have a system in place that is used to monitor the effectiveness of the company's hedging strategy.

5. The Company must have a stated maximum tolerance for differences between the expected performance of the hedge and the actual results of the hedge.

Option Replication

1. Required equivalence of characteristics between the target of an option replication strategy employed, and the options imbedded in the liabilities with respect to specific contract features such as: index, averaging features, option type, strike price, term, etc.

2. At the end of each quarter, the notional amount of the target of the option replication strategy must be greater than or equal to the sum of the Specified Percentages of each contract's account value. The Specified Percentage varies by the length of the remaining option guarantee (some annual ratchet products may have a term of several years, but the participation rates are only guaranteed for one year, so the "term" for this purpose is 1 year), and allows the company to assume no more than 3% per year of elective benefit decrements, unless the Commissioner agrees to a higher limit. For example, if a point-to-point contract has five years remaining, the Specified Percentage for that contract would be: SP% = $(1 - .03)^5$ = 86%. Appropriate assumptions for non-elective decrements such as mortality may be added to the assumption for elective decrements.

3. The company must have a specific plan for hedging risks associated with interim death benefits, early surrenders, etc.

4. The Company must have system in place that is used to monitor the effectiveness of the company's hedging strategy.

5. The Company must have a stated maximum tolerance for differences between the expected performance of the hedge and the actual results of the hedge. The maximum tolerance test and compliance evaluation test must meet the following minimum requirements. The compliance evaluation criteria will be a retrospective correlation test performed at least on a weekly basis.

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The Company will compare the change in the market value, from the beginning of the calendar quarter, of the hedge portfolio with the change in the market value of the options embedded in the liability portfolio. The maximum dollar amount of difference permitted between these two changes is 10% of the beginning of period market value of the options embedded in the liabilities. If the difference exceeds this limit, the following steps must be taken:

- If for a second time during a quarter the dollar amount of difference exceeds 10% of the beginning of period market value of the options embedded in the liabilities, but is less than 25% of the beginning of period market value of the options embedded in the liabilities, the Company must notify the Commissioner of Insurance in each state in which the insurer is licensed. The notification must indicate the dollar amount of reserves being hedged by the option replication strategy.

- If at any of the weekly intervals, the difference between the two changes exceeds 25% of the beginning of period market value of the options embedded in the liabilities, the Company must notify the Commissioner of Insurance in each state in which the insurer is licensed. The notification must indicate the dollar amount of reserves being hedged by the option replication strategy and the impact on surplus of reporting the reserves based on the CARVM-UMV.

- If at any point in time during the quarter the difference between the two changes exceeds 35% of the beginning of period market value of options embedded in the liabilities, the insurer is deemed to be out of compliance with the "Hedged as Required" criteria, and the Company must notify the Commissioner of Insurance in each state in which the insurer is licensed. The notification must indicate the dollar amount of reserves being hedged by the option replication strategy and the impact on surplus of reporting the reserves based on the CARVM-UMV.

Drafting Note: The requirements discussed above deal with the situation in which the actual hedge underperforms relative to the expected hedge performance. The ability of an insurer to over-hedge may be constrained by other components of a state's regulatory framework including the state's investment article and regulations concerning the use of derivative instruments. For purposes of this Drafting Note, over-hedged means that at a particular point in time, the hedge portfolio exceeds the portfolio of liabilities being hedged. If over-hedged, the excess hedging instruments are excluded from the measurements required in Item 5 of the Hedged as Required Criteria.

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ATTACHMENT 3
Reasonableness of Assumptions Certification

The following certification must be filed in conjunction with each quarterly and annual statutory financial statement filed with the appropriate regulatory official in each state in which the insurer does business. The certification must be signed by the appointed actuary.

I, (state name and professional designation), am the appointed actuary for (company name). I have reviewed the assumptions underlying the values assigned to all equity options used in the determination of the initial statutory reserves under the Enhanced Discounted Intrinsic Method for all equity indexed deferred annuity products issued or reinsured by (company name) and reported in the statutory financial statement as of (the date of valuation). The assumptions used to determine such option market values are reasonable in light of the relevant economic conditions prevalent at the time of issue of each policy valued using the Enhanced Discounted Intrinsic Method.

_____

(Name of actuary)

_____

(Signature of actuary)

_____

(Date of certification)

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ATTACHMENT 4
Reasonableness and Consistency of Assumptions Certification

The following certification must be filed in conjunction with each quarterly and annual statutory financial statement filed with the appropriate regulatory official in each state in which the insurer does business. The certification must be signed by the appointed actuary.

I, (state name and professional designation), am the appointed actuary for (company name). I have reviewed the assumptions underlying the values assigned to all equity options used in the determination of statutory reserves for all equity indexed annuity products issued or reinsured by (company name) insurance company and reported in the statutory financial statement as of (the date of valuation). The assumptions used to determine such option market values are:

1. reasonable in light of current relevant economic conditions as of the date of valuation, and

2. are consistent with the comparable assumptions used to determine the statement value of any derivative instruments used to hedge the equity indexed based obligations embedded in the equity indexed annuities subject to this certification.

_____

(Name of actuary)

_____

(Signature of actuary)

_____

(Date of certification)

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Actuarial Guideline XXXVI

THE APPLICATION OF THE COMMISSIONERS RESERVE VALUATION METHOD TO EQUITY INDEXED LIFE INSURANCE POLICIES

Background

The purpose of this Actuarial Guideline is to clarify statutory and regulatory requirements for the valuation of reserves for equity indexed universal life insurance policies. This Guideline codifies the interpretation of the Commissioners Reserve Valuation Method (CRVM) by clarifying the computational methodologies that are deemed to comply with the intent of the Standard Valuation Law (SVL) and the Universal Life Insurance Model Regulation. These methodologies will be deemed to be consistent with CRVM.

Equity indexed universal life insurance policies include interest credits that are a combination of a guaranteed interest rate and an interest rate based on a percentage of the increase in an equity index, such as the S&P 500. Currently, there are only a few products in the market and the product designs have been straightforward. As new product designs emerge, this Actuarial Guideline may have to be revised.

In order that all insurers issuing equity indexed universal life insurance policies establish reserves for statutory reporting purposes that are consistent with CRVM minimum statutory formula reserves, this Actuarial Guideline identifies a computational method deemed to be consistent when specific operational criteria called “Hedged as Required” criteria are met. In addition, two other computational methods are defined that are deemed to be consistent with CRVM in the event the “Hedged as Required” criteria are not met.

Scope

This Actuarial Guideline applies to all equity indexed universal life insurance policies, regardless of the date of issue, that are subject to CRVM and would otherwise be subject to the reserve requirements under the Universal Life Insurance Model Regulation.

Definitions

Appointed Actuary. The appointed actuary, for purposes of this guideline, is the actuary appointed by the company’s board of directors to provide opinions in accordance with Standard Valuation Law and the model Actuarial Opinion and Memorandum regulation.

Credited. Index-based benefits will be considered to be credited when they are added to the fund and treated in the same manner as other interest credits to the fund.

Term. An index-based benefit crediting period.

Computational Methods

Computational methods deemed to be consistent with CRVM can be classified into three groups, Type 1 methods, Type 2a methods and Type 2 methods. The following computational method is considered a Type 1 method: the Implied Guarantee Rate Method (IGRM). Type 1 computational methods are deemed to be consistent with CRVM only if the “Hedged as Required” criteria are met. The following is considered a Type 2a method: the Commissioners Reserve Valuation Method with Updated Average Market Value (CRVM with UAMV). The following is considered a Type 2 method: the Commissioners Reserve Valuation Method with Updated Market Value (CRVM with UMV). For a complete description of these methods, consult Attachment 1.

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The minimum reserve for equity indexed life insurance policies is the statutory reserve calculated under the Universal Life Insurance Model Regulation for an identical policy with no guaranteed index-based benefits. If the reserve produced by Type 1, Type 2a or Type 2, as appropriate, is greater than the minimum reserve, then that Type 1, Type 2a or Type 2 reserve is the minimum reserve.

Type 1 Methods

A Type 1 computational method is deemed to be consistent with CRVM if an insurer using the method complies with the "Hedged as Required" Criteria (Attachment 2) and provides a certification (Attachment 3) as to compliance with the criteria. The appointed actuary must sign the certification. The certification shall be provided with each annual and quarterly statutory financial statement filed with the appropriate insurance regulatory official in each state in which the insurer writes or reinsures equity indexed universal life insurance business.

For purposes of determining compliance with the "equivalence of characteristics" requirement in the "Hedged as Required" criteria, the current term of an equity indexed universal life insurance policy is one year or less. This should be interpreted consistently when a separate index-based benefit guarantee is made on each premium received.

The IGRM computational method is deemed to be consistent with CRVM under the following conditions:

1. The implied guaranteed rate for terms after the first, determined at issue using the method of Attachment 1, paragraph 3 of the IGRM method, is less than or equal to the appropriate maximum valuation interest rate.

2. Index-based benefit terms cannot be greater than one year. This should be interpreted consistently when a separate index- based benefit guarantee is made on each premium received.

3. The appointed actuary has demonstrated at time of filing or in conjunction with a change to a Type 1 Method, to the satisfaction of the regulatory officials in each state in which the insurer writes or reinsures equity indexed universal life insurance business, prior to the use of the IGRM that the requirements in (1) and (2) above have been met.

Type 2a Methods

A Type 2a computational method is deemed to be consistent with CRVM if an insurer using the method complies with Type 2a Prerequisite Criteria below, and provides Reasonableness and Consistency of Assumptions Certification (Attachment 4). The appointed actuary must sign the certification. The certification shall be provided with each annual and quarterly statutory financial statement filed with the appropriate insurance regulatory official in each state in which the insurer writes or reinsures equity indexed universal life insurance business.

Type 2a Prerequisite Criteria are as follows:

1. At issue, the policy satisfies (a) or (b) as follows:

   (a) The implied guaranteed rate for terms after the first, determined at issue using the method of Attachment 1, paragraph 3 of the CRVM with UAMV method, is less than or equal to the appropriate maximum valuation interest rate; or

   (b) Policies with identical renewal guarantees issued in three of the past five years would have satisfied condition 1 for the Type 1 method.

2. Index-based benefit terms cannot be greater than one year. This should be interpreted consistently when a separate index- based benefit guarantee is made on each premium received.

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3. The appointed actuary has demonstrated at time of filing or in conjunction with a change to a Type 2a Method, to the satisfaction of the regulatory officials in each state in which the insurer writes or reinsures equity indexed universal life insurance business, prior to the use of the CRVM with UAMV that the requirements in (1) and (2) above have been met.

Type 2 Methods

The use of a Type 2 method is not conditioned upon the requirement to meet the "Hedged as Required" criteria or the Type 2a Prerequisite Criteria. However, an insurer using a Type 2 method must provide a certification (Attachment 5) signed by the appointed actuary with each annual and quarterly statutory financial statement filed with the appropriate insurance regulatory official in each state in which the insurer writes or reinsures equity indexed universal life insurance business. This certification deals with the assumptions underlying the option market values included in the calculation of reserves using a Type 2 method and the consistency in assumptions between these option market values and the statement value of any options owned by the insurer to support the equity indexed universal life insurance business being valued.

Required Change in Method

In the event an insurer that is using a Type 1 computational method for a block of business fails to meet the applicable "Hedged as Required" criteria, the required actuarial certification must disclose this fact. If the reason for failing the "Hedged as Required" criteria is not corrected within one quarterly financial reporting period of the initial disclosure of the failure in the actuarial certification, the insurer must choose to use a Type 2a or a Type 2 computational method for determining minimum statutory formula reserves for this block of business.

If, at a later date, the insurer can demonstrate to the satisfaction of its domiciliary commissioner that it is meeting the applicable "Hedged as Required" criteria, the insurer may, with the approval of the domiciliary commissioner, resume using a Type 1 computational method. In addition, the insurer must notify the appropriate regulatory official in each state in which the insurer does business subject to the change in computational method.

Optional Change in Method

An insurer using either a Type 1, Type 2a or Type 2 computational method for a block of business may, with the approval of its domiciliary commissioner and after notifying the appropriate regulatory official in all the other states in which the insurer writes this block of business, use a computational method of another type. If the change in computational methods involves a change from a Type 2 or Type 2a computational method to a Type 1 computational method the request to the domiciliary commissioner for approval of the change in method must be accompanied with a demonstration of compliance with the applicable "Hedged as Required" criteria. If the change in computational methods involves a change from a Type 2 computational method to a Type 2a or Type 1 computational method, the request to the domiciliary commissioner for approval of the change in method must be accompanied with a demonstration of compliance with the "Type 2a Prerequisite Criteria" or the requirements specified in the section captioned "Type 1 Methods."

Asset Adequacy Testing of Reserves

To the extent required by law, regulation, or regulatory requirements, reserves established for equity indexed life policies must be tested for adequacy using appropriate methods and assumptions.

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Attachment 1
Description of Computational Methods

Implied Guaranteed Rate Method (IGRM)

To use this computational method, companies must satisfy the "Hedged as Required" criteria, which are set out in Attachment 2. On the asset side, options will be held in accordance with the rules of the NAIC Accounting and Procedures Manual.

The following describes how the IGRM works:

1. Issue date calculations:

   Calculate an implied guaranteed rate, determined at issue, for the period of the initial term equal to: (a) the guaranteed interest rate for the period of the initial term; plus (b) the accumulated option cost expressed as a percent of the policy value to which the indexed benefit is to be applied. The accumulated option cost, determined at issue, is the option cost, which will provide the index-based benefit in excess of any other interest rate guarantee for the initial term, accumulated to the end of the term at the appropriate maximum valuation rate. The option cost should be as of the issue date.

   Calculate an implied guaranteed rate, determined at issue, for the terms after the first. The implied guaranteed rates for terms after the first term will be based on historical moving average option costs according to (3) below.

   Using the Universal Life Insurance Model Regulation, with the guaranteed interest rates equal to the implied guaranteed rates, calculate the Guaranteed Maturity Premium, Guaranteed Maturity Fund, and net premium for the policy based on guarantees at issue.

2. Valuation date calculations:

   Calculate the implied guaranteed rate for the current term based on the current term's index-based benefit and the option cost at the start of the current term that will provide the indexed benefit, in excess of any other interest rate guarantee, for the current term. The method of calculating the current term implied guaranteed rate is the same as for calculating the rate for the initial term. The implied guaranteed rate for terms after the current is not recalculated as long as neither the interest rate guarantees nor the index-based benefit guarantee have changed. (If guarantees have improved, then the new implied guaranteed rates for future terms will be based on option costs determined at issue according to (3) below.)

   Continue the calculation of the reserve according to the Universal Life Insurance Model Regulation. Use the recalculated current term implied guaranteed rate and the implied guaranteed rate for future terms, as determined according to (3) below, when computing future guaranteed benefits at the valuation date. Do not recalculate the Guaranteed Maturity Premium, Guaranteed Maturity Fund, or net premium. This section should be interpreted consistently when a separate index-based benefit guarantee is made on each premium received.

   In determining reserves, the net premiums, as determined in Section 1 above, are payable over the period that benefits are projected to be available, but not beyond the end of the net premium payment period determined at issue.

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3. Index-based benefit guarantees beyond the current term should be handled as follows:

Calculate an implied guaranteed rate, determined at issue, for the terms after the current term equal to: (a) the guaranteed interest rate for the period of the term; plus (b) the accumulated option cost expressed as a percent of the policy value to which the indexed benefit is to be applied. The accumulated option cost is the historical moving average cost of the option whose term begins at the beginning of the term, which will provide the index-based benefit in excess of any other interest rate guarantee for the term, accumulated for the length of the term at the appropriate maximum valuation rate.

The historical moving average cost of the option will be calculated based on the averages over the sixty months previous to the calendar year of issue of each of the following items: (a) 3% plus the annualized daily actual index volatility as the estimated implied volatility for a one year European At-The-Money option, e.g. if the average index volatility is 15%, the implied volatility for the base case option cost is 18%; (b) index dividend rate; and (c) risk free rate. The base case cost is for a one year European At-The–Money option and must be adjusted to the characteristics of the policy.

In those states that require, by regulation, that the policy valuation interest rates not exceed the "minimum guaranteed interest rate" in the policy, the "minimum guaranteed interest rate" for IGRM is the implied guaranteed rate.

Commissioners Reserve Valuation Method Updated Average Market Value (CRVM with UAMV)

To use this computational method, companies must satisfy the Type 2a Prerequisite Criteria. On the asset side, options will be held in accordance with the rules of the NAIC Accounting and Procedures Manual. Similarly, reinsurance reserve credit will be in accordance with the rules of the NAIC Accounting and Procedures Manual.

The following describes how the CRVM with UAMV works:

1. Issue date calculations:

Calculate an implied guaranteed rate, determined at issue, for the period of the initial term equal to: (a) the guaranteed interest rate for the period of the initial term; plus (b) the accumulated option cost expressed as a percent of the policy value to which the indexed benefit is to be applied. The accumulated option cost, determined at issue, is the option cost that will provide the index-based benefit in excess of any other interest rate guarantee for the initial term, accumulated to the end of the term at the appropriate maximum valuation rate. The option cost should be as of the issue date.

Calculate an implied guaranteed rate, determined at issue, for the terms after the first. The implied guaranteed rates for terms after the first term will be based on historical moving average option costs according to (3) below.

Using the Universal Life Insurance Model Regulation, with the guaranteed interest rates equal to the implied guaranteed rates, calculate the Guaranteed Maturity Premium, Guaranteed Maturity Fund, and net premium for the policy based on guarantees at issue.

2. Valuation date calculations:

When calculating the present value of future guaranteed policy benefits at the valuation date by projecting a fund equal to the greater of the Guaranteed Maturity Fund or the policy value, this fund should be projected to the end of the current term at the guaranteed interest rate and added to

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the accumulated option cost for the current term. The option cost should be determined as of the valuation date.

The option should provide for the index-based benefit in excess of any other interest rate guarantee for the current term based on a fund equal to the greater of the Guaranteed Maturity Fund or the policy value. The option cost should be accumulated to the end of the current term at the appropriate maximum valuation rate in accordance with the SVL.

This combined amount should then be projected forward using the implied guaranteed rates for future terms, as determined according to (3) below.

The implied guaranteed rates for terms after the current are recalculated on the valuation date. The implied guaranteed rates for future terms will be based on historical moving average option costs on the valuation date according to (3) below.

Do not recalculate the Guaranteed Maturity Premium, Guaranteed Maturity Fund, or net premium. This section should be interpreted consistently when a separate index-based benefit guarantee is made on each premium received.

In determining reserves, the net premiums, as determined in Section 1 above, are payable over the period that benefits are projected to be available, but not beyond the end of the net premium payment period determined at issue.

3. Index-based benefit guarantees beyond the current term should be handled as follows:

Calculate an implied guaranteed rate, determined either at issue or at a valuation date, for the terms after the current term equal to: (a) the guaranteed interest rate for the period of the term; plus (b) the accumulated option cost expressed as a percent of the policy value to which the indexed benefit is to be applied. The accumulated option cost is the historical moving average cost of the option whose term begins at the beginning of the term, which will provide the index-based benefit in excess of any other interest rate guarantee for the term, accumulated for the length of the term at the appropriate maximum valuation rate.

The historical moving average cost of the option will be set equal to the option cost calculated based on the averages of each of the following items over the sixty months previous to the calendar year of the determination date: (a) 3% plus the annualized daily actual index volatility as the estimated implied volatility for a one year European At-The-Money option, e.g. if the average index volatility is 15%, the implied volatility for the base case option cost is 18%; (b) index dividend rate; and (c) risk free rate. The base case cost is for a one year European At-The–Money option and must be adjusted to the characteristics of the policy.

In those states that require, by regulation, that the policy valuation interest rates not exceed the “minimum guaranteed interest rate” in the policy, the “minimum guaranteed interest rate” for CRVM with UAMV is the implied guaranteed rate.

CRVM with Updated Market Value (UMV) Method

CRVM with UMV applies the Universal Life Insurance Model Regulation to equity indexed life insurance policies using the following methods:

1. Issue date calculations:

When calculating the present value of future guaranteed policy benefits at issue by projecting fund values, the fund should be projected to the end of the initial term at the guaranteed interest rate and added to the accumulated option cost for the initial term. This combined amount should

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then be projected forward, using the policy guarantees to determine future death and endowment benefits. The option should provide for the indexed benefit in excess of any other interest rate guarantee for the initial term. The option cost should be as of the issue date. The option cost should be accumulated to the end of the initial term at the appropriate maximum valuation rate in accordance with the SVL. Any index-based benefit guarantees beyond the initial term should be determined as described in (3) below.

Using this method of determining the present value of future guaranteed benefits, calculate the Guaranteed Maturity Premium, Guaranteed Maturity Fund, and net premium for the policy based on guarantees at issue.

2. Valuation date calculations:

When calculating the present value of future guaranteed policy benefits at the valuation date by projecting a fund equal to the greater of the Guaranteed Maturity Fund or the policy value, this fund should be projected to the end of the current term at the guaranteed interest rate and added to the accumulated option cost for the current term. The option cost should be determined as of the valuation date. This combined amount should then be projected forward, using the policy guarantees to determine future death and endowment benefits. The option should provide for the index-based benefit in excess of any other interest rate guarantee for the current term, based on a fund equal to the greater of the Guaranteed Maturity Fund or the policy value. The option cost should be accumulated to the end of the current term at the appropriate maximum valuation rate in accordance with the SVL. Any index-based benefit guarantees beyond the current term should be treated as described in (3) below. Do not recalculate the Guaranteed Maturity Premium, Guaranteed Maturity Fund, or net premium. This section should be interpreted consistently when a separate index-based benefit guarantee is made on each premium received.

In determining reserves, the net premiums, as determined in Section 1 above, are payable over the period that benefits are projected to be available, but not beyond the end of the net premium payment period determined at issue.

3. Index-based benefit guarantees beyond the current term should be handled as follows:

At the time of calculation, fund values projected to the end of the current term should be further projected to the end of the next term at the guaranteed interest rate. This should be added to the accumulated option cost for that term. This should be done successively for each subsequent term, using the appropriate option cost for each term. The option for each term should provide for the index-based benefit in excess of any other interest rate guarantee for the term. The cost for each option should recognize the current relevant economic condition on the calculation date and be priced as if the term began on that date. The option cost for each future term should be accumulated to the end of the term at the appropriate maximum valuation rate in accordance with the SVL.

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Attachment 2
Hedged as Required Criteria - Life Products

In order to use a Type 1 computational method, the appointed actuary needs to certify quarterly that it meets either the "Basic" or "Option Replication" criteria.

Basic

1. Required equivalence of characteristics between the option policies held and the options embedded in the policies for the current term with respect to specific policy features such as: index; averaging features; option type; strike price; term; etc.

2. The amount of hedge owned must substantially cover the greater of the account value or reserve. "Substantially" is measured by the guarantees in the specific policy (some policies may have longer term guarantees than others), and allows the company to assume no more than 6% per year of elective benefit decrements, unless the Commissioner agrees to a higher limit. Benefit decrements due to charges in the policy should be taken into account in the same way as they are in the indexed interest formula in the policy (i.e., if indexed interest is credited on an average fund value, then it is the projected average fund value on each policy which should be hedged).

3. The company must have a specific plan for hedging risks associated with death benefits, early surrenders, unexpected premium payment patterns, and other potentialities. This plan must be available at issue and updated at every valuation date, or as often as the valuation actuary requirements may warrant.

4. The company must have a system in place that is used to monitor the effectiveness of its hedging strategy.

5. The company must have a stated maximum tolerance for differences between expected performance of the hedge and the actual results of the hedge.

Option Replication

1. Required equivalence of characteristics between the target of an option replication strategy employed and the options imbedded in the liabilities for the current term with respect to specific policy features such as: index; averaging features; option type; strike price; term; etc.

2. At the end of each quarter, the notional amount of the target of the option replication strategy must substantially cover the greater of the account value or reserve. "Substantially" is measured by the guarantees in the specific policy (some policies may have longer term guarantees than others), and allows the company to assume no more than 6% per year of elective benefit decrements, unless the Commissioner agrees to a higher limit. Benefit decrements due to charges in the policy should be taken into account in the same way as they are in the indexed interest formula in the policy (i.e., if indexed interest is credited on an average fund value, then it is the projected average fund value on each policy which should be hedged).

3. The company must have a specific plan for hedging risks associated with death benefits, early surrenders, unexpected premium payment patterns and other potentialities. This plan must be available at issue and updated at every valuation date, or as often as the valuation actuary requirements may warrant.

4. The company must have a system in place that is used to monitor the effectiveness of the company's hedging strategy.

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5. The company must have a stated maximum tolerance for differences between the expected performance of the hedge and the actual results of the hedge. The maximum tolerance test and compliance evaluation test must meet the following minimum requirements. The compliance evaluation criterion will be a retrospective correlation test performed at least on a weekly basis. The company will compare the change in the market value, from the beginning of the calendar quarter, of the hedge portfolio with the change in the market value of the target of the option replication strategy. The maximum dollar amount of difference permitted between these two changes is 10% of the beginning of period market value of the target of the option replication strategy. If the difference exceeds this limit, the following steps must be taken:

   - If for a second time during a quarter the dollar amount of difference exceeds 10% of the beginning of period market value of the target of the option replication strategy, but is less than 25% of the beginning of period market value of the target of the option replication strategy, the company must notify the Commissioner in each state in which the insurer is licensed. The notification must indicate the dollar amount of reserves being hedged by the option replication strategy.

   - If at any of the weekly intervals the difference between the two changes exceeds 25% of the beginning of period market value of the target of the option replication strategy, the company must notify the Commissioner in each state in which the insurer is licensed. The notification must indicate the dollar amount of reserves being hedged by the option replication strategy and the impact on surplus of reporting the reserves based on CRVM with UMV, or CRVM with UAMV if the conditions for that method are satisfied.

   - If at any point in time during the quarter the difference between the two changes exceeds 35% of the beginning of period market value of target of the option replication strategy, the insurer is deemed to be out of compliance with the "Hedged as Required" criteria, and the company must notify the Commissioner in each state in which the insurer is licensed. The notification must indicate the dollar amount of reserves being hedged by the option replication strategy and the impact on surplus of reporting the reserves based on the CRVM with UMV, or CRVM with UAVM if the conditions for that method are satisfied.

The requirements discussed above deal with the situation in which the actual hedge underperforms relative to the expected hedge performance. The ability of an insurer to over-hedge may be constrained by other components of a state's regulatory framework including the state's investment article and regulations concerning the use of derivative instruments. For purposes of this Guideline, over-hedged mean that at a particular point in time, the hedge portfolio exceeds the portfolio of liabilities being hedged. If over-hedged, the excess hedging instruments are excluded from the measurements required in Item 5 of the Hedged as Required Criteria.

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Attachment 3
Reasonableness of Assumptions Certification
for Implied Guaranteed Rate Method

The following certification must be filed in conjunction with each quarterly and annual statutory financial statement filed with the appropriate regulatory official in each state in which the insurer does business. The appointed actuary must sign the certification.

I, (state name and professional designation) am the appointed actuary for (company name). The company meets the Hedged as Required criteria for policies reserved under the Implied Guarantee Rate Method. I have reviewed the assumptions underlying the values assigned to all equity index options used in the determination of the implied guaranteed rate used in the calculation of reserves under the Implied Guaranteed Rate Method for all equity indexed universal life insurance policies issued or reinsured by (company name) and reported in the statutory financial statement as of (the date of valuation).

The assumptions at the start of the current term used to determine such option values for the current term are:

1. Reasonable in light of current relevant economic conditions at the start of the current term; and
2. Consistent with the comparable assumptions used to determine the statement of value of any derivative instruments as of the valuation date used to hedge the equity index-based obligations embedded in the equity indexed life policies subject to this certification.

The assumptions at issue used to determine equity index option values for terms subsequent to the current term are:

1. Determined in accordance with the Implied Guaranteed Rate Method
2. Based on quantitative data for the base case option (1-year European At-The-Money) of 3% plus ___._% average annualized daily actual volatility over the 60 months previous to the calendar year of issue.
3. Reasonably adjusted to reflect the following variances from the base case due to benefit design and capital market reasons (all material adjustments should be listed)
   a. skew adjustments
   b. _____(to be described by appointed actuary)
4. Reliant on the following source(s) for assumptions not prescribed by this Actuarial Guideline:
   a. _____(to be described by appointed actuary)

_____

(Name of actuary)

_____

(Signature of actuary)

_____

(Date of certification)

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Attachment 4
Reasonableness and Consistency of Assumptions Certification for Commissioners Reserve Valuation Method with Updated Average Market Value

The following certification must be filed in conjunction with each quarterly and annual statutory financial statement filed with the appropriate regulatory official in each state in which the insurer does business. The appointed actuary must sign the certification.

I, (state name and professional designation) am the appointed actuary for (company name). I have reviewed the assumptions underlying the values assigned to all equity index options used in the determination of statutory reserves using a Type 2a computational method for all equity indexed universal life insurance policies issued or reinsured by (company name) insurance company and reported in the statutory financial statement as of (the date of valuation).

The assumptions used to determine such option values for the current term are:

1. Reasonable in light of current relevant economic conditions as of the date of valuation; and
2. Consistent with the comparable assumptions used to determine the statement of value of any derivative instruments as of the valuation date used to hedge the equity index-based obligations embedded in the equity indexed life policies subject to this certification.

The assumptions used to determine equity index option values for terms subsequent to the current term are:

1. Determined in accordance with the Commissioners Reserve Valuation Method with Updated Average Market Value
2. Based on quantitative data for the base case option (1-year European At-The-Money) of 3% plus ___._% 60 -month moving average annualized daily actual volatility
3. Reasonably adjusted to reflect the following variances from the base case due to benefit design and capital market reasons (all material adjustments should be listed)
   a. skew adjustments
   b. _____(to be described by appointed actuary)
4. Reliant on the following source(s) for assumptions not prescribed by this Actuarial Guideline:
   a. _____(to be described by appointed actuary)

_____

(Name of actuary)

_____

(Signature of actuary)

_____

(Date of certification)

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Attachment 5
Reasonableness and Consistency of Assumptions Certification for Commissioners Reserve Valuation Method with Updated Market Value

The following certification must be filed in conjunction with each quarterly and annual statutory financial statement filed with the appropriate regulatory official in each state in which the insurer does business. The appointed actuary must sign the certification.

I, (state name and professional designation) am the appointed actuary for (company name). I have reviewed the assumptions underlying the values assigned to all equity index options used in the determination of statutory reserves using a Type 2 computational method for all equity indexed universal life insurance policies issued or reinsured by (company name) insurance company and reported in the statutory financial statement as of (the date of valuation). The assumptions used to determine such option values are:

1. Reasonable in light of current relevant economic conditions as of the date of valuation; and
2. Consistent with the comparable assumptions used to determine the statement of value of any derivative instruments as of the valuation date used to hedge the equity index-based obligations embedded in the equity indexed life policies subject to this certification.

_____

(Name of actuary)

_____

(Signature of actuary)

_____

(Date of certification)

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Actuarial Guideline XXXVII

VARIABLE LIFE INSURANCE RESERVES FOR GUARANTEED MINIMUM DEATH BENEFITS

Background

This guideline's primary focus is to clarify the appropriate projection assumptions and methodologies used to determine statutory reserve liabilities for Guaranteed Minimum Death Benefits (GMDBs) offered with variable life insurance products.

For many years, insurance companies have not applied uniform reserve standards to variable life insurance policies in general, and to GMDBs in particular. Four regulatory sources are often looked to for guidance. First, the Standard Valuation Law (SVL) requires that CRVM be based on the present value of future guaranteed benefits. Second, the Variable Life Insurance Model Regulation as revised in 1983 and again in 1989 states "Reserve liabilities for variable life insurance policies shall be established under [SVL] in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees." Third is the Universal Life Insurance Model Regulation and most recently the Valuation of Life Insurance Policies Model Regulation.

GMDBs are common features of variable life products. Recently, reserve methods for universal life secondary guarantees have been clarified in the Valuation of Life Insurance Policies Model Regulation. These secondary guarantees are similar to GMDBs offered with variable life policies. A Guaranteed Minimum Death Benefit is any guarantee which provides death benefit protection which would not otherwise be provided in the absence of such a guaranteed benefit or provision. An example of a GMDB is a policy in which death benefits continue in-force even if the policy value is zero. This benefit may be contingent on additional qualifications being met, such as cumulative premiums meeting some limit.

Additional examples of GMDBs are provided below. This list is not intended to include all types of GMDBs.

- A Minimum Death Benefit Provision or No Lapse provision where death benefits are guaranteed to remain in-force for a period of time even if the policy value is not greater than zero subject only to certain conditions being met such as cumulative premiums meeting a minimum amount, or if a theoretical policy value is sufficient to meet a minimum amount.

- Death Benefits that are guaranteed to be at least as large as the original face amount, regardless of investment performance which might generate negative Paid Up Additions on a traditional fixed premium variable life insurance policy.

The Variable Life Insurance Model Regulation defines the reserve methodology for variable life policies. However, currently two versions of the model regulation exist and this results in inconsistent treatment by state. These two versions include the 1983 revisions and the 1989 revisions to the model regulation. Many states have not passed either revision and therefore require direct interpretation of SVL. In practice, companies have interpreted these regulations inconsistently with regard to assumptions and/or application to current products available today. The 1983 version of the regulation treats flexible premium policies differently than scheduled premium policies. The 1983 version of the regulation did not anticipate the types of GMDBs available today which require contingent conditions to be met to maintain a death benefit guarantee, for instance specified premiums must be paid. Thus, confusion exists with regard to which valuation method is appropriate. The 1989 version makes no distinction between the scheduled premium and flexible premium policies.

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This Guideline codifies the basic interpretation of reserve liabilities for variable life GMDBs by clarifying the projection assumptions and methodologies that comply with the SVL. Minimum valuation standards that may be used to determine this reserve and are not specifically addressed in this guideline are defined by SVL and other applicable state regulations. This guideline focuses on the methodology of the 1989 revisions to interpret SVL, as we believe the 1989 revision more appropriately considers the types of products and GMDBs available today.

Interpretations of both the 1983 and 1989 versions reflect the comments made in the December 1972 report which concluded that an acceptable GMDB reserve system should have the following characteristics:

1. The GMDB reserve should be held in the general account of the company so that it will be backed by the general assets of the company, most of which are debt obligations valued at amortized cost and, therefore, are of a fixed dollar nature. It would not be proper to hold the GMDB reserve in the separate account, assuming the reserve is not supported by fixed dollar assets but by assets that are moving in the opposite direction from the risk, i.e. value moving downward while the risk increases and vice versa.

2. The GMDB reserve should be adequate to cover the GMDB death claims for the next year in all but the most extreme circumstances so that the regulatory authorities can be assured the company will not run into financial trouble from this source before the next annual statement is filed.

3. The GMDB reserve should react slowly but steadily through an extended period of poor investment experience of the separate account.

4. The GMDB reserve should not cause unnecessary fluctuations in surplus by increasing too rapidly in a sharp market downswing. Also, the reserve should not decrease too rapidly in a sharp market upswing after a period of poor market performance.

This guideline maintains the four principles above in interpreting the Standard Valuation Law as it relates to variable life business and the methods defined in both the 1983 and 1989 versions of the Variable Life Insurance Model Regulation.

Reserve methodologies which recognize the variable nature of GMDB are defined in the Variable Life Insurance Model Regulation and include a One-Year Term reserve recognizing a 1/3 drop in separate account assets, the Attained Age Level Reserve (AALR) methodology and in the 1983 version, a methodology for flexible premium policies. Reserves for GMDBs are held in the general account.

This guideline recognizes the following principles when determining appropriate reserves for GMDB.

- Determine the guaranteed death benefits which are not valued in the basic policy reserves.

- Establish a reserve for these benefits over the period of time in which revenue is collected to pay for such benefits; however, no greater than the period of time these guaranteed benefits are provided.

- Collected revenue should not be de-minimus in order to reduce the reserve.

- The reserve established is in addition to basic reserves

This guideline interprets the standards for applying these methodologies. This guideline also interprets the projection assumptions to be applied to determine excess guaranteed death benefits. The guideline clarifies the use of the AALR methodology for flexible premium variable life policies with contingent

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GMDB benefit structures similar to specified premium contracts. This guideline is based on the belief that the 1983 revisions did not anticipate these types of GMDB benefits on flexible premium contracts. Thus, it makes sense to interpret the 1983 revisions for these types of GMDB benefits by applying the AALR methodology when there is a contingent GMDB structure. For flexible premium plans with other types of GMDBs, the flexible premium language of the 1983 revision is used where applicable.

The AALR methodology, along with the one-year term reserve is generally consistent with the principles above in that additional reserves are established in recognition of all death benefit guarantees not reflected in basic reserves. If multiple guarantees exist all guarantees must be valued and the greatest additional reserve is held. Consecutive GMDBs are treated as a single guarantee. These reserves are funded over the period of time GMDB Revenue will be collected through either policy charges or premiums, however, not to exceed the GMDB benefit period. The AALR methodology funds any GMDB Revenue deficiency over the period of time the Revenue is collected, however, no longer than the end of the guarantee period.

GMDB reserves are held in addition to basic reserves unless the appointed actuary provides satisfactory documentation to the state of domicile insurance department stating why such reserves are redundant. For example, for traditional variable life product designs where reserves are generally determined on a tabular basis and use an assumed interest rate (AIR), if basic reserves are determined based on at least the guaranteed face amount, (i.e. ignoring any negative additions) then the guaranteed death benefit is fully reflected in the basic reserves; therefore, an additional GMDB reserve is redundant. Neither this guideline nor the 1989 amendments specifically address traditional variable life product designs, nor does this guideline specifically exclude these designs from its scope.

An additional purpose of this guideline is to emphasize the impact of Sections 3A(3) and 3A(4) in the Valuation of Life Insurance Policies Model Regulation (“XXX”) relative to reserving for variable life and variable universal life products.

Scope

The guideline applies to all variable life insurance contracts to which the Standard Valuation Law applies and which provide Guaranteed Minimum Death Benefits (GMDBs) either explicitly or implicitly.

Definitions

Attained age level reserve (AALR): The AALR is a methodology described in the 1983 and 1989 revisions to the Variable Life Insurance Model Regulation.

Catch-up provision: A Catch-up provision is a provision in the policy that gives the policyholder the right to catch up on any contingent requirements in order to maintain the GMDB.

Guaranteed Period: The guaranteed period is the period of time over which a GMDB is guaranteed regardless of the basic guarantees in the policy. A policy may have multiple guaranteed periods and GMDBs.

Guaranteed Minimum Death Benefit (GMDB): A Guaranteed Minimum Death Benefit (GMDB) is any guarantee which provides continued death benefit protection which would not otherwise be provided in the absence of such a guaranteed benefit or provision. A policy may have multiple GMDBs.

One-Year Term (OYT) reserve: The OYT reserve covers a period of no more than one year following a 1/3-asset drop. This reserve is fully described in the 1989 revision to the Variable Life Insurance Model Regulation. This guideline clarifies the methodology and the assumptions used to determine OYT reserves.

Policy Value: Policy value means, as of the valuation date, the greater of (a) zero and (b) the amount to which separately identified interest credits and/or investment return and mortality, expense, or other

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charges are made under a variable life insurance policy. Subsequent to the valuation date, "policy value" means the amount determined in accordance with the procedures specified in this guideline.

Projection Assumptions: The Projection Assumptions are used to determine guaranteed death benefits. This projection of policy values uses the following assumptions:

1. Cost of insurance rates are equal to the minimum valuation mortality.

2. The GMDB is assumed to be in effect for the maximum period of the GMDB. All minimum requirements necessary to maintain the GMDB in force subsequent to the valuation date are assumed to be met at the latest point in time sufficient to maintain the GMDB through its maximum period. Contingent requirements, if any, required to reinstate or catch-up as of the valuation date are assumed to occur on the valuation date. If the GMDB would continue in effect subsequent to the valuation date with no additional actions required, contingent requirements are assumed not to resume until the latest point in time which would prevent the termination of the GMDB.

3. The general account policy values and separate account policy values are projected at the valuation interest rate. The assumed investment rate, if any, is used when determining the OYT reserve.

4. The guaranteed period covered is determined assuming all contingent requirements are met.

5. Policy options and benefits are assumed to continue unchanged as of the valuation date. Examples include fixed and variable account allocation and the death benefit option.

6. The projection of policy values is made for the entire guarantee period, regardless of whether projected policy values are positive or negative at any point in the projection. Any negative policy value would be set to zero.

The policy value is projected forward from the valuation date with valuation interest rate credits, any payments required to maintain the guarantee and valuation mortality charges (and no other credits or charges). The Guideline stipulates that "A death benefit in the absence of the guarantee is assumed to be provided as long as the projected policy value is greater than zero," and "Any negative policy value would be set to zero." An AALR need not be established for a VUL policy to provide for any period during which there would be a death benefit in the absence of the guarantee, since this benefit would be provided for by the policy's basic reserve. This means that for an AALR to develop, the mortality charges must exceed the required payments plus interest credits by enough to reduce the policy value to zero during the guarantee period. Surrender charges are not relevant to this determination.

GMDB Revenue: GMDB Revenue is policy charges or premium, either implicit or explicit. These charges or premiums may or may not be explicitly stated to cover GMDB benefits. An example of an implicit premium is a positive premium necessary to maintain a target policy value in order to maintain benefits.

Term cost: Term costs are based on the guaranteed minimum death benefits in excess of the death benefits that would be provided in absence of such guarantee based on a projection of policy values using the Projection Assumptions defined above. These costs are then discounted to the valuation date. The term costs are based on minimum valuation mortality standards and a discount rate not to exceed the maximum valuation interest rate.

1/3-Asset Drop: A 1/3 reduction in separate account assets that is used in the calculation of the one-year term reserve. This 1/3 drop is not applied to fixed account assets.

Text

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1. Basic Reserves:

Basic Reserves include the reserve held for death benefits provided in the absence of a GMDB. Reserve liabilities for variable life insurance policies shall be established consistent with the methodologies described in the Standard Valuation Law and in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees. Reserve methods described in the Variable Life Insurance Model Regulation and the Universal Life Insurance Model Regulation may be appropriately utilized to determine reserve liabilities such that application of these methods is consistent with the principles of the Standard Valuation Law.

2. Guaranteed Minimum Death Benefit Reserves:

Additional reserves are required to provide for liabilities of GMDB provisions which provide benefits that would not be provided in the absence of the guarantee. In measuring these liabilities, the basic reserve provides for death benefits which occur in the absence of the guarantee. GMDB reserves provide for the contingency of death occurring when the guaranteed minimum death benefit exceeds the death benefit that would be paid in absence of the guarantee. A consistent reserve methodology should be used regardless of whether a contract has scheduled premiums or flexible premiums.

When a contract provides multiple GMDBs and/or multiple guarantee periods, a reserve is established based on the guaranteed period which produces the greatest reserve as of the valuation date. Consecutive GMDBs are treated as a single guarantee period. The reserve methodology reflects all potential guarantee periods assuming that contingent requirements are met such as: contingent premiums paid, Catch-up Provisions or any pre-funding of contingent requirements.

For a policy under the 1989 revisions or a flexible premium policy with contingent GMDBs similar to a specified premium contract under the 1983 revision, the GMDB reserve equals the greater of (1) and (2) where (1) equals "the aggregate total of term costs" (OYT) which covers a period of no more than one year following a 1/3-asset drop, and (2) equals the AALR as described below.

For a flexible premium policy under the 1983 revisions not covered above, (where the GMDB guarantee is not contingent on any policyholder requirement), reserve liabilities for any guaranteed minimum death benefit shall be maintained in the general account of the insurer and shall be not less than the aggregate total of the term costs, if any, covering the period provided for in the guarantee not otherwise provided for by the reserves held in the separate account assuming a 1/3-asset drop, projected at the valuation interest rate.

a) One Year Term Reserves (OYT):

This reserve component equals the "aggregate total of term costs", if any, covering a period of one full year from the valuation date, or, if less, covering the period of time death benefits are provided which are not otherwise provided for by the basic reserves. This reserve assumes any contingent requirements to maintain the GMDB are met by reflecting any Catch-up Provisions or any pre-funding of contingent requirements.

"Aggregate total term costs" equals the present value of guaranteed minimum death benefits in excess of death benefits that would be provided in absence of such guarantee, if any, prior to the end of one full year or the end of the guaranteed period if sooner. A death benefit in the absence of the guarantee is assumed to be provided as long as the projected policy value is greater than zero. Death benefits are determined by projecting the policy value following a 1/3-asset drop and using the Projection Assumptions defined above. Present values are determined using valuation mortality rates and the maximum valuation interest rate.

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b) Attained Age Level Reserves (AALR):

This reserve component allows for funding GMDBs over no longer than the guaranteed period. This reserve assumes contingent requirements are met to maintain the GMDB and reflect any prepaid contingent requirements or Catch-up provisions. A death benefit in the absence of the guarantee is assumed to be provided as long as the projected policy value is greater than zero. This reserve component exists until no later than the end of the guarantee period if, on any prior valuation date, projected policy values resulted in guaranteed minimum death benefits in excess of death benefits that would be provided in absence of such guarantee. To the extent long term favorable investment performance results in redundant reserves, the valuation actuary may request permission from the state of domicile insurance department to release all or a portion of the redundant GMDB reserves. This projection of policy value is based on the Projection Assumptions defined above and does not incorporate a 1/3-asset drop.

The AALR reserve component shall not be less than zero and shall equal the "residue," as described in paragraph (1) below, of the prior year's AALR on the contract, with any such "residue," increased or decreased by a "payment" computed on an attained age basis as described in paragraph (2) below.

(1) The "residue" of the prior year's AALR on each variable life insurance contract shall not be less than zero and shall be determined by adding interest at the maximum valuation interest rate to such prior year's reserve, deducting the tabular claims based on the "excess", if any, of the guaranteed minimum death benefit over the death benefit that would be payable in absence of such guarantee, and dividing the result by the tabular probability of survival. Hence, tabular costs are only deducted for years where, in the absence of the guarantee, coverage would be less than the guaranteed coverage.

(2) The "payment" used to increase or decrease the "residue" above shall be computed so that the present value of a level payment of that amount each year over the future period for which GMDB Revenue will be collected under the contract is equal to (A) minus (B) minus (C), where, (A) is the present value of future guaranteed minimum death benefits. The future guaranteed minimum death benefits are the projected future death benefits including the GMDB. (B) is the present value of the projected future death benefits that would be payable in the absence of the GMDB. The guaranteed benefit for (A) and (B) should be calculated for the life of the policy. Both (A) and (B) are calculated based on the Projection Assumptions. (C) is any "residue," as described in paragraph (1) above, of the prior year's AALR on such variable contract. Minimum standards of valuation mortality assumptions and maximum valuation interest rates are used to determine present values and net level payments. The period of time in which GMDB Revenue will be collected is limited to the period of time policy values are sufficient to collect policy charges or the period of time contingent requirements will be paid to maintain the GMDB. In no event will the time period be greater than the time to the end of the guarantee period. It should also be noted that the "payment" may be negative resulting in the reserve running off over the remaining guarantee period.

c) Other Flexible Premium Policies under the 1983 revisions not included above:

The present value of potential guaranteed minimum death benefits in excess of death benefits that would be provided in absence of such guarantee is determined by using

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minimum standards of valuation mortality assumptions and maximum valuation interest rates.

3. Issues:

Sections 3A(3) and 3A(4) of "XXX" state the following:

3A(3): This regulation shall not apply to any variable life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts.

3A(4): This regulation shall not apply to any variable universal life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts.

The language of these sections is clear. The reserving for variable life and variable universal life is in no way affected by the provisions of "XXX." In particular, the 19-year select factors and the "X" factor are not applicable to the calculation of reserves for variable life and variable universal life products.

Effective Date

This guideline affects all variable life insurance contracts issued. Where the application of this Guideline produces higher reserves than the company had otherwise established by their previously used interpretation, such company must comply with this guideline effective December 31, 2001. However, such company may request a grade in period, not to exceed three (3) years, from the domiciliary Commissioner upon satisfactory demonstration of the previous interpretation and that such delay of implementation will not cause a hazardous financial condition or potential harm to its policyholders.

Retroactive application of the guideline to in-force policies to develop the current residue portion of the AALR will generally not be feasible. Therefore, the residue as of 12/31/2000 should be set equal to the greater of the amount established by the company under its current method or $0 if the company did not previously calculate an AALR.

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Actuarial Guideline XXXVIII

THE APPLICATION OF THE VALUATION OF LIFE INSURANCE POLICIES MODEL REGULATION

Introduction

The revised version of the *Valuation of Life Insurance Policies Model Regulation* (Model #830) was adopted by the NAIC in March 1999. Since that date, some questions have been raised regarding whether and how Model #830 applies to various product designs. The purpose of this guideline is to provide direction as to the application of Model #830 to such products. Specifically, this guideline provides examples of various policy features that constitute "guarantees" and gives directions on how to reserve for these guarantees in accordance with Model #830.

Obviously, new policy designs will emerge subsequent to the development of this document. No statute, regulation, or guideline can anticipate every future product design, and common sense and professional responsibility are needed to assure compliance with both the letter and the spirit of the law. While Model #830 is a complex regulation, its intent is clear: reserves need to be established for the guarantees provided by a policy. Policy designs which are created to simply disguise those guarantees or exploit a perceived loophole must be reserved in a manner similar to more typical designs with similar guarantees.

Text

The following product designs have been brought to the attention of the NAIC Life Actuarial (A) Task Force. The list below specifies reserving approaches which the Task Force regards as being most consistent with the letter and spirit of Model #830. However, the specified reserving approaches should be modified as needed to comply with the intent of this guideline that similar reserves be established for policy designs that contain similar guarantees.

1. An initial level premium rate is guaranteed for 10 years followed by increased guaranteed premiums for an additional 20 years. However, the company cannot increase premiums after year 10 (i.e., the initial premium continues to be charged) unless some specified event occurs.

   The initial reserve segment is 30 years. Since the contract contains provisions that limit the company's ability to increase premiums, then the initial premium should be treated as guaranteed for the entire 30-year period. It would be contrary to the conservative nature of statutory accounting to treat this policy the same as one in which the ability to raise premiums is unrestricted.

2. A term policy has an illustrated level premium for 30 years, the first 10 of which are guaranteed. Additionally, there is a refund option which provides that a specified refund will be paid if the premium ever increases. The refund must be requested within a limited time (e.g., 30 days) of receiving notice of the increase. Coverage terminates if the option is exercised.

   This example differs from the one above in that there is no specified event that has to occur in order for the company to impose a premium increase; however, the company must provide an additional benefit to the policyholder if it exercises this right. Thus the company does not have an unrestricted right to impose an increase after 10 years. If the contract contains provisions that require that additional benefits be provided to the policyholder in the event of a premium increase, even if these benefits are lost if not claimed within a stated time frame, then the initial premiums should be treated as guaranteed for the entire 30 year period. It would be contrary to the conservative nature of statutory accounting to treat this policy the same as one in which the

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ability to raise premiums does not require that additional benefits be provided. Therefore, the initial segment for this policy is 30 years.

3. An initial level premium rate is guaranteed for 10 years followed by increased guaranteed premiums for an additional 20 years. However, after year 10 the policyholder is protected against premiums being increased above the initial level, with the protection provided by a second company through either reinsurance, a second policy issued to the consumer, or an agreement between the companies.

   The combined reserves of the direct writer and the second company should be no less than the amount which the direct writer would hold if (a) there were no second company and (b) the initial reserve segment were 30 years. If this condition is not met, reserve credits for the direct writer should be disallowed. The reserve held by the direct writer should be based on the initial level premium being guaranteed for 30 years.

4. A product has relatively high gross premiums but with a guaranteed dividend or guaranteed refund schedule, or by some other means guarantees a low net cost to the policyholder.

   The net amount of premium (i.e., gross premium less dividends or refunds) should be used in the reserve calculation. That represents the amount the insured actually pays for coverage.

   For products reinsured on either a coinsurance or modified coinsurance basis, the reinsurer's reserve calculation should also be based on the net premium (i.e., gross premiums less dividends or refunds guaranteed to be paid to the policyholder).

5. a) A re-entry term product has an initial rate guarantee for 10 years, with loose or non-existent re-entry underwriting, allowing the policyholder to re-enter for an additional 20 years at specified favorable rates.

   b) A universal life policy has provisions such that, if the UL policy lapses prior to the 10th policy anniversary because the actual accumulation value (or cash value, depending on design) falls below zero but stipulated premiums have been paid, a substitute policy is guaranteed to be issued providing the same amount of insurance coverage at the same stipulated premium for the remainder of the 10-year period plus an additional 20 years.

   The reentry periods and premiums should be treated as a continuation of the initial guarantees for reserve calculation purposes. The initial reserve segment applicable to the original policy should be 30 years if the stipulated premium for the substitute policy is not high enough to trigger a new reserve segment. When the substitute policy is issued, reserves should be determined as if the coverage had been issued at the issue age and issue date of the original policy. Effectively, the company has guaranteed coverage for 30 years at the time the initial policy is issued, and the reserves established should reflect that guarantee.

6. A reinsurance treaty provides for 30 years of level premiums on a current scale but directly guarantees those premiums for only the first 10 years. However, if the reinsurer increases the premiums after 10 years, the reinsurer agrees to increase the expense allowance such that the net payments (premium minus allowance) by the direct writer remains unchanged.

   Relative to the reinsurer's reserve calculation, the initial reserve segment should be 30 years and the valuation premium should be level over that period. In this instance, the additional "expense allowance" has no relationship to the expenses actually incurred by the direct writer in administering the reinsured policies. Although a bona fide expense allowance would typically not be considered in determining the valuation premiums and reserve segments, in this instance the

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additional "expense allowance" has no relationship to the expenses actually incurred by the direct writer in administering the reinsured policies.

7. A universal life policy has a cumulative "premium catch-up provision" in which the coverage is guaranteed to remain in force as long as a stipulated premium is paid each year, and if the insured is paying less than is required to maintain the guarantee, there is an unlimited right to make up past premium deficiencies.

Model #830 requires that "when a policy contains more than one secondary guarantee, the minimum reserve shall be the greatest of the respective minimum reserves at that valuation date of each unexpired secondary guarantee, ignoring all other secondary guarantees." Since secondary guarantees with "catch-up" provisions are capable of being reinstated up to the end of the secondary guarantee period, they constitute "unexpired secondary guarantees" which must be incorporated into the calculation of "the greatest of the respective minimum reserves at that valuation date of each unexpired secondary guarantee, ignoring all other secondary guarantees."

The basic and deficiency reserves for a secondary guarantee with a catch-up provision should be computed as if the stipulated premium requirement had been met. The basic reserve shall be reduced by the product of (a) the "catch-up amount," if any, which would be required on the valuation date and (b) the ratio of the "initial" (i.e., before adjustment) basic reserve to the sum of the "initial" basic and deficiency reserves. In no event shall the "reduced" basic reserve be reduced below zero. The deficiency reserve shall be reduced by the product of (a) the "catch-up amount," if any, which would be required on the valuation date and (b) the ratio of the "initial" deficiency reserve to the sum of the "initial" basic and deficiency reserves. In no event shall the "reduced" deficiency reserve be reduced below zero.

If a universal life policy with a "premium catch up provision" has a shadow account below the level necessary to maintain the secondary guarantee, then the reserve for the secondary guarantee shall be valued according to this example. The basic and deficiency reserves, before deduction for the catch-up amount, shall be calculated as specified in Section 8A, Section 8B, Section 8C or Section 8E, as applicable.

8A. For policies and certificates issued prior to July 1, 2005: A universal life policy guarantees the coverage to remain in force as long as the accumulation of premiums paid satisfies the secondary guarantee requirement.

First, the minimum gross premiums (determined at issue) that will satisfy the secondary guarantee requirement must be derived.

Second, for purposes of applying Sections 7B and 7C of Model #830, the "specified premiums" are the minimum gross premiums derived in "Step One."

Third, a determination should be made of the amount of actual premium payments in excess of the minimum gross premiums. For policies utilizing shadow accounts, this will be the amount of the shadow account. For policies with no shadow accounts but which specify cumulative premium requirements, this excess will be the amount of the cumulative premiums paid in excess of the cumulative premium requirements; the cumulative premium payments and requirements should include any interest credited under the secondary guarantee (with interest credited at the rate specified under the secondary guarantee).

Fourth, a determination should be made of the single payment necessary at the valuation date to fully fund the remaining secondary guarantee assuming that the minimum gross premiums have been paid, up through the valuation date, during the secondary guarantee period. The result from "Step Three" should be divided by this number.

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Fifth, compute the net single premium on the valuation date for the coverage provided by the secondary guarantee for the remainder of the secondary guarantee period, using any valuation table and select factors authorized in Section 5A of Model #830.

Sixth, the "net amount of additional premiums" is determined by multiplying the ratio from "Step Four" by the difference between the net single premium from "Step Five" and the basic and deficiency reserve, if any, computed in "Step Two."

Seventh, a "reduced deficiency reserve" should be computed by multiplying the deficiency reserve, if any, by the one minus the ratio from "Step Four," but not less than zero. This "reduced deficiency reserve" is the deficiency reserve to be used for purposes of Section 7D(1) of Model #830.

Eighth, the actual reserve used for purposes of Section 7D(1) of Model #830 is the lesser of: (1) the net single premium from "Step Five," and (2) the amount of the excess from "Step Six" plus the basic reserve and the deficiency reserve, if any, computed in "Step Two." Reduce this result by the applicable policy surrender charges, i.e., the account value less the cash surrender value. If the resulting amount is less than the sum of the basic and deficiency reserve from Step Two, then the basic and deficiency reserves to be used for the purposes of Section 7D(1) are those calculated in Step Two, and no further calculation is required.

Ninth, an "increased basic reserve" should be computed by subtracting the "reduced deficiency reserve" in "Step Seven" from the reserve computed in "Step Eight." This "increased basic reserve" is the basic reserve to be used for purposes of Section 7D(1) of Model #830.

8B. For policies and certificates issued on or after July 1, 2005 and on or prior to December 31, 2006: A universal life policy guarantees the coverage to remain in force as long as the accumulation of premiums paid satisfies the secondary guarantee requirement.

First, the minimum gross premiums (determined at issue) that will satisfy the secondary guarantee requirement must be derived.

Second, for purposes of applying Sections 7B and 7C of Model #830, the "specified premiums" are the minimum gross premiums derived in "Step One." Consistent with Model #830, the remaining steps in this guideline should be calculated on a segmented basis, using the segments that Model #830 defines for the product. Therefore, in the remaining steps, the term "fully fund the guarantee" should be interpreted to mean fully funding the guarantee to the end of each possible segment. The term "remainder of the secondary guarantee period" should be interpreted to mean the remainder of each possible segment. The total reserve should equal the greatest of all possible segmented reserves.

Third, a determination should be made of the amount of actual premium payments in excess of the minimum gross premiums. For policies utilizing shadow accounts, this will be the amount of the shadow account. For policies with no shadow accounts but which specify cumulative premium requirements, this excess will be the amount of the cumulative premiums paid in excess of the cumulative premium requirements; the cumulative premium payments and requirements should include any interest credited under the secondary guarantee (with interest credited at the rate specified under the secondary guarantee).

Fourth, as of the valuation date for the policy being valued, for policies utilizing shadow accounts, determine the minimum amount of shadow account required to fully fund the guarantee. For policies with no shadow accounts but which specify cumulative premium requirements, determine the amount of the cumulative premiums paid in excess of the cumulative

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premium requirements that would result in no future premium requirements to fully fund the guarantee; the cumulative premium payments and requirements should include any interest credited under the secondary guarantee (with interest credited at the rate specified under the secondary guarantee). For any policy for which the secondary guarantee can not be fully funded in advance, solve for the minimum sum of any possible excess funding (either the amount in the shadow account or excess cumulative premium payments depending on the product design) and the present value of future premiums (using the maximum allowable valuation interest rate and the minimum mortality standards allowable for calculating basic reserves) that would fully fund the guarantee. The amount determined above for this step is to then be divided by one minus a 7% premium load allowance (0.93). The result from "Step Three" should be divided by this number, with the resulting ratio capped at 1. The ratio is intended to measure the level of prefunding for a secondary guarantee which is used to establish reserves. Assumptions within the numerator and denominator of the ratio therefore must be consistent in order to appropriately reflect the level of prefunding. The denominator is allowed to be inconsistent only by the amount of the premium load allowance as defined in this step. As used here, "assumptions" include any factor or value, whether assumed or known, which is used to calculate the numerator or denominator of the ratio.

[DRAFTING NOTE: The 7% premium load allowance approximates an average premium load level as evidenced by policies currently sold in the market. Rather than have the funding ratio vary according to the actual policy loads (which can fluctuate greatly by company and product), all companies will use an identical premium load allowance at a level approximately equal to the current industry average.]

Fifth, compute the net single premium on the valuation date for the coverage provided by the secondary guarantee for the remainder of the secondary guarantee period, using any valuation table and select factors authorized in Section 5A of Model #830.

Sixth, the "net amount of additional premiums" is determined by multiplying the ratio from "Step Four" by the difference between the net single premium from "Step Five" and the basic and deficiency reserve, if any, computed in "Step Two."

Seventh, a "reduced deficiency reserve" should be computed by multiplying the deficiency reserve, if any, by the one minus the ratio from "Step Four," but not less than zero. This "reduced deficiency reserve" is the deficiency reserve to be used for purposes of Section 7D(1) of Model #830.

Eighth, the actual reserve used for purposes of Section 7D(1) of Model #830 is the lesser of: (1) the net single premium from "Step Five," and (2) the amount of the excess from "Step Six" plus the basic reserve and the deficiency reserve, if any, computed in "Step Two." Reduce this result by the applicable policy surrender charges, i.e., the account value less the cash surrender value. Multiply this surrender charge by the ratio of the net level premium for the secondary guarantee period divided by the net level premium for whole life insurance. Calculate both net premiums using the maximum allowable valuation interest rate and the minimum mortality standards allowable for calculating basic reserves. However, if no future premiums are required to support the guarantee period being valued, there is no reduction for surrender charges. If the resulting amount is less than the sum of the basic and deficiency reserve from Step Two, then the basic and deficiency reserves to be used for the purposes of Section 7D(1) of Model #830 are those calculated in Step Two, and no further calculation is required.

Ninth, an "increased basic reserve" should be computed by subtracting the "reduced deficiency reserve" in "Step Seven" from the reserve computed in "Step Eight." This "increased basic reserve" is the basic reserve to be used for purposes of Section 7D(1) of Model #830.

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8C. For all policies and certificates issued on or after January 1, 2007 and on or prior to December 31, 2012: A universal life policy guarantees the coverage to remain in force as long as the accumulation of premiums paid satisfies the secondary guarantee requirement.

First, the minimum gross premiums (determined at issue) that will satisfy the secondary guarantee requirement must be derived.

Second, for purposes of applying Sections 7B and 7C of Model #830, the "specified premiums" are the minimum gross premiums derived in "Step One." Consistent with Model #830, the remaining steps in this guideline should be calculated on a segmented basis, using the segments that Model #830 defines for the product. Therefore, in the remaining steps, the term "fully fund the guarantee" should be interpreted to mean fully funding the guarantee to the end of each possible segment. The term "remainder of the secondary guarantee period" should be interpreted to mean the remainder of each possible segment. The total reserve should equal the greatest of all possible segmented reserves. Additionally, for purposes of applying Sections 7B and 7C of Model #830, a lapse rate of no more than 2% per year for the first 5 years, followed by no more than 1% per year to the policy anniversary specified in the following table based on issue age, and 0% per year thereafter may be used. If the duration in the table is less than 5, then a lapse rate of no more than 2% per year may be used through that duration, and 0% per year thereafter.

Issue Age	Duration
0-50	30th policy anniversary
51-60	Policy anniversary age 80
61-70	20th policy anniversary
71-89	Policy anniversary age 90
90 and over	No lapse

Third, a determination should be made of the amount of actual premium payments in excess of the minimum gross premiums. For policies utilizing shadow accounts, this will be the amount of the shadow account. For policies with no shadow accounts but which specify cumulative premium requirements, this excess will be the amount of the cumulative premiums paid in excess of the cumulative premium requirements; the cumulative premium payments and requirements should include any interest credited under the secondary guarantee (with interest credited at the rate specified under the secondary guarantee).

Fourth, as of the valuation date for the policy being valued, for policies utilizing shadow accounts, determine the minimum amount of shadow account required to fully fund the guarantee. For policies with no shadow accounts but which specify cumulative premium requirements, determine the amount of the cumulative premiums paid in excess of the cumulative premium requirements that would result in no future premium requirements to fully fund the guarantee; the cumulative premium payments and requirements should include any interest credited under the secondary guarantee (with interest credited at the rate specified under the secondary guarantee). For any policy for which the secondary guarantee can not be fully funded in advance, solve for the minimum sum of any possible excess funding (either the amount in the shadow account or excess cumulative premium payments depending on the product design) and the present value of future premiums (using the maximum allowable valuation interest rate and the minimum mortality standards allowable for calculating basic reserves) that would fully fund the guarantee. The amount determined above for this step is to then be divided by one minus a 7% premium load allowance (0.93). The result from "Step Three" should be divided by this number, with the resulting ratio capped at 1. The ratio is intended to measure the level of prefunding for a secondary guarantee which is used to establish reserves. Assumptions within the numerator and denominator of the ratio therefore must be consistent in order to appropriately reflect the level of prefunding. The denominator is allowed to be inconsistent only by the amount

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of the premium load allowance as defined in this step. As used here, "assumptions" include any factor or value, whether assumed or known, which is used to calculate the numerator or denominator of the ratio.

[DRAFTING NOTE: The 7% premium load allowance approximates an average premium load level as evidenced by policies currently sold in the market. Rather than have the funding ratio vary according to the actual policy loads (which can fluctuate greatly by company and product), all companies will use an identical premium load allowance at a level approximately equal to the current industry average.]

Fifth, compute the net single premium on the valuation date for the coverage provided by the secondary guarantee for the remainder of the secondary guarantee period, using any valuation table and select factors authorized in Section 5A of Model #830. For purposes of calculating the net single premium, a lapse rate subject to the same criteria as the lapse rate used in applying Step 2 of 8C above may be used.

Sixth, the "net amount of additional premiums" is determined by multiplying the ratio from "Step Four" by the difference between the net single premium from "Step Five" and the basic and deficiency reserve, if any, computed in "Step Two."

Seventh, a "reduced deficiency reserve" should be computed by multiplying the deficiency reserve, if any, by the one minus the ratio from "Step Four," but not less than zero. This "reduced deficiency reserve" is the deficiency reserve to be used for purposes of Section 7D(1) of Model #830.

Eighth, the actual reserve used for purposes of Section 7D(1) of Model #830 is the lesser of: (1) the net single premium from "Step Five," and (2) the amount of the excess from "Step Six" plus the basic reserve and the deficiency reserve, if any, computed in "Step Two." Reduce this result by the applicable policy surrender charges, i.e., the account value less the cash surrender value. Multiply this surrender charge by the ratio of the net level premium for the secondary guarantee period divided by the net level premium for whole life insurance. Calculate both net premiums using the maximum allowable valuation interest rate and the minimum mortality standards allowable for calculating basic reserves. If the resulting amount is less than the sum of the basic and deficiency reserve from Step Two, then the basic and deficiency reserves to be used for the purposes of Section 7D(1) of Model #830 are those calculated in Step Two, and no further calculation is required.

Ninth, an "increased basic reserve" should be computed by subtracting the "reduced deficiency reserve" in "Step Seven" from the reserve computed in "Step Eight." This "increased basic reserve" is the basic reserve to be used for purposes of Section 7D(1) of Model #830.

Business reserved pursuant to Section 8C must be supported by an asset adequacy analysis specific to this business. This asset adequacy analysis must be performed pursuant to the requirements of Section 3 of the Standard Valuation Law. Reserves required by Section 8C shall be increased by any additional reserves required by the asset adequacy analysis.

8D. This Section 8D applies to policies and certificates (1) issued on and after July 1, 2005, (2) issued prior to January 1, 2013, and (3) in force on December 31, 2012, or on any valuation date thereafter: Under a universal life policy with a secondary guarantee, the coverage is guaranteed to remain in force as long as the accumulation of premiums paid satisfies the secondary guarantee requirement.

Notwithstanding the requirements of any of the other sections of this Actuarial Guideline (and in addition to any testing that may be required under Section 8C), this Section 8D describes the

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reserving requirements with respect to universal life with secondary guarantee products, with or without a shadow account, with multiple sets of interest rate or other credits, or multiple sets of cost of insurance, expense, or other charges that may become applicable to the calculation of the secondary guarantee measures in any one policy year. This Section 8D does not apply if the minimum gross premiums for the policies are determined by applying the set of charges and credits that produces the lowest premiums, regardless of the imposition of constraints, contingencies, or conditions that would otherwise limit the application of those credits and charges. The requirements of this Section 8D apply to a company on December 31, 2012, and on any subsequent valuation date if (1) on the applicable date, the in force face amount (direct plus assumed) of universal life insurance to which this Section 8D would otherwise apply exceeds 2% of the company's face amount of individual permanent life insurance in force, or (2) on the applicable date, the company's face amount of insurance in force subject to this Section 8D exceeds $1,000,000,000 (one billion dollars). Any company otherwise meeting these criteria may seek an exemption to the requirements under this Section 8D by filing an exemption request with its state of domicile, which will provide a copy of the request to the NAIC Financial Analysis (E) Working Group (FAWG). If the state of domicile agrees with the exemption request, then the requirements of this Section 8D do not apply to such company, provided FAWG does not conclude that the exemption would allow the company to use a reserving methodology that is not appropriate in relation to the benefits and the pattern of premiums for the plans covered.

a. Primary Reserve Methodology

The company's aggregate gross reserve before reinsurance for the business subject to this Section 8D to be reported in the December 31, 2012, and subsequent annual statutory financial statements of the company will be the aggregate reserve under 1 below, plus any excess of the aggregate reserve determined as defined in 2 below, over 1:

1. The basic and deficiency reserve as of the valuation date determined by the company according to the reserve methodology and assumptions used by the company for the statutorily-reported reserve for the business subject to this Section 8D as of December 31, 2011.

2. The reserve amount as of the valuation date determined according to the same requirements for determining the deterministic reserve in the version of the *Valuation Manual* specified under Section 11 of the *Standard Valuation Law* (Model #820) and adopted by the NAIC to govern the principle-based valuation on the valuation date, but with the two modifications identified below, determined as follows:

   a) First, future year-by-year cash flows for the block of business subject to this Section 8D are projected as of the valuation date. In making this projection:

      (I) the projected net investment earnings from the starting assets shall be the lesser of (i) the actual portfolio net investment returns and (ii) net investment returns based on a portfolio of A-rated corporate bonds purchased in the year of issue of the policies based on yields available in the year of issue for those bonds.

      (II) the projected net investment rate for the reinvestment assets shall be the lesser of (i) the average over a period of 12 months, ending on the June 30 prior to the valuation date, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investor Services, Inc. and (ii) 7% per annum.

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b) Second, future year-by-year net investment returns are determined from the cash flows generated in Section 8D(a)(2)(a).

c) Third, the reserve for the policies is computed using the year-by-year net investment returns determined in Section 8D(a)(2)(b) to discount the cash flows applicable to those policies.

The company may calculate the reserves as of any December 31 as of a date no earlier than three months before that December 31 valuation date, using relevant company data, provided an appropriate method is used to adjust those reserves to the valuation date.

If the aggregate reserve determined pursuant to the second calculation above exceeds the aggregate reserve determined pursuant to the first calculation, the additional reserve to be held is deemed to be required pursuant to Model #820, Section 3 and Section 6, which provide for an analysis of reserves pursuant to an asset adequacy analysis with margins for moderately adverse assumptions. Any such excess shall be allocated to each policy in proportion to the Step 1 reserve for that policy.

b. Alternative Reserve Methodology

The requirements of subsection a. above shall not apply to a company that holds a total gross reserve amount, before reinsurance, for the business subject to this Section 8D at least equal to the total reserve determined in accordance with the November 1, 2011 Life Actuarial (A) Task Force Statement on Actuarial Guideline XXXVIII, except that for purposes of determining any deficiency reserves under Model #830, using mortality and lapse assumptions according to the same requirements for determining the deterministic reserve in the *Valuation Manual*.

c. Documentation and Reporting

Under the direction of one or more qualified actuaries, the company shall prepare a stand-alone Actuarial Memorandum covering the reserve analysis performed on the business described in this Section 8D in compliance with Section 7 of the *Actuarial Opinion and Memorandum Regulation* (Model #822) to document the assumptions, analyses and results of the reserve calculations described above. The Actuarial Memorandum shall be prepared regardless of whether the company used the Primary Reserve Methodology described in Section 8D(a) or the Alternative Reserve Methodology described in Section 8D(b). Documentation in the submitted Actuarial Memorandum must be sufficient for another actuary qualified in the same practice area to evaluate the assumptions, analyses and results, and to enable regulatory review and verification that the assumptions, analyses and results satisfy the requirements described above, as they relate to the company. In the event that the *Valuation Manual* is incomplete or unclear as to any matter, the actuary preparing the Actuarial Memorandum shall use his or her best judgment in applying the requirements of the *Valuation Manual* and shall document his or her decisions in the Actuarial Memorandum. For any business subject to this Section 8D that has been ceded by the company, the Actuarial Memorandum shall provide a listing of the assuming companies with face amount, reserve credit taken, and form of reinsurance for such business. The Actuarial Memorandum shall be submitted to the state of domicile of the company by the April 30 following the valuation date.

For reporting years prior to 2015: The state of domicile shall provide a copy of the Actuarial Memorandum to FAWG and, upon request, to any other state in which the company is licensed.

For reporting years 2015 and after: The state of domicile shall provide a copy of the Actuarial Memorandum to FAWG upon request and, upon request, to any other state in which the company is licensed.

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For those companies that used the Primary Reserve Methodology described above, the Actuarial Memorandum shall also provide with respect to the business subject to this Section 8D a description of the simplifications, approximations and modeling efficiency (aggregation) techniques used to calculate the reserve amount set forth in Subsection 2 of the Primary Reserve Methodology (i.e., Section 8D(a)(2)) and a clear indication that, upon request, information may be obtained that is adequate to permit the audit of any subgroup of the aggregated reserve amounts to ensure that the total of the seriatim (policy-by-policy) reserve calculations produces a reserve not materially different than the aggregated reserve amount determined pursuant to Subsection 2 of the Primary Reserve Methodology (i.e., Section 8D(a)(2)).

Along with the filing of the Actuarial Memorandum pertaining to the December 31, 2012 valuation date, those companies using the Primary Reserve Methodology above shall also submit a report to its state of domicile indicating what the gross reserve before reinsurance for the business subject to this Section 8D would be as of December 31, 2012 if the reserve had been determined pursuant to the methodology and experience assumptions used to determine the reserve set forth in Subsection 2 of the Primary Reserve Methodology (i.e., Section 8D(a)(2)), except using a net reinvestment return rate assumption not greater than the maximum valuation interest rate for the year of issue of each policy set forth in Model #820. The company shall include in this report what its (i) total adjusted capital and (ii) company action level risk based capital would be if the company held the reserve calculated pursuant to this methodology rather than the reserve actually reported for the applicable business in the annual statement submitted by the company to the NAIC. The report described in this paragraph will be provided by the company to the state of domicile, which will forward a copy to FAWG. Upon request, the state of domicile will also forward a copy of this report to any other state in which the company is licensed. The state of domicile, FAWG, and any other state receiving the report will treat it as containing confidential information. The report is to be provided for informational purposes only, and it is to be considered and used as one additional piece of information to be evaluated in the context of the company's overall financial position.

For reporting years prior to 2015: The domestic state will perform a review of the Actuarial Memorandum in consultation with FAWG to ensure the company's reserve calculations have been performed according to the requirements of this Section 8D.

If:

- the company reports in its financial statements the reserve level required above, adjusted for any phase-in period approved by the company's state of domicile, and
- the company complies with any applicable phase-in period made by the state of domicile with respect to such additional reserves, and
- FAWG agrees with the state of domicile's decisions,

FAWG shall issue a confidential report to non-domiciliary states indicating that the company's reserving methodology is appropriate in relation to the benefits and the pattern of premiums for the plans covered. If FAWG does not agree with the state of domicile's decisions, FAWG shall issue a confidential report to non-domiciliary states indicating that the company's reserving methodology is not appropriate in relation to the benefits and the pattern of premiums for the plans covered.

For reporting years 2015 and after: The domestic state will perform a review of the Actuarial Memorandum to ensure the company's reserve calculations have been performed according to the requirements of this Section 8D and may consult with FAWG regarding this review.

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If FAWG does not agree with the state of domicile's decisions, FAWG shall issue a confidential report to non-domiciliary states indicating that the company's reserving methodology is not appropriate in relation to the benefits and the pattern of premiums for the plans covered.

8E. For policies and certificates issued on or after January 1, 2013, except for ULSG policies and certificates for which the company elects or is required to apply VM-20 as the reserve standard, per *Valuation Manual* requirements: For a universal life policy or certificate that guarantees the coverage to remain in force as long as the accumulation of premiums paid satisfies the secondary guarantee requirement.

Step 1: The first step is to derive the minimum gross premiums for the policy or certificate (to be determined at issue). Except as indicated for policies and certificates described in Method I Policy Design #3 (described below), the minimum premiums so derived must satisfy the secondary guarantee requirement. Model #830, Section 7A(4) does not apply in determining the minimum gross premiums for policies and certificates described in this Section 8E.

I) Methodology for determining the minimum gross premiums for certain designs ("Method I").

1. Policy Design #1: For a policy containing a secondary guarantee that uses a shadow account with a single set of charges and credits, the minimum gross premium for any policy year is the premium that, when paid into a policy with a zero shadow account value at the beginning of the policy year, produces a zero shadow account value at the end of the policy year, using the guaranteed shadow account charges and credits (e.g., interest credited rate, mortality charges, premium loads and expense charges) specified under the secondary guarantee.

2. Policy Design #2: For a policy that compares paid accumulated premiums to minimum required accumulated premiums (cumulative premium policy), with both accumulations based on a single set of charges and credits specified under the secondary guarantee, the minimum gross premium for any policy year is the premium that, when paid into a policy for which the accumulated premiums equals the minimum required accumulated premiums at the beginning of the policy year, results in the paid accumulated premiums being equal to the minimum required accumulated premiums at the end of the policy year.

3. Policy Design #3: If, for any policy year, a shadow account secondary guarantee, a cumulative premium secondary guarantee design, or other secondary guarantee design, provides for multiple sets of charges and/or credits, then the minimum gross premiums shall be determined by applying the set of charges and credits in that policy year that produces the lowest premiums, ignoring the constraint that such minimum premiums satisfy the secondary guarantee requirement and ignoring any contingencies or conditions that would otherwise limit the application of those charges and credits.

Notwithstanding the language in the approaches described above, the guaranteed (including conditionally guaranteed) policy credits for each year shall be limited as to magnitude in order for minimum gross premiums to be determined consistent with any of the policy designs above. The limitations must be met at the time of each product filing and also when guaranteed credits or charges for each such product are revised. For this purpose, policy credits based on the interest or accumulation rates in the policy shall not exceed the "Index" (defined in the next sentence) plus 3% per annum. The Index used to establish the limitation as to magnitude shall be either (i) the monthly average of the composite yield on seasoned corporate bonds as published by Moody's Investors Service, Inc., for the month immediately preceding the date of the Actuarial Opinion required under this Section 8E and described below, or (ii) the monthly average over a period of twelve months, ending on the June 30 preceding the date of the Actuarial Opinion required below, of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc. The averaging period chosen by the company must be elected at time of product

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filing and consistently used for that product thereafter even if guaranteed credits or charges are subsequently revised for that product.

II) Methodology for determining the minimum gross premiums for other designs ("Method II").

Unless otherwise provided in this Section 8E, the minimum gross premiums shall be the lowest schedule of premiums that keep the policy in force over the life of the secondary guarantee period and that produce the greatest deficiency reserve at issue. If deficiency reserves produced at issue are all zero, then the smallest absolute value of the difference between "quantity A" set forth in Model #830, Section 5B, over the basic reserve shall be considered the greatest deficiency reserve. For purposes of this Step 1, in deriving the deficiency reserve associated with a particular schedule of gross premiums, the X factors used shall be set equal to 1 for all durations, issue ages, and risk classes.

For policies that use a shadow account, and for cumulative premium policies, the schedule of premiums that keep the policy in force over the life of the secondary guarantee period and that produce the greatest deficiency reserve at issue shall be determined assuming the following premium-paying patterns for premiums actually paid under the policy:

- Level premiums for the life of the secondary guarantee but not beyond the duration that premiums may be paid under the policy, and
- Increasing premiums over the life of the secondary guarantee (including any resulting reserve segments created), but not beyond the durations that premiums may be paid under the policy, and
- Combinations of the above premium patterns including higher initial premiums for funding levels to have access to better charges and credits with combinations of level and increasing premium patterns thereafter.

For all policies and certificates subject to this Step 1 of Method II of this Section 8E, the company shall also perform a good faith high-level analytical review of the product design with respect to the premium payment patterns to be expected with respect to that design. The review should consider whether there are situations whereby the product design is likely to elicit a pattern of premium payments that, if paid, would provide the insured with access to lower charges and/or higher credits than those that would apply assuming the premium paying patterns required to be tested under this Section 8E and thereby result in the need for a deficiency reserve significantly in excess of that determined using the schedules of minimum gross premiums determined pursuant to the premium payment patterns required to be tested under this Section 8E. To the extent identified, the company shall use such other premium payment patterns it determines are likely to result in the need for a greater deficiency reserve than implied by the premium payment patterns required to be tested under this Section 8E in determining the schedule of minimum gross premiums and related deficiency reserve. In performing this analytic review, the company shall consider payment patterns which keep the policy in force over the lifetime of the secondary guarantee.

Step 2: For purposes of applying Section 7B and Section 7C of Model #830, the "specified premiums" are the minimum gross premiums derived in Step 1. Consistent with Model #830, the remaining steps in this guideline should be calculated on a segmented basis, using the segments that Model #830 defines for the product. Therefore, in the remaining steps, the term "fully fund the guarantee" should be interpreted to mean fully funding the guarantee to the end of each possible segment. The term "remainder of the secondary guarantee period" should be interpreted to mean the remainder of each possible segment. The total reserve should equal the greatest of all possible segmented reserves. Additionally, for purposes of applying Section 7B and Section 7C of Model #830, the lapse rate used shall be no more than 2% per year for the first 5 years,

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followed by no more than 1% per year to the policy anniversary specified in the following table based on issue age, and 0% per year thereafter. If the duration in the table is less than 5, then a lapse rate of no more than 2% per year may be used through that duration, and 0% per year thereafter.

Issue Age	Duration
0-50	30th policy anniversary
51-60	Policy anniversary age 80
61-70	20th policy anniversary
71-89	Policy anniversary age 90
90 and over	No lapse

Step 3: A determination should be made of the amount of actual premium payments greater than or less than the minimum gross premiums. For policies using shadow accounts and qualifying under one of the Policy Designs of Method I, this will be the amount of the shadow account. For policies using shadow accounts whose minimum gross premium is determined under Method II, this will be the amount of the shadow account minus the amount that would be in the shadow account if the minimum gross premiums used to calculate basic and deficiency reserves in Step 2 were paid. This result may be negative. For cumulative premium policies whose minimum gross premiums are determined under Method I, this excess will be the amount of cumulative premiums paid over the cumulative premium requirements. For cumulative premium policies whose minimum gross premiums are determined under Method II, this excess will be the amount of the cumulative premiums paid minus the cumulative premium using the minimum gross premiums used to calculate basic and deficiency reserves in Step 2. This result may be negative. The cumulative premium payments and requirements should include any interest credited under the secondary guarantee (with interest credited at the rate specified under the secondary guarantee).

Step 4: As of the valuation date for the policy being valued, for policies using shadow accounts, determine the minimum amount of shadow account required to fully fund the guarantee. For cumulative premium policies, determine the minimum amount of the cumulative premiums required to fully fund the guarantee less the cumulative premium requirements. For any policy for which the secondary guarantee cannot be fully funded in advance, solve for the minimum sum of any possible excess funding (either the amount in the shadow account or excess cumulative premium payments depending on the product design) and the present value of future premiums (using the maximum allowable valuation interest rate and the minimum mortality standards allowable for calculating basic reserves) that would fully fund the guarantee. For shadow account policies, if the minimum gross premium is determined according to Method II and the Step 3 amount is positive then the amount determined above for this step is reduced by any positive shadow account based on minimum gross premiums. For cumulative premium policies, if the minimum gross premium is determined according to Method II and the Step 3 amount is positive then the amount determined above for this step is reduced by the excess of cumulative premiums, assuming minimum gross premiums are paid, over the cumulative premium requirements. For shadow account policies, if the minimum gross premium is determined according to Method II and the Step 3 amount is negative then the amount determined above for this step is replaced by the amount of the shadow account based on the minimum gross premiums. For cumulative premium policies, if the minimum gross premiums are determined by Method II and the Step 3 amount is negative then the amount determined above for this step is replaced by the excess of cumulative premiums, assuming minimum gross premiums are paid, over the cumulative premium requirements.

The amount determined above for this step is then divided by one minus a 7% premium load allowance (0.93).

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The result from Step 3 should be divided by the number above, with the resulting ratio capped at 1 and no less than (-1). The ratio is intended to measure the level of prefunding for a secondary guarantee and is used to establish reserves. Assumptions within the numerator and denominator of the ratio therefore must be consistent in order to appropriately reflect the level of prefunding. The denominator is allowed to be inconsistent only by the amount of the premium load allowance as defined in this step. As used here, "assumptions" include any factor or value, whether assumed or known, that is used to calculate the numerator or denominator of the ratio.

[DRAFTING NOTE: The 7% premium load allowance approximates an average premium load level as evidenced by policies currently sold in the market. Rather than have the funding ratio vary according to the actual policy loads (which can fluctuate greatly by company and product), all companies will use an identical premium load allowance at this 7% level, which is approximately equal to the current industry average.]

Step 5: Compute the net single premium on the valuation date for the coverage provided by the secondary guarantee for the remainder of the secondary guarantee period, using any valuation table and select factors authorized in Section 5A of Model #830. For purposes of calculating the net single premium, a lapse rate subject to the same criteria as the lapse rate used in applying Step 2 may be used.

Step 6: If the amount in Step 3 is positive the "net amount of additional premiums" is determined by multiplying the ratio from Step 4 by the difference between the net single premium from Step 5 and the basic and deficiency reserve, if any, computed in Step 2.

If the amount in Step 3 is negative, the "net amount of additional premiums" is determined by multiplying the ratio from Step 4 by the basic reserves, if any, computed in Step 2. This result will be negative or zero. Subtract the deficiency reserve calculated in Step 2 from this result and then add the following amount, depending on whether the policy is a shadow account policy or a cumulative premium policy:

a) If a shadow account policy add the following:
   The deficiency reserve at issue calculated using X factors associated with the premium paying pattern used in determining the greatest deficiency reserve in Method II, Step 1, multiplied by one minus the ratio of the amount of the shadow account divided by minimum amount in the shadow account that would fully fund the guarantee. This amount in Step 6(a) is not to be less than zero.

b) If a cumulative premium policy add the following:
   The deficiency reserve at issue calculated using X factors associated with the premium paying pattern used in determining the greatest deficiency reserve in Method II, Step 1, multiplied by one minus the ratio of the amount of cumulative premiums paid divided by the minimum amount of cumulative premiums required to fully fund the guarantee. This amount in Step 6(b) is not to be less than zero.

Step 7: A "reduced deficiency reserve" shall be computed by multiplying the deficiency reserve, if any, by one minus the ratio (such ratio not to be set less than zero) from Step 4; this final amount also not to be set less than zero. This "reduced deficiency reserve" is the deficiency reserve to be used for purposes of Section 7D(1) of Model #830.

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Step 8: The reserve used for purposes of Model #830, Section 7D(1), is as follows.

a) Take the lesser of:
1) the "net amount of additional premiums" from Step 6 plus the basic reserve and the deficiency reserve, if any, computed in Step 2, and
2) the net single premium from Step 5.

b) Reduce the result in Step 8(a) by the applicable policy surrender charges (i.e., the account value less the cash surrender value). Multiply this surrender charge by the ratio of the net level premium for the secondary guarantee period divided by the net level premium for whole life insurance. Calculate both net premiums using the maximum allowable valuation interest rate and the minimum mortality standards allowable for calculating basic reserves.

c) Calculate the reserve floor:
1) If the result in Step 3 is negative, then the reserve floor shall equal the sum of the Step 2 basic and deficiency reserves and the amount from Step 6.
2) If the result in Step 3 is not negative, then the reserve floor shall equal the sum of the Step 2 basic and deficiency reserves without any adjustment.

The reserve to be used for purposes of Model #830, Section 7D(1) is the greater of the resulting amount from Step 8(b) above and the reserve floor.

Step 9: An "increased basic reserve" shall be computed by subtracting the "reduced deficiency reserve" in Step 7 from the reserve computed in Step 8. This "increased basic reserve" is the basic reserve to be used for purposes of Model #830, Section 7D(1).

Actuarial Opinion and Company Representation Requirements

If a company uses one of the Policy Design methodologies described above in Method I of this Section 8E to determine the minimum gross premiums in Step 1, the company shall submit to its state of domicile at the time of filing/approval of a new product, or by December 31, 2012, for current products that will be issued in 2013 or thereafter, and at any time when rates and/or charges are changed, an Actuarial Opinion signed by the Appointed Actuary and a Representation of the Company signed by a Senior Officer of the company regarding the applicable policy form(s) that states:

Actuarial Opinion

"I, (name and professional designation), am the appointed actuary for (company name). I have examined the actuarial assumptions and actuarial methods used in determining the reserves described herein, and, in my opinion: (1) the product referenced herein meets the definition of Policy Design # ___ described in Method I in Section 8E of Actuarial Guideline XXXVIII (AG 38); (2) notwithstanding the language in Policy Design # ___, the guaranteed (including conditionally guaranteed) policy credits in the product available for any year do not exceed the "Index" defined in Method I in Section 8E of AG 38 plus 3% per annum; and (3) the minimum gross premiums determined under Policy Design # ___ are not inconsistent with the minimum premiums, charges and credits that are expected to apply under the policy."

(Name of actuary, printed or typed)
(Signature of actuary)
(Date signed)

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Company Representation

"(company name) hereby represents: (1) that the product referenced herein meets the definition of Policy Design # ___ described in Method I in Section 8E of Actuarial Guideline XXXVIII (AG 38); (2) notwithstanding the language in Policy Design # ___, the guaranteed (including conditionally guaranteed) policy credits in the product available for any year do not exceed the "Index" defined in Method I in Section 8E of AG 38 plus 3% per annum; and (3) the minimum gross premiums determined under Policy Design # ___ are not inconsistent with the minimum premiums, charges and credits that are expected to apply under the policy."

(Name of company Officer, printed or typed)
(Signature of company Officer)
(Date signed)

For reporting years prior to 2015: The state of domicile shall provide a copy of the Actuarial Opinion and the Company Representation to FAWG and, upon request, to any state in which the company plans to issue the policy that is the subject of the Actuarial Opinion and Company Representation.

For reporting years 2015 and after: The state of domicile shall provide a copy of the Actuarial Opinion and the Company Representation to FAWG, upon request, and, upon request, to any state in which the company plans to issue the policy that is the subject of the Actuarial Opinion and Company Representation.

Policy Design

For reporting years prior to 2015: If a company develops reserves based on Method II of this Section 8E, the company shall submit a report from its Appointed Actuary prior to issuing policies on that form to its state of domicile, which will provide a copy to FAWG and (upon request) to any state in which the company plans to issue the product, that briefly describes the analytical review performed, the company's conclusions following the analytical review, and whether any additional premium payment patterns other than those required by this Section 8E were tested as a result of the review. If FAWG agrees with the state of domicile's decisions with respect to the company's Method II reserving methodology, FAWG shall issue a confidential report to non-domiciliary states indicating that the company's reserving methodology is appropriate in relation to the benefits and the pattern of premiums for the plans covered. If FAWG does not agree with the state of domicile's decisions with respect to the company's Method II reserving methodology, FAWG shall issue a confidential report to non-domiciliary states indicating that the company's reserving methodology is not appropriate in relation to the benefits and the pattern of premiums for the plans covered.

For reporting years 2015 and after: If a company develops reserves based on Method II of this Section 8E, the company shall submit a report from its Appointed Actuary prior to issuing policies on that form to its state of domicile, which will provide a copy to FAWG, upon request, and (upon request) to any state in which the company plans to issue the product, that briefly describes the analytical review performed, the company's conclusions following the analytical review, and whether any additional premium payment patterns other than those required by this Section 8E were tested as a result of the review. If FAWG does not agree with the state of domicile's decisions with respect to the company's Method II reserving methodology, FAWG shall issue a confidential report to non-domiciliary states indicating that the company's reserving methodology is not appropriate in relation to the benefits and the pattern of premiums for the plans covered.

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Effective Date

With the exception of Steps 3 through Step 9 of Section 8A and all of Section 8B, Section 8C, Section 8D and Section 8E, the scope of this guideline shall be inclusive of policies issued on and after the earlier of a state's adoption of the revised Model #830 (adopted by the NAIC in March 1999) or the statutory accounting practices and procedures as set forth in the NAIC *Accounting Practices and Procedures Manual*. All of Section 8A, Section 8B, Section 8C, Section 8D and Section 8E shall be applicable to policies and certificates issued on or after the later of the date of a state's adoption of the revised Model #830 and January 1, 2003, subject to the dates and/or applicable scope specified in Section 8A, Section 8B, Section 8C, Section 8D and Section 8E.

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Actuarial Guideline XXXIX

RESERVES FOR VARIABLE ANNUITIES WITH GUARANTEED LIVING BENEFITS

Actuarial Guideilne XXXIX sunset on December 30, 2009, and was replaced by *Actuarial Guideline XVIII—CARVM for Variable Annuities*, effective December 31, 2009.

Actuarial Guideline XL

GUIDELINE FOR VALUATION RATE OF INTEREST FOR FUNDING AGREEMENTS AND GUARANTEED INTEREST CONTRACTS (GICS) WITH BAIL-OUT PROVISIONS

PURPOSE

The purpose of this Guideline is to interpret the Standard Valuation Law (SVL) for assignment of appropriate valuation interest rates to risks embedded in bail-out provisions under Funding Agreements and Guaranteed Interest Contracts.

BACKGROUND

Funding Agreements (FAs) and other types of Guaranteed Interest Contracts (GICs) typically issued to tax-exempt municipal bonds, money market funds and securities lending funds, often contain bail-out provisions that allow the contractholders to get their money back at full book value. Such provisions may be triggered by the credit rating downgrade of the issuer below a given level or may be at a given period's notice to the contractholder, e.g. 7, 30, 90 or 180 days' notice. The contract language for these provisions may be as follows:

1. In the event that the investment provider (i.e. the insurance company) is downgraded below *A-/A3* by S & P and/or Moody's respectively, the contract holder has the right to terminate the contract and receive the remaining principal and accrued interest without penalty. [In most cases the issuer has the alternate option to provide a replacement contract or post collateral or do a credit wrap.]

2. Each party has the right to terminate the contract before maturity by giving the other at least *7/30/90 or 180-days* notice in writing. At such termination the principal and accrued interest is payable with no penalty.

Contracts with downgrade provision

The bulk of the contracts issued with a downgrade provision are fixed rate FAs or GICs issued in connection with tax-exempt municipal bonds. These contracts can be short-term or long-term. Short-term contracts typically have an average life of around one-year, and are intended for municipal bond funds for construction, acquisition, housing, tax revenue anticipation notes (TRANS), etc. In these types of funds the cash-flow projections are provided when the case is underwritten, but there may be variability in the actual withdrawals. Any outstanding principal and interest is payable at maturity.

Long-term contracts are issued in connection with the debt service reserve (DSR) or the float fund of the bond issue, and mature at the same time as the bonds, which can be as long as 30 years. The float fund takes in deposits, and pays out the half-yearly interest and principal (if any is due) on the bonds. It runs to near zero about twice a year, after each half-yearly coupon payment. The DSR is a contingent fund for a rainy day to prevent a missed coupon or principal payment on the bond. The DSR has a single deposit that is typically 10% of the bond issue.

Contracts with put provision

FAs or GICs with put provisions are generally issued to money market funds subject to Rule 2a-7 of the Investment Company Act. Rule 2a-7 provides guidelines on liquidity, requiring funds available at book value subject to certain notification periods. Additionally, these contracts usually have downgrade provisions. Even if the downgrade provision is not in the contract, it can be assumed that the put will be exercised on downgrade, since a certain level of credit is also a Rule 2a-7 requirement.

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Typically, these FAs or GICs guarantee a floating rate of interest linked to an index like LIBOR, which is paid out and reset periodically. Most contracts have fixed maturity dates when the principal is returned. Generally the FAs or GICs are the higher yielding assets of the money market funds, and therefore puts are not expected to be exercised.

Risks

Both the downgrade and the put provisions present liquidity or concentration type of risks to the issuer, i.e. if a critical event occurs, a substantial part of the whole block of business is likely to be liquidated. Sufficient asset liquidity, prudent A/L management, cash flow testing, hedging strategies, etc. can mitigate these risks. Also, companies generally have contractual provisions providing alternative options.

Downgrade provision:
The main risk here is that, upon downgrade to the trigger level, a company may have to realize its assets at a market loss in order to pay out at book. If the downgrade happens in a falling interest rate environment there is no risk of a market loss as the underlying assets are likely to be at a higher market value. On the other hand if the downgrade occurs in a rising interest rate environment, market value losses would occur when the company sells assets to pay out liabilities at book value.

Companies have written provisions in their contracts that provide alternate options to paying at book value in a rising interest rate environment:

"Novation/Assignment" option: The novation/assignment option allows the company to transfer its liabilities to another funding agreement provider that meets the credit rating requirements of the contractholder. In a rising interest rate environment, the new provider should be willing to pay a "premium" to assume a liability crediting a below market interest rate. In a perfectly efficient market this "premium" should precisely offset the market value loss upon the sale of the asset. In practice, however, it is less likely that the "premium" would fully offset the market value loss since:

- The new provider may view the liability risk somewhat differently
- The new provider may try and take advantage of the situation of the downgraded company
- There may be a large volume of these types of contracts in the market, etc.

However, the "premium" payable by the new provider could provide a substantial offset against the market value loss incurred by the downgraded company.

"Collateralization" option: This option allows the company to post assets as collateral for the benefit of the contractholder, as an alternative to payment at book value. The collateral posted would have to meet the credit requirements of the contractholder, which could be government or agency securities. Usually the collateral posted is required to have a cushion, typically ranging from 102% to 105%.

Upon trigger of the downgrade provision, the company would need to have suitable assets in its portfolio that are available for use as collateral, and also acceptable to the contractholder. In addition, there will be administrative and custodial expenses/fees of establishing and monitoring collateral levels. In some states there may also be legal restrictions on encumbering assets that back policyholder claims.

If the downgraded company can overcome the above constraints, then collateralization is another alternative of maintaining the contract and not having to pay out at book value.

"Credit Wrap" option: Under this arrangement the contract is issued out of a separate account which is guaranteed by a financial guarantee insurer. Effectively, the credit rating of the guarantor passes through to meet the credit requirement of the FA or GIC. [A number of FAs or GICs requiring a higher credit rating are currently being written in this way.]

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The contract being wrapped has to meet certain criteria before the financial guarantee insurers are willing to wrap. Generally, the guarantor would also require higher credit rated securities in the separate account, which could be government or agency, and would require these in the 102% to 105% range. There will also be administrative and custodial expenses of establishing and monitoring the separate account in addition to the wrap fee payable to the mono-line insurer.

Although at significant cost, this option does provide the downgraded company a viable alternative to paying out at book value.

Put provision:
The put provision is not tied to a particular event but can contractually be exercised by giving the required days' notice. It has been argued that this provision is there to meet the Rule 2a-7 liquidity requirements and in practice is unlikely to be exercised, particularly since the FAs or GICs are one of the higher yielding assets of the money market portfolio. However, it is a contractual option and if, for example, the issuer were in financial difficulties, it will be exercised. Past experience suggests this is the case.

The put provision therefore presents a liquidity or concentration risk similar to that of downgrade——it is likely to be exercised in bulk upon happening of a critical event. Similar considerations apply, i.e. in a rising interest rate environment market value losses would occur when the company sells assets to pay out liabilities at book value.

Reserves

For reserving the Standard Valuation Law applies. However, when the SVL was enacted, these types of bail-out provisions did not exist, and were therefore not addressed explicitly. The purpose of this Guideline is to interpret the SVL for assignment of appropriate valuation interest rates to risks embedded in these bail-out provisions.

Other Actuarial Guidelines have provided similar interpretations. For example, Guideline XIII addresses interest bailout provisions under annuity contracts, Guideline XXX provides for participant directed withdrawal provisions under GICs, and Guideline XXXIII covers the elective and non-elective benefits under individual annuity contracts.

Plan Types

The SVL utilizes a concept known as Plan Type, which was designed to distinguish between the various levels of disintermediation risks—the greater the disintermediation risk for a company, the more conservative is the resulting valuation rate. Plan Types designated in the model SVL are defined as follows:

Plan Type A: At any time policyholder may withdraw funds only (l) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) without such adjustment but in installments over five years or more, or (3) as an immediate life annuity, or (4) no withdrawal permitted.

Plan Type B: Before expiration of the interest rate guarantee, policyholder may withdraw funds only (1) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) without such adjustment but in installments over five years or more, or (3) no withdrawal permitted. At the end of interest rate guarantee, funds may be withdrawn without an adjustment in a single sum or installments over less than five years.

Plan Type C: Policyholder may withdraw funds before expiration of interest rate guarantee in a single sum or installments over less than five years either (1) without adjustment to reflect changes in interest

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rates or asset values since receipt of the funds by the insurance company, or (2) subject only to a fixed surrender charge stipulated in the contract as a percentage of the fund.

TEXT

For the purpose of the application of the Standard Valuation Law to FAs and GICs, the annuities and GIC valuation interest rates are to be used. The bailout provisions described above shall be treated as a withdrawal by the policyholder at book value, and the underlying contracts shall be classified as Plan Type C.

However, for contracts containing written provisions that allow the insurance company alternate options to paying out at book value, the valuation actuary may use a valuation rate of interest higher than Type C. In no event may the valuation interest rate be greater than that applicable to similar contracts with no put or bailout provisions. If a provision requires over-collateralization and/or use of high credit quality assets, this should be adequately reflected in the reserves.

If a higher interest rate than Type C is used, the valuation actuary must be satisfied and be able to demonstrate that the written provisions substantially reduce the liquidity risk. In addition, the valuation actuary must be satisfied, and should periodically review, that there are other risk management measures in place to reduce the liquidity or concentration risk, taking into consideration at least the following:

Readily liquidated assets at nil or minimal market-value loss
Cash-flow testing results
Standby lines of credit available and other liquidity facilities established
Hedges in place with liquidity options
High credit quality assets available for use as collateral.

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Actuarial Guideline XLI

PROJECTION OF GUARANTEED NONFORFEITURE BENEFITS UNDER CARVM

I. Background

The following is an excerpt from the October 21, 2003, Report of the American Academy of Actuaries' Life Valuation Subcommittee:

Annuity SNFL Impact on Reserves

Per the Standard Valuation Law, Commissioner's Annuity Reserve Valuation Method (CARVM) is:

"the greatest of the respective excesses of the present values, at the date of valuation, of the future guaranteed benefits, *including guaranteed nonforfeiture benefits*, provided for by the contracts at the end of each respective contract year, over the present value, at the date of valuation, of any future valuation considerations derived from future gross considerations, required by the terms of the contract, that become payable prior to the end of the respective contract year."

Historically the guaranteed nonforfeiture benefit calculation has been determined at issue (e.g. 90 percent of premiums accumulated at three percent interest). The recent change to the Standard Nonforfeiture Law for Individual Deferred Annuities has changed this.

Nonforfeiture Rate

The new Standard Nonforfeiture Law for Individual Deferred Annuities has changed the nonforfeiture rate from being static to being dynamic. Under the old law, the nonforfeiture interest rate was three percent. The revised law bases the nonforfeiture rate on the five-year Constant Maturity Treasury Rate less 125 basis points (bps). The nonforfeiture rate is subject to a minimum of one percent and a maximum of three percent. Additional enhancements include the ability to reset the nonforfeiture rate at a date predetermined in the contract and allowing an additional reduction (offset) for Equity Indexed Annuities.

The nonforfeiture rate can be reset at a date predetermined in the contract (e.g. five years from issue) and based on a formula specified in the contract. The same requirements applicable to the initial rate apply to the re-determined rate.

The revised law allows an additional offset to the nonforfeiture rate for contracts that provide substantive participation in an equity indexed benefit. This offset ranges from 0 bps to 100 bps.

The ability to re-determine the nonforfeiture rate and that the EIA offset may be reevaluated in the future raises some issues with the CARVM calculation.

In doing a CARVM projection, what should be the assumed interest rate? Should the option depend on whether there are re-determination provisions? Should the option depend on whether the product relies on an equity indexed offset?

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The Report further states:

> The minimum guaranteed interest rate in the contract might be different than the minimum nonforfeiture rate. To the extent that the guaranteed values in the contract are always greater than the minimum nonforfeiture benefits, then the nonforfeiture values do not come into play.

This Guideline specifies how to determine the nonforfeiture interest rate used in determining the minimum nonforfeiture benefits guaranteed under the contract. As noted in the Report, the minimum nonforfeiture benefits may be less the guaranteed values otherwise provided by the contract. Where this is the case, the higher guaranteed values are used in the CARVM calculation, and "the nonforfeiture values do not come into play."

It should also be noted that requirements for projecting guarantees exist in other regulations and guidelines, such as the specifications in Actuarial Guideline XXXV ("The Application of the Commissioners Annuity Reserve Method to Equity Indexed Annuities") for projecting equity-indexed guarantees. The specifications of this Guideline are in addition to any other requirements.

II. Scope

This Guideline applies to contracts subject to CARVM and the Standard Nonforfeiture Law for Individual Deferred Annuities ("SNLIDA").

III. Text

The following assumptions shall be made on the valuation date for purposes of determining the future nonforfeiture interest rate when this rate is not known in advance. For purposes of (B) below, "NI" shall refer to the nonforfeiture interest rate, "VI" shall refer to the valuation interest rate, and "CNI" shall refer to the current nonforfeiture interest rate which will be adjusted for any future durations pursuant to "A" below.

A. For the period of time during which the additional EIA offset is not known, the additional offset shall be zero.

B. For the period of time during which the nonforfeiture interest rate is not known,

$$NI = \min [\max \{VI, CNI\}, 3\%]$$

If the redetermination of the nonforfeiture interest rate is based on changes to the value of the underlying index (this will be the five-year Constant Maturity Treasure Rate in the case of the nonforfeiture interest rate), then for purposes of this Guideline it shall be assumed that such rate is not known as of the first date on which the rate may be subject to redetermination.

IV. Applicability

This Guideline is effective December 31, 2006 and affects all contracts issued on or after January 1, 1981.

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Actuarial Guideline XLII

THE APPLICATION OF THE MODEL REGULATION PERMITTING THE RECOGNITION OF PREFERRED MORTALITY TABLES FOR USE IN DETERMINING MINIMUM RESERVE LIABILITIES

1. Purpose

The purpose of this Guideline is to provide rules and guidance in the selection of the proper set of mortality rates when a company chooses to use either the 2001 CSO Preferred Class Structure Mortality Table or the 2017 CSO Preferred Class Structure Mortality Table as authorized under a state's requirements.

2. Effective Date and Scope

The 2001 CSO Preferred Class Structure Mortality Table is available for valuation purposes for individual life policy forms (and certain group life products sold to individuals by certificate with premium rates guaranteed from issue for at least two years) for issues as provided by the state's requirements which may be based on the NAIC *Model Regulation Permitting The Recognition of Prefered Mortablity Tables for Use in Determining Minimum Reserve Liabilities* (Model #815) and which may use the NAIC *Valuation Manual*.

The 2017 CSO Preferred Class Structure Mortality Table is available for valuation purposes for individual life policy forms (and certain group life products sold to individuals by certificate with premium rates guaranteed from issue for at least two years), for issues as provided by a state's requirements which may use the NAIC *Valuation Manual*.

The applicable CSO Preferred Class Structure Mortality Table is either the 2001 CSO Preferred Class Structure Mortality Table or the 2017 CSO Preferred Class Structure Mortality Table as applicable in context.

3. Definitions

A. "Anticipated mortality" means the appointed actuary's assumption about the mortality to be experienced in the future on a group of insured lives.

B. "Appointed actuary" means any individual who is appointed or retained in accordance with the requirements set forth in the Actuarial Opinion and Memorandum Regulation.

C. "Basic reserves" means reserves calculated in accordance with Section 5 of the Standard Valuation Law.

D. "Class" means a group of policies under one or more plans of insurance that has similar anticipated mortality, as grouped together by the insurer.

E. "Credibility" means a measure of the predictive value in a given application that the appointed actuary attaches to a particular body of data (predictive is used here in the statistical sense and not in the sense of predicting the future).

F. "Deficiency reserves" means the excess over basic reserves, if any, of minimum reserves established in accordance with Section 8 of the Standard Valuation Law.

G. "Full credibility" means the level at which a particular body of data is assigned full predictive value based on a selected confidence interval.

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H. "Preferred class certification" means the certification required by Section 5 of the Model.

I. "Underwriting-based justification" means the incorporation of underwriting criteria for use in setting the anticipated mortality assumption.

J. "Underwriting class" means the insurer's designation of insureds into a particular premium rate structure, e.g. super preferred, preferred, or standard.

4. Selection of Table within the Applicable CSO Preferred Class Structure Mortality Table

VM-20, Section 3C of the *Valuation Manual* contains the requirements governing the set of mortality rates to be used for the purpose of calculating reserves based on the applicable CSO Preferred Class Structure Mortality Table. The election of the applicable CSO Preferred Class Structure Mortality Table is on a policy form and calendar year of issue basis, although once a calendar year cohort of policy forms is placed on the applicable CSO Preferred Class Mortality Structure Table basis, it may not subsequently revert back to the standard applicable CSO basis without the approval of the commissioner. This would be considered a basis change for annual statement reporting purposes. For those calendar years of issue in which a company opts to use the applicable CSO Preferred Class Structure Mortality Table, it must use the entire applicable CSO Preferred Class Structure Mortality Table for the chosen policy forms, i.e. a company may not use the preferred classes from the applicable CSO Preferred Class Structure Mortality Table and use the applicable Standard CSO Mortality Table for the non-preferred class(es). Additionally, if the company sells two similar policy forms in the same market the appointed actuary must use the same version of the table for both forms and may not use the applicable CSO Preferred Class Structure Mortality Table on one and the applicable Standard CSO Mortality Table on the other. A characteristic of this two-form scenario is that preferred lives would be attracted to one form and non-preferred lives would be attracted to the other.

The Model contains a requirement that at the time of election and annually thereafter, except for business valued under the applicable Residual Standard Nonsmoker Table or the applicable Residual Standard Smoker Table, the appointed actuary shall certify that the following tests of sufficiency were passed:

a. For each class, the present value of death benefits over the next ten years after the valuation date using the anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class is less than the present value of death benefits using the valuation basic table corresponding to the valuation table being used for that class.

b. For each class, the present value of death benefits over the future life of the contracts using anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class is less than the present value of death benefits using the valuation basic table corresponding to the valuation table being used for that class.

In the event that the class does not contain any policies with expiry dates ten or more years into the future, the sufficiency test based on the present value over the future life of the contracts shall be the only test required.

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In order to choose the proper set of mortality rates within the applicable CSO Preferred Class Structure Mortality Table and to develop the preferred class certification, the following considerations shall be made:

A. Creation of Classes

The appointed actuary should consider the composition and characteristics of the policies issued under a plan of insurance in determining the appropriate classes that will be applicable under that plan. The policies that comprise classes generally have similar underwriting or mortality experience characteristics. When classes are similar across various plans of insurance, these classes may be combined into a single aggregate class. The appointed actuary shall not combine classes that are expected to have dissimilar anticipated mortality as a means to produce reserves that are materially lower than those developed if the classes were not combined.

The appointed actuary should consider the presence of reinsurance in creating classes. Anticipated mortality should be assessed and classes should be created on a gross basis. To the extent that anticipated mortality on reinsurance ceded or assumed is materially different from that on direct business, the appointed actuary should consider creating separate classes to properly reflect the anticipated mortality.

If, due to differences in actual experience by policy form and underwriting class, groupings of classes are changed from those used in the prior actuarial certifications, the change and the effect of the change shall be disclosed to the commissioner in the actuarial certification.

Separate classes may be established for a single policy form if there are significant anticipated mortality differences for different cohorts of insured lives, such as age groups or policy sizes. For instance, if a company has different underwriting thresholds for policies with face amounts of $1 million or more, it may be appropriate to have a class for policies with face amounts of less than $1 million and a separate class for policies of $1 million or more.

B. Deriving Anticipated Mortality

i. If relevant company experience for a particular class is available and has full credibility, the appointed actuary shall use that experience as the basis for deriving anticipated mortality.

ii. In situations where relevant company experience for a particular class is available but does not have full credibility, the appointed actuary shall derive the anticipated mortality by blending the relevant company experience for the class with actual relevant, credible experience and past trends in experience of other similar types of business, either in the same company, in other companies (including reinsurance companies), or from other sources, generally in that order of preference provided that the appointed actuary supplies underwriting-based justification. The blending process shall be based on a credibility methodology that is recognized by the actuarial profession as acceptable practice as provided for in published transactions and scientific journals.

iii. In situations where relevant company experience for a particular class is not available (e.g. a new product), the appointed actuary may derive the anticipated mortality using actual relevant credible experience and past trends in experience of other similar types of business either in the same company, in other companies (including reinsurance companies), or from other sources, generally in that order

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of preference, provided that the appointed actuary supplies underwriting-based justification.

iv. Underwriting-based justification shall include an analysis of the relationship between the underwriting-based criteria for the class where no experience data is available or does not have full credibility and the underwriting-based criteria that underlie the actual relevant credible experience data.

v. If no sufficient underwriting-based or experienced-based justification is made to derive anticipated mortality for a class, the company shall not use the applicable CSO Preferred Class Structure Mortality Table for valuation.

C. Periodic Assessment of Anticipated Mortality

The appointed actuary shall annually review relevant emerging experience and underwriting methods for the purpose of assessing the appropriateness of anticipated mortality for each class and, in aggregate, for all classes combined. If the results of statistical or other testing indicate that previously anticipated mortality for a given class is inappropriate, then the appointed actuary shall set a new anticipated mortality assumption for the class. After analyzing the appropriateness of the anticipated mortality for each class, the appointed actuary shall analyze the appropriateness of the anticipated mortality assumptions at the aggregate level. If the analysis at the aggregate level indicates that aggregate anticipated mortality is inadequate, then the appointed actuary shall adjust the anticipated mortality assumption for one or more of the classes until the appointed actuary is satisfied that the anticipated mortality assumptions are adequate at the aggregate level.

D. Tests of Sufficiency

After the anticipated mortality is established, each class must be tested for sufficiency. If a class fails any required sufficiency test, the class must be re-valued using a different set of mortality rates from the applicable CSO Preferred Class Structure Mortality Table. A company must choose a set of mortality rates under which all required tests of sufficiency can be passed.

E. Calculation of Present Value

When a class is tested for sufficiency, the calculation of the present value of death benefits shall be based on a projection of death benefits, without the effect of lapse, at the valuation interest rate used to determine basic reserves for the class. If the class contains policies with several valuation interest rates, the lowest valuation interest rate used to determine the base reserves for any policy within the class shall be used for that class.

F. Right of Commissioner to Change the Table Used by the Company

The commissioner may require a company to change the mortality table if it is determined by the commissioner that inadequate justification of anticipated mortality is provided by the company.

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5. Communications and Disclosures

The appointed actuary shall provide to the commissioner an annual certification that, as of the valuation date, the anticipated mortality experience of each class of business (other than Residual Standard Class) meets the criteria of 4(a) and 4(b) above. Additionally, the appointed actuary shall prepare an annual report in support of the certification. The report shall include the following items:

A. The certification that the report supports;

B. The specified plans of insurance for which the company has elected to use the Preferred Class Structure Table, briefly describing each plan and the amount of in force business (count, face amount, and reserves) on each plan on the valuation date;

C. Compliance with the certification criteria;

D. Description of sources of information used as a basis for determining anticipated mortality;

E. Analysis performed to evaluate the credibility of relevant historical company experience when establishing anticipated mortality for each class;

F. Analysis performed to evaluate the relationship between the underwriting-based criteria and the anticipated mortality established in each class.

G. Statistical or other quantitative analyses performed in assessing the continued appropriateness of the anticipated mortality assumption for each class and for all classes in aggregate, and a summary of changes made as a result of the analyses;

H. Anticipated Mortality, without recognition of mortality improvement beyond the date of valuation, for each class and for all classes in aggregate;

I. For each class, the ratio of Anticipated Mortality to the mortality rates in the Valuation Basic Table corresponding to the set of valuation mortality rates being used for that class;

J. Any changes made in the approach or parameters applied to the statistical analyses or tests performed compared to those performed at the last annual valuation; and,

K. Disclosure of the financial impact of any change in the chosen set of valuation mortality rates

Drafting Note: Annual actuarial opinions, certifications and reports for the use of "X" factors have been required since the implementation of the NAIC *Valuation of Life Insurance Model Regulation*. The work and analysis to be performed for Preferred Class Certification is very similar to the requirements for the use of the "X" factors and the appointed actuary may combine the selection and analysis of "X" factors and the selection and analysis of applicable CSO Preferred Class Structure Mortality Table into one actuarial opinion, certification and annual experience report, if the appointed actuary wishes to do so.

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6. Other Items of Note

A. If a class of business is assigned to a different set of mortality rates within the applicable CSO Preferred Class Structure Mortality Table (either a higher or lower level of mortality rates) from that used in the prior valuation, the change is not considered a basis change, and the reserve change must be accounted for in the calculation of gain from operations.

B. Multiple underwriting classes on a policy form can be mapped into the same set of mortality rates within the applicable CSO Preferred Class Structure Mortality Table, if, in aggregate, the underwriting classes can be shown to have anticipated mortality no greater than the valuation basic table underlying the set of mortality rates selected.

C. If a company chooses to use the applicable CSO Preferred Class Structure Mortality Table for basic reserves, the same table must be the basis for the calculation of deficiency reserves, if applicable.

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Actuarial Guideline XLIII

CARVM FOR VARIABLE ANNUITIES

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Section I) Background

The purpose of this Actuarial Guideline (Guideline) is to interpret the standards for the valuation of reserves for variable annuity and other contracts involving certain guaranteed benefits similar to those offered with variable annuities. The Guideline codifies the basic interpretation of the Commissioners Annuity Reserve Valuation Method (CARVM) by clarifying the assumptions and methodologies that will comply with the intent of the Standard Valuation Law (SVL). It also applies similar assumptions and methodologies to contracts that contain characteristics similar to those described in the scope, but that are not directly subject to CARVM.

For many years regulators and the industry have struggled with the issue of applying a uniform reserve standard to these contracts and in particular some of the guaranteed benefits referenced above. Current approaches make assumptions about product design, contractholder behavior and economic relationships and conditions. The economic volatility seen over the last few decades, combined with an increase in the complexity of these products, have made attempts to use these approaches for measuring economic-related risk less successful.

The Guideline addresses these issues by including an approach that applies principles of asset adequacy analysis directly to the risks associated with these products and guarantees.

The NAIC is currently using a similar approach to calculate risk-based capital (RBC) for similar contracts (i.e., the C-3 Phase II project). The methodology in the Guideline is based on that approach, and the intent of the Guideline is to, where possible, facilitate a framework whereby companies may determine both reserve and RBC in a consistent calculation.

In developing the Guideline, two regulatory sources were looked to for guidance. First, the SVL requires that CARVM be based on the greatest present value of future guaranteed benefits. Second, the NAIC Model Variable Annuity Regulation (VAR) states that the "reserve liability for variable annuities shall be established pursuant to the requirements of the Standard Valuation Law in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees."

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The Guideline requires that reserves for contracts falling within its scope be based on a minimum floor determined using a standard scenario (referred to as the Standard Scenario Amount) plus the excess over this minimum floor, if any, of a reserve calculated using a projection of the assets and estimated liabilities supporting these contracts over a broad range of stochastically generated projection scenarios and using prudent estimate assumptions (referred to as the Conditional Tail Expectation Amount). Within each of these scenarios, the greatest of the present values of accumulated losses ignoring Federal Income Tax is determined. The assumed fund performance for these scenarios must meet the mandated calibration standards contained in the Guideline. The reserve calculated using projections is based on a Conditional Tail Expectation measure of the results for each scenario.

Conditional Tail Expectation (CTE) is a statistical risk measure that provides enhanced information about the tail of a distribution above that provided by the traditional use of percentiles. Instead of only identifying a value at a particular percentile and thus ignoring the possibility of extremely large values in the tail, CTE recognizes a portion of the tail by providing the average over all values in the tail beyond the CTE percentile. Thus where the tail of the distribution of losses approximates that of a standard normal distribution, CTE (70) will approximate the 88th percentile; where the tail is "fatter" than that of a standard normal distribution, CTE (70) will exceed the 88th percentile; and where the tail is not as "fat" as a standard normal distribution, CTE (70) will be lower than the 88th percentile. Therefore, for distributions with "fat tails" from low probability, high impact events, such as those covered by the Guideline, the use of CTE will provide a more revealing measure than use of a single percentile requirement.

For certain products (e.g., variable annuities with Guaranteed Minimum Death Benefits only), a company can use an Alternative Methodology in place of the modeling approach outlined above to determine the Conditional Tail Expectation Amount.

The projection methodology used to calculate the Conditional Tail Expectation Amount, as well as the approach used to develop the Alternative Methodology, is based on the following set of principles. These principles should be followed when applying the methodology in the Guideline and analyzing the resulting reserves:[1]

> **Principle 1.** The objective of the approach used to determine the Conditional Tail Expectation Amount is to quantify the amount of statutory reserves needed by the company to be able to meet contractual obligations in light of the risks to which the company is exposed.
>
> **Principle 2.** The calculation of the Conditional Tail Expectation Amount is based on the results derived from an analysis of asset and liability cash flows produced by the application of a stochastic cash flow model to equity return and interest rate scenarios. For each scenario the greatest present value of accumulated surplus deficiency is calculated. The analysis reflects Prudent Estimate (see the definition of Prudent Estimate in Section III) assumptions for deterministic variables and is performed in aggregate (subject to limitations related to contractual provisions)[2] to allow the natural offset of risks within a given scenario. The methodology utilizes a projected total statutory balance sheet approach by including all projected income, benefit and expense items related to the business in the model and sets the Conditional Tail Expectation Amount at a degree of confidence using the conditional tail expectation measure applied to the set

[1] Note the following when considering these principles:
a. The principles should be considered in their entirety.
b. The Guideline requires companies to meet these principles with respect to only those contracts that fall within the scope of the Guideline and are inforce as of the valuation date to which the requirements are applied.

[2] Examples where full aggregation between contracts may not be possible include experience rated group contracts and the operation of reinsurance treaties.

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of scenario specific greatest present values of accumulated statutory deficiencies that is deemed to be reasonably conservative over the span of economic cycles.

Principle 3. The implementation of a model involves decisions about the experience assumptions and the modeling techniques to be used in measuring the risks to which the company is exposed. Generally, assumptions are to be based on the conservative end of the actuary's confidence interval. The choice of a conservative estimate for each assumption may result in a distorted measure of the total risk. Conceptually,[3] the choice of assumptions and the modeling decisions should be made so that the final result approximates what would be obtained for the Conditional Tail Expectation Amount at the required CTE level if it were possible to calculate results over the joint distribution of all future outcomes. In applying this concept to the actual calculation of the Conditional Tail Expectation Amount, the actuary should be guided by evolving practice and expanding knowledge base in the measurement and management of risk.

Principle 4. While a stochastic cash flow model attempts to include all real world risks relevant to the objective of the stochastic cash flow model and relationships among the risks, it will still contain limitations because it is only a model. The calculation of the Conditional Tail Expectation Amount is based on the results derived from the application of the stochastic cash flow model to scenarios while the actual statutory reserve needs of the company arise from the risks to which the company is (or will be) exposed in reality. Any disconnect between the model and reality should be reflected in setting Prudent Estimate assumptions to the extent not addressed by other means.

Principle 5. Neither a cash flow scenario model, nor a method based on factors calibrated to the results of a cash flow scenario model, can completely quantify a company's exposure to risk. A model attempts to represent reality, but will always remain an approximation thereto and hence uncertainty in future experience is an important consideration when determining the Conditional Tail Expectation Amount. Therefore, the use of assumptions, methods, models, risk management strategies (e.g., hedging), derivative instruments, structured investments or any other risk transfer arrangements (such as reinsurance) that serve solely to reduce the calculated Conditional Tail Expectation Amount without also reducing risk on scenarios similar to those used in the actual cash flow modeling are inconsistent with these principles. The use of assumptions and risk management strategies should be appropriate to the business and not merely constructed to exploit 'foreknowledge' of the components of the required methodology.

The methodology prescribed in the Guideline is applied to a company's entire portfolio of variable annuities (whether or not they contain guaranteed benefits), as well as other affected products that contain guaranteed benefits. Current guaranteed benefits include Guaranteed Minimum Death Benefits, Guaranteed Minimum Accumulation Benefits, Guaranteed Minimum Income Benefits, Guaranteed Minimum Withdrawal Benefits, Guaranteed Lifetime Withdrawal Benefits, and Guaranteed Payout Annuity Floors. It is also expected that the methodology in the Guideline will be applied to future variations on these designs and to new guarantee designs.

Since statutory reporting requires companies to report reserves prior to reinsurance, the Guideline clarifies standards for adjusting the various components of the reserve so that the reserve may be reported both prior to and net of reinsurance.

The Guideline also requires an allocation of the total reported reserve between the General and Separate Accounts and prescribes a method for doing this allocation.

[3] The intent of Principle 3 is to describe the conceptual framework for setting assumptions. Appendix 9 provides the requirements and guidance for setting contractholder behavior and includes alternatives to this framework if the actuary is unable to fully apply this principle.

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Actuarial certification of the work done to calculate reserves is required by the Guideline. A qualified actuary (referred to throughout the Guideline as "the actuary") shall certify that the work has been done in a way that meets all applicable Actuarial Standards of Practice.

For more details on the development of these requirements, including the development of the calibration criteria, see the American Academy of Actuaries recommendation on C-3 Phase II risk-based capital.

This Guideline and its Appendices require the actuary to make various determinations, verifications and certifications. The company shall provide the actuary with the necessary information sufficient to permit the actuary to fulfill the responsibilities set forth in this Guideline and its Appendices and responsibilities arising from applicable Actuarial Standards of Practice, including ASOP No. 23, *Data Quality*.

The risks reflected in the calculation of reserves under this Guideline arise from actual or potential events or activities which are both:

a) Directly related to the contracts falling under the scope of this Guideline or their supporting assets; and
b) Capable of materially affecting the reserve.

Categories and examples of risks reflected in the reserve calculations include but are not necessarily limited to:

a) Asset Risks
    (i) Separate Account fund performance;
    (ii) Credit risks (e.g., default or rating downgrades);
    (iii) Commercial mortgage loan rollover rates (roll-over of bullet loans);
    (iv) Uncertainty in the timing or duration of asset cash flows (e.g., shortening (prepayment risk) and lengthening (extension risk));
    (v) Performance of equities, real estate, and Schedule BA assets;
    (vi) Call risk on callable assets;
    (vii) Risk associated with hedge instrument (includes basis, gap, price, parameter estimation risks, and variation in assumptions); and
    (viii) Currency risk.
b) Liability Risks
    (i) Reinsurer default, impairment or rating downgrade known to have occurred before or on the valuation date;
    (ii) Mortality/longevity, persistency/lapse, partial withdrawal and premium payment risks;
    (iii) Utilization risk associated with guaranteed living benefits;
    (iv) Anticipated mortality trends based on observed patterns of mortality improvement or deterioration, where permitted;
    (v) Annuitization risks; and
    (vi) Additional premium dump-ins (high interest rate guarantees in low interest rate environments);
c) Combination Risks
    (i) Risks modeled in the company's risk assessment processes that are related to the contracts, as described above;
    (ii) Disintermediation risk (including such risk related to payment of surrender or partial withdrawal benefits); and
    (iii) Risks associated with Revenue Sharing Income.

The risks not necessarily reflected in the calculation of reserves under this Guideline are:

a) Those not reflected in the determination of Risk-Based Capital; and

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b) Those reflected in the determination of Risk-Based Capital but arising from obligations of the company not directly related to the contracts falling under the scope of this Guideline, or their supporting assets, as described above.

Categories and examples of risks not reflected in the reserve calculations include but are not necessarily limited to:

a) Asset Risks
Liquidity risks associated with a "run on the bank."

b) Liability Risks
(i) Reinsurer default, impairment or rating downgrade occurring after the valuation date;
(ii) Catastrophic events (e.g., epidemics or terrorist events);
(iii) Major breakthroughs in life extension technology that have not yet fundamentally altered recently observed mortality experience; and
(iv) Significant future reserve increases as an unfavorable scenario is realized.

c) General Business Risks
(i) Deterioration of reputation;
(ii) Future changes in anticipated experience (reparameterization in the case of stochastic processes) which would be triggered if and when adverse modeled outcomes were to actually occur;
(iii) Poor management performance;
(iv) The expense risks associated with fluctuating amounts of new business;
(v) Risks associated with future economic viability of the company;
(vi) Moral hazards; and
(vii) Fraud and theft.

Section II) Scope

A) The Guideline applies to contracts, whether directly written or assumed through reinsurance, falling into any of the following categories:

1) Variable deferred annuity contracts subject to the Commissioner's Annuity Reserve Valuation Method (CARVM), whether or not such contracts contain Guaranteed Minimum Death Benefits (GMDBs), or Variable Annuity Guaranteed Living Benefits (VAGLBs);

2) Variable immediate annuity contracts, whether or not such contracts contain GMDBs or VAGLBs;

3) Group annuity contracts that are not subject to CARVM, but contain guarantees similar in nature[4] to GMDBs, VAGLBs, or any combination thereof; and

4) All other products that contain guarantees similar in nature to GMDBs or VAGLBs, even if the insurer does not offer the mutual funds or variable funds to which these guarantees relate, where there is no other explicit reserve requirement.[5]

[4] The term "similar in nature," as used in sections II)A)3) and II)A)4) is intended to capture both current products and benefits as well as product and benefit designs that may emerge in the future. Examples of the currently known designs are listed in footnote #5 below. Any product or benefit design that does not clearly fit the Scope should be evaluated on a case-by-case basis taking into consideration factors that include, but are not limited to, the nature of the guarantees, the definitions of GMDB and VAGLB in sections III)A)1) and III)A)2) and whether the contractual amounts paid in the absence of the guarantee are based on the investment performance of a market-value fund or market-value index (whether or not part of the company's separate account).

[5] For example, a group life contract that wraps a GMDB around a mutual fund would generally fall under the scope of the Guideline since there is not an explicit reserve requirement for this type of group life contract. However, for an individual

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If such a benefit is offered as part of a contract that has an explicit reserve requirement and that benefit does not currently have an explicit reserve requirement:

a) The Guideline shall be applied to the benefit on a standalone basis (i.e., for purposes of the reserve calculation, the benefit shall be treated as a separate contract);

b) The reserve for the underlying contract is determined according to the explicit reserve requirement; and

c) The reserve held for the contract shall be the sum of a) and b).

B) The Guideline does not apply to contracts falling under the scope of the NAIC Model Modified Guaranteed Annuity Regulation (MGAs); however, it does apply to contracts listed above that include one or more subaccounts containing features similar in nature to those contained in MGAs (e.g., market value adjustments).

C) Separate account products that guarantee an index and do not offer GMDBs or VAGLBs are excluded from the scope of the Guideline.

Section III) Definitions

A) Definitions of Benefit Guarantees

1) Guaranteed Minimum Death Benefit (GMDB). A GMDB is a guaranteed benefit providing, or resulting in the provision that, an amount payable on the death of a contractholder, annuitant, participant, or insured will be increased and/or will be at least a minimum amount. Only such guarantees having the potential to produce a contractual total amount payable on death that exceeds the account value, or in the case of an annuity providing income payments, an amount payable on death other than continuation of any guaranteed income payments, are included in this definition. GMDBs that are based on a portion of the excess of the account value over the net of premiums paid less partial withdrawals made (e.g., an Earnings Enhanced Death Benefit) are also included in this definition.

2) Variable Annuity Guaranteed Living Benefit (VAGLB). A VAGLB is a guaranteed benefit providing, or resulting in the provision that, one or more guaranteed benefit amounts payable or accruing to a living contractholder or living annuitant, under contractually specified conditions (e.g., at the end of a specified waiting period, upon annuitization, or upon withdrawal of premium over a period of time), will increase contractual benefits should the contract value referenced by the guarantee (e.g., account value) fall below a given level or fail to achieve certain performance levels. Only such guarantees having the potential to provide benefits with a present value as of the benefit commencement date that exceeds the contract value referenced by the guarantee are included in this definition. Payout annuities without minimum payout or performance guarantees are neither considered to contain nor to be VAGLBs.

3) Guaranteed Minimum Income Benefit (GMIB). A GMIB is a VAGLB design for which the benefit is contingent on annuitization of a variable deferred annuity or similar contract. The benefit is typically expressed as a contractholder option, on one or more option dates, to have a minimum amount applied to provide periodic income using a specified purchase basis.

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variable life contract with a GMDB and a benefit similar in nature to a VAGLB, the Guideline would generally apply only to the VAGLB-type benefit, since there is an explicit reserve requirement that applies to the variable life contract and the GMDB.

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4) Guaranteed Payout Annuity Floor (GPAF). A GPAF is a VAGLB design guaranteeing that one or more of the periodic payments under a variable immediate annuity will not be less than a minimum amount.

B) Definitions of Reserve Methodology Terminology

1) Scenario. A scenario consists of a set of asset growth rates and investment returns from which assets and liabilities supporting a set of contracts may be determined for each year of a projection.

2) Cash Surrender Value. For purposes of the Guideline, the Cash Surrender Value for a contract is the amount available to the contractholder upon surrender of the contract. Generally, it is equal to the account value less any applicable surrender charges, where the surrender charge reflects the availability of any free partial surrender options. For contracts where all or a portion of the amount available to the contractholder upon surrender is subject to a market value adjustment, however, the Cash Surrender Value shall reflect the market value adjustment consistent with the required treatment of the underlying assets. That is, the Cash Surrender Value shall reflect any market value adjustments where the underlying assets are reported at market value, but shall not reflect any market value adjustments where the underlying assets are reported at book value.

3) Scenario Greatest Present Value. For a given scenario, the Scenario Greatest Present Value is the sum of:
   a) The greatest of the present values, as of the projection start date, of the projected Accumulated Deficiencies for the scenario; and
   b) The Starting Asset Amount, as defined below.

4) Conditional Tail Expectation Amount. The Conditional Tail Expectation Amount is equal to the numerical average of the 30 percent largest values of the Scenario Greatest Present Values.

5) Working Reserve. The Working Reserve is the assumed reserve used in the projections of Accumulated Deficiencies supporting the calculation of the Scenario Greatest Present Values. At any point in the projections, including at the start of the projection, the Working Reserve shall equal the projected Cash Surrender Value.

   For a variable payout annuity without a Cash Surrender Value, the Working Reserve shall equal the present value, at the valuation interest rate and the valuation mortality table specified for such a product by the Standard Valuation Law of future income payments projected using a return based on the valuation interest rate less appropriate asset based charges. For annuitizations that occur during the projection, the valuation interest rate as of the current valuation date may be used in determining the Working Reserve. Alternatively, if an integrated model of equity returns and interest rates is used, a future estimate of valuation interest rates may be incorporated into the Working Reserve.

   For contracts not covered above, the actuary shall determine the Working Reserve in a manner that is consistent with the above requirements.

6) Accumulated Deficiency. Accumulated Deficiency is an amount measured as of the end of a projection year and equals the projected Working Reserve less the amount of

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projected assets, both as of the end of the projection year. Accumulated Deficiencies may be positive or negative.[6]

7) Starting Asset Amount. The Starting Asset Amount equals the value of the assets at the start of the projection, as defined in section A1.4)A) of Appendix 1.

8) Prudent Estimate. The deterministic assumptions to be used for projections are to be the actuary's Prudent Estimate. This means that they are to be set at the conservative end of the actuary's confidence interval as to the true underlying probabilities for the parameter(s) in question, based on the availability of relevant experience and its degree of credibility.

A Prudent Estimate assumption is developed by applying a margin for uncertainty to the "Anticipated Experience" assumption. The margin for uncertainty shall provide for estimation error and margins for adverse deviation. The resulting Prudent Estimate assumption shall be reasonably conservative over the span of economic cycles and over a plausible range of expected experience, in recognition of the Principles described in Section I. "Anticipated Experience" would typically be the actuary's reasonable estimate of future experience for a risk factor given all available, relevant information pertaining to the contingencies being valued. Recognizing that assumptions are simply assertions of future unknown experience, the margin should be directly related to uncertainty in the underlying risk factor. The greater the uncertainty, the larger the margin. Each margin should serve to increase the Aggregate Reserve that would otherwise be held in its absence (i.e., using only the Anticipated Experience assumption).

For example, assumptions for circumstances that have never been observed require more margins for error than those for which abundant and relevant experience data are available.

This means that valuation assumptions not stochastically modeled are to be consistent with the stated Principles in Section I, be based on any relevant and credible experience that is available, and should be set to produce, in concert with other Prudent Estimate assumptions, a Conditional Tail Expectation Amount that is consistent with the stated CTE level.

The actuary shall follow the principles discussed in Appendices 9 and 10 in determining Prudent Estimate assumptions.

9) Gross Wealth Ratio. The Gross Wealth Ratio is the cumulative return for the indicated time period and percentile (e.g., 1.0 indicates that the index is at its original level).

10) Clearly Defined Hedging Strategy. The designation of Clearly Defined Hedging Strategy applies to strategies undertaken by a company to manage risks through the future purchase or sale of hedging instruments and the opening and closing of hedging positions. In order to qualify as a Clearly Defined Hedging Strategy, the strategy must meet the principles outlined in the Background section of the Guideline (particularly Principle 5) and shall, at a minimum, identify:
    a) The specific risks being hedged (e.g., delta, rho, vega, etc.),
    b) The hedge objectives,

[6] Note that a positive Accumulated Deficiency means that there is a cumulative loss and a negative Accumulated Deficiency means that there is a cumulative gain.

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c) The risks not being hedged (e.g., variation from expected mortality, withdrawal, and other utilization or decrement rates assumed in the hedging strategy, etc.),
d) The financial instruments that will be used to hedge the risks,
e) The hedge trading rules including the permitted tolerances from hedging objectives,
f) The metric(s) for measuring hedging effectiveness,
g) The criteria that will be used to measure effectiveness,
h) The frequency of measuring hedging effectiveness,
i) The conditions under which hedging will not take place, and
j) The person or persons responsible for implementing the hedging strategy.

The hedge strategy may be dynamic, static, or a combination thereof.

It is important to note that strategies involving the offsetting of the risks associated with variable annuity guarantees with other products outside of the scope of the Guideline (e.g., equity-indexed annuities) do not currently qualify as a Clearly Defined Hedging Strategy under the Guideline.

11) Revenue Sharing. Revenue Sharing, for purposes of the Guideline, means any arrangement or understanding by which an entity responsible for providing investment or other types of services makes payments to the company (or to one of its affiliates). Such payments are typically in exchange for administrative services provided by the company (or its affiliate), such as marketing, distribution and recordkeeping. Only payments that are attributable to charges or fees taken from the underlying variable funds or mutual funds supporting the contracts that fall under the scope of the Guideline shall be included in the definition of Revenue Sharing.

12) Domiciliary Commissioner. For purposes of the Guideline, this term refers to the chief insurance regulatory official of the state of domicile of the company.

13) Aggregate Reserve. The minimum reserve requirement as of the valuation date for the contracts falling within the scope of the Guideline.

14) 1994 Variable Annuity MGDB Mortality Table. This mortality table is shown in Appendix 11.

Section IV) Definition of General Reserve Methodology

A) General Description. The Aggregate Reserve for contracts falling within the scope of the Guideline shall equal the Conditional Tail Expectation Amount but not less than the Standard Scenario Amount, where the Aggregate Reserve is calculated as the Standard Scenario Amount plus the excess, if any, of the Conditional Tail Expectation Amount over the Standard Scenario Amount.

B) Impact of Reinsurance Ceded. Where reinsurance is ceded for all or a portion of the contracts, both components in the above general description (and thus the Aggregate Reserve) shall be determined net of any reinsurance treaties that meet the statutory requirements that would allow the treaty to be accounted for as reinsurance.

An Aggregate Reserve before reinsurance shall also be calculated if needed for regulatory reporting or other purposes, using methods described in Appendix 2.

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C) The Standard Scenario Amount. The Standard Scenario Amount is the aggregate of the reserves determined by applying the Standard Scenario method to each of the contracts falling within the scope of the Guideline. The Standard Scenario method is outlined in Appendix 3.

D) The Conditional Tail Expectation Amount. The Conditional Tail Expectation Amount shall be determined based on a projection of the contracts falling within the scope of the Guideline, and the assets supporting these contracts, over a broad range of stochastically generated projection scenarios and using Prudent Estimate assumptions.

The stochastically generated projection scenarios shall meet the Scenario Calibration Criteria described in Appendix 5.

The Conditional Tail Expectation Amount may be determined in aggregate for all contracts falling within the scope of the Guideline (i.e., a single grouping). At the option of the company, it may be determined by applying the methodology outlined below to sub-groupings of contracts, in which case, the Conditional Tail Expectation Amount shall equal the sum of the amounts computed for each such sub-grouping.

The Conditional Tail Expectation Amount shall be determined using the following steps:

1) For each scenario, projected aggregate Accumulated Deficiencies are determined at the start of the projection (i.e., "time 0") and at the end of each projection year as the sum of the Accumulated Deficiencies for each contract grouping.

2) The Scenario Greatest Present Value is determined for each scenario based on the sum of the aggregate Accumulated Deficiencies[7] and aggregate Starting Asset Amounts for the contracts for which the Aggregate Reserve is being computed.

3) The Scenario Greatest Present Values for all scenarios are then ranked from smallest to largest and the Conditional Tail Expectation Amount is the average of the largest 30 percent of these ranked values.

The projections shall be performed in accordance with Appendix 1. The actuary shall document the assumptions and procedures used for the projections and summarize the results obtained as described in Appendix 2 and Appendix 8.

E) Alternative Methodology. For variable deferred annuity contracts that contain either no guaranteed benefits or only GMDBs (i.e., no VAGLBs), the Conditional Tail Expectation Amount may be determined using the Alternative Methodology described in Appendix 4 rather than using the approach described in subsection D) above. However, in the event the approach described in subsection D) has been used in prior valuations the Alternative Methodology may not be used without approval from the Domiciliary Commissioner.

The Conditional Tail Expectation Amount for the group of contracts to which the Alternative Methodology is applied shall not be less than the aggregate Cash Surrender Value of those contracts.

The actuary shall document the assumptions and procedures used for the Alternative Methodology and summarize the results obtained as described in Appendix 2 and Appendix 8.

[7] The Scenario Greatest Present Value is therefore based on the greatest projected Accumulated Deficiency, in aggregate, for all contracts for which the Aggregate Reserve is computed hereunder, rather than based on the sum of the greatest projected Accumulated Deficiency for each grouping of contracts.

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F) Allocation of Results to Contracts. The Aggregate Reserve shall be allocated to the contracts falling within the scope of the Guideline using the method outlined in Appendix 6.

G) Reserve as of January 1, 2009. The reserve as of January 1, 2009 shall be the sum of the reserves from the asset adequacy analysis requirements in Actuarial Guideline XXXIV and Actuarial Guideline XXXIX.

Section V) Effective Date

The Guideline affects all contracts issued on or after January 1, 1981, effective December 31, 2009. Where the application of the Guideline produces higher reserves than the company had otherwise established by their previously used interpretation, such company may request a grade-in period, not to exceed three (3) years, from the Domiciliary Commissioner upon satisfactory demonstration of the previous interpretation and that such delay of implementation will not cause a hazardous financial condition or potential harm to its policyholders. The grading shall be done only on the reserves on the contracts in-force as of December 31, 2009. The reserves under the old basis and new basis shall be compared each year - 2/3 of the difference shall be subtracted from the reserve under the new basis in 2009 and 1/3 of the difference shall be subtracted from the reserve under the new basis in 2010.

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APPENDIX 1 - Determination of Conditional Tail Expectation Amount Based on Projections

A1.1) Projection of Accumulated Deficiencies

A) General Description of Projection. The projection of Accumulated Deficiencies shall be made ignoring Federal Income Tax and reflect the dynamics of the expected cash flows for the entire group of contracts, reflecting all product features, including the guarantees provided under the contracts. Insurance company expenses (including overhead and investment expense), fund expenses, contractual fees and charges, revenue sharing income received by the company (net of applicable expenses) and cash flows associated with any reinsurance or hedging instruments are to be reflected on a basis consistent with the requirements herein. Cash flows from any fixed account options shall also be included. Any market value adjustment assessed on projected withdrawals or surrenders shall also be included (whether or not the Cash Surrender Value reflects market value adjustments). Throughout the projection, where estimates are used, such estimates shall be on a Prudent Estimate basis.

Federal Income Tax shall not be included in the projection of Accumulated Deficiencies.

B) Grouping of Variable Funds and Subaccounts. The portion of the Starting Asset Amount held in the Separate Account represented by the variable funds and the corresponding account values may be grouped for modeling using an approach that recognizes the investment guidelines and objectives of the funds. In assigning each variable fund and the variable subaccounts to a grouping for projection purposes, the fundamental characteristics of the fund shall be reflected and the parameters shall have the appropriate relationship to the required calibration points of the S&P 500. The grouping shall reflect characteristics of the efficient frontier (i.e., returns generally cannot be increased without assuming additional risk).

An appropriate proxy for each variable subaccount shall be designed in order to develop the investment return paths. The development of the scenarios for the proxy funds is a fundamental step in the modeling and can have a significant impact on results. As such, the actuary must map each variable account to an appropriately crafted proxy fund normally expressed as a linear combination of recognized market indices (or sub-indices).

C) Grouping of Contracts. Projections may be performed for each contract inforce on the date of valuation or by grouping contracts into representative cells of model plans using all characteristics and criteria having a material impact on the size of the reserve. Grouping shall be the responsibility of the actuary but may not be done in a manner that intentionally understates the resulting reserve.

D) Modeling of Hedges. The appropriate costs and benefits of hedging instruments that are currently held by the company in support of the contracts falling under the scope of the Guideline shall be included in the projections. If the company is following a Clearly Defined Hedging Strategy and the hedging strategy meets the requirements of Appendix 7, the projections shall take into account the appropriate costs and benefits of hedge positions expected to be held in the future through the execution of that strategy.

To the degree either the currently held hedge positions or the hedge positions expected to be held in the future introduce basis, gap, price, or assumption risk, a suitable reduction for effectiveness of hedges shall be made. The actuary is responsible for verifying compliance with a Clearly Defined Hedging Strategy and the requirements in Appendix 7 for all hedge instruments included in the projections.

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While hedging strategies may change over time, any change in hedging strategy shall be documented and include an effective date of the change in strategy.

The use of products not falling under the scope of the Guideline (e.g., equity-indexed annuities) as a hedge shall not be recognized in the determination of Accumulated Deficiencies.

These requirements do not supersede any statutes, laws, or regulations of any state or jurisdiction related to the use of derivative instruments for hedging purposes and should not be used in determining whether a company is permitted to use such instruments in any state or jurisdiction.

Upon request of the company's domiciliary commissioner and for information purposes to show the effect of including future hedge positions in the projections, the company shall show the results of performing an additional set of projections reflecting only the hedges currently held by the company in support of the contracts falling under the scope of the Guideline. Because this additional set of projections excludes some or all of the derivative instruments, the investment strategy used may not be the same as that used in the determination of the Conditional Tail Expectation Amount.

E) Revenue Sharing.

1) Projections of Accumulated Deficiencies may include income from projected future Revenue Sharing, as defined in Section III) net of applicable projected expenses ("Net Revenue Sharing Income") if the following requirements are met:
   a) The Net Revenue Sharing Income is received[8] by the company,[9]
   b) Signed contractual agreement or agreements are in place as of the valuation date and support the current payment of the Net Revenue Sharing Income; and
   c) The Net Revenue Sharing Income is not already accounted for directly or indirectly as a company asset.

2) The amount of Net Revenue Sharing Income to be used shall reflect the actuary's assessment of factors that include but are not limited to the following (not all of these factors will necessarily be present in all situations):
   a) The terms and limitations of the agreement(s), including anticipated revenue, associated expenses and any contingent payments incurred or made by either the company or the entity providing the Net Revenue Sharing as part of the agreement(s);
   b) The relationship between the company and the entity providing the Net Revenue Sharing Income that might affect the likelihood of payment and the level of expenses;
   c) The benefits and risks to both the company and the entity paying the Net Revenue Sharing Income of continuing the arrangement.

[8] For purposes of this section, Net Revenue Sharing Income is considered to be received by the company if it is paid directly to the company through a contractual agreement with either the entity providing the Net Revenue Sharing Income or an affiliated company that receives the Net Revenue Sharing Income. Net Revenue Sharing Income would also be considered to be received, if it is paid to a subsidiary that is owned by the company and if 100% of the statutory income from that subsidiary is reported as statutory income of the company. In this case the actuary needs to assess the likelihood that future Net Revenue Sharing Income is reduced due to the reported statutory income of the subsidiary being less than future Net Revenue Sharing Income received.

[9] As in other sections of the Guideline, the term "the company" is used exclusively as a reference to the insurance company writing the business falling under the scope of the Guideline. The term "entity providing the Net Revenue Sharing Income" is self-explanatory and is used consistently in this subsection.

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d) The likelihood that the company will collect the Net Revenue Sharing Income during the term(s) of the agreement(s) and the likelihood of continuing to receive future revenue after the agreement(s) has ended;

e) The ability of the company to replace the services provided to it by the entity providing the Net Revenue Sharing Income or to provide the services itself, along with the likelihood that the replaced or provided services will cost more to provide; and

f) The ability of the entity providing the Net Revenue Sharing Income to replace the services provided to it by the company or to provide the services itself, along with the likelihood that the replaced or provided services will cost more to provide.

3) The amount of projected Net Revenue Sharing Income shall also reflect a margin (which decreases the assumed Net Revenue Sharing Income) directly related to the uncertainty of the revenue. The greater the uncertainty, the larger the margin. Such uncertainty is driven by many factors including the potential for changes in the securities laws and regulations, mutual fund board responsibilities and actions, and industry trends. Since it is prudent to assume that uncertainty increases over time, a larger margin shall be applied as time that has elapsed in the projection increases.

4) All expenses required or assumed to be incurred by the company in conjunction with the arrangement providing the Net Revenue Sharing Income, as well as any expenses assumed to be incurred by the company in conjunction with the assumed replacement of the services provided to it (as discussed in subsection 2)e) above) shall be included in the projections as a company expense under the requirements of section A1.1)A). In addition, expenses incurred by either the entity providing the Net Revenue Sharing Income or an affiliate of the company shall be included in the applicable expenses discussed in section A1.1)A) and A1.1)E)1) that reduce the Net Revenue Sharing Income.

5) The actuary is responsible for reviewing the revenue sharing agreements, verifying compliance with these requirements, and documenting the rationale for any source of Net Revenue Sharing Income used in the projections.

6) The amount of Net Revenue Sharing Income assumed in a given scenario shall not exceed the sum of a) and b), where:

a) Is the contractually guaranteed Net Revenue Sharing Income projected under the scenario, and

b) Is the actuary's estimate of non-contractually guaranteed Net Revenue Sharing Income before reflecting any margins for uncertainty multiplied by the following factors:

(i) 1.0 in the first projection year;
(ii) 0.9 in the second projection year;
(iii) 0.8 in the third projection year;
(iv) 0.7 in the fourth projection year;
(v) 0.6 in the fifth projection year;
(vi) 0.5 in the sixth and all subsequent projection years. The resulting amount of non-contractually guaranteed Net Revenue Sharing Income after application of this factor shall not exceed 0.25% per year on separate account assets in the sixth and all subsequent projection years.

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F) Length of Projections. Projections of Accumulated Deficiencies shall be run for as many future years as needed so that no materially greater reserve value would result from longer projection periods.

G) AVR/IMR. The AVR and the IMR shall be handled consistently with the treatment in the company's cash flow testing.

A1.2) Determination of Scenario Greatest Present Values

A) Scenario Greatest Present Values. For a given scenario, the Scenario Greatest Present Value is the sum of:

1) The greatest present value, as of the projection start date, of the projected Accumulated Deficiencies defined in Section III)B)6); and

2) The Starting Asset Amount.

B) Discount Rates. In determining the Scenario Greatest Present Values, Accumulated Deficiencies shall be discounted using the same interest rates at which positive cash flows are invested, as determined in section A1.4)D). Such interest rates shall be reduced to reflect expected credit losses. Note that the interest rates used do not include a reduction for Federal Income Taxes.

A1.3) Projection Scenarios

A) Minimum Required Scenarios. The number of scenarios for which projected greatest present values of Accumulated Deficiencies shall be computed shall be the responsibility of the actuary and shall be considered to be sufficient if any resulting understatement in total reserves, as compared with that resulting from running additional scenarios, is not material.

B) Scenario Calibration Criteria. Returns for the groupings of variable funds shall be determined on a stochastic basis such that the resulting distribution of the Gross Wealth Ratios of the scenarios meets the Scenario Calibration Criteria specified in Appendix 5.

A1.4) Projection Assets

A) Starting Asset Amount. For the projections of Accumulated Deficiencies, the value of assets at the start of the projection shall be set equal to the approximate value of statutory reserves at the start of the projection. Assets shall be valued consistently with their annual statement values. The amount of such asset values shall equal the sum of the following items, all as of the start of the projection:

1) All of the Separate Account assets supporting the contracts;

2) An amount of assets held in the General Account equal to the approximate value of statutory reserves as of the start of the projections less the amount in 1), above.

In many instances the initial General Account assets may be negative, resulting in a projected interest expense. General Account assets chosen for use as described above shall be selected on a consistent basis from one reserve valuation hereunder to the next.

Any hedge assets meeting the requirements described in section A1.1)D) shall be reflected in the projections and included with other General Account assets under item 2) above. To the extent the sum of the value of such hedge assets and the value of assets in item 1) above is greater than

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the approximate value of statutory reserves as of the start of the projections, then item 2) above may include enough negative General Account assets or cash such that the sum of items 1) and 2) above equals the approximate value of statutory reserves as of the start of the projections.[10]

The actuary shall document which assets were used as of the start of the projection, the approach used to determine which assets were chosen and shall verify that the value of the assets equals the approximate value of statutory reserves at the start of the projection.

B) Valuation of Projected Assets. For purposes of determining the projected Accumulated Deficiencies, the value of projected assets shall be determined in a manner consistent with their value at the start of the projection. For assets assumed to be purchased during a projection, the value shall be determined in a manner consistent with the value of assets at the start of the projection that have similar investment characteristics.

C) Separate Account Assets. For purposes of determining the Starting Asset Amounts in subsection A) and the valuation of projected assets in subsection B), assets held in a Separate Account shall be summarized into asset categories determined by the actuary as discussed in section A1.1)B).

D) General Account Assets. General Account assets shall be projected, net of projected defaults, using assumed investment returns consistent with their book value and expected to be realized in future periods as of the date of valuation. Initial assets that mature during the projection and positive cash flows projected for future periods shall be invested at interest rates, which, at the option of the actuary, are one of the following:

1) The forward interest rates implied by the swap curve[11] in effect as of the valuation date,

2) The 200 interest rate scenarios available as prescribed for Phase I, C-3 Risk Based Capital calculation, coupled with the Separate Account return scenarios by mating them up with the first 200 such scenarios and repeating this process until all Separate Account return scenarios have been mated with a Phase I scenario, or

3) Interest rates developed for this purpose from a stochastic model that integrates the development of interest rates and the Separate Account returns.

When the option described in 1) above (the forward interest rates implied by the swap curve) is used, an amount shall be subtracted from the interest rates to reflect the current market expectations about future interest rates using the process described in section A1.5)A).

The actuary may switch from 1) to 2), from 1) to 3) or from 2) to 3) from one valuation date to the next, but may not switch in the other direction without approval from the Domiciliary Commissioner.

A1.5) Projection of Annuitization Benefits (including GMIBs)

A) Assumed Annuitization Purchase Rates at Election. For purposes of projecting annuitization benefits (including annuitizations stemming from the election of a GMIB), the projected annuitization purchase rates shall be determined assuming that market interest rates available at the time of election are the interest rates used to project General Account Assets, as determined in

[10] Further elaboration on potential practices with regard to this issue may be included in a practice note.

[11] The swap curve is based on the Federal Reserve H.15 interest swap rates. The rates are for a Fixed Rate Payer in return for receiving three month LIBOR. One place where these rates can be found is *http://www.federalreserve.gov/releases/h15/default.htm*.

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A1.4)D). However, where the interest rates used to project General Account Assets are based upon the forward interest rates implied by the swap curve in effect as of the valuation date (i.e., the option described in section A1.4)D)1) is used, herein referred to as a point estimate), the margin between the cost to purchase an annuity using the guaranteed purchase basis and the cost using the interest rates prevailing at the time of annuitization shall be adjusted as discussed below.

If a point estimate is being used, it is important that the margin assumed reflects the current market expectations about future interest rates at the time of annuitization, as described more fully below, and a downward adjustment to the interest rate assumed in the purchase rate basis. The latter adjustment is necessary since a greater proportion of contractholders will select an annuitization benefit when it is worth more than the cash surrender value then when it is not. As a practical matter, this effect can be approximated by using an interest rate assumption in the purchase rate basis that is 0.30 percent below that implied by the forward swap curve, as described below.

To calculate market expectations of future interest rates, the par or current coupon swap curve is used (documented daily in Federal Reserve H.15 with some interpolation needed). Deriving the expected rate curve from this swap curve at a future date involves the following steps:

1) Calculate the implied zero-coupon rates. This is a well documented "bootstrap" process. For this process we use the equation $100=C^n * (v + v^2 + \ldots + v^n) + 100v^n$ where the "v^t" terms are used to stand for the discount factors applicable to cash flows 1,2,…n years hence and C^n is the n-year swap rate. Each of these discount factors are based on the forward curve and therefore are based on different rates, however (i.e. "v^2" does not equal v times v). Given the one year swap rate, one can solve for v. Given v and the two year swap rate one can then back into v^2, and so on.

2) Convert the zero coupon rates to one year forward rates by calculating the discount factor needed to get from v^{t-1} to v^t.

3) Develop the expected rate curve.

   This recognizes that, for example, the five-year forward one-year rate is not the rate the market expects on one year instruments five years from now. The reason is that as the bond gets shorter the "risk premium" in the rate diminishes. This is sometimes characterized as "rolling down" the yield curve. Table A shows the historic average risk premium at various durations. From this table, one can see that to get the rate the market expects a 1 year swap to have five years from now; one must subtract the risk premium associated with six year rates (.95%) and add back that associated with 1 year rates (.50%). This results in a net reduction of .45%.

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Table A: Risk Premium by Duration

Duration	Risk Premium	Duration	Risk Premium
1	0.500%	6	0.950%
2	0.750%	7	1.000%
3	0.750%	8	1.100%
4	0.850%	9+	1.150%
5	0.900%		

The Exhibit below combines the three steps. Columns A through D convert the swap curve to the implied forward rate for each future payment date. Columns E through H remove the current risk premium, add the risk premium t years in the future (the Exhibit shows the rate curve five years in the future), and uses that to get the discount factors to apply to the 1 year, 2 year,…5 year cash flows 5 years from now.

Exhibit: Derivation of discount rates expected in the future

A	B	C	D	E	F	G	H
Projection Years	Swap Curve Rate	PV of Zero Coupon	Forward 1 Year Rate	Risk Premium	Risk Premium 5 Years Out	Expected Forward Rate In 5 Years	PV of Zero Coupon In 5 Years
1	2.57%	0.97494	2.5700%	0.50000%			
2	3.07%	0.94118	3.5879%	0.75000%			
3	3.44%	0.90302	4.2251%	0.75000%			
4	3.74%	0.86231	4.7208%	0.85000%			
5	3.97%	0.82124	5.0010%	0.90000%			
6	4.17%	0.77972	5.3249%	0.95000%	0.50000%	4.8749%	0.95352
7	4.34%	0.73868	5.5557%	1.00000%	0.75000%	5.3057%	0.90547
8	4.48%	0.69894	5.6860%	1.10000%	0.75000%	5.3360%	0.85961
9	4.60%	0.66050	5.8209%	1.15000%	0.85000%	5.5209%	0.81463
10	4.71%	0.62303	6.0131%	1.15000%	0.90000%	5.7631%	0.77024
Cell formulas for Projection Year 10:		=(1-B13*SUM(C4:C12))/(1+B13)	=C12/C13-1		=E8	=D13-E13+F13	=H12/(1+G13)

Where interest rates are projected stochastically using an integrated model, although one would "expect" the interest rate n years hence to be that implied for an appropriate duration asset by the forward swap curve as described above, there is a steadily widening confidence interval about that point estimate with increasing time until the annuitization date. The "expected margin" in the

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purchase rate is less than that produced by the point estimate based on the expected rate, since a greater proportion of contractholders will have an annuitization benefit whose worth is in excess of cash surrender value when margins are low than when margins are high. As a practical matter, this effect can be approximated by using a purchase rate margin based on an earnings rate .30 percent below that implied by the forward swap curve. If a stochastic model of interest rates is used instead of a point estimate then no such adjustment is needed.

B) Projected Election of Guaranteed Minimum Income Benefit and other Annuitization Options. For contracts projected to elect annuitization options (including annuitizations stemming from the election of a GMIB), the projections may assume one of the following at the actuary's option:

1) The contract is treated as if surrendered at an amount equal to the statutory reserve that would be required at such time for the payout annuity benefits, or

2) The contract is assumed to stay inforce, the projected periodic payments are paid, and the Working Reserve is equal to one of the following:
   a) The statutory reserve required for the payout annuity, if it is a fixed payout annuity, or
   b) If it is a variable payout annuity, the Working Reserve for a variable payout annuity as defined in Section III)B)5).

If the projected payout annuity is a variable payout annuity containing a floor guarantee (such as a GPAF) under a specified contractual option, only option 2) above shall be used.

Where mortality improvement is used to project future annuitization purchase rates, as discussed in A) above, mortality improvement shall also be reflected on a consistent basis in either the determination of the reserve in 1) above or the projection of the periodic payments in 2) above.

A1.6) Relationship to Risk Based Capital Requirements

A) The Guideline anticipates that the projections described herein may be used for the determination of Risk Based Capital (the "RBC requirements") for some or all of the contracts falling within the scope of the Guideline. There are several differences between the requirements of the Guideline and the RBC requirements, and among them are two major differences. First, the Conditional Tail Expectation level is different (CTE (70) for the Guideline and CTE (90) for the RBC requirements). Second, the projections described in the Guideline are performed on a basis that ignores Federal Income Tax. That is, under the Guideline, the Accumulated Deficiencies do not include projected Federal Income Tax and the interest rates used to discount the Scenario Greatest Present Value (i.e., the interest rates determined in section A1.4)D)) contain no reduction for Federal Income Tax. Under the RBC requirements, the projections do include projected Federal Income Tax and the discount interest rates used in the RBC requirement do contain a reduction for Federal Income Tax.

B) To further aid the understanding of the Guideline and any instructions relating to the RBC requirement, it is important to note the equivalence in meaning between the following terms, subject to the differences noted above:

1) The amount that is added to the Starting Asset Amount in Section III)B)6) of the Guideline is similar to the Additional Asset Requirement referenced in the RBC requirement.

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2) The Conditional Tail Expectation Amount referenced in the Guideline is similar to the Total Asset Requirement referenced in the RBC requirement.

A1.7) Compliance with Actuarial Standards of Practice (ASOPs)

When determining the Conditional Tail Expectation Amount using projections, the analysis shall conform to the Actuarial Standards of Practice as promulgated from time to time by the Actuarial Standards Board.

A1.8) Compliance with Principles

When determining the Conditional Tail Expectation Amount using projections, any interpretation and application of the requirements of the Guideline shall follow the principles discussed in the Section I) Background.

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APPENDIX 2 - Reinsurance and Statutory Reporting Issues

A2.1) Treatment of Reinsurance Ceded in the Aggregate Reserve

A) Aggregate Reserve Net of and Prior to Reinsurance Ceded. As noted in Section IV)B), the Aggregate Reserve is determined net of reinsurance ceded. Therefore, it is necessary to determine the components needed to determine the Aggregate Reserve (i.e., the Standard Scenario Amount, and either the Conditional Tail Expectation Amount determined using projections or the Conditional Tail Expectation Amount determined using the Alternative Methodology) on a net of reinsurance basis. In addition, as noted in Section IV)B), it may be necessary to determine the Aggregate Reserve determined on a "direct" basis, or prior to reflection of reinsurance ceded. Where this is needed, each of these components shall be determined prior to reinsurance. Sections B) through D) below discuss methods necessary to determine these components on both a "net of reinsurance" and a "prior to reinsurance" basis. Note that due allowance for reasonable approximations may be used where appropriate.

B) Conditional Tail Expectation Amount Determined using Projections. In order to determine the Aggregate Reserve net of reinsurance ceded, Accumulated Deficiencies, Scenario Greatest Present Values, and the resulting Conditional Tail Expectation Amount shall be determined reflecting the effects of reinsurance treaties that meet the statutory requirements that would allow the treaty to be accounted for as reinsurance within the projections. This involves including, where appropriate, all anticipated reinsurance premiums or other costs and all reinsurance recoveries, where both premiums and recoveries are determined by recognizing any limitations in the reinsurance treaties, such as caps on recoveries or floors on premiums.

In order to determine the Conditional Tail Expectation Amount prior to reinsurance ceded, Accumulated Deficiencies, Scenario Greatest Present Values, and the resulting Conditional Tail Expectation Amount shall be determined ignoring the effects of reinsurance within the projections. One acceptable approach involves a projection based on the same Starting Asset Amount as for the Aggregate Reserve net of reinsurance and by ignoring, where appropriate, all anticipated reinsurance premiums or other costs and all reinsurance recoveries in the projections.

C) Conditional Tail Expectation Amount Determined using the Alternative Methodology. If a company chooses to use the Alternative Methodology, as allowed in Section IV)E), it is important to note that the methodology produces reserves on a prior to reinsurance ceded basis. Therefore, where reinsurance is ceded, the Alternative Methodology must be modified to reflect the reinsurance costs and reinsurance recoveries under the reinsurance treaties in the determination of the Aggregate Reserve net of reinsurance. In addition, the Alternative Methodology, unadjusted for reinsurance, shall be applied to the contracts falling under the scope of the Guideline to determine the Aggregate Reserve prior to reinsurance.

D) Standard Scenario Amount. Where reinsurance is ceded, the Standard Scenario Amount shall be calculated as described in Appendix 3 to reflect the reinsurance costs and reinsurance recoveries under the reinsurance treaties. If it is necessary, the Standard Scenario Amount shall be calculated prior to reinsurance ceded using the methods described in Appendix 3, but ignoring the effects of the reinsurance ceded.

A.2.2) Aggregate Reserve to be held in the General Account

The amount of the reserve held in the General Account shall not be less than the excess of the Aggregate Reserve over the sum of the Basic Reserve, as defined in section A3.2), attributable to the variable portion of all such contracts.

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A.2.3) Actuarial Certification and Memorandum

A) Actuarial Certification. Actuarial Certification of the work done to determine the Aggregate Reserve shall be required. The actuary shall certify that the work performed has been done in a way that substantially complies with all applicable Actuarial Standards of Practice. The scope of this certification does not include an opinion on the adequacy of the Aggregate Reserve,[12] the company's surplus or the company's future financial condition. The actuary shall also note any material change in the model or assumptions from that used previously and the estimated impact of such changes.

Appendix 8 contains more information on the contents of the required Actuarial Certification.

B) Required Memorandum. An actuarial memorandum shall be constructed documenting the methodology and assumptions upon which the Aggregate Reserve is determined. The memorandum shall also include sensitivity tests that the actuary feels appropriate, given the composition of the company's block of business (i.e., identifying the key assumptions that, if changed, produce the largest changes in the Aggregate Reserve). This memorandum shall have the same confidential status as the actuarial memorandum supporting the actuarial opinion[13] and shall be available to regulators upon request.

Appendix 8 contains more information on the contents of the required memorandum.

C) Conditional Tail Expectation Amount Determined using the Alternative Methodology. Where the Alternative Methodology is used, there is no need to discuss the underlying assumptions and model in the required memorandum. Certification that expense, revenue, fund mapping, and product parameters have been properly reflected, however, shall be required.

Appendix 8 contains more information on the contents of the required Actuarial Certification and memorandum.

D) Material Changes. If there is a material change in results due to a change in assumptions from the previous year, the memorandum shall include a discussion of such change in assumptions and an estimate of the impact it has on the results.

[12] The adequacy of total company reserves, which includes the Aggregate Reserve, is addressed in the company's Actuarial Opinion as required by the NAIC Model Actuarial Opinion and Memorandum Regulation.

[13] This is consistent with Section 3D(8) of the Standard Valuation Law, which states: "Except as provided in Paragraphs (12), (13) and (14), documents, materials or other information in the possession or control of the Department of Insurance that are a memorandum in support of the opinion, and any other material provided by the company to the commissioner in connection with the memorandum, shall be confidential by law and privileged, shall not be subject to [insert open records, freedom of information, sunshine or other appropriate phrase], shall not be subject to subpoena, and shall not be subject to discovery or admissible in evidence in any private civil action. However, the commissioner is authorized to use the documents, materials or other information in the furtherance of any regulatory or legal action brought as a part of the commissioner's official duties."

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APPENDIX 3 - Standard Scenario Requirements

A3.1) Overview

A) Application to Determine Reserves. A Standard Scenario Reserve shall be determined for each of the contracts falling under the scope of the Guideline by applying section A3.3). This includes those contracts to which the Alternative Methodology is applied.

The Standard Scenario Reserve for a contract with guaranteed living benefits or guaranteed death benefits is based on a projection of the account value based on specified returns for supporting assets equal to the account value. An initial drop is applied to the supporting assets and account value on the valuation date. Subsequently, account values are projected at specified rates earned by the supporting assets less contract and fund charges. The assumptions for the projection of account values and margins are prescribed in section A3.3)C). For any contract with guarantees the Standard Scenario Reserve includes the greatest present value of the benefit payments in excess of account values applied over the present value of revenue produced by the margins.

B) The Standard Scenario Amount

1) The Standard Scenario Amount is defined in Section IV)C) of this Guideline as the aggregate of the reserves determined by applying the Standard Scenario Method to each of the contracts falling under the scope of the Guideline. Except as provided in subsection A3.3)B)1), the Standard Scenario Amount equals the sum over all contracts of the Standard Scenario Reserve determined for each contract as of the statement date as described in A3.1)B)2).

2) The Standard Scenario Method requires the Standard Scenario Amount to not be less than the sum over all contracts of the Standard Scenario Reserve determined for the contract as of the statement date as described in section A3.3), where the Discount Rate is equal to *DR*, which is defined as the valuation interest rate specified by the Standard Valuation Law for annuities valued on an issue year basis, using Plan Type A and a Guarantee Duration greater than 10 years but not more than 20 years. The presence of guarantees of interest on future premiums and/or cash settlement options is to be determined using the terms of the contracts.

C) Illustrative Application of the Standard Scenario to a Projection or Model Office. If the Conditional Tail Expectation Amount is determined based on a projection of an inforce prior to the statement date and/or by the use of a model office, which is a grouping of contracts into representative cells, then additional determinations of A3.1)B)2) shall be performed on the prior inforce and/or model office. The calculations are for illustrative purposes to assist in validating the reasonableness of the projection and/or the model office.

The following table identifies the illustrative additional determinations required by this section using the Discount Rate, *DR*, as defined in A3.1)B)2). The additional determinations required are based on how the Conditional Tail Expectation projection or Alternative Methodology is applied. For completeness, the table also includes the determinations required by section A3.1)B)2).

1) Run A in the table is required for all companies by section A3.1)B)2). No additional determinations are required if a company's stochastic or alternative methodology result is calculated on individual contracts as of the statement date.

2) A company that uses a model office as of the statement date to determine its stochastic or alternative methodology result must provide an additional determination for the model office based on the Discount Rate *DR*, run B.

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3) A company that uses a contract by contract listing of a prior inforce to determine its stochastic or alternative methodology with result PS and then projects requirements to the statement date with result S must provide an additional determination for the prior inforce based on the Discount Rate *DR*, run C.

4) A company that uses a model office of a prior inforce to determine its stochastic or alternative methodology requirements with result PM and then projects requirements to the statement date with result S must provide an additional determination for the prior model office based on the Discount Rate *DR*, run D.

Standard Scenario Run	Guideline Variations	Validation Measures	
		Model Office Projection	Projection of Prior Inforce
A. Valuation on the statement date on inforce contracts with discount rate *DR*	None	None	None
B. Valuation on the statement date on the model office with discount rate *DR*	If not material to model office validation	A/B compare to 1.00	None
C. Valuation on a prior inforce date on prior inforce contracts with discount rate *DR*	If not material to projection validation	None	A/C - S/PS compare to 0
D. Valuation on a prior inforce date on a model office with discount rate *DR*	If not material to model office or projection validation.	(A/D – S/PM) compare to 0	

Modification of the requirements in section A3.3) when applied to a prior inforce or a model office is permitted if such modification facilitates validating the projection of inforce or the model office. All such modifications should be documented.

A3.2) Basic and Basic Adjusted Reserve - Application of Actuarial Guideline XXXIII

A) The Basic Reserve for a given contract shall be determined by applying statutory statement valuation requirements applicable immediately prior to adoption of the Guideline to the contract ignoring any guaranteed death benefits in excess of account values or guaranteed living benefits applying proceeds in excess of account values.

B) The calculation of the Basic Reserve shall assume a return on separate account assets based on the year of issue statutory valuation rate less appropriate asset based charges, including charges for any guaranteed death benefits or guaranteed living benefits. It shall also assume a return for any fixed separate account and general account options equal to the rates guaranteed under the contract.

C) The Basic Reserve shall be no less than the Cash Surrender Value on the valuation date, as defined in Section III)B) of the Guideline.

D) The Basic Adjusted Reserve shall be that determined based on A3.2)A) and A3.2)B) except in A3.2)A) free partial withdrawal provisions shall be disregarded when determining surrender charges in applying the statutory statement valuation requirement prior to adoption of the Guideline. Section A3.2)C) shall not apply to the Basic Adjusted Reserve.

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A3.3) Standard Scenario Reserve - Application of the Standard Scenario Method

A) General. Where not inconsistent with the guidance given here, the process and methods used to determine the Standard Scenario Reserve under the Standard Scenario Method shall be the same as required in the calculation of the Conditional Tail Expectation Amount as described in Section IV) of the Guideline. Any additional assumptions needed to determine the Standard Scenario Reserve shall be explicitly documented.

B) Results for the Standard Scenario Method. For each contract, the Standard Scenario Reserve is the reserve based on 1) or 2) where:

1) For contracts without any guaranteed benefits, as defined in Section III)A) of the Guideline and where not subsequently disapproved by the Domiciliary Commissioner, the Standard Scenario Reserve is the Basic Reserve described in section A3.2)A), A3.2)B) and A3.2)C).

2) For all other contracts the Standard Scenario Reserve is equal to the greater of Cash Surrender Value on the valuation date, as defined in Section III)B) of the Guideline, and the quantity a) + b) - c), where:
   a) Is the Basic Adjusted Reserve calculated for the contract, as described in section A3.2)D);
   b) Is the greater of zero and the greatest present value at the Discount Rate measured as of the end of each projection year of the negative of the Accumulated Net Revenue described below using the assumptions described in A3.3)C). The Accumulated Net Revenue at the end of a projection year is equal to (i) + (ii) - (iii), where:
      (i) Is the Accumulated Net Revenue at the end of the prior projection year accumulated at the Discount Rate to the end of the current projection year; the Accumulated Net Revenue at the beginning of the projection (i.e., time 0) is zero;
      (ii) Are the margins generated during the projection year on account values accumulated at the Discount Rate to the end of the projection year (the factors and assumptions to be used in calculating the margins and account values are in A3.3)C)); and
      (iii) Are the contract benefits in excess of account values applied, Individual reinsurance premiums and Individual reinsurance benefits payable or receivable during the projection year accumulated at the Discount Rate to the end of the projection year. Individual reinsurance is defined in A3.3)C)2).
   c) Is the contract's allocation of the value of hedges and Aggregate reinsurance as described in section A3.3)D). Aggregate reinsurance is defined in section A3.3)C)2).

No reinsurance shall be considered in the Standard Scenario Amount if such reinsurance does not meet the statutory requirements that would allow the treaty to be accounted for as reinsurance. The actuary shall determine the projected reinsurance premiums and benefits reflecting all treaty limitations and assuming any options in the treaty to the other party are exercised to decrease the value of reinsurance to the reporting company (e.g., options to increase premiums or terminate coverage). The positive value of any reinsurance treaty that is not guaranteed to the insurer or its successor shall be excluded from the value of reinsurance. The commissioner may require the exclusion of a reinsurance treaty or any portion of a reinsurance treaty if the terms of the

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reinsurance) treaty or the portion required to be excluded serves solely to reduce the calculated Standard Scenario Reserve without also reducing risk on scenarios similar to those used to determine the Conditional Tail Expectation Reserve. Any reinsurance reflected in the Standard Scenario Reserve shall be appropriate to the business and not merely constructed to exploit 'foreknowledge' of the components of the Standard Scenario Method.

C) Assumptions for use in paragraph A3.3)B)2)b) for Accumulated Net Revenue and Account Values.

1) Account Value Return Assumptions. The bases for return assumptions on assets supporting the Account Value are shown in Table I. The "Initial" returns shall be applied to the account value supported by each asset class on the valuation date as immediate drops, resulting in the Account Value at time 0. The "Year 1," "Years 2 – 5," and "Year 6+" returns for the equity, bond and balanced classes are gross annual effective rates of return and are used (along with other decrements and/or increases) to produce the Account Value as of the end of each projection interval. For purposes of this section, money market funds supporting Account Value shall be considered part of the Bond class.

The Fixed Fund rate is the greater of the minimum rate guaranteed in the contract or 4% but not greater than the current rates being credited to Fixed Funds on the valuation date.

Account Values shall be projected using the appropriate gross rates from Table I for equity, bond and balanced classes applied to the supporting assets less all fund and contract charges according to the provisions of the funds and contract and applying the Fixed funds rate from Table I as if it were the resulting net rate after deduction for fund or contract charges.

The annual margins on Account Value are defined as follows:

a) During the Surrender Charge Amortization Period, as determined following the step outlined in section A3.3)E) below:
   (i) 0.20% of Account Value; plus
   (ii) Any Net Revenue Sharing Income, as defined in section A1.1)E), that is contractually guaranteed to the insurer and its liquidator, receiver, and statutory successor; plus
   (iii) For all of the guaranteed living benefits of a given contract combined,[14] the greater of:
      - 0.20% of Account Value; or
      - Explicit and optional contract charges for guaranteed living benefits; plus
   (iv) For all guaranteed death benefits of a given contract combined,[15] the greater of:
      - 0.20% of Account Value; or
      - Explicit and optional contract charges for guaranteed death benefits.

b) After the Surrender Charge Amortization Period:

[14] This excludes any guaranteed living benefit that is added to the contract simply for the purpose of increasing the revenue allowed under this section.

[15] This excludes any guaranteed death benefit that is added to the contract simply for the purpose of increasing the revenue allowed under this section.

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The amount determined in a) above; plus 50% of the excess, if any, of all contract charges (excluding Net Revenue Sharing Income) over the sum of a)(i) , a)(iii) and a)(iv) above.

However, on fixed funds after the surrender charge period, a margin of up to the amount in a) above plus .4% may be used.

Table I

	Initial	Year 1	Years 2 – 5	Year 6+
Equity Class	-13.5%	0%	4.0%	5.50%
Bond Class	0%	0%	4.85%	4.85%
Balanced Class	-8.1%	0%	4.34%	5.24%
Fixed Separate Accounts and General Account (net)	0%	Fixed Fund Rate	Fixed Fund Rate	Fixed Fund Rate

2) Reinsurance Credit. Individual reinsurance is defined as reinsurance where the total premiums for and benefits of the reinsurance can be determined by applying the terms of the reinsurance to each contract covered without reference to the premiums or benefits of any other contract covered and summing the results over all contracts covered. Reinsurance that is not Individual is Aggregate.

Individual reinsurance premiums projected to be payable on ceded risk and receivable on assumed risk shall be included in the Projected Net Revenue. Similarly, Individual reinsurance benefits projected to be receivable on ceded risk and payable on assumed risk shall be included in the Projected Net Revenue. No Aggregate reinsurance shall be included in Projected Net Revenue.

3) Lapses, Partial Withdrawals, and In-The-Moneyness. Partial withdrawals elected as guaranteed living benefits, see A3.3)C)7), or required contractually (e.g., a contract operating under an automatic withdrawal provision on the valuation date) are to be deducted from the Account Value in each projection interval consistent with the projection frequency used, as described in A3.3)C)6), and according to the terms of the contract. No other partial withdrawals, including free partial withdrawals, are to be deducted from Account Value. All lapse rates should be applied as full contract surrenders.

For purposes of determining the dynamic lapse assumptions shown in Table II below, a guaranteed living benefit is in the money (ITM) for any projection interval if the Account Value at the beginning of the projection interval is less than the Current Value of the guaranteed living benefit (as defined below) also at the beginning of that projection interval.

The Current Value of the guaranteed living benefit at the beginning of any projection interval is either the amount of the current lump sum payment (if exercisable) or the present value of future lump sum or income payments. More specific guidance is provided below. For the purpose of determining the present value, the discount rate shall be equal *DR* as defined in A3.1)B)2). If future living benefit payments are life contingent (i.e., either the right of future exercise or the right to future income benefits expires with

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the death of the annuitant or the owner), then the company shall determine the present value of such payments using the mortality table specified in A3.3)C)5).

If a guaranteed living benefit is exercisable (withdrawal can start or, in the case of a GMWB, has begun) at the beginning of the projection interval, then the Current Value of the guaranteed living benefit shall be determined assuming immediate or continued exercise of that benefit.

If a guaranteed living benefit is not exercisable (e.g., due to minimum age or duration requirements) at the beginning of that projection interval, then the Current Value of the guaranteed living benefit shall be determined assuming exercise of the guaranteed living benefit at the earliest possible future projection interval. If the right to exercise the guaranteed living benefit is contingent on the survival of the annuitant or the owner, then the Current Value of the guaranteed living benefit shall assume survival to the date of exercise using the mortality table specified in A3.3)C)5).

Determination of the Current Value of a guaranteed living benefit that is exercisable or payable at a future projection interval shall take account of any guaranteed growth in the basis for the guarantee (e.g., where the basis grows according to an index or an interest rate).

For a GMWB, the Current Value shall be determined assuming the earliest penalty-free withdrawal of guaranteed benefits after withdrawals begin and by applying the constraints of any applicable maximum or minimum withdrawal provisions. If the GMWB is currently exercisable and the right to future GMWB payments is contingent upon the survival of the annuitant or owner, then the Current Value shall assume survival using the mortality table specified in A3.3)C)5). After a GMWB that has payments that are contingent upon the survival of the annuitant or owner has commenced, then the Current Value shall assume survival using the Annuity 2000 Mortality Table.

For an unexercised GMIB, the Current Value shall be determined assuming the option with a reserve closest to the reserve for a 10 year certain and life option. The reserve values and the value of the GMIB on the assumed date of exercise shall be determined using the discount rate *DR* specified in A3.1)B)2) and for life contingent payments, the Annuity 2000 Mortality Table. The Current Value of an unexercised GMIB, however, shall be set equal to the Account Value if the contractholder can receive higher income payments on the assumed date of exercise by electing the same option under the normal settlement option provisions of the contract.

For the purpose of applying the lapse assumptions specified in Table II below or contractholder elections rates specified in A3.3)C)7), the contract shall be considered "out of the money" (OTM) for a projection interval if the Current Value of the guaranteed living benefit at the beginning of the projection interval is less than or equal to the Account Value at the beginning of the same projection interval. If the Current Value of the guaranteed living benefit at the beginning of the projection interval is greater than the Account Value also at the beginning of the projection interval, the contract shall be considered 'in the money' (ITM) and the percent ITM shall equal:

100 * ((Current Value of the guaranteed living benefit /Account Value) - 1)

If a contract has multiple living benefit guarantees then the guarantee having the largest Current Value shall be used to determine the percent in the money.

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Table II - Lapse Assumptions

	During Surrender Charge Period	After Surrender Charge Period		
Death Benefit Only Contracts	5%	10%		
All Guaranteed Living Benefits OTM	5%	10%		
		ITM < 10%	10%<=ITM< 20%	20%<=ITM
Any Guaranteed Minimum Accumulation Benefit ITM	2%	2%	0%	0%
Any Other Guaranteed Living Benefits ITM	3%	7%	5%	2%

4) Account Transfers and Future Deposits. No transfers between funds shall be assumed in the projection used to the determine the greatest present value amount required under section A3.3)B)2)b) unless required by the contract (e.g., transfers from a dollar cost averaging fund or contractual rights given to the insurer to implement a contractually specified portfolio insurance management strategy or a contract operating under an automatic re-balancing option). When transfers must be modeled, to the extent not inconsistent with contract language, the allocation of transfers to funds must be in proportion to the contract's current allocation to funds.

Margins generated during a projection interval on funds supporting account value are transferred to the Accumulation of Net Revenue and are subsequently accumulated at the Discount Rate. Assets for each class supporting account values are to be reduced in proportion to the amount held in each asset classes at the time of transfer of margins or any portion of Account Value applied to the payment of benefits.

No future deposits to Account Value shall be assumed unless required by the terms of the contract to prevent contract or guaranteed benefit lapse, in which case they must be modeled. When future deposits must be modeled, to the extent not inconsistent with contract language, the allocation of the deposit to funds must be in proportion to the contract's current allocation to such funds.

5) Mortality. Mortality at 70% of the 1994 Variable Annuity MGDB Mortality Tables (1994 MGDB tables) through age 85 increasing by 1% each year to 100% of the 1994 MGDB tables at age 115 shall be assumed in the projection used to the determine the greatest present value amount required under section A3.3)B)2)b).

6) Projection Frequency. The projection used to determine the greatest present value amount required under section A3.3)B)2)b) shall be calculated using an annual or more frequent time step, such as quarterly. For time steps more frequent than annual, assets supporting Account Values at the start of a year may be retained in such funds until year-end (i.e., margin earned during the year will earn the fund rates instead of the Discount Rate until year end) or removed after each time step. However, the same approach shall be applied for all years. Similarly, projected benefits, lapses, elections and other contractholder activity can be assumed to occur annually or at the end of each time step, but the approach shall be consistent for all years.

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7) Contractholder Election Rates. Contractholder election rates for exercisable ITM guaranteed living benefits other than GMWBs shall be 5% per annum in every projection interval where the living benefit is less than 10% ITM, 15% per annum in every projection interval where the living benefit is 10% or more ITM and less than 20% ITM, and 25% per annum in every projection interval where the living benefit is more than 20% ITM. In addition, the election rate for an exercisable ITM guaranteed living benefit shall be 100% at the last model duration to elect such benefit. This 100% election rate shall be used when a Guaranteed Minimum Accumulation Benefit is at the earliest date that the benefit is exercisable and in-the-money. However, the contractholder election rate for any exercisable ITM guaranteed living benefit shall be zero if exercise would cause the extinction of a guaranteed living benefit having a larger Current Value. For this purpose, GMDBs are not benefits subject to election.

For guaranteed minimum withdrawal benefits, a partial withdrawal, if allowed by contract provisions, equal to the applicable percentage in Table III applied to the contract's maximum allowable partial withdrawal shall be assumed. However, if the contract's minimum allowable partial withdrawal exceeds the partial withdrawal from applying the rate in Table III to the contract's maximum allowable partial withdrawal, then the contract's minimum allowable partial withdrawal shall be assumed.

Table III - Guaranteed Withdrawal Assumptions			
	Attained Age less than 50	Attained Age 50 to 59	Attained Age 60 or Greater
Withdrawals do not reduce other elective Guarantees that are in the money	50%	75%	100%
Withdrawals reduce elective Guarantees that are in the money	25%	50%	75%

8) Indices. If an interest index is required to determine projected benefits or reinsurance obligations, the index must assume interest rates have not changed since the last reported rates before the valuation date. If an equity index is required the index shall be consistent with the last reported index before the valuation date, the initial drop in equity returns and the subsequent equity returns in the standard scenario projection. The sources of information and how they are used to determine the indexes shall be documented and, to the extent possible, consistent from year to year.

D) Assumptions for use in Section A3.3)B)2)c).

1) The Value of Aggregate Reinsurance. The value of Aggregate reinsurance shall be calculated separately from the Accumulated Net Revenue. The value of Aggregate reinsurance is the discounted value, using the statutory valuation rate described in the following paragraph, of the excess of (a) the projected benefit payments from the reinsurance; over (b) the projected gross reinsurance premiums, where (a) and (b) are determined under the assumptions described in section A3.3)C) for all applicable contracts in aggregate.

In order for the value of the Aggregate reinsurance to be consistent with the underlying Standard Scenario reserve, the discount rate shall be a weighted average of the valuation

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rates (*DR*) of the contracts that are supported by the Aggregate reinsurance treaty. The weights used to determine this discount rate shall be reasonably related to the risks that are being covered by the Aggregate reinsurance (e.g., account value or values of guaranteed benefits) and shall be applied consistently from year to year. If an appropriate method to determine this discount rate does not exist, the value of the Aggregate reinsurance shall be determined using the statutory valuation rate in effect on the valuation date for annuities valued on an issue year basis using Plan Type A and a Guarantee Duration greater than 10 years but not more than 20 years, determined assuming there are cash settlement options but no interest guarantees on future premiums.

2) The Value of Approved Hedges. The value of approved hedges shall be calculated separately from the Accumulated Net Revenue. The value of approved hedges is the difference between: a) the discounted value at the 1-year CMT[16] as of the valuation date of the pre-tax cash flows from the approved hedges; less b) their statement values on the valuation date.

To be an approved hedge for purposes of the Standard Scenario Reserve, a derivative or other investment has to be an actual asset held by the company on the valuation date, be used as a hedge supporting the contracts falling under the scope of the Guideline, and comply with any statutes, laws, or regulations (including applicable documentation requirements) of the domiciliary state or jurisdiction related to the use of derivative instruments.

The Domiciliary Commissioner may require the exclusion of any portion of the value of approved hedges upon a finding that the company's documentation, controls, measurement, execution of strategy or historical results are not adequate to support a future expectation of risk reduction commensurate with the value of approved hedges.

The cash flow projection for approved hedges that expire in less than one year from the valuation date should be based on holding the hedges to their expiration. For hedges with an expiration of more than 1 year, the value of hedges should be based on liquidation of the hedges one year from the valuation date. Where applicable, the liquidation value of hedges shall be consistent with the assumed returns in the Standard Scenario from the start of the projection to the date of liquidation, Black-Scholes pricing, a risk free rate equal to the 5-year CMT as of the valuation date and the annual volatility implicit as of the valuation date in the statement value of the hedges when the statement value of hedges are valued with Black-Scholes pricing and a risk-free rate equal to the 5-year CMT as of the valuation date.[17]

There is no credit in the Standard Scenario for dynamic hedging beyond the credit that results from hedges actually held on the valuation date.

3) Allocation of the Value of Hedges and the Value of Aggregate Reinsurance. The value of approved hedges and Aggregate reinsurance shall be allocated to the contracts which are

[16] For purposes of this Appendix, the term CMT refers to the nominal yields on actively traded non-inflation-indexed issues adjusted to constant maturities, as released daily by the Federal Reserve Board. As of this writing, the current and historical one-year rates may be found at *http://www.federalreserve.gov/datadownload/Build.aspx?rel=H15* and the current and historical five-year rates may be found at *http://www.federalreserve.gov/releases/h15/data/Business_day/H15_TCMNOM_Y5.txt*.

[17] Conceptually, the item being hedged, the contract guarantees, and the approved hedges are accounted for at the average present value of the worst 30% of all scenarios, the tail scenarios for a CTE (70) measure. However, the statement value of approved hedges is at market. Therefore, the standard scenario value of approved hedges is a proxy of the adjustment needed to move approved hedges from a market value to a tail value.

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supported by the applicable Aggregate reinsurance agreements and approved hedges. A contract's allocation shall be the lesser of the amount in A3.3)B)2)b) for the contract or the product of a) and b) where:

a) Is the sum of the value of the applicable approved hedges plus the value of the applicable Aggregate reinsurance for all contracts supported by the same hedges and/or the Aggregate reinsurance agreement; and

b) Is the ratio of the amount in A3.3)B)2)b) for the contract to the sum of the amount in A3.3)B)2)b) for all contracts supported by the same hedges and/or the Aggregate reinsurance agreement.

4) Retention of components. For the seriatim Standard Scenario Reserve on the statement date under each of Sections A3.1)B)1) and A3.1)B)2), the actuary should have available to the Commissioner the following values for each contract:

a) The Standard Scenario Reserve prior to adjustment under paragraph A3.3)D)3)

b) The Standard Scenario Reserve net of the adjustment in A3.3)D)3).

E) Determination of the Surrender Charge Amortization Period to be used in section A3.3)C)1)a) and b).

The purpose of the Surrender Charge Amortization Period is to help determine how much of the surrender charge is amortized in the Basic Adjusted Reserve portion of the Standard Scenario Amount and how much needs to be amortized in the Accumulated Net Revenue portion. Once determined, the Surrender Charge Amortization Period determines the duration over which the lower level of margins, as described in A3.3)C)1)a), is used. After that duration, the higher level of margins, as described in A3.3)C)1)b), is used.

A separate Surrender Charge Amortization Period is determined for each contract and is based on amounts determined in the calculation of the Basic Adjusted Reserve for that contract. A key component of the calculation is the amount of the surrender charge that is not amortized in the Basic Adjusted Reserve calculation for that contract. This is represented by the difference between the account value and the cash surrender value projected within the Basic Adjusted Reserve calculation for the contract.

The Surrender Charge Amortization Period for a given contract is determined by following the steps:

1) Measure the duration of the greatest present value used in the Basic Adjusted Reserve. The Basic Adjusted Reserve is determined for a contract by taking the greatest present value of a stream of projected benefits. The benefit stream that determines the greatest present value typically includes an "ultimate" event (e.g., 100% surrender, 100% annuitization, or maturity). The "BAR Duration" is the length of time between the valuation date and the projected "ultimate" event.

2) Determine the amount of the surrender charge not amortized in the Basic Adjusted Reserve. The surrender charge not amortized in the Basic Adjusted Reserve is the difference between the projected account value and the projected cash surrender value at the BAR Duration (i.e., at the time of that projected "ultimate" event). This value for a given contract shall not be less than zero.

3) Determine the Surrender Charge Amortization Period before rounding. This equals a) time b) plus c), where:

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a) Equals the ratio of the amount determined in step 2 to the Account Value on the valuation date;
b) Equals 100; and
c) Equals the BAR Duration determined in step 1.

4) Determine the Surrender Charge Amortization Period for the contract. This is the amount determined in step 3, rounded to the nearest number that represents a projection duration, taking into account the projection frequency described in A3.3)C)6). For example, step 3 produces a value of 2.15 and the projection frequency is quarterly, the Surrender Charge Amortization Period for the contract is 2.25.

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APPENDIX 4 - Alternative Methodology

A4.1) General Methodology

A) General Methodology Description. For variable deferred annuity contracts that either contain no guaranteed benefits or only GMDBs[18] (i.e., no VAGLBs), the Conditional Tail Expectation Amount may be determined by using the method outlined below rather than by using the approach described in Section IV)D) (i.e., based on projections), provided the approach described in Section IV)D) has not been used in prior valuations or else approval has been obtained from the Domiciliary Commissioner.

The Conditional Tail Expectation Amount determined using the Alternative Methodology for a group of contracts with GMDBs shall be determined as the sum of amounts obtained by applying factors to each contract inforce as of a valuation date and adding this to the contract's Cash Surrender Value.[19] The resulting Conditional Tail Expectation Amount shall not be less than the Cash Surrender Value in aggregate for the group of contracts to which the Alternative Methodology is applied.

The Conditional Tail Expectation Amount determined using the Alternative Methodology for a group of contracts that contain no guaranteed benefits[20] shall be determined using an application of Actuarial Guideline XXXIII, as described below.

For purposes of performing the Alternative Methodology, materially similar contracts within the group may be combined together into subgroups to facilitate application of the factors. Specifically, all contracts comprising a "subgroup" must display substantially similar characteristics for those attributes expected to affect reserves (e.g., definition of guaranteed benefits, attained age, contract duration, years-to-maturity, market-to-guaranteed value, asset mix, etc.). Grouping shall be the responsibility of the actuary but may not be done in a manner that intentionally understates the resulting reserve.

B) Definitions of Terms Used in this Appendix.

1) Annualized Account Charge Differential. This term is the charge as percentage account value (revenue for the company) minus the expense as percentage of account value.

2) Asset Exposure. Asset Exposure refers to the greatest possible loss to the insurance company from the value of assets underlying general or separate account contracts falling to zero.

3) Benchmark. Benchmarks have similar risk characteristics to the entity (e.g., asset class, index, or fund) to be modeled.

4) Deterministic Calculations. In a Deterministic Calculation, a given event (e.g., asset returns going up by 7% then down by 5%) is assumed to occur with certainty. In a stochastic calculation, events are assigned probabilities.

[18] This includes "earnings enhanced death benefits," as discussed in Section III)A)1).

[19] The amount that is added to a contract's Cash Surrender Value may be negative, zero or positive, thus resulting in a reserve for a given contract that could be less than, equal to, or greater than, the Cash Surrender Value.

[20] The term "contracts that contain no guaranteed benefits" means that there are no guaranteed benefits at any time during the life of the contract (past, present or future).

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5) Foreign Securities. Securities issued by entities outside the United States and Canada.

6) Grouped Fund Holdings. Grouped Fund Holdings relate to guarantees that apply across multiple deposits or for an entire contract instead of on a deposit-by-deposit basis.

7) Guaranteed Value. The Guaranteed Value is the benefit base or a substitute for the account value (if greater than the account value) in the calculation of living benefits or death benefits. The methodology for setting the Guaranteed Value is defined in the variable annuity contract.

8) High-Yield Bonds. High-Yield Bonds are below investment grade, with NAIC designations (if assigned) of 3, 4, 5, or 6. Compared to investment grade bonds, these bonds have higher risk of loss due to credit events. Funds containing securities predominately containing securities that are not NAIC designated as 1 or 2 (or similar agency ratings) are considered to be High-Yield.

9) Investment Grade Fixed Income Securities. Securities with NAIC designations of 1 or 2 are Investment Grade. Funds containing securities predominately with NAIC designations of 1 or 2 or with similar agency ratings are considered to be Investment Grade.

10) Liquid Securities. These securities can be sold and converted into cash at a price close to its true value in a short period of time.

11) Margin Offset. Margin Offset is the portion of charges plus any Revenue Sharing allowed under section A1.1)E) available to fund claims and amortization of the unamortized surrender charges allowance.

12) Multi-Point Linear Interpolation. This methodology is documented in mathematical literature and calculates factors based on multiple attributes categorized with discrete values where the attributes' actual values may be between the discrete values.

13) Model Office. A Model Office converts many contracts with similar features into one contract with specific features for modeling purposes.

14) Pre-Packaged Scenarios. The Pre-Packaged Scenarios are the year-by-year asset returns that may be used (but are not mandated) in projections related to the alternative methodology. These scenarios are available on an American Academy of Actuaries website.

15) Quota-Share Reinsurance. In this type of reinsurance treaty, the same proportion is ceded on all cessions. The reinsurer assumes a set percentage of risk for the same percentage of the premium, minus an allowance for the ceding company's expenses.

16) Resets. A Reset benefit results in a future minimum guaranteed benefit being set equal to the contract's account value at previous set date(s) after contract inception.

17) Risk Mitigation Strategy. A Risk Mitigation Strategy is a device to reduce the probability and/or impact of a risk below an acceptable threshold.

18) Risk Profile. Risk Profile in the Guideline relates to the prescribed asset class categorized by the volatility of returns associated with that class.

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19) Risk Transfer Arrangements. A Risk Transfer Arrangement shifts risk exposures (e.g., the responsibility to pay at least a portion of future contingent claims) away from the original insurer.

20) Roll-Up. A Roll-Up benefit results in the guaranteed value associated with a minimum contractual guarantee increasing at a contractually defined interest rate.

21) Volatility. Volatility refers to the annualized standard deviation of asset returns.

C) Contract-by-Contract Application for Contracts that Contain No Guaranteed Living or Death Benefits. The Alternative Methodology reserve for each contract that contains no guaranteed living or death benefits shall be determined by applying Actuarial Guideline XXXIII. The application shall assume a return on separate account assets equal to the year of issue valuation interest rate less appropriate asset based charges. It shall also assume a return for any fixed separate account and general account options equal to the rates guaranteed under the contract.

The reserve for such contracts shall be no less than the Cash Surrender Value on the valuation date, as defined in Section III)B).

D) Contract-by-Contract Application for Contracts that Contain GMDBs only. For each contract, factors are used to determine a dollar amount, equal to $R\times(CA+FE)+GC$ (as described below), that is to be added to that contract's Cash Surrender Value as of the valuation date. The dollar amount to be added for any given contract may be negative, zero, or positive. The factors that are applied to each contract shall reflect the following attributes as of the valuation date:

1) The contractual features of the variable annuity product,

2) The actual issue age, period since issue, attained age, years-to-maturity, and gender applicable to the contract,

3) The account value and composition by type of underlying variable or fixed fund,

4) Any surrender charges,

5) The GMDB and the type of adjustment made to the GMDB for partial withdrawals (e.g., proportional or dollar-for-dollar adjustment), and

6) Expenses to be incurred and revenues to be received by the company as estimated on a Prudent Estimate basis as described in Section III)B)8) and complying with the requirements for Revenue Sharing as described in section A1.1)E).

E) Factor Components. Factors shall be applied to determine each of the following components.[21]

CA = Provision for amortization of the unamortized surrender charges calculated by the insurer based on each contract's surrender charge schedule, using prescribed assumptions, except that lapse rates shall be based on the insurer's Prudent Estimate, but with no provision for Federal Income Taxes or mortality;

[21] Material to assist in the calculation of the components is available on the American Academy of Actuaries' website, at *https://www.actuary.org/content/c3-phase-ii-rbc-and-reserves-project*.

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FE = Provision for fixed dollar expenses less fixed dollar revenue calculated using prescribed assumptions, the contract's actual expense charges, the insurer's anticipated actual expenses and lapse rates, both estimated on a Prudent Estimate basis, and with no provision for Federal Income Taxes or mortality;

GC = Provision for the costs of providing the GMDB less net available spread-based charges determined by the formula $F \times GV - G \times AV \times R$, where GV and AV are as defined in section A4.3)A);

R = A scaling factor that is a linear function of the ratio of the margin offset to Total Account Charges (*W*) and takes the form $R(\beta_0, \beta_1) = \beta_0 + \beta_1 \times W$. The intercept and slope factors for this linear function vary according to:

a) Product type,
b) Pro-rata or dollar-for-dollar reductions in guaranteed value following partial withdrawals,
c) Fund class,
d) Attained age,
e) Contract duration,
f) Asset-based charges, and
g) 90% of the ratio of account value to guaranteed value, determined in the aggregate for all contracts sharing the same product characteristics.

Tables of factors for *F*, *G*, β_0, and β_1 values, reflecting a 65% confidence level and ignoring Federal Income Tax, are available from the National Association of Insurance Commissioners. In calculating $R(\beta_0, \beta_1)$ directly from the linear function provided above, the margin ratio *W* must be constrained to values greater than or equal to 0.2 and less than or equal to 0.6.

Interpolated values of F, *G* and *R* (calculated using the linear function described above) for all contracts having the same product characteristics and asset class shall be derived from the pre-calculated values using multi-point linear interpolation over the following four contract-level attributes:

1) Attained age,

2) Contract duration,

3) Ratio of account value to GMDB, and

4) The total of all asset based charges, including any fund management fees or allowances based on the underlying variable annuity funds received by the insurer.

The gross asset-based charges for a product shall equal the sum of all contractual asset-based charges plus fund management fees or allowances based on the underlying variable annuity funds received by the insurer determined by complying with the requirements for Prudent Estimate described in Section III)B)8) and Revenue Sharing described in section A1.1)E). Net asset-based charges equal gross asset-based charges less any company expenses assumed to be incurred expressed as a percentage of account value. All expenses that would be assumed if the Conditional Tail Expectation Amount were being computed as described in section A1.1)A) should be reflected either in the calculation of the net asset based charges or in the expenses reflected in the calculation of the amount *FE*.

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No adjustment is made for Federal Income Taxes in any of the components listed above.

For purposes of determining the Conditional Tail Expectation Amount using the Alternative Methodology, any interpretation and application of the requirements of the Guideline shall follow the principles discussed in the Section I) Background.

A4.2) Calculation of *CA* and *FE*

A) General Description. Components *CA* and *FE* shall be calculated for each contract, thus reflecting the actual account value and GMDB, as of the valuation date, which is unique to each contract.

Components *CA* and *FE* are defined by deterministic "single-scenario" calculations that account for asset growth, interest and inflation at prescribed rates. Mortality is ignored for these two components. Lapse rates shall be determined on a Prudent Estimate basis as described in Section III)B)8). Lapse rates shall be adjusted by the formula shown below (the Dynamic Lapse Multiplier, λ), which bases the relationship of the GMDB (denoted as GV in the formula) to the account value (denoted as AV in the formula) on the valuation date. Thus, projected lapse rates are smaller when the GMDB is greater than the account value and larger when the GMDB is less than the account value.

$$\lambda = MIN\left[U, MAX\left[L, 1 - M \times \left(\frac{GV}{AV} - D\right)\right]\right],$$

where U=1, L=0.5, M=1.25, and D=1.1.

Present values shall be computed over the period from the valuation date to contract maturity at a discount rate of 5.75%.

Projected fund performance underlying the account values is as shown in the table below. Unlike the *GC* component, which requires the entire account value to be mapped, using the Fund Categorization Rules set forth in section A4.4, to a single "equivalent" asset class (as described in A4.4)C)), the *CA* and *FE* calculation separately projects each variable subaccount (as mapped to the 8 prescribed categories shown in section A4.4)) using the net asset returns shown in the following table. If surrender charges are based wholly on deposits or premiums as opposed to account value, use of this table may not be necessary.

Asset Class / Fund	Net Annualized Return
Fixed Account	Guaranteed Rate
Money Market	0%
Fixed Income (Bond)	0%
Balanced	–1%
Diversified Equity	–2%
Diversified International Equity	–3%
Intermediate Risk Equity	–5%
Aggressive or Exotic Equity	–8%

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B) Component *CA*. Component *CA* is computed as the present value of the projected change in surrender charges plus the present value of an implied borrowing cost of 25 basis points at the beginning of each future period applied to the surrender charge at such time.

This component can be interpreted as the "amount needed to amortize the unamortized surrender charge allowance for the *persisting* policies plus the implied borrowing cost." By definition, the amortization for non-persisting lives in each time period is exactly offset by the collected surrender charge revenue (ignoring timing differences and any waiver upon death). The unamortized balance must be projected to the end of the surrender charge period using the net asset returns and Dynamic Lapse Multiplier, λ, both as described above and the year-by-year amortization discounted also as described above. For simplicity, mortality is ignored in the calculations. Surrender charges and free partial withdrawal provisions are as specified in the contract. Lapse and withdrawal rates are determined on a Prudent Estimate basis, and may vary according to the attributes of the business being valued, including, but not limited to, attained age, contract duration, etc.

C) Component *FE*. Component *FE* establishes a provision for fixed dollar expenses (e.g., allocated costs, including overhead expressed as "per contract" *and* those expenses defined on a "per contract" basis) less any fixed dollar revenue (e.g., annual administrative charges or contract fees) through the earlier of contract maturity or 30 years. *FE* is computed as the present value of the company's assumed fixed expenses projected at an assumed annual rate of inflation starting in the second projection year. This rate grades uniformly from the current inflation rate ("CIR") into an ultimate inflation rate of 3% per annum in the 8th year after the valuation date. The CIR is the greater of 3% and the inflation rate assumed for expenses in the company's most recent asset adequacy analysis for similar business.

A4.3) Calculation of the *GC* Component

A) *GC* Factors. *GC* is calculated as $F \times GV - G \times AV \times R$, where *GV* is the amount of GMDB and *AV* is the contract account value, both as of the valuation date. *F*, *G* and the slope and intercept for the linear function used to determine *R* (identified symbolically as β_0 and β_1) are pre-calculated factors available from the National Association of Insurance Commissioners and known herein as the "Pre-Calculated Factors." These factors shall be interpolated as described in subsection F), below, and modified as necessary as described in sections A4.3)G) and A4.3)H).

B) Five Steps. There are five major steps in determining the *GC* component for a given contract:

1) Classifying the asset exposure (as specified in subparagraph C), below);

2) Determining the risk attributes (as specified in subparagraphs D) and E), below);

3) Retrieving the appropriate nodal factors from the factor grid (as described in subparagraph F) below;

4) Interpolating the nodal factors, where applicable (optional) also as described in subparagraph F), below; and

5) Applying the factors to the contract values.

C) Classifying Asset Exposure. For purposes of calculating *GC* (unlike what is done for components *CA* and *FE*), the entire account value for each contract must be assigned to one of the eight prescribed fund classes shown in section A4.4), using the Fund Categorization rules in section A4.4).

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D) Product Designs. Factors *F*, *G* and $R(\beta_1,\beta_2)$ are available within the Pre-Calculated Factors for the following GMDB product designs:

1) Return of Premium ("ROP"),

2) Premiums less withdrawals accumulated at 3% per annum, capped at 2.5 times premiums less withdrawals, with no further increase beyond age 80 ("ROLL3"),

3) Premiums less withdrawals accumulated at 5% per annum, capped at 2.5 times premiums less withdrawals, with no further increase beyond age 80 ("ROLL5"),

4) An annual ratchet design (maximum anniversary value), for which the guaranteed benefit never decreases and is increased to equal the previous contract anniversary account value, if larger, with no further increases beyond age 80 ("MAV"),

5) A design having a guaranteed benefit equal to the larger of the benefits in designs 3 and 4, above ("HIGH"),

6) An enhanced death benefit ("EDB") equal to 40% of the net earnings on the account (i.e., 40% of account value less total premiums paid plus withdrawals made) with this latter benefit capped at 40% of premiums less withdrawals ("EDB"),

E) Other Attributes. Factors *F*, *G* and $R(\beta_1,\beta_2)$ are available within the Pre-Calculated Factors for the following set of attributes:

1) Two Partial Withdrawal Rules – one for contracts having a pro-rata reduction in the GMDB and another for contracts having a dollar-for-dollar reduction,

2) The eight asset classes described in section A4.4)B),

3) Eight attained ages, with a 5-year age setback for females,

4) Five contract durations,

5) Seven values of GV/AV, and

6) Three levels of asset-based income.

F) Interpolation of *F*, *G* and $R(\beta_1,\beta_2)$.

1) Values of *F*, *G* and $R(\beta_1,\beta_2)$ apply to a contract having the product characteristics listed in section A4.5)A) and shall be determined by selecting values for the appropriate partial withdrawal rule and asset class and then using multi-point linear interpolation among published values for the last four attributes shown in section A4.3)E).

2) Interpolation over all four dimensions is not required, but if not performed over one or more dimensions, the factor used must result in a conservative (higher) value of *GC*. However, simple linear interpolation using the $AV \div GV$ ratio is mandatory. In this case, the company must choose nodes for the other three dimensions according to the following rules: next highest attained age, nearest duration, and nearest Annualized

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Account Charge Differential, as listed in A4.5)C) (i.e., capped at +100 and floored at –100 bps).

3) For $R(\beta_1, \beta_2)$, the interpolation should be performed on the Scaling Factors *R* calculated using β_1, β_2, using the ratio of Margin Offset to Total Asset Charges (*W*), not on the factors β_1 and β_2 themselves.

4) An Excel® workbook, Excel® add-in and companion dynamic link library (.dll) program is available from the National Association of Insurance Commissioners that can be used to determine the correct values and perform the multi-point linear interpolation.

5) Alternatively, published documentation can be referenced on performing multi-point linear interpolation and the required sixteen values determined using a key that is documented in the table "*Components of Key Used for GC Factor Look-Up*" located in section A4.5)C).

G) Adjustments to *GC* for Product Variations & Risk Mitigation/Transfer. In some cases, it may be necessary to make adjustments to the published factors due to:

1) A variation in product form wherein the definition of the guaranteed benefit is materially different from those for which factors are available (see section A4.3)H)); and/or

2) A risk mitigation or other management strategy, other than a hedging strategy, that cannot be accommodated through a straightforward and direct adjustment to the published values.

Adjustments may not be made to *GC* for hedging strategies.

Any adjustments to the published factors must be fully documented and supported through stochastic analysis. Such analysis may require stochastic simulations, but would not ordinarily be based on full inforce projections. Instead, a representative "model office" should be sufficient. Use of these adjusted factors must be supported by a periodic review of the appropriateness of the assumptions and methods used to perform the adjustments, with changes made to the adjustments when deemed necessary by such review.

Note that minor variations in product design do not necessarily require additional effort. In some cases, it may be reasonable to use the factors/formulas for a different product form (e.g., for a roll-up GMDB near or beyond the maximum reset age or amount, the ROP GMDB factors/formulas shall be used, possibly adjusting the guaranteed value to reflect further resets, if any). In other cases, the reserves may be based on two different guarantee definitions and the results interpolated to obtain an appropriate value for the given contract/cell. Likewise, it may be possible to adjust the Alternative Methodology results for certain risk transfer arrangements without significant additional work (e.g., quota-share reinsurance without caps, floors or sliding scales would normally be reflected by a simple pro-rata adjustment to the "gross" *GC* results).

However, if the contract design is sufficiently different from those provided and/or the risk mitigation strategy is non-linear in its impact on the Conditional Tail Expectation Amount, and there is no practical or obvious way to obtain a good result from the prescribed factors/formulas, any adjustments or approximations must be supported using stochastic modeling. Notably this modeling need not be performed on the whole portfolio, but can be undertaken on an appropriate set of representative policies.

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H) Adjusting *F* and *G* for Product Design Variations. This subsection describes the typical process for adjusting *F* and *G* factors due to a variation in product design. Note that *R* (as determined by the slope and intercept terms in the factor table) would not be adjusted.

1) Select a contract design among those described in section A4.3)D) that is similar to the product being valued. Execute cash flow projections using the documented assumptions (see table of *Liability Modeling Assumptions & Product Characteristics* in section A4.5)A) and table of *Asset Based Fund Charges* in section A4.5)B)) and the pre-packaged scenarios for a set of representative cells (combinations of attained age, contract duration, asset class, AV/GMDB ratio and asset-based charges). These cells should correspond to nodes in the table of pre-calculated factors. Rank (order) the sample distribution of results for the present value of net cost.[22] Determine those scenarios that comprise CTE (65).

2) Using the results from step 1, average the present value of cost for the CTE (65) scenarios and divide by the current guaranteed value. For the J^{th} cell, denote this value by F_J. Similarly, average the present value of margin offset revenue for the same subset of scenarios and divide by account value. For the J^{th} cell, denote this value by G_J.

3) Extract the corresponding pre-calculated factors. For each cell, calibrate to the published tables by defining a "model adjustment factor" (denoted by asterisk) separately for the "cost" and "margin offset" components:

$$F_J^* = \frac{f(\tilde{\theta})}{F_J} \text{ and } G_J^* = \frac{\hat{g}(\tilde{\theta})}{G_J}$$

4) Execute "product specific" cash flow projections using the documented assumptions and pre-packaged scenarios for the same set of representative cells. Here, the company should model the actual product design. Rank (order) the sample distribution of results for the present value of net cost. Determine those scenarios that comprise CTE (65).

5) Using the results from step 4, average the present value of cost for the CTE (65) scenarios and divide by the current guaranteed value. For the J^{th} cell, denote this value by $\overline{F}_J$. Similarly, average the present value of margin offset revenue for the same subset of scenarios and divide by account value. For the J^{th} cell, denote this value by $\overline{G}_J$.

6) To calculate the Conditional Tail Expectation Amount for the specific product in question, the company should implement the Alternative Methodology as documented, but use $\overline{F}_J \times F_J^*$ in place of *F* and $\overline{G}_J \times G_J^*$ instead of *G*. The same *R* factors as appropriate for the product evaluated in step 1 shall be used for this step (i.e., the product used to calibrate the cash flow model).

I) Adjusting *GC* for Mortality Experience. The factors that have been developed for use in determining *GC* assume male mortality at 100% of the 1994 Variable Annuity MGDB ALB Mortality Table. Companies electing to use the Alternative Methodology that have not conducted an evaluation of their mortality experience shall use these factors. Other companies should use the procedure described below to adjust for the actuary's Prudent Estimate of mortality. The development of Prudent Estimate mortality shall follow the requirements and guidance of

[22] Present value of net cost = PV [guaranteed benefit claims in excess of account value] – PV [margin offset]. The discounting includes cash flows in all future years (i.e., to the earlier of contract maturity and the end of the horizon).

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Appendix 10. Once a company uses the modified method for a block of business, the option to use the unadjusted factors is no longer available for that part of its business. In applying the factors to actual inforce business, a 5-year age setback should be used for female annuitants.

1) Develop a set of mortality assumptions based on Prudent Estimate. In setting these assumptions, the actuary shall be guided by the definition of Prudent Estimate and the principles discussed in Appendices 9 and 10 of the Guideline.

2) Calculate two sets of net single premiums (NSP) at each attained age: one valued using 100% of the 1994 Variable Annuity MGDB ALB Mortality Table (with the aforementioned 5-year age setback for females) and the other using Prudent Estimate mortality. These calculations shall assume an interest rate of 3.75% and a lapse rate of 7% per year.

3) The *GC* factor is multiplied by the ratio, for the specific attained age being valued, of the NSP calculated using the Prudent Estimate mortality to the NSP calculated using the 1994 Variable Annuity MGDB ALB Mortality Table (with the aforementioned 5-year age setback for females).

A4.4) Fund Categorization

A) Criteria. The following criteria should be used to select the appropriate factors, parameters and formulas for the exposure represented by a specified guaranteed benefit. When available, the volatility of the long-term annualized total return for the fund(s) – or an appropriate benchmark – should conform to the limits presented. For this purpose, "long-term" is defined as twice the average projection period that would be applied to test the product in a stochastic model (generally, at least 30 years).

Where data for the fund or benchmark are too sparse or unreliable, the fund exposure should be moved to the next higher volatility class than otherwise indicated. In reviewing the asset classifications, care should be taken to reflect any additional volatility of returns added by the presence of currency risk, liquidity (bid-ask) effects, short selling and speculative positions.

B) Asset Classes. Variable subaccounts must be categorized into one of the following eight (8) asset classes. For purposes of calculating *CA* or *FE*, each contract will have one or more of the following asset classes represented, whereas for component *GC*, all subaccounts will be mapped into a single asset class.

1) Fixed Account. This class is credited interest at guaranteed rates for a specified term or according to a 'portfolio rate' or 'benchmark' index. This class offers a minimum positive guaranteed rate that is periodically adjusted according to company policy and market conditions.

2) Money Market/Short-Term. This class is invested in money market instruments with an average remaining term-to-maturity of less than 365 days.

3) Fixed Income. This class is invested primarily in investment grade fixed income securities. Up to 25% of the funds within this class may be invested in diversified equities or high-yield bonds. The expected volatility of the returns for this class will be lower than the Balanced fund class.

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4) Balanced. This class is a combination of fixed income securities with a larger equity component. The fixed income component should exceed 25% of the portfolio. Additionally, any aggressive or 'specialized' equity component should not exceed one-third (33.3%) of the total equities held. Should the fund violate either of these constraints, it should be categorized as an equity fund. This class usually has a long-term volatility in the range of 8% – 13%.

5) Diversified Equity. This class is invested in a broad-based mix of U.S. and foreign equities. The foreign equity component (maximum 25% of total holdings) must be comprised of liquid securities in well-developed markets. Funds in this class would exhibit long-term volatility comparable to that of the S&P500. These funds should usually have a long-term volatility in the range of 13% – 18%.

6) Diversified International Equity. This class is similar to the Diversified Equity class, except that the majority of fund holdings are in foreign securities. This class should usually have a long-term volatility in the range of 14% – 19%.

7) Intermediate Risk Equity. This class has a mix of characteristics from both the Diversified and Aggressive Equity Classes. This class has a long-term volatility in the range of 19% – 25%.

8) Aggressive or Exotic Equity. This class comprises more volatile funds where risk can arise from: underdeveloped markets, uncertain markets, high volatility of returns, narrow focus (e.g., specific market sector), etc. This class (or market benchmark) either does not have sufficient history to allow for the calculation of a long-term expected volatility, or the volatility is very high. This class would be used whenever the long-term expected annualized volatility is indeterminable or exceeds 25%.

C) Selecting Appropriate Investment Classes. The selection of an appropriate investment type should be done at the level for which the guarantee applies. For guarantees applying on a deposit-by-deposit basis, the fund selection is straightforward. However, where the guarantee applies across deposits or for an entire contract, the approach can be more complicated. In such instances, the approach is to identify for each contract where the "grouped holdings" fit within the categories listed and to classify the associated assets on this basis.

A seriatim process is used to identify the "grouped" fund holdings, to assess the risk profile of the current fund holdings (possibly calculating the expected long-term volatility of the funds held with reference to the indicated market proxies), and to classify the entire 'asset exposure' into one of the specified choices. Here, 'asset exposure' refers to the underlying assets (separate and/or general account investment options) on which the guarantee will be determined. For example, if the guarantee applies separately for each deposit year within the contract, then the classification process would be applied separately for the exposure of each deposit year.

In summary, mapping the benefit exposure (i.e., the asset exposure that applies to the calculation of the guaranteed minimum death benefits) to one of the prescribed asset classes is a multi-step process:

1) Map each separate and/or general account investment option to one of the prescribed asset classes. For some funds, this mapping will be obvious, but for others it will involve a review of the fund's investment policy, performance benchmarks, composition and expected long-term volatility.

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2) Combine the mapped exposure to determine the expected long-term "volatility of current fund holdings." This will require a calculation based on the expected long-term volatility for each fund and the correlations between the prescribed asset classes as given in the table "*Correlation Matrix for Prescribed Asset Classes*," in section A4.4)D).

3) Evaluate the asset composition and expected volatility (as calculated in step 2) of current holdings to determine the single asset class that best represents the exposure, with due consideration to the constraints and guidelines presented earlier in this section.

In step 1, the company should use the fund's actual experience (i.e., historical performance, inclusive of reinvestment) only as a guide in determining the expected long-term volatility. Due to limited data and changes in investment objectives, style and/or management (e.g., fund mergers, revised investment policy, different fund managers, etc.); the company may need to give more weight to the expected long-term volatility of the fund's benchmarks. In general, the company should exercise caution and not be overly optimistic in assuming that future returns will consistently be less volatile than the underlying markets.

In step 2, the company should calculate the "volatility of current fund holdings" (for the exposure being categorized) by the following formula:

$$\sigma = \sqrt{\sum_{i=1}^{n}\sum_{j=1}^{n} w_i w_j \rho_{ij} \sigma_i \sigma_j}$$

using the volatilities and correlations in the following table where $w_i = \frac{AV_i}{\sum_k AV_k}$ is the relative value of fund i expressed as a proportion of total contract value, ρ_{ij} is the correlation between asset classes i and j and σ_i is the volatility of asset class i. An example is provided after the table.

D) Correlation Matrix for Prescribed Asset Classes.

ANNUAL VOLATILITY		FIXED ACCOUNT	MONEY MARKET	FIXED INCOME	BALANCED	DIVERSE EQUITY	INTL EQUITY	INTERM EQUITY	AGGR EQUITY
1.0%	FIXED ACCOUNT	**1**	0.50	0.15	0	0	0	0	0
1.5%	MONEY MARKET	0.50	**1**	0.20	0	0	0	0	0
5.0%	FIXED INCOME	0.15	0.20	**1**	0.30	0.10	0.10	0.10	0.05
10.0%	BALANCED	0	0	0.30	**1**	0.95	0.60	0.75	0.60
15.5%	DIVERSE EQUITY	0	0	0.10	0.95	**1**	0.60	0.80	0.70
17.5%	INTL EQUITY	0	0	0.10	0.60	0.60	**1**	0.50	0.60
21.5%	INTERM EQUITY	0	0	0.10	0.75	0.80	0.50	**1**	0.70
26.0%	AGGR EQUITY	0	0	0.05	0.60	0.70	0.60	0.70	**1**

E) Fund Categorization Example. As an example, suppose three funds (Fixed Income, diversified U.S. Equity and Aggressive Equity) are offered to clients on a product with a contract level guarantee (i.e., across all funds held within the contract). The current fund holdings (in dollars) for five sample contracts are shown in the following table.

	1	**2**	**3**	**4**	**5**
MV Fund X (Fixed Income):	5,000	4,000	8,000	-	5,000
MV Fund Y (Diversified Equity):	9,000	7,000	2,000	6,000	-
MV Fund Z (Aggressive Equity):	1,000	4,000	-	4,000	5,000
Total Market Value:	15,000	15,000	10,000	10,000	10,000
Total Equity Market Value:	10,000	11,000	2,000	10,000	5,000
Fixed Income % (*A*):	33%	27%	80%	0%	50%
Fixed Income Test (*A*>75%):	No	No	Yes	No	No
Aggressive % of Equity (B):	10%	36%	n/a	40%	100%
Balanced Test (*A*>25% & *B*<33.3%):	Yes	No	n/a	No	No
Volatility of Current Fund Holdings:	10.9%	13.2%	5.3%	19.2%	13.4%
Fund Classification:	**Balanced**	**Diversified*[23]**	**Fixed Income**	**Intermediate**	**Diversified**

[23] Although the volatility suggests "Balanced Fund," the Balanced Fund criteria were not met. Therefore, this 'exposure' is moved "up" to Diversified Equity. For those funds classified as Diversified Equity, additional analysis would be required to assess whether they should be instead designated as "Diversified International Equity."

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As an example, the "Volatility of Current Fund Holdings" for contract #1 is calculated as $\sqrt{A+B}$ where:

$$A = \left(\frac{5}{15}\times 0.05\right)^2 + \left(\frac{9}{15}\times 0.155\right)^2 + \left(\frac{1}{15}\times 0.26\right)^2$$

$$B = 2\cdot\left(\frac{5}{15}\cdot\frac{9}{15}\right)(0.1\times 0.05\times 0.155) + 2\cdot\left(\frac{5}{15}\cdot\frac{1}{15}\right)(0.05\times 0.05\times 0.26) + 2\cdot\left(\frac{9}{15}\cdot\frac{1}{15}\right)(0.7\times 0.155\times 0.26)$$

So the volatility for contract #1 = $\sqrt{0.0092+0.0026}$ = 0.109 or 10.9%.

A4.5) Tables

A) Liability Modeling Assumptions & Product Characteristics used for *GC* Factors.

Asset Based Charges (MER)	Vary by fund class. See section A4.5)B).
Base Margin Offset	100 basis points per annum.
GMDB Description	1. ROP = return of premium ROP. 2. ROLL3 = 3% roll-up, capped at 2.5 × premium, frozen at age 80. 3. ROLL5 = 5% roll-up, capped at 2.5 × premium, frozen at age 80. 4. MAV = annual ratchet (maximum anniversary value), frozen at age 80. 5. HIGH = Higher of 5% roll-up and annual ratchet. 6. EDB = 40% Enhanced Death Benefit (capped at 40% of deposit). Note that the Pre-Calculated Factors were originally calculated with a combined ROP benefit, but they have been adjusted to remove the effect of the ROP. Thus, the factors for this benefit 5 are solely for the Enhanced Death Benefit.
Adjustment to GMDB Upon Partial Withdrawal	Separate factors for "Pro-Rata by Market Value" and "Dollar-for-Dollar."
Surrender Charges	Ignored (i.e., zero). Included in the *CA* component.
Single Premium / Deposit	$100,000. No future deposits; no intra-contract fund rebalancing.
Base Contract Lapse Rate (Total Surrenders)	• Pro-rata by MV: 10% p.a. at all contact durations (before dynamics) • Dollar-for-dollar: 2% p.a. at all contract durations (no dynamics)
Partial Withdrawals	• Pro-rata by MV: None (i.e., zero) • Dollar-for-dollar: Flat 8% p.a. at all contract durations (as a % of AV). No dynamics or anti-selective behavior.
Mortality	100% of the 1994 Variable Annuity MGDB Mortality Table (MGDB 94 ALB). For reference, 1000 × q_x rates at ages 65 and 70 for 100% of MGDB 94 ALB Male are 18.191 and 29.363 respectively. Note that section A4.3)I) allows modification to this assumption.
Gender /Age Distribution	100% male. Methodology accommodates different attained ages. A 5-year age setback will be used for female annuitants.
Max. Annuitization Age	All policies terminate at age 95.
Fixed Expenses	Ignored (i.e., zero). Included in the *FE* component.

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Annual Fee and Waiver	Ignored (i.e., zero). Included in the *FE* component.
Discount Rate	5.75% pre-tax.
Dynamic Lapse Multiplier (Applies only to policies where GMDB is adjusted "pro-rata by MV" upon withdrawal)	$\lambda = MIN\left[U, MAX\left[L, 1 - M \times \left(\frac{GV}{AV} - D\right)\right]\right]$ U=1, L=0.5, M=1.25, D=1.1 ▪ Applied to the 'Base Contract Lapse Rate' ▪ Does not apply to partial withdrawals.

B) Asset-Based Fund Charges (bps per annum).

Asset Class / Fund	**Account Value Charge**
Fixed Account	0
Money Market	110
Fixed Income (Bond)	200
Balanced	250
Diversified Equity	250
Diversified International Equity	250
Intermediate Risk Equity	265
Aggressive or Exotic Equity	275

C) Components of Key Used for *GC* Factor Look-Up.

(First Digit Always "1")

Contract Attribute	Key : Possible Values & Description	
Product Definition, P	0 : 0	Return-of-premium.
	1 : 1	Roll-up (3% per annum).
	2 : 2	Roll-up (5% per annum).
	3 : 3	Maximum Anniversary Value (MAV).
	4 : 4	High of MAV and 5% Roll-up.
	5 : 5	Enhanced Death Benefit (excludes the ROP GMDB, which would have to be added separately if the contract in question has an ROP benefit.)
GV Adjustment Upon Partial Withdrawal, A	0 : 0	Pro-rata by market value.
	1 : 1	Dollar-for-dollar.
Fund Class, F	0 : 0	Fixed Account.
	1 : 1	Money Market.
	2 : 2	Fixed Income (Bond).
	3 : 3	Balanced Asset Allocation.
	4 : 4	Diversified Equity.
	5 : 5	International Equity.
	6 : 6	Intermediate Risk Equity.
	7 : 7	Aggressive / Exotic Equity.

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Attained Age (Last Birthday), X	0 : 35 1 : 45 2 : 55 3 : 60	4 : 65 5 : 70 6 : 75 7 : 80
Contract Duration (years-since-issue), D	0 : 0.5 2 : 6.5 4 : 12.5	1 : 3.5 3 : 9.5
Account Value-to-Guaranteed Value Ratio, ϕ	0 : 0.25 1 : 0.50 2 : 0.75 3 : 1.00	4 : 1.25 5 : 1.50 6 : 2.00
Annualized Account Charge Differential from A4.5)B) Assumptions	0 : –100 bps 1 : +0 2 : +100	

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APPENDIX 5 - Scenario Calibration Criteria

A5.1) General

This Appendix outlines the requirements for the stochastic models used to simulate fund performance.[24] Specifically, it sets certain standards that must be satisfied and offers guidance to the actuary in the development and validation of the scenario models. Background material and analysis are presented to support the recommendation. The Appendix focuses on the S&P 500 as a proxy for returns on a broadly diversified U.S. equity fund, but there is also advice on how the techniques and requirements would apply to other types of funds. General modeling considerations such as the number of scenarios and projection frequency are also discussed.

The calibration points given in this Appendix are applicable to gross returns (before the deduction of any fees or charges). To determine the net returns appropriate for the projections required by the Guideline, the actuary shall reflect applicable fees and contractholder charges in the development of projected account values. The projections shall also include the costs of managing the investments and converting the assets into cash when necessary.

As a general rule, funds with higher expected returns should have higher expected volatilities and in the absence of well-documented mitigating factors (e.g., a highly reliable and favorable correlation to other fund returns), should lead to higher reserve requirements.[25]

State or path dependent models are not prohibited, but must be justified by the historic data and meet the calibration criteria. To the degree that the model uses mean-reversion or path-dependent dynamics, this must be well supported by research and clearly documented in the Memorandum supporting the required actuarial certification.

The equity scenarios used to determine reserves must be available in an electronic format to facilitate any regulatory review.

A5.2) Gross Wealth Ratios

Gross Wealth Ratios derived from the stochastic return scenarios for use with a Separate Account variable fund category for diversified U.S. equities must satisfy calibration criteria consistent with that for the S&P 500 shown in the following table. Under these calibration criteria, Gross Wealth Ratios for quantiles less than 50 percent may not exceed the value from the table corresponding to the quantile, while at quantiles greater than 50 percent; Gross Wealth Ratios may not be less than the corresponding value for the quantile from the table. Gross Wealth Ratios must be tested for holding period 1, 5, 10 and 20 years throughout the projections, except as noted in section A5.3).

The "wealth factors" are defined as gross accumulated values (i.e., before the deduction of fees and charges) with complete reinvestment of income and maturities, starting with a unit investment. These can be less than 1, with "1" meaning a zero return over the holding period.

S&P 500 Total Return Gross Wealth Ratios at the Calibration Points

[24] For more details on the development of these requirements, including the development of the calibration points, see the American Academy of Actuaries recommendation on C-3 Phase II risk-based capital.

[25] While the model need not strictly adhere to 'mean-variance efficiency,' prudence dictates some form of consistent risk/return relationship between the proxy investment funds. In general, it would be inappropriate to assume consistently 'superior' expected returns (i.e., risk/return point above the frontier).

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Calibration Point	One Year	Five Year	Ten Year	Twenty Year
2.5%	0.78	0.72	0.79	
5.0%	0.84	0.81	0.94	1.51
10.0%	0.90	0.94	1.16	2.10
90.0%	1.28	2.17	3.63	9.02
95.0%	1.35	2.45	4.36	11.70
97.5%	1.42	2.72	5.12	

The scenarios need not strictly satisfy all calibration points, but the actuary should be satisfied that any differences do not materially reduce the resulting reserves.[26] In particular, the actuary should be mindful of which tail most affects the business being valued. If reserves are less dependent on the right (left) tail for all products under consideration (e.g., a return of premium guarantee would primarily depend on the left tail, an enhanced death benefit equal to a percentage of the gain would be most sensitive to the right tail, etc.), it is not necessary to meet the right (left) calibration points.

For models that require starting values for certain state variables,[27] long-term ('average' or 'neutral') values should be used for calibration. The same values should normally be used to initialize the models for generating the actual projection scenarios unless an alternative assumption can be clearly justified.[28] It should be noted that a different set of initialization parameters might produce scenarios that do not satisfy all the calibration points shown in the above table. However, the S&P 500 scenarios used to determine reserves must meet the calibration criteria.

A5.3) Calibration Requirements Beyond Twenty Years

It is possible to parameterize some path and/or state dependent models to produce higher volatility (and/or lower expected returns) in the first 20 years in order to meet the calibration criteria, but with lower volatility (and/or higher expected returns) for other periods during the forecast horizon. While this property may occur for certain scenarios (e.g., the state variables would evolve over the course of the projection and thereby affect future returns), it would be inappropriate and unacceptable for a company to alter the model parameters and/or its characteristics for periods beyond year 20 in a fashion not contemplated at the start of the projection and primarily for the purpose(s) of reducing the volatility and/or severity of ultimate returns.[29]

A5.4) Other Funds

Calibration of other markets (funds) is left to the judgment of the actuary, but the scenarios so generated must be consistent with the calibration points in the table in section A5.2). This does not imply a strict functional relationship between the model parameters for various markets/funds, but it would generally be inappropriate to assume that a market or fund consistently "outperforms" (lower risk, higher expected return relative to the efficient frontier) over the long term.

[26] See the Preamble to the *Accounting Practices and Procedures Manual* for an explanation of materiality.

[27] For example, a stochastic log volatility ("SLV") model requires the starting volatility. Also, the regime-switching lognormal model requires an assumption about the starting regime.

[28] A clear justification exists when state variables are observable or "known" to a high degree of certainty and not merely estimated or inferred based on a "balance of probabilities."

[29] Such adjustments must be clearly documented and justified by the historic data.

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The actuary shall document the actual 1-, 5-, 10- and 20-year wealth factors of the scenarios at the same frequencies as in the "S&P 500 Total Return Gross Wealth Ratios at the Calibration Points" table in section A5.2). The annualized mean and standard deviation of the wealth factors for the 1-, 5-, 10- and 20-year holding periods must also be provided. For equity funds, the actuary shall explain the reasonableness of any significant differences from the S&P500 calibration points.

When parameters are fit to historic data without consideration of the economic setting in which the historic data emerged, the market price of risk may not be consistent with a reasonable long-term model of market equilibrium. One possibility for establishing 'consistent' parameters (or scenarios) across all funds would be to assume that the market price of risk is constant (or nearly constant) and governed by some functional (e.g., linear) relationship. That is, higher expected returns can only be garnered by assuming greater risk.[30]

Specifically, two return distributions X and Y would satisfy the following relationship:

$$\text{Market Price of Risk} = \left(\frac{\text{E}[\text{R}_X] - \text{r}}{\sigma_X} \right) = \left(\frac{E[R_Y] - \text{r}}{\sigma_Y} \right)$$

where $E[R]$ and σ are respectively the (unconditional) expected returns and volatilities and r is the expected risk-free rate over a suitably long holding period commensurate with the projection horizon. One approach to establish consistent scenarios would set the model parameters to maintain a near-constant market price of risk.

A closely related method would assume some form of 'mean-variance' efficiency to establish consistent model parameters. Using the historic data, the mean-variance (alternatively, 'drift-volatility') frontier could be a constructed from a plot of (mean, variance) pairs from a collection of world market indices. The frontier could be assumed to follow some functional form,[31] with the coefficients determined by standard curve fitting or regression techniques. Recognizing the uncertainty in the data, a 'corridor' could be established for the frontier. Model parameters would then be adjusted to move the proxy market (fund) inside the corridor.

Clearly, there are many other techniques that could be used to establishing consistency between the scenarios. While appealing, the above approaches do have drawbacks[32] and the actuary should not be overly optimistic in constructing the model parameters or the scenarios.

Funds can be grouped and projected as a single fund if such grouping is not anticipated to materially reduce reserves. However, care should be taken to avoid exaggerating the benefits of diversification. The actuary must document the development of the investment return scenarios and be able to justify the mapping of the company's variable accounts to the proxy funds used in the modeling.

[30] As an example, the standard deviation of log returns is often used as a measure of risk.

[31] Quadratic polynomials and logarithmic functions tend to work well.

[32] For example, mean-variance measures ignore the asymmetric and fat-tailed profile of most equity market returns.

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A5.5) Correlation of Fund Returns

In constructing the scenarios for the proxy funds, the company may require parameter estimates for a number of different market indices. When more than one index is projected, it is generally necessary to allow for correlations in the simulations. It is not necessary to assume that all markets are perfectly positively correlated, but an assumption of independence (zero correlation) between the equity markets would inappropriately exaggerate the benefits of diversification. An examination of the historic data suggests that correlations are not stationary and that they tend to increase during times of high volatility or negative returns. As such, the actuary should take care not to underestimate the correlations in those scenarios used for the reserve calculations.

If the projections include the simulation of interest rates (other than for discounting surplus strain) as well as equity returns, the processes may be independent provided that the actuary can demonstrate that this assumption (i.e., zero correlation) does not materially underestimate the resulting reserves.

A5.6) Number of Scenarios and Efficiency in Estimation

For straight Monte Carlo simulation (with equally probable "paths" of fund returns), the number of scenarios should typically equal or exceed 1000. The appropriate number will depend on how the scenarios will be used and the materiality of the results. The actuary should use a number of scenarios that will provide an acceptable level of precision.

Fewer than 1000 scenarios may be used provided that the actuary has determined through prior testing (perhaps on a subset of the portfolio) that the CTE values so obtained materially reproduce the results from running a larger scenario set.

Variance reduction and other sampling techniques are intended to improve the accuracy of an estimate more efficiently than simply increasing the number of simulations. Such methods can be used provided the actuary can demonstrate that they do not lead to a material understatement of results. Many of the techniques are specifically designed for estimating means, not tail measures, and could in fact reduce accuracy (and efficiency) relative to straight Monte Carlo simulation.[33]

The above requirements and warnings are not meant to preclude or discourage the use of valid and appropriate sampling methods, such as Quasi Random Monte Carlo (QRMC), importance sampling or other techniques designed to improve the efficiency of the simulations (relative to pseudo-random Monte Carlo methods). However, the actuary should maintain documentation that adequately describes any such techniques used in the projections. Specifically, the documentation should include the reasons why such methods can be expected not to result in systematic or material under-statement of the resulting reserves compared to using pseudo-random Monte Carlo numbers.

A5.7) Frequency of Projection and Time Horizon

Use of an annual cashflow frequency ("timestep") is generally acceptable for benefits/features that are not sensitive to projection frequency. The lack of sensitivity to projection frequency should be validated by testing wherein the actuary should determine that the use of a more frequent (i.e., shorter) time step does not materially increase reserves. A more frequent time increment should always be used when the product features are sensitive to projection period frequency.

[33] However, with careful implementation, many variance reduction techniques can work well for CTE estimators. For example, see Manistre, B.J. and Hancock, G. (2003), "Variance of the CTE Estimator," 2003 Stochastic Modeling Symposium, Toronto, ON, September 2003.

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Care must be taken in simulating fee income and expenses when using an annual time step. For example, recognizing fee income at the end of each period after market movements, but prior to persistency decrements, would normally be an inappropriate assumption. It is also important that the frequency of the investment return model be linked appropriately to the projection horizon in the liability model. In particular, the horizon should be sufficiently long so as to capture the vast majority of costs (on a present value basis) from the scenarios.[34]

A5.8) Pre-Packaged Scenarios

The American Academy of Actuaries has provided 10,000 scenarios on its website[35] for the following nineteen asset classes.[36]

1) 3-month U.S. Treasury yields

2) 6-month U.S. Treasury yields

3) 1-year U.S. Treasury yields

4) 2-year U.S. Treasury yields

5) 3-year U.S. Treasury yields

6) 5-year U.S. Treasury yields

7) 7-year U.S. Treasury yields

8) 10-year U.S. Treasury yields

9) 20-year U.S. Treasury yields

10) 30-year U.S. Treasury yields

11) Money Market / Short-Term

12) U.S. Intermediate Term Government Bonds

13) U.S. Long Term Corporate Bonds

14) Diversified Fixed Income

15) Diversified Balanced Allocation

16) Diversified Large Capitalized U.S. Equity

[34] As a general guide, the forecast horizon should not be less than 20 years.

[35] The pre-packaged scenarios can be found at *https://www.soa.org/resources/tables-calcs-tools/research-scenario/* and are fully documented at *http://www.actuary.org/pdf/life/c3supp_march05.pdf*.

[36] Because the reserves calculated using projections involve cash flow projections, the pre-packaged scenarios were developed under the "real world" probability measure (as opposed to a "risk-neutral" basis). Therefore, the pre-packaged scenarios may not be appropriate for purposes of projecting the market value of future hedge instruments within a projection (to the extent such instruments are used in the projections). For this purpose, it may be more appropriate to use risk neutral scenarios to determine the market value of hedge instruments in the cash flow projections that are based on real world scenarios.

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17) Diversified International Equity

18) Intermediate Risk Equity

19) Aggressive or Specialized Equity

The scenarios are available as gross monthly accumulation factors (or U.S. Treasury yields) over a 30-year horizon in comma-separated value format (**.csv*). These scenarios have been appropriately correlated so that the K^{th} scenario for each asset class must be used together and considered one 'future investment return scenario.'[37] Hence, the scenarios can be combined (by blending the accumulation factors[38]) to create additional 'proxy' scenarios for the company's funds.

For example, suppose the actuary wanted to construct scenarios for a 'balanced fund' that targets a 60/40 allocation between bonds and U.S. equities. If we denote $[AF^{X}]$ as the matrix of accumulation factors for asset class X, then the balanced scenarios would be defined by $[AF^{BAL}] = 0.60 \times [AF^{BOND}] + 0.40 \times [AF^{S\&P500}]$. Care should be taken to avoid exaggerating the benefits of diversification. The actuary shall document the development of the investment return scenarios and be able to justify the mapping of the company's variable accounts to the proxy funds used in the modeling.

The U.S. Treasury yields are expressed as nominal semi-annual bond equivalent yields in decimal format. All other returns are expressed as periodic (not cumulative) market accumulation factors (i.e., monthly "gross wealth ratios"). Interest rates are assumed to change at the start of each month, hence the value in column T applies for month T-1. The market accumulation factor in column T represents the growth in month T-1.

If all or a portion of these scenarios are used, then the actuary shall verify that the scenario calibration criteria are met.

[37] It is inappropriate to misalign the ordering of scenarios (e.g., scenario J for "Diversified U.S. Equity" cannot be combined with scenario K for "Diversified International Equity," where $J \neq K$).

[38] It is important to blend the accumulation factors (not the returns) in order to achieve the desired asset mix.

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APPENDIX 6 - Allocation of the Aggregate Reserves to the Contract Level

Section IV states that the Aggregate Reserve shall be allocated to the contracts falling within the scope of the Guideline. When the Conditional Tail Expectation Amount is greater that the Standard Scenario Amount, this allocation requires that the excess be allocated to the contracts falling within the scope of the Guideline.

A6.1) Allocation when the Aggregate Reserve equals the Conditional Tail Expectation Amount

A) Single sub-grouping. When the Aggregate Reserve is equal to the Conditional Tail Expectation Amount and the Conditional Tail Expectation Amount is determined in aggregate for all contracts falling within the scope of the Guideline (i.e., a single grouping), as described in Section IV)D), the excess of the Conditional Tail Expectation Amount over the Standard Scenario Amount shall be allocated to each contract on the basis of the difference between the Standard Scenario Reserve and the Cash Surrender Value[39] on the valuation date for the contract. If the cash surrender value is not defined or not available, the Standard Scenario Amount will be the basis of allocation.

B) Multiple sub-groupings. When the Aggregate Reserve is equal to the Conditional Tail Expectation Amount and the Conditional Tail Expectation Amount is determined using more than one sub-grouping, as described in Section IV)D), the allocation of the excess of the Conditional Tail Expectation Amount over the Standard Scenario Amount and shall reflect that sub-grouping of contracts used to determine the Conditional Tail Expectation Amount, as described in Section IV)D).

For example, when the Conditional Tail Expectation Amount is determined using sub-grouping, the excess of the aggregate (i.e., the total for all contracts within the scope of the Guideline) Conditional Tail Expectation Amount over the aggregate Standard Scenario Amount shall be allocated only to those contracts that are part of sub-groupings whose contributions to the Conditional Tail Expectation Amount exceed their contribution to the Standard Scenario Amount.

In the case of such sub-groupings, the excess of the aggregate Conditional Tail Expectation Amount over the aggregate Standard Scenario Amount shall be allocated to each sub-grouping in proportion to the difference between the Conditional Tail Expectation and the Standard Scenario Reserve for each sub-grouping for which that excess is positive.

Once the allocation to each sub-grouping is determined, the excess of the reserve allocated to such sub-grouping over the Standard Scenario Amount determined for that sub-grouping shall be allocated to each contract within that sub-grouping on the basis of the difference between the Standard Scenario Reserve and the Cash Surrender Value on the valuation date for the contracts. If the cash surrender value is not defined or not available, the Standard Scenario Amount will be the basis of allocation.

[39] Note that since the Standard Scenario Reserve for a contract is, by definition, greater than or equal to the Cash Surrender Value, it is understood that the difference between the Standard Scenario Reserve and the Cash Surrender Value for each contract will never be less than zero.

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As an example, consider a company with the results of the following three sub-groupings:

Sub-grouping	A	B	C	Total
Conditional Tail Expectation Amount	28	40	52	120
Standard Scenario Amount	20	45	30	95
Aggregate Reserve				**120**
(1) – (2)	8	-5	22	25
Allocation	6.67	0	18.33	25

In this example, the excess of the Conditional Tail Expectation Amount over the Standard Scenario Amount, in aggregate, equals 25 (i.e., the "Total" column of row 1 less row 2, or 120 – 95). This excess of 25 would be allocated only to those contracts that are part of sub-groupings whose contributions to the Conditional Tail Expectation Amount exceed their contributions to the Standard Scenario Amount. In this example, that would be contracts in sub-groupings A and C (since in sub-grouping B, the contribution to the Standard Scenario Amount exceeds the contribution to the Conditional Tail Expectation Amount). Therefore, the excess of 25 would be allocated to the contracts in sub-groupings A and C in proportion to the difference between the Conditional Tail Expectation Amount and the Standard Scenario Reserve for those sub-groupings (i.e. row 4). In this example, the total difference between the Conditional Tail Expectation Amount and the Standard Scenario Reserve for the contracts in sub-groupings A and C equals 8 + 22, or 30. This would result in 8/30 of the excess of the Conditional Tail Expectation Amount over the Standard Scenario Amount (or 6.67) to be allocated to the contracts in sub-groupings A and 22/30 of the excess of the Conditional Tail Expectation Amount over the Standard Scenario Amount (or 18.33) to be allocated to the contracts in sub-groupings C as shown on line (5) above.

In this example, the allocation of the Aggregate Reserve to contracts within sub-grouping B would equal the Standard Scenario Reserve for those contracts (as described in section A6.2) below). For sub-groupings A and C, the difference between the allocation of the Aggregate Reserve to each of those sub-grouping and the Standard Scenario Amount determined for each of those sub-grouping would be allocated to each contract within each of those sub-groupings based on the difference between the Standard Scenario Reserve and the Cash Surrender Value for each of the contracts within the relevant sub-group. The result would be an allocated Aggregate Reserve for a given contract that would be equal to the Standard Scenario Reserve for that contract plus the amount of the difference between 1) and 2) below that is allocated to that contract, where:

1) Equals the allocation of the Aggregate Reserve to that contract's sub-grouping; and

2) Equals the Standard Scenario Amount determined for that contract's sub-grouping.

A6.2) Allocation when the Aggregate Reserve equals the Standard Scenario Amount

The Standard Scenario Amount, as required by Section IV)C), is calculated on a contract-by-contract basis, as described in Appendix 3. Therefore, when the Aggregate Reserve is equal to the Standard Scenario Amount, the reserve allocated to each contract shall be the reserve calculated for each contract under the Standard Scenario method.

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APPENDIX 7 – Modeling of Hedges

A7.1) Initial Considerations

The appropriate costs and benefits of hedging instruments that are currently held by the company in support of the contracts falling under the scope of the Guideline (excluding those that involve the offsetting of the risks associated with variable annuity guarantees with other products outside of the scope of the Guideline, such as equity-indexed annuities) shall be included in the calculation of the Conditional Tail Expectation Amount, determined in accordance with Section IV)D) and section A1.4) of the Guideline (i.e., Conditional Tail Expectation Amount using projections). If the company is following a Clearly Defined Hedging Strategy ("hedging strategy"), as defined in Section III, in accordance with an investment policy adopted by the Board of Directors, or a committee of Board members, the company is eligible to reduce the amount of the Conditional Tail Expectation Amount using projections otherwise calculated. The investment policy must clearly articulate the company's hedging objectives, including the metrics that drive rebalancing/trading. This specification could include maximum tolerable values for investment losses, earnings, volatility, exposure, etc. in either absolute or relative terms over one or more investment horizons vis-à-vis the chance of occurrence. Company management is responsible for developing, documenting, executing and evaluating the investment strategy, including the hedging strategy, used to implement the investment policy.

For this purpose, the investment assets refer to all the assets including derivatives supporting covered products and guarantees. This is also referred to as the investment portfolio. The investment strategy is the set of all asset holdings at all points in time in all scenarios. The hedging portfolio, which is also referred to as the hedging assets, is a subset of the investment assets. The hedging strategy is the hedging asset holdings at all points in time in all scenarios. There is no attempt to distinguish what is the hedging portfolio and what is the investment portfolio in this Appendix. Nor is the distinction between investment strategy and hedging strategy formally made here. Where necessary to give effect to the intent of this Appendix, the requirements applicable to the hedging portfolio or the hedging strategy are to apply to the overall investment portfolio and investment strategy.

This particularly applies to restrictions on the reasonableness or acceptability of the models that make up the stochastic cash flow model used to perform the projections, since these restrictions are inherently restrictions on the joint modeling of the hedging and non-hedging portfolio. To give effect to these requirements, they must apply to the overall investment strategy and investment portfolio.

The cost and benefits of hedging instruments that are currently held by the company in support of the contracts falling under the scope of the Guideline shall be included in the stochastic cash flow model used to calculate the Conditional Tail Expectation Amount in accordance with Section IV)D) (the "model"). If the company is following a Clearly Defined Hedging Strategy, the model shall take into account the cost and benefits of hedge positions expected to be held by the company in the future based on the operation of the hedging strategy.

Before either a new or revised hedging strategy can be used to reduce the amount of the Conditional Tail Expectation Amount otherwise calculated, the hedging strategy should be in place (i.e., effectively implemented by the company) for at least three months. The company may meet the time requirement by having evaluated the effective implementation of the hedging strategy for at least three months without actually having executed the trades indicated by the hedging strategy (e.g., mock testing or by having effectively implemented the strategy with similar annuity products for at least three months).

These requirements do not supersede any statutes, laws, or regulations of any state or jurisdiction related to the use of derivative instruments for hedging purposes and should not be used in determining whether a company is permitted to use such instruments in any state or jurisdiction.

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A7.2) Background

The analysis of the impact of the hedging strategy on cash flows is typically performed using either one of two methods as described below. Although a hedging strategy would normally be expected to reduce risk provisions, the nature of the hedging strategy and the costs to implement the strategy may result in an increase in the amount of the Conditional Tail Expectation Amount otherwise calculated.

The fundamental characteristic of the first method is that all hedging positions, both the currently held positions and those expected to be held in the future, are included in the stochastic cash flow model used to determine the Scenario Greatest Present Value, as discussed in Section IV)D), for each scenario.

The fundamental characteristic of the second method is that the effectiveness of the current hedging strategy (including currently held hedge positions) on future cash flows is evaluated, in part or in whole, outside of the stochastic cash flow model. In this case, the reduction to the Conditional Tail Expectation Amount otherwise calculated should be commensurate with the degree of effectiveness of the hedging strategy in reducing accumulated deficiencies otherwise calculated.

Regardless of the methodology used by the company, the ultimate effect of the current hedging strategy (including currently held hedge positions), on the Conditional Tail Expectation Amount needs to recognize all risks, associated costs, imperfections in the hedges and hedging mismatch tolerances associated with the hedging strategy. The risks include, but are not limited to: basis, gap, price, parameter estimation, and variation in assumptions (mortality, persistency, withdrawal, annuitization, etc.). Costs include, but are not limited to: transaction, margin (opportunity costs associated with margin requirements) and administration. In addition, the reduction to the Conditional Tail Expectation Amount attributable to the hedging strategy may need to be limited due to the uncertainty associated with the company's ability to implement the hedging strategy in a timely and effective manner. The level of operational uncertainty varies indirectly with the amount of time that the new or revised strategy has been in effect or mock tested.

No hedging strategy is perfect. A given hedging strategy may eliminate or reduce some but not all risks, transforms some risks into others, introduces new risks or has other imperfections. For example, a delta-only hedging strategy does not adequately hedge the risks measured by the "Greeks" other than delta. Another example is that financial indices underlying typical hedging instruments typically do not perform exactly like the separate account funds, and hence the use of hedging instruments has the potential for introducing basis risk.

A7.3) Calculation of CTE Amount (reported)

The company should begin by calculating "CTE Amount (best efforts)" – the results obtained when the Conditional Tail Expectation Amount (or "CTE Amount") is based on incorporating the hedging strategy (including currently held hedge positions) into the stochastic cash flow model, including all of the factors and assumptions needed to execute the hedging strategy (e.g., stochastic implied volatility).

Because most models will include at least some approximations or idealistic assumptions, CTE Amount (best efforts) may overstate the impact of the hedging strategy. To compensate for potential overstatement of the impact of the hedging strategy, the company shall recalculate the Conditional Tail Expectation Amount assuming the company has no dynamic hedging strategy (i.e., reflect only hedge positions held by the company on the valuation date. The result so obtained is called "CTE Amount (adjusted)." In some situations the determination of CTE Amount (adjusted) may include both direct and indirect techniques.

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Finally, the reported value for the Conditional Tail Expectation Amount is given by:

$$\text{CTE Amount (reported)} = E \times \text{CTE Amount (best efforts)} + (1 - E) \times \text{CTE Amount (adjusted)}$$

The value for E (an "effectiveness factor") reflects the actuary's view as to the level of sophistication of the stochastic cash flow model and its ability to properly reflect the parameters of the hedging strategy (i.e., the "Greeks" being covered by the strategy) as well as the associated costs, risks, and benefits E will be no greater than 0.70. As the sophistication of the stochastic cash flow model increases, the value for E increases (i.e., the greater the ability of the CTE Amount (best efforts) model to capture all risks and uncertainties, the higher the value of E). If the model used to determine the "CTE Amount (best efforts)" effectively reflects all of the parameters used in the hedging strategy, the value of E may be up to 0.70. If certain economic risks are not hedged, yet the model does not generate scenarios that sufficiently capture those risks, E must be in the lower end of the range. If hedge cash flows are not modeled directly, E will be no greater than 0.30. Simplistic hedge cash flow models will have a value of E in the low range between 0.00 and 0.70.

Additionally, the company shall demonstrate that, based on an analysis of at least the most recent 12 months, the model is able to replicate the hedging strategy in a way that justifies the value used for E. A company that does not have 12 months of experience to date shall set E to a value no greater than 0.30.

A7.4) Specific Considerations and Requirements

As part of the process of choosing a methodology and assumptions for estimating the future effectiveness of the current hedging strategy (including currently held hedge positions) for purposes of reducing the Conditional Tail Expectation Amount, the actuary should review actual historical hedging effectiveness. The actuary shall evaluate the appropriateness of the assumptions on future trading, transaction costs, and other elements of the model, the strategy, the mix of business, and other items that are likely to result in materially adverse results. This includes an analysis of model assumptions that, when combined with the reliance on the hedging strategy, are likely to result in adverse results relative to those modeled. The parameters and assumptions shall be adjusted (based on testing contingent on the strategy used and other assumptions) to levels that fully reflect the risk based on historical ranges and foreseeable future ranges of the assumptions and parameters. If this is not possible by parameter adjustment, the model shall be modified to reflect them at either Anticipated Experience or adverse estimates of the parameters.

A discontinuous hedging strategy is a hedging strategy where the relationships between the sensitivities to equity markets and interest rates (commonly referred to as the Greeks) associated with the guaranteed contractholder options embedded in the variable annuities and other in-scope products and these same sensitivities associated with the hedging assets are subject to material discontinuities. This includes, but is not limited to, a hedging strategy where material hedging assets will be obtained when the variable annuity account balances reach a predetermined level in relationship to the guarantees. Any hedging strategy, including a delta hedging strategy, can be a discontinuous hedging strategy if implementation of the strategy permits material discontinuities between the sensitivities to equity markets and interest rates associated with the guaranteed contractholder options embedded in the variable annuities and other in-scope products and these same sensitivities associated with the hedging assets. There may be scenarios that are particularly costly to discontinuous hedging strategies, especially where those result in large discontinuous changes in sensitivities (Greeks) associated with the hedging assets. Where discontinuous hedging strategies contribute materially to a reduction in the Conditional Tail Expectation Amount, the actuary must evaluate the interaction of future trigger definitions and the discontinuous hedging strategy, in addition to the items mentioned in the previous paragraph. This includes an analysis of model assumptions that, when combined with the reliance on the discontinuous hedging strategy, may result in adverse results relative to those modeled.

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Implementing a strategy that has a strong dependence on acquiring hedging assets at specific times that depend on specific values of an index or other market indicators may not be implemented as precisely as planned.

The combination of elements of the stochastic cash flow model, including the initial actual market asset prices, prices for trading at future dates, transaction costs, and other assumptions should be analyzed by the actuary as to whether the stochastic cash flow model permits hedging strategies that make money in some scenarios without losing a reasonable amount in some other scenarios. This includes, but is not limited to:

A) Hedging strategies with no initial investment that never lose money in any scenario and in some scenarios make money; or

B) Hedging strategies that with a given amount of initial money never make less than accumulation at the one-period risk free rates in any scenario but make more than this in one or more scenarios.

If the stochastic cash flow model allows for such situations, the actuary should be satisfied that the results do not materially rely directly or indirectly on the use of such strategies. In addition, the actuary should disclose the situations and provide supporting documentation as to why the actuary believes the situations are not material for determining the Conditional Tail Expectation Amount. If the results do materially rely directly or indirectly on the use of such strategies, the strategies may not be used to reduce the Conditional Tail Expectation Amount otherwise calculated.

In addition to the above, the method used to determine prices of financial instruments for trading in scenarios should be compared to actual initial market prices. If there are substantial discrepancies, the actuary should disclose the substantial discrepancies and provide supporting documentation as to why the model-based prices are appropriate for determining the Conditional Tail Expectation Amount. In addition to comparisons to initial market prices, there should be testing of the pricing models that are used to determine subsequent prices when scenarios involve trading financial instruments. This testing should consider historical relationships. For example, if a method is used where recent volatility in the scenario is one of the determinants of prices for trading in that scenario, then that model should approximate actual historic prices in similar circumstances in history.

A7.5) Certification and Documentation

The actuary must provide a certification that the values for E, CTE Amount (adjusted) and CTE Amount (best efforts) were calculated using the process discussed above and the assumptions used in the calculations were reasonable for the purpose of determining the Conditional Tail Expectation Amount. The actuary shall document the method(s) and assumptions (including data) used to determine CTE Amount (adjusted) and CTE Amount (best efforts) and maintain adequate documentation as to the methods, procedures and assumptions used to determine the value of E.

The actuary must provide a certification as to whether the Clearly Defined Hedging Strategy is fully incorporated into the stochastic cash flow model and any supplementary analysis of the impact of the hedging strategy on the Conditional Tail Expectation Amount. The actuary must document the extent to which elements of the hedging strategy (e.g., time between portfolio rebalancing) are not fully incorporated into the stochastic cash flow model and any supplementary analysis to determine the impact, if any. In addition, the actuary must provide a certification and maintain documentation to support the certification that the hedging strategy designated as the Clearly Defined Hedging Strategy meets the requirements of a Clearly Defined Hedging Strategy including that the implementation of the hedging strategy in the stochastic cash flow model and any supplementary analysis does not include knowledge of

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events that occur after any action dictated by the hedging strategy (i.e. the model cannot use information about the future that would not be known in actual practice).

A financial officer of the company (e.g., Chief Financial Officer, Treasurer or Chief Investment Officer) or a person designated by them who has direct or indirect supervisory authority over the actual trading of assets and derivatives must certify that the hedging strategy meets the definition of a Clearly Defined Hedging Strategy and that the Clearly Defined Hedging Strategy is the hedging strategy being used by the company in its actual day to day risk mitigation efforts.

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APPENDIX 8 – Certification Requirements

A8.1) Management Certification

Management must provide signed and dated written representations as part of the valuation documentation that the valuation appropriately reflects management's intent and ability to carry out specific courses of actions on behalf of the entity where such is relevant to the valuation. This certification will be submitted no later than March 1. Upon written request by the company, the commissioner may grant an extension of the date for submission of the certification.

A8.2) Actuarial Certification

A) General Description. The certification shall be provided by a qualified actuary and consist of at least the following:

1) A paragraph identifying the actuary and his or her qualifications;

2) A scope paragraph identifying the reserves as of the valuation date for contracts included in the certification categorized by the approaches used to determine the reserves (e.g., Alternative Methodology, Projections, Standard Scenario);

3) A reliance paragraph describing those areas, if any, where the certifying actuary has relied on other experts;
   a) A reliance statement from each of those relied on should accompany the certification.
   b) The reliance statements should note the information being provided and a statement as to the accuracy, completeness or reasonableness, as applicable, of the information.

4) A paragraph certifying that the reserve was calculated in accordance with the principles and requirements of the Guideline;

5) A paragraph certifying that the assumptions used for these calculations are Prudent Estimate assumptions for the products, scenarios, and purpose being tested; and

6) A paragraph stating that the qualified actuary is not opining on the adequacy of the company's surplus or its future financial condition.

7) This certification will be submitted no later than March 1. Upon written request by the company, the commissioner may grant an extension of the date for submission of the certification.

A8.3) Supporting Memorandum

A) General Description. A supporting memorandum shall be created to document the methodology and assumptions used to determine the Aggregate Reserve. The information shall include the comparison of the Standard Scenario Amount to the Conditional Tail Expectation Amount required by Section IV)A) in the determination of the Aggregate Reserve.

B) Alternative Methodology using Published Factors.

1) If a seriatim approach was not used, disclose how contracts were grouped.

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2) Disclosure of assumptions to include:
   a) Component CA
      (i) Mapping to prescribed asset categories
      (ii) Lapse and withdrawal rates
   b) Component FE
      (i) Determination of fixed dollar costs and revenues
      (ii) Lapse and withdrawal rates
      (iii) Inflation rates
   c) Component GC
      (i) Disclosure of contract features and how the company mapped the contract form to those forms covered by the Alternative Methodology factors
         - Product Definition - If not conservatively assigned to a published factor, company specific factors or stochastic modeling is required.
         - Partial Withdrawal Provision
         - Fund Class - Disclose the process used to determine the single asset class that best represents the exposure for a contract. If individual funds are mapped into prescribed categories, the process used to map the individual funds should be disclosed.
         - Attained Age
         - Contract Duration
         - Ratio of Account Value to Guaranteed Value
         - Annualized Account Charge Differential from Base Assumption
      (ii) Derivation of Equivalent Account Charges
      (iii) Derivation of margin offset
      (iv) Disclosure of interpolation procedures and confirmation of node determination

3) Disclosure, if applicable, of reinsurance that exists and how it was handled in applying published factors (For some reinsurance, creation of company-specific factors or stochastic modeling may be required.).
   a) Discuss how reserves before reinsurance were determined.

C) Alternative Factors based on Company-Specific Factors.

1) Disclosure of requirements consistent with Published Factors, as noted in subsection B) above.

2) Stochastic analysis supporting adjustments to published factors should be fully documented. This analysis needs to be submitted when initially used and be available upon request in subsequent years. Adjustments may include:
   a) Contract design;
   b) Risk mitigation strategy (excluding hedging); and
   c) Reinsurance.

D) Stochastic Modeling.

1) Assets
   a) Description including type and quality
   b) Investment & disinvestment assumptions

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c) Describe assets used at the start of the projection
d) Source of asset data
e) Asset valuation basis
f) Documentation of assumptions
  (i) Default costs
  (ii) Prepayment functions
  (iii) Market value determination
  (iv) Yield on assets acquired
  (v) Mapping and grouping of funds to modeled asset classes
g) Hedging Strategy
  (i) Documentation of strategy
  (ii) Identification of current positions
  (iii) Description on how strategy was incorporated into modeling
    - Basis risk, gap risk, price risk, assumption risk
    - Document the methods and criterion used to estimate the a priori effectiveness of the hedging strategy
  (iv) Documentation required for specific consideration raised in section A7.4).
  (v) Documentation and certification required by section A7.5).

2) Liabilities
a) Product descriptions
b) Source of Liabilities
c) Grouping of contracts
d) Reserve method and modeling (e.g., Working Reserves were set to CSV)
e) Investment Reserves
f) Describe how reinsurance was handled in the models, including how reserves gross of reinsurance were modeled.
g) Documentation of assumptions (i.e., list assumptions, discuss the sources and the rationale for using the assumptions).
  (i) Premiums and subsequent deposits
  (ii) Withdrawal, Lapse and Termination Rates
    - Partial Withdrawal (including treatment of dollar-for-dollar offsets on GMDBs and VAGLBs, and Required Minimum Distributions
    - Lapses / Surrenders
  (iii) Crediting Strategy
  (iv) Mortality
  (v) Annuitization rates
  (vi) Income Purchase rates
  (vii) GMIB and GMWB Utilization rates
  (viii) Commissions
  (ix) Expenses
  (x) Persistency Bonuses
  (xi) Investment / Fund Choice
  (xii) Revenue Sharing
  (xiii) Asset Allocation, Rebalancing and Transfer Assumptions
    - Dollar Cost Averaging
h) The section showing the assumptions used for lapse and utilization assumptions for contracts with guaranteed living benefits in the development of the Conditional Tail Expectation Amount, as described in section A9.7).

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3) Scenarios
   a) Description of scenario generation for interest rates and equity returns
      (i) Disclose the number "n" of scenarios used and the methods used to determine the sampling error of the CTE (70) statistic when using "n" scenarios.
      (ii) Time step of model (e.g., monthly, quarterly, annual)
      (iii) Correlation of fund returns
   b) Calibration
      (i) Gross Wealth Ratios for equity funds
         - Disclosure of adjustments to model parameters, if any.
         - Disclosure of 1-year, 5-year and 10-year wealth factors, as well as mean and standard deviation.
      (ii) Consistency of other funds to equity funds
      (iii) Correlation between all funds
      (iv) Estimate of market return volatility assumptions underlying the generated scenarios compared to actual observed volatility underlying market values.
   c) Extent of use of pre-packaged scenarios and support for mapping variable accounts to proxy funds

4) Description and results of sensitivity tests performed. At the request of the domiciliary commissioner, the company shall provide a sensitivity test showing an estimate of the impact of the market return volatility assumption when market volatility is materially higher than assumed in the generated scenarios.

5) Documentation of all material changes in the model or assumptions from that used previously and the estimated impact of such changes. This documentation, or a summary of this documentation, shall be included in an executive summary or some other prominent place in the memorandum.

6) A description of the methods used to validate the model and a summary of the results of the validation testing.

E) Standard Scenario.

1) For the amounts in 2), 3) and 4) below report the Basic Reserve in A3.3)B)2)a), the projection requirements in A3.3)B)2)b), the value of Aggregate reinsurance in A3.3)D)1), the value of hedges in A3.3)D)2), the total allocation of the value of hedges and Aggregate reinsurance in A3.3)B)2)c) and the Standard Scenario Reserve.

2) Report the Standard Scenario Amount as of the valuation date.

3) If applicable, report the Standard Scenario Amount on the inforce prior to the valuation date that was used to project the reserve requirements to the valuation date.

4) If applicable, report the Standard Scenario Amount on the model office used to represent the inforce.

5) Discuss modifications, if any, in the application of the standard scenario requirements to produce the amounts in 2), 3) and 4) above.

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6) Document any assumptions, judgments or procedures not prescribed in the Standard Scenario Method or in the Guideline that are used to produce the Standard Scenario Amount.

7) If applicable, documentation of approval by the commissioner to use the Basic Reserve as the Standard Scenario Amount.

8) Document the company's calculation of DR.

9) Document the allocation of funds to Equity, Bond, Balanced and Fixed classes.

10) A statement by the actuary that none of the reinsurance treaties included in the Standard Scenario serve solely to reduce the calculated Standard Scenario Reserve without also reducing risk on scenarios similar to those used to determine the Conditional Tail Expectation Reserve. This should be accompanied by a description of any reinsurance treaties that have been excluded from the Standard Scenario along with an explanation of why the treaty was excluded.

F) The memorandum shall be made available for examination by the commissioner upon his or her request but shall be returned to the company after such examination and shall not be considered a record of the insurance department or subject to automatic filing with the commissioner.

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APPENDIX 9 – Contractholder Behavior

A9.1) General

Contractholder behavior assumptions encompass actions such as lapses, withdrawals, transfers, recurring deposits, benefit utilization, option election, etc. Contractholder behavior is difficult to predict and behavior assumptions can significantly impact the results. In the absence of relevant and fully credible empirical data, the actuary should set behavior assumptions on the conservative end of the plausible spectrum (consistent with the definition of Prudent Estimate).

In setting behavior assumptions, the actuary should examine, but not be limited by, the following considerations:

1) Behavior can vary by product, market, distribution channel, fund performance, time/product duration, etc.

2) Options embedded in the product may impact behavior.

3) Options may be elective or non-elective in nature. Living benefits are often elective and death benefit options are generally non-elective.

4) Elective contractholder options may be more driven by economic conditions than non-elective options.

5) As the value of a product option increases, there is an increased likelihood that contractholders will behave in a manner that maximizes their financial interest (e.g., lower lapses, higher benefit utilization, etc.).

6) Behavior formulas may have both rational and irrational components (irrational behavior is defined as situations where some contractholders may not always act in their best financial interest). The rational component should be dynamic but the concept of rationality need not be interpreted in strict financial terms and might change over time in response to observed trends in contractholder behavior based on increased or decreased financial efficiency in exercising their contractual options.

7) Options that are ancillary to the primary product features may not be significant drivers of behavior. Whether an option is ancillary to the primary product features depends on many things such as:
   a) For what purpose was the product purchased?
   b) Is the option elective or non-elective?
   c) Is the value of the option well known?

8) External influences, including emergence of viatical / life settlement companies, may impact behavior.

A9.2) Aggregate vs. Individual Margins

As noted in Section III)B)8), Prudent Estimate assumptions are developed by applying a margin for uncertainty to the Anticipated Experience assumption. The issue of whether the level of the margin applied to the Anticipated Experience assumption is determined in aggregate or independently for each and every behavior assumption is discussed in Principle 3 in Section II) of this Guideline, which states:

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> The choice of a conservative estimate for each assumption may result in a distorted measure of the total risk. Conceptually, the choice of assumptions and the modeling decisions should be made so that the final result approximates what would be obtained for the Conditional Tail Expectation Amount at the required CTE level if it were possible to calculate results over the joint distribution of all future outcomes. In applying this concept to the actual calculation of the Conditional Tail Expectation Amount, the actuary should be guided by evolving practice and expanding knowledge base in the measurement and management of risk.

Although this Principle discusses the concept of determining the level of margins in aggregate, it notes that the application of this concept shall be guided by evolving practice and expanding knowledge. From a practical standpoint, it may not always be possible to completely apply this concept to determine the level of margins in aggregate for all behavior assumptions.

Therefore, the actuary shall determine Prudent Estimate assumptions independently for each behavior (e.g., mortality lapses, and benefit utilization), using the requirements and guidance in this Appendix and throughout the guideline, unless the actuary can demonstrate that an appropriate method was used to determine the level of margin in aggregate for two or more behaviors.

A9.3) Sensitivity Testing

The impact of behavior can vary by product, time period, etc. Sensitivity testing of assumptions is required and shall be more complex than e.g., base lapse assumption minus 1% across all contracts. A more appropriate sensitivity test in this example might be to devise parameters in a dynamic lapse formula to reflect more out-of-the-money contracts lapsing and/or more holders of in-the-money contracts persisting and eventually utilizing the guarantee. The actuary should apply more caution in setting assumptions for behaviors where testing suggests that stochastic modeling results are sensitive to small changes in such assumptions. For such sensitive behaviors, the actuary shall use higher margins when the underlying experience is less than fully relevant and credible.

A9.4) Specific Considerations and Requirements

Within materiality considerations, the actuary should consider all relevant forms of contractholder behavior and persistency, including but not limited to the following:

1) Mortality (additional guidance and requirements regarding mortality is contained in Appendix 10)

2) Surrenders

3) Partial Withdrawals (Systematic and Elective)

4) Fund Transfers (Switching/Exchanges)

5) Resets/Ratchets of the Guaranteed Amounts (Automatic and Elective)

6) Future Deposits

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It may be acceptable to ignore certain items that might otherwise be explicitly modeled in an ideal world, particularly if the inclusion of such items reduces the calculated provisions. For example:

1) The impact of fund transfers (intra-contract fund "switching") might be ignored, unless required under the terms of the contract (e.g., automatic asset re-allocation/rebalancing, dollar cost averaging accounts, etc.)

2) Future deposits might be excluded from the model, unless required by the terms of the contracts under consideration and then only in such cases where future premiums can reasonably be anticipated (e.g., with respect to timing and amount).

However, the actuary should exercise caution in assuming that current behavior will be indefinitely maintained. For example, it might be appropriate to test the impact of a shifting asset mix and/or consider future deposits to the extent they can reasonably be anticipated and increase the calculated amounts.

Normally, the underlying model assumptions would differ according to the attributes of the contract being valued. This would typically mean that contractholder behavior and persistency may be expected to vary according to such characteristics as (this is not an exhaustive list):

1) Gender

2) Attained age

3) Issue age

4) Contract duration

5) Time to maturity

6) Tax status

7) Fund value

8) Investment option

9) Guaranteed benefit amounts

10) Surrender charges, transaction fees or other contract charges

11) Distribution channel

Unless there is clear evidence to the contrary, behavior assumptions should be no less conservative than past experience. Margins for contractholder behavior assumptions shall assume, without relevant and credible experience or clear evidence to the contrary, that contractholders' efficiency will increase over time.

In determining contractholder behavior assumptions, the company shall use actual experience data directly applicable to the business segment (i.e., direct data) if it is available. In the absence of direct data, the company should then look to use data from a segment that are similar to the business segment (i.e., other than direct experience), whether or not the segment is directly written by the company. If data from a similar business segment are used, the assumption shall be adjusted to reflect differences between the two segments. Margins shall reflect the data uncertainty associated with using data from a similar but not

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identical business segment. The actuary shall document any significant similarities or differences between the two business segments, the data quality of the similar business segment and the adjustments and the margins applied.

Where relevant and fully credible empirical data do not exist for a given contractholder behavior assumption, the actuary shall set the contractholder behavior assumption to reflect the increased uncertainty such that the contractholder behavior assumption is shifted towards the conservative end of the plausible range of expected experience that serves to increase the Aggregate Reserve. If there are no relevant data, the actuary shall set the contractholder behavior assumption to reflect the increased uncertainty such that the contractholder behavior assumption is at the conservative end of the range. Such adjustments shall be consistent with the definition of Prudent Estimate, with the Principles described in Section I, and with the guidance and requirements in this Appendix.

Ideally, contractholder behavior would be modeled dynamically according to the simulated economic environment and/or other conditions. It is important to note, however, that contractholder behavior should neither assume that all contractholders act with 100% efficiency in a financially rational manner nor assume that contractholders will always act irrationally.

A9.5) Dynamic Assumptions

Consistent with the concept of Prudent Estimate assumptions described earlier, the liability model should incorporate margins for uncertainty for all risk factors which are not dynamic (i.e., the non-scenario tested assumptions) and are assumed not to vary according to the financial interest of the contractholder.

The actuary should exercise care in using static assumptions when it would be more natural and reasonable to use a dynamic model or other scenario-dependent formulation for behavior. With due regard to considerations of materiality and practicality, the use of dynamic models is encouraged, but not mandatory. Risk factors which are not scenario tested, but could reasonably be expected to vary according to a stochastic process, or future states of the world (especially in response to economic drivers) may require higher margins and/or signal a need for higher margins for certain other assumptions.

Risk factors that are modeled dynamically should encompass the plausible range of behavior consistent with the economic scenarios and other variables in the model, including the non-scenario tested assumptions. The actuary shall test the sensitivity of results to understand the materiality of making alternate assumptions and follow the guidance discussed above on setting assumptions for sensitive behaviors.

A9.6) Consistency with the CTE Level

All behaviors (i.e., dynamic, formulaic and non-scenario tested) should be consistent with the scenarios used in the CTE calculations (generally, the approximately top 1/3 of the loss distribution). To maintain such consistency, it is not necessary to iterate (i.e., successive runs of the model) in order to determine exactly which scenario results are included in the CTE measure. Rather, in light of the products being valued, the actuary should be mindful of the general characteristics of those scenarios likely to represent the tail of the loss distribution and consequently use Prudent Estimate assumptions for behavior that are reasonable and appropriate in such scenarios. For variable annuities, these “valuation” scenarios would typically display one or more of the following attributes:

1) Declining and/or volatile separate account asset values;

2) Market index volatility, price gaps and/or liquidity constraints;

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3) Rapidly changing interest rates.

The behavior assumptions should be logical and consistent both individually and in aggregate, especially in the scenarios that govern the results. In other words, the actuary should not set behavior assumptions in isolation, but give due consideration to other elements of the model. The interdependence of assumptions (particularly those governing customer behaviors) makes this task difficult and by definition requires professional judgment, but it is important that the model risk factors and assumptions:

1) Remain logically and internally consistent across the scenarios tested;

2) Represent plausible outcomes; and

3) Lead to appropriate, but not excessive, asset requirements.

The actuary should remember that the continuum of "plausibility" should not be confined or constrained to the outcomes and events exhibited by historic experience.

Companies should attempt to track experience for all assumptions that materially affect their risk profiles by collecting and maintaining the data required to conduct credible and meaningful studies of contractholder behavior.

A9.7) Additional Considerations and Requirements for Assumptions Applicable to Guaranteed Living Benefits

Experience for contracts without guaranteed living benefits may be of limited use in setting a lapse assumption for contracts with in-the-money or at-the-money guaranteed living benefits. Such experience may only be used if it is appropriate (e.g., lapse experience on contracts without a living benefit may have relevance to the early durations of contracts with living benefits) and relevant to the business and is accompanied by documentation that clearly demonstrates the relevance of the experience, as discussed in the following paragraph.

The supporting memorandum required by Appendix 8 of this Guideline, shall include a separately identifiable section showing the assumptions used for lapse and utilization assumptions for contracts with guaranteed living benefits in the development of the Conditional Tail Expectation Amount. This section shall be considered part of the supporting memorandum and shall show the formulas used to set the assumptions and describe the key parameters affecting the level of the assumption (e.g., age, duration, in-the-moneyness, during and after the surrender charge period). The section shall include a summary that shows the lapse and utilization rates that result from various combinations of the key parameters. The section shall show any experience data used to develop the assumptions and describe the source, relevance and credibility of that data. If relevant and credible data were not available, the section should discuss how the assumption is consistent with the requirement that the assumption is to be on the conservative end of the plausible range of expected experience. The section shall also discuss the sensitivity tests performed to support the assumption. This separately identifiable section shall be made available on a standalone basis if requested by the Domiciliary Commissioner. If it is requested, the section shall have the same confidential status as the supporting memorandum and the actuarial memorandum supporting the actuarial opinion, as discussed in section A2.3)B).

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Regarding lapse assumptions for contracts with guaranteed living benefits, the section shall include, at a minimum, the following:

1) Actual to expected lapses on two bases, where "expected" equals one of the following:
   a) Prudent estimate assumptions used in the development of the Conditional Tail Expectation Amount;
   b) The assumptions used in the Standard Scenario;

2) The lapse assumptions used in the development of Conditional Tail Expectation Amount and corresponding actual experience separated by:
   a) Logical blocks of business (based on company's assessment);
   b) Duration (at a minimum this should show during the surrender charge period vs. after the surrender charge period);
   c) In-the-moneyness (consistent with how dynamic assumptions are determined); and
   d) Age (to the extent age impacts the election of benefits lapse).

This data shall be separated by experience incurred in the following periods:
   a) In the past year;
   b) In the past three years; and
   c) All years.

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APPENDIX 10 – Specific Guidance and Requirements for Setting Prudent Estimate Mortality Assumptions

A10.1) Overview

A) Intent. The guidance and requirements in this Appendix apply for setting Prudent Estimate mortality assumptions when determining the Conditional Tail Expectation Amount (whether using projections or the Alternative Methodology). The intent is for Prudent Estimate mortality assumptions to be based on facts, circumstances and appropriate actuarial practice (where more than one approach to appropriate actuarial practice exists, the actuary should select the practice that the actuary deems most appropriate under the circumstances) with only a limited role for unsupported actuarial judgment.

B) Description. Prudent Estimate mortality assumptions are determined by first developing expected mortality curves based on either available experience or published tables. Where necessary, margins are applied to the experience to reflect data uncertainty. The expected mortality curves are then adjusted based on the credibility of the experience used to determine the expected mortality curve. Section A10.2) addresses guidance and requirements for determining expected mortality curves and section A10.3) addresses guidance and requirements for adjusting the expected mortality curves to determine Prudent Estimate mortality.

Finally, the credibility-adjusted tables shall be adjusted for mortality improvement (where such adjustment is permitted or required) using the guidance and requirements in section A10.4).

C) Business Segments. For purposes of setting Prudent Estimate mortality assumptions, the products falling under the scope of the Guideline shall be grouped into business segments with different mortality assumptions. The grouping should generally follow the pricing, marketing, management and/or reinsurance programs of the company. Where less refined segments are used for setting the mortality assumption than is used in business management the documentation should address the impact, if material, of the less refined segmentation on the resulting reserves.

D) Margin for Data Uncertainty. The expected mortality curves that are determined in section A10.2) may need to include a margin for data uncertainty. The margin could be in the form of an increase or a decrease in mortality, depending on the business segment under consideration. The margin shall be applied in a direction (i.e., increase or decrease in mortality) that results in a higher reserve. A sensitivity test may be needed to determine the appropriate direction of the provision for uncertainty to mortality. The test could be a prior year mortality sensitivity analysis of the business segment or an examination of current representative cells of the segment.

For purposes of this Appendix, if mortality must be increased (decreased) to provide for uncertainty the business segment is referred to as a plus (minus) segment.

It may be necessary, because of a change in the mortality risk profile of the segment, to reclassify a business segment from a plus (minus) segment to a minus (plus) segment to the extent compliance with this subsection requires such a reclassification.

A10.2) Determination of Expected Mortality Curves

A) Experience Data. In determining expected mortality curves the company shall use actual experience data directly applicable to the business segment (i.e., direct data) if it is available. In the absence of direct data, the company should then look to use data from a segment that is similar to the business segment (i.e., other than direct experience). See section B) below for

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additional considerations. Finally, if there is no data, the company shall use the applicable table, as required in subsection C) below.

B) Data Other than Direct Experience. If expected mortality curves for a segment are being determined using data from a similar business segment (whether or not directly written by the company), the actuary shall document any similarities or differences between the two business segments (e.g., type of underwriting, marketing channel, average policy size, etc.). The actuary shall also document the data quality of the mortality experience of the similar business. Adjustments shall be applied to the data to reflect differences between the business segments and margins shall be applied to the adjusted expected mortality curves to reflect the data uncertainty associated with using data from a similar but not identical business segment. The actuary shall document the adjustments and the margins applied.

To the extent the mortality of a business segment is reinsured, any mortality charges that are consistent with the company's own pricing and applicable to a substantial portion of the mortality risk may also be a reasonable starting point for the determination of the company's expected mortality curves. The actuary shall document the application of such reinsurance charges and how they were used to set the company's expected mortality curves for the segment.

C) No Data Requirements. When little or no experience or information is available on a business segment, the company shall use expected mortality curves that would produce expected deaths no less than using 100% of the 1994 Variable Annuity MGDB mortality table for a plus segment and expected deaths no greater than 100% of the Annuity 2000 table for a minus segment. If mortality experience on the business segment is expected to be atypical (e.g., demographics of target markets are known to have higher (lower) mortality than typical), these "no data" mortality requirements may not be adequate.

D) Additional Considerations Involving Data. The following considerations shall apply to mortality data specific to the business segment for which assumptions are being determined (i.e., direct data discussed in subsection A) above or other than direct data discussed in subsection B) above).

1) Underreporting of deaths. Mortality data shall be examined for possible underreporting of deaths. Adjustments shall be made to the data if there is any evidence of underreporting. Alternatively, exposure by lives or amounts on contracts for which death benefits were in the money may be used to determine expected mortality curves. Underreporting on such exposures should be minimal; however, this reduced subset of data will have less credibility.

2) Experience by contract duration. Experience of a plus segment shall be examined to determine if mortality by contract duration increases materially due to selection at issue. In the absence of information, the actuary shall assume that expected mortality will increase by contract duration for an appropriate select period. As an alternative, if the actuary determines that mortality is impacted by selection, the actuary could apply margins to the expected mortality in such a way that the actual mortality modeled does not depend on contract duration.

3) Modification and Relevance of data. Even for a large company the quantity of life exposures and deaths are such that a significant amount of smoothing may be required to determine expected mortality curves from mortality experience. Expected mortality curves, when applied to the recent historic exposures (e.g., 3 to 7 years), should not result in an estimate of aggregate number of deaths less (greater) than the actual number deaths during the exposure period for plus (minus) segments. If this condition is not satisfied,

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the actuary must document the rationale in support of using expected mortality that differs from recent mortality experience.

In determining expected mortality curves (and the credibility of the underlying data), older data may no longer be relevant. The "age" of the experience data used to determine expected mortality curves should be documented. There should be commentary in the documentation on the relevance of the data (e.g., any actual and expected changes in markets, products and economic conditions over the historic and projected experience).

4) Other considerations. In determining expected mortality curves, consideration should be given to factors that include, but are not limited to, trends in mortality experience, trends in exposure, volatility in year-to-year A/E mortality ratios, mortality by lives relative to mortality by amounts, changes in the mix of business and product features that could lead to mortality selection.

E) Documentation Requirements.

1) All Segments. The documentation should include any material considerations necessary to understand the development of mortality assumptions for the statutory valuation even if such considerations are not explicitly mentioned in this section. The documentation should be explicit when material judgments were required and such judgments had to be made without supporting historic experience.

The documentation shall:

a) Explain the rationale for the grouping of contracts into different segments for the determination of mortality assumptions and characterize the type and quantity of business that constitute each segment.
b) Describe how each segment was determined to be a plus or minus segment.
c) Summarize any mortality studies used to support mortality assumptions, quantify the exposures and corresponding deaths, describe the important characteristics of the exposures and comment on unusual data points or trends.
d) Document the age of the experience data used to determine expected mortality curves and comment on the relevance of the data.
e) Document the mathematics used to adjust mortality based on credibility and summarize the result of applying credibility to the mortality segments.
f) Discuss any assumptions made on mortality improvements, the support for such assumptions and how such assumptions adjusted the modeled mortality.
g) Describe how the expected mortality curves compare to recent historic experience and comment on any differences.
h) Discuss how the mortality assumptions are consistent with the goal of achieving the required CTE level over the joint distribution of all future outcomes, in keeping with Principle #3 and Appendix 9.

If the study was done on a similar business segment, identify the differences in the business segment on which the data were gathered and the business segment on which the data were used to determine mortality assumptions for the statutory valuation. Describe how these differences were reflected in the mortality used in modeling.

If mortality assumptions for the statutory valuation were based in part on reinsurance rates, document how the rates were used to set expected mortality (e.g., assumptions made on loadings in the rates and/or whether the assuming company provided their expected mortality and the rationale for their assumptions).

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2) Plus Segments. For a plus segment, the documentation shall also discuss the examination of the mortality data for the underreporting of deaths and experience by duration, and describe any adjustments that were made as a result of the examination.

3) Minus Segments. For a minus segment the documentation shall also discuss how the mortality deviations on minus segments compare to those on any plus segments. To the extent the overall margin is reduced, the documentation should include support for this assumption.

A10.3) Adjustment for Credibility to Determine Prudent Estimate Mortality

A) Adjustment for Credibility. The expected mortality curves determined in section A10.2) shall be adjusted based on the credibility of the experience used to determine the curves in order to arrive at Prudent Estimate mortality. The adjustment for credibility shall result in blending the expected mortality curves with a mortality table consistent with a statutory valuation mortality table. For a plus segment, the table shall be consistent with 100% of the 1994 Variable Annuity MGDB table (or a more recent mortality table adopted by the NAIC to replace this table). For a minus segment, the table shall be consistent with 100% of the 2000 Annuity table (or a more recent mortality table adopted by the NAIC to replace that table). The approach used to adjust the curves shall suitably account for credibility.[40]

B) Adjustment of Statutory Valuation Mortality for Improvement. For purposes of the adjustment for credibility, the statutory valuation mortality table for a plus segment may be and the statutory valuation mortality table for a minus segment must be adjusted for mortality improvement. Such adjustment shall reflect applicable published industrywide experience from the effective date of the respective statutory valuation mortality table to the experience weighted average date underlying the data used to develop the expected mortality curves (discussed in section A10.2)).

C) Credibility Procedure. The credibility procedure used shall:

1) Produce results that are reasonable in the professional judgment of the actuary,

2) Not tend to bias the results in any material way,

3) Be practical to implement,

4) Give consideration to the need to balance responsiveness and stability,

5) Take into account not only the level of aggregate claims but the shape of the mortality curve, and

6) Contain criteria for full credibility and partial credibility that have a sound statistical basis and be appropriately applied.

Documentation of the credibility procedure used shall include a description of the procedure, the statistical basis for the specific elements of the credibility procedure, and any material changes from prior credibility procedures.

[40] For example, when credibility is zero, an appropriate approach should result in a mortality assumption consistent with 100% of the statutory valuation mortality table used in the blending.

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D) Further Adjustment of the Credibility-adjusted Table for Mortality Improvement. The credibility-adjusted table used for plus segments may be and the credibility adjusted date used for minus segments must be adjusted for applicable published industrywide experience from the experience weighted average date underlying the company experience used in the credibility process to the valuation date.

Any adjustment for mortality improvement beyond the valuation date is discussed in section A10.4).

A10.4) Future Mortality Improvement

The mortality assumption resulting from the requirements of section A10.3) shall be adjusted for mortality improvements beyond the valuation date if such an adjustment would serve to increase the resulting Conditional Tail Expectation Amount. If such an adjustment would reduce the Conditional Tail Expectation Amount, such assumptions are permitted, but not required. In either case, the assumption must be based on current relevant data with a margin for uncertainty (increasing assumed rates of improvement if that results in a higher reserve, reducing them otherwise).

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APPENDIX 11 - 1994 Variable Annuity MGDB Mortality Table

FEMALE Age Last Birthday

AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$
1	0.519	24	0.344	47	1.371	70	16.957	93	192.270
2	0.358	25	0.346	48	1.488	71	18.597	94	210.032
3	0.268	26	0.352	49	1.619	72	20.599	95	228.712
4	0.218	27	0.364	50	1.772	73	22.888	96	248.306
5	0.201	28	0.382	51	1.952	74	25.453	97	268.892
6	0.188	29	0.403	52	2.153	75	28.372	98	290.564
7	0.172	30	0.428	53	2.360	76	31.725	99	313.211
8	0.158	31	0.455	54	2.589	77	35.505	100	336.569
9	0.154	32	0.484	55	2.871	78	39.635	101	360.379
10	0.159	33	0.514	56	3.241	79	44.161	102	385.051
11	0.169	34	0.547	57	3.713	80	49.227	103	411.515
12	0.185	35	0.585	58	4.270	81	54.980	104	439.065
13	0.209	36	0.628	59	4.909	82	61.410	105	465.584
14	0.239	37	0.679	60	5.636	83	68.384	106	488.958
15	0.271	38	0.739	61	6.460	84	75.973	107	507.867
16	0.298	39	0.805	62	7.396	85	84.432	108	522.924
17	0.315	40	0.874	63	8.453	86	94.012	109	534.964
18	0.326	41	0.943	64	9.611	87	104.874	110	543.622
19	0.333	42	1.007	65	10.837	88	116.968	111	548.526
20	0.337	43	1.064	66	12.094	89	130.161	112	550.000
21	0.340	44	1.121	67	13.318	90	144.357	113	550.000
22	0.343	45	1.186	68	14.469	91	159.461	114	550.000
23	0.344	46	1.269	69	15.631	92	175.424	115	1000.000

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APPENDIX 11 - 1994 Variable Annuity MGDB Mortality Table

MALE Age Last Birthday

AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$
1	0.587	24	0.760	47	2.366	70	29.363	93	243.533
2	0.433	25	0.803	48	2.618	71	32.169	94	264.171
3	0.350	26	0.842	49	2.900	72	35.268	95	285.199
4	0.293	27	0.876	50	3.223	73	38.558	96	305.931
5	0.274	28	0.907	51	3.598	74	42.106	97	325.849
6	0.263	29	0.935	52	4.019	75	46.121	98	344.977
7	0.248	30	0.959	53	4.472	76	50.813	99	363.757
8	0.234	31	0.981	54	4.969	77	56.327	100	382.606
9	0.231	32	0.997	55	5.543	78	62.629	101	401.942
10	0.239	33	1.003	56	6.226	79	69.595	102	422.569
11	0.256	34	1.005	57	7.025	80	77.114	103	445.282
12	0.284	35	1.013	58	7.916	81	85.075	104	469.115
13	0.327	36	1.037	59	8.907	82	93.273	105	491.923
14	0.380	37	1.082	60	10.029	83	101.578	106	511.560
15	0.435	38	1.146	61	11.312	84	110.252	107	526.441
16	0.486	39	1.225	62	12.781	85	119.764	108	536.732
17	0.526	40	1.317	63	14.431	86	130.583	109	543.602
18	0.558	41	1.424	64	16.241	87	143.012	110	547.664
19	0.586	42	1.540	65	18.191	88	156.969	111	549.540
20	0.613	43	1.662	66	20.259	89	172.199	112	550.000
21	0.642	44	1.796	67	22.398	90	188.517	113	550.000
22	0.677	45	1.952	68	24.581	91	205.742	114	550.000
23	0.717	46	2.141	69	26.869	92	223.978	115	1000.000

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APPENDIX 11 - 1994 Variable Annuity MGDB Mortality Table

FEMALE Age Nearest Birthday

AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$
1	0.628	24	0.344	47	1.316	70	16.239	93	184.435
2	0.409	25	0.344	48	1.427	71	17.687	94	201.876
3	0.306	26	0.348	49	1.549	72	19.523	95	220.252
4	0.229	27	0.356	50	1.690	73	21.696	96	239.561
5	0.207	28	0.372	51	1.855	74	24.107	97	259.807
6	0.194	29	0.392	52	2.050	75	26.832	98	281.166
7	0.181	30	0.415	53	2.256	76	29.954	99	303.639
8	0.162	31	0.441	54	2.465	77	33.551	100	326.956
9	0.154	32	0.470	55	2.713	78	37.527	101	350.852
10	0.155	33	0.499	56	3.030	79	41.826	102	375.056
11	0.163	34	0.530	57	3.453	80	46.597	103	401.045
12	0.175	35	0.565	58	3.973	81	51.986	104	428.996
13	0.195	36	0.605	59	4.569	82	58.138	105	456.698
14	0.223	37	0.652	60	5.250	83	64.885	106	481.939
15	0.256	38	0.707	61	6.024	84	72.126	107	502.506
16	0.287	39	0.771	62	6.898	85	80.120	108	518.642
17	0.309	40	0.839	63	7.897	86	89.120	109	531.820
18	0.322	41	0.909	64	9.013	87	99.383	110	541.680
19	0.331	42	0.977	65	10.215	88	110.970	111	547.859
20	0.335	43	1.037	66	11.465	89	123.714	112	550.000
21	0.339	44	1.091	67	12.731	90	137.518	113	550.000
22	0.342	45	1.151	68	13.913	91	152.286	114	550.000
23	0.344	46	1.222	69	15.032	92	167.926	115	1000.000

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APPENDIX 11 - 1994 Variable Annuity MGDB Mortality Table

MALE Age Nearest Birthday

AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$	AGE	$1000q_x$
1	0.701	24	0.738	47	2.246	70	28.068	93	234.658
2	0.473	25	0.782	48	2.486	71	30.696	94	255.130
3	0.393	26	0.824	49	2.751	72	33.688	95	276.308
4	0.306	27	0.860	50	3.050	73	36.904	96	297.485
5	0.280	28	0.892	51	3.397	74	40.275	97	317.953
6	0.268	29	0.922	52	3.800	75	44.013	98	337.425
7	0.257	30	0.948	53	4.239	76	48.326	99	356.374
8	0.238	31	0.971	54	4.706	77	53.427	100	375.228
9	0.230	32	0.992	55	5.234	78	59.390	101	394.416
10	0.233	33	1.003	56	5.854	79	66.073	102	414.369
11	0.245	34	1.004	57	6.601	80	73.366	103	436.572
12	0.267	35	1.006	58	7.451	81	81.158	104	460.741
13	0.302	36	1.020	59	8.385	82	89.339	105	484.644
14	0.352	37	1.054	60	9.434	83	97.593	106	506.047
15	0.408	38	1.111	61	10.629	84	105.994	107	522.720
16	0.463	39	1.182	62	12.002	85	115.015	108	534.237
17	0.509	40	1.268	63	13.569	86	125.131	109	542.088
18	0.544	41	1.367	64	15.305	87	136.815	110	546.908
19	0.573	42	1.481	65	17.192	88	150.191	111	549.333
20	0.599	43	1.599	66	19.208	89	164.944	112	550.000
21	0.627	44	1.725	67	21.330	90	180.886	113	550.000
22	0.658	45	1.867	68	23.489	91	197.834	114	550.000
23	0.696	46	2.037	69	25.700	92	215.601	115	1000.000

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Actuarial Guideline XLIII

CARVM FOR VARIABLE ANNUITIES

Table of Contents

Section I Background
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Section I) Background

This Actuarial Guideline (Guideline) interprets the standards for the valuation of reserves for variable annuity and other contracts involving certain guaranteed benefits similar to those offered with variable annuities. The Guideline codifies the basic interpretation of the Commissioners Annuity Reserve Valuation Method (CARVM) by clarifying the assumptions and methodologies that will comply with the intent of the Standard Valuation Law. It also applies similar assumptions and methodologies to contracts that contain characteristics similar to those described in the scope, but that are not directly subject to CARVM.

In developing the Guideline, two regulatory sources provided guidance. First, the Standard Valuation Law defines CARVM as the greatest present value of future guaranteed benefits. Second, the NAIC Model Variable Annuity Regulation (VAR) states that the "reserve liability for variable annuities shall be established pursuant to the requirements of the Standard Valuation Law in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees."

During 2019 this Guideline was amended to follow the reserve requirements provided in VM-21 of the *Valuation Manual*. This was done for uniformity for all coverages within scope regardless of whether they were issued prior to or on and after the operative date of the *Valuation Manual*. This was also done to reflect the extensive analysis carried out by the NAIC, Oliver Wyman consulting for the NAIC, and industry participants for improvements to the variable annuity framework.

Section II) Scope

A) The Guideline applies to contracts, and product features on contracts, issued on or after January 1, 1981, and prior to the date that the *Valuation Manual* becomes effective in the applicable jurisdiction, whether directly written or assumed through reinsurance, falling into any of the following categories:

1) Variable deferred annuity contracts subject to the Commissioner's Annuity Reserve Valuation Method (CARVM), whether or not such contracts contain Guaranteed Minimum Death Benefits (GMDBs), or Variable Annuity Guaranteed Living Benefits (VAGLBs);

2) Variable immediate annuity contracts, whether or not such contracts contain GMDBs or VAGLBs;

3) Group annuity contracts that are not subject to CARVM, but contain guarantees similar in nature[1] to GMDBs, VAGLBs, or any combination thereof; and

[1] The term "similar in nature," as used in sections II)A)3) and II)A)4) is intended to capture both current products and benefits as well as product and benefit designs that may emerge in the future. Examples of the currently known designs are listed in footnote 2. Any product or benefit design that does not clearly fit the Scope should be evaluated on a case-by-case basis taking into consideration factors that include, but are not limited to, the nature of the guarantees, the definitions of GMDB and VAGLB in

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4) All other products that contain guarantees similar in nature to GMDBs or VAGLBs, even if the insurer does not offer the mutual funds or variable funds to which these guarantees relate, where there is no other explicit reserve requirement.[2]

If such a benefit is offered as part of a contract that has an explicit reserve requirement and that benefit does not currently have an explicit reserve requirement:

a) The Guideline shall be applied to the benefit on a standalone basis (i.e., for purposes of the reserve calculation, the benefit shall be treated as a separate contract);

b) The reserve for the underlying contract is determined according to the explicit reserve requirement; and

c) The reserve held for the contract shall be the sum of a) and b).

B) The company may elect to apply these requirements to contracts and product features on contracts, whether directly written or assumed through reinsurance, falling into any of the categories defined in Section II.A. and issued prior to January 1, 1981.

C) The Guideline does not apply to contracts falling under the scope of the NAIC Model Modified Guaranteed Annuity Regulation (Model #255); however, it does apply to contracts listed above that include one or more subaccounts containing features similar in nature to those contained in Modified Guaranteed Annuities (e.g., market value adjustments).

D) Separate account annuity contracts that guarantee an index and do not offer GMDBs or VAGLBs are excluded from the scope of the Guideline.

Section III) Reserve Requirements

A) Reserves shall be determined by following the requirements in VM-21 from the version of the NAIC *Valuation Manual* applicable for that valuation date. For purposes of determining reserves, at the election of the company, the contracts subject to this Guideline may be aggregated with the contracts subject to VM-21 of the *Valuation Manual*. Alternatively, the company may elect to not aggregate the contracts subject to this Guideline with those subject to VM-21 of the *Valuation Manual*, and value these as a separate group of contracts.

B). The development of the reserves shall be documented following the requirements in VM-31 of the NAIC *Valuation Manual* applicable for that valuation date.

Section IV) Effective Date and Transition

A) This Actuarial Guideline applies for valuations on or after January 1, 2020. The phase-in provisions of VM-21 also apply for the contracts and product features subject to the Guideline.

VM-01 and whether the contractual amounts paid in the absence of the guarantee are based on the investment performance of a market-value fund or market-value index (whether or not part of the company's separate account).

[2] For example, a group life contract that wraps a GMDB around a mutual fund would generally fall under the scope of the Guideline since there is not an explicit reserve requirement for this type of group life contract. However, for an individual variable life contract with a GMDB and a benefit similar in nature to a VAGLB, the Guideline would generally apply only to the VAGLB-type benefit, since there is an explicit reserve requirement that applies to the variable life contract and the GMDB.

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B) A company may elect to apply these requirements for the valuation on December 31, 2019, in lieu of the requirements of the prior version of this Guideline. If so elected, the reserves will be established by following the requirements of VM-21 from the 2020 NAIC *Valuation Manual* and the documentation requirements of VM-31 from the 2020 NAIC *Valuation Manual*.

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Actuarial Guideline XLIV

GROUP TERM LIFE WAIVER OF PREMIUM DISABLED LIFE RESERVES

I. Background

Section 4.G. of the Standard Valuation Law establishes tables approved by the commissioner as the minimum standard for computing reserves for group life insurance and special benefits. The purpose of this Actuarial Guideline (Guideline) is to determine the minimum standard of valuation for group term life waiver of premium disabled life benefits and to recognize the 2023 Group Term Life Waiver (GTLW) Mortality and Recovery Valuation Tables. The Guideline also maintains recognition of the 2005 Group Term Life Waiver Mortality and Recovery Tables for purposes outlined in Section V of the Guideline.

Claims subject to Section V of the Guideline (applicable to individuals who become disabled on or after January 1, 2009, and on or before December 31, 2022) may be valued under Section VI (applicable to individuals who become disabled on or after January 1, 2023) at the election of the insurer provided these claims, for all future valuation dates, are valued under that section or any newer succeeding section at the insurer's election.

Group term life policies do not maintain contract reserves beyond the duration of the policy issued to the group policyholder. However, some policies guarantee an extended death benefit to an individual insured who is disabled according to the terms of the policy. Thus, to the extent such guarantees are made, a disabled life reserve must be maintained for each individual that is so disabled. However, prior to the creation of this guideline, there has been no formal guidance regarding the calculation of these disabled life reserves.

II. Scope

This guideline applies to group term life certificates on individuals who become disabled on or after January 1, 2009. Based on the provisions of Section 4.G. of the Standard Valuation Law, companies may apply this to group term life certificates on individuals who became disabled prior to January 1, 2009, provided they obtain permission from the commissioner.

III. Definitions

"2005 GTLW Mortality Table", "2005 GTLW Recovery Table", "2023 GTLW Mortality Valuation Table", and "2023 GTLW Recovery Valuation Table" mean the tables found at https://content.naic.org/sites/default/files/actuary-acadamy-soari-glwp-table-rates.xlsx.

IV. The Group Waiver of Premium Reserve Calculation

A. The minimum standard of valuation for group term life waiver of premium disabled life benefits shall be the present value of the death benefit payable discounted for interest and recovery. Since there is not a contract reserve based upon an aggregate table, the discounted value of waived premiums is inadequate to support this liability.

B. The maximum interest rate to be used in determining the minimum valuation standard for any group term life waiver of premium disabled life benefit incurred on or after the effective date of this guideline shall be the maximum rate permitted by law in the valuation of life insurance of the same guaranteed duration issued on the same date as the claim incurral date of disability. For most groups and companies this rate shall be the rate for life insurance with guaranteed duration greater than 20 years. The guaranteed duration used to determine the life insurance rate of interest is equal to the largest term in years between the point at which any individual in the group may become

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disabled and the point at which no death benefit is available. Thus, if a person could become disabled at age 20, and remain disabled, and receive a benefit upon death before age 65, the guaranteed duration would be 45 years.

C. The valuation tables were derived from employer-employee group life experience. Other forms of group term life insurance are also subject to the same requirements if they contain similar extended death benefit provisions.

V. Group Term Life Certificates on Individuals Who Become Disabled on or After January 1, 2009, and on or Before December 31, 2022

Claims subject to this section of the Guideline may be valued under Section VI (applicable to disabilities incurred January 1, 2023 and later) at the election of the insurer provided these claims, for all future valuation dates, are valued under that section or any newer succeeding section at the insurer's election. The 2005 GTLW Mortality and Recovery Tables and the 2023 GTLW Mortality and Recovery Valuation Tables can be found here: https://content.naic.org/sites/default/files/actuary-acadamy-soari-glwp-table-rates.xlsx.

A. Group Waiver of Premium Reserve Calculation

1. Except as provided in Section V.B., the 2005 GTLW Mortality and Recovery Tables shall be used for determining the minimum standard of valuation for any group term life waiver of premium disabled life benefit incurred during the effective period of this section of this Guideline. Section V.B. offers ways to modify the underlying rates of mortality or recovery if they differ from those associated with the underlying experience in the valuation table.

B. Use of Company Experience

1. The Appointed Actuary shall review company experience at least once every five years. The review of company experience can range from a detailed experience study to a high level analysis. The extent of the review must be sufficient to enable the Appointed Actuary to defend any conclusion reached. Company experience shall:

i. Be segmented into policies with similar benefits, on individuals of each gender;

ii. Be experience-specific to the company;

iii. Include all relevant experience in the past three most recent years;

iv. Exclude experience that is not in the past six most recent years;

v. Otherwise be relevant, in accordance with the professional judgment of the Appointed Actuary; and

vi. Not be deemed irrelevant by the commissioner.

2. The commissioner may require a company to use its experience based upon the most recent review referenced in Section V.B.1. to establish its specific valuation tables if:

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i. Actual mortality experience is reasonably expected to be greater than 90% of the 2005 GTLW Mortality Tables; or

ii. Actual recovery experience is reasonably expected to be less than 125% of the 2005 GTLW Recovery Tables.

Under these circumstances, the commissioner may require a company to use the process set out in Section V.B.4. and establish for the company a minimum value for Z.

3. A company may use its experience exclusively without reference to the standard tabular mortality expected experience or to the standard tabular recovery expected experience to create its specific valuation tables if:

i. The Appointed Actuary can demonstrate and certify the following:

a) The company-specific valuation tables are based on company experience with allowances for graduation and margins for adverse experience;

b) The company-specific mortality valuation tables used for computing minimum reserves for group term life waiver of premium benefits are such that there is at least an 85% statistical confidence that the actual annual aggregate mortality will be less than the mortality in the company-specific-mortality valuation tables; and

c) The company-specific recovery valuation tables used for computing minimum reserves for group term life waiver of premium benefits are such that there is at least an 85% statistical confidence that the actual annual aggregate recoveries will be greater than the recoveries in the company-specific recovery valuation tables.

ii. The company has written permission from the domiciliary commissioner to use the company-specific valuation tables.

iii. Unless otherwise exempted or required, the specific valuation tables shall apply to the computation of minimum reserves for group term life waiver of premium disabled life benefits for claims incurred during or after the calendar year in which the study was performed.

iv. The company shall not use mortality and recovery tables with rates that produce reserves less than the reserves produced by using 75% of the 2005 GTLW Mortality Tables and 160% of the 2005 GTLW Recovery Tables for all durations of disability combined.

4. If not invoking Section V.B.3., a company may use a credibility-weighted combination of company mortality experience with the 2005 GTLW Mortality Tables and/or of company recovery experience with the 2005 GTLW Recovery Tables to create its specific valuation tables.

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i. The blended tables for each gender and type of experience (mortality and recovery) shall be computed using the formula Blended Table = T x S, where:

a) Z shall be a credibility weighting factor, between 0 and 1, developed by the Appointed Actuary using credibility theory methods not unacceptable to the commissioner;

b) F shall be the ratio of the company's actual experience to the expected experience for the 2005 GTLW Mortality and Recovery Tables for each gender and type of experience (mortality and recovery);

c) M shall be 1.12 for mortality tables and 0.80 for recovery tables. The values provide a smooth transition between the 2005 tables and company experience when Z = 1;

d) S shall be the 2005 GTLW Mortality and Recovery Tables; and

e) T shall be computed using the following steps:

Step 1: Compute the raw value of T = [Z x (F x M) + (1 – Z)].

Step 2: Round T to the nearest 5%.

Step 3: If the absolute difference between the T produced in step 2 and the value of T utilized immediately prior to the study is less than 10%, then set T equal to the value of T utilized immediately prior to the study.

Step 4: For all durations of disability, combined for each gender, set the value of T to the greater of 75% and the T resulting from step 3 for mortality and set the value of T to the lesser of 160% and the T resulting from step 3 for recovery.

ii. The company has written permission from the domiciliary commissioner to use the blended valuation tables.

iii. Unless otherwise exempted or required, the specific valuation tables shall apply to the computation of minimum reserves for group term life waiver of premium disabled life benefits for claims incurred during or after the calendar year in which the study was performed.

VI. Group Term Life Certificates on Individuals Who Become Disabled on or After January 1, 2023

A. When the insurer follows the instructions provided in this Guideline, the selected claim mortality rates and recovery rates automatically meet the minimum standard for computing reserves as established by Section 4.G. of the Standard Valuation Law.

B. Valuation Table Modifications for Company Experience

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If not invoking the small company exception specified in Section VI.D., a company must use a credibility-weighted combination of its own claim mortality experience and claim recovery experience with the 2023 GTLW Mortality and Recovery Valuation Tables to create its specific valuation table.

i. For claim durations within the elimination period, mortality rates and recovery rates may be developed as below consistent with other Duration Groups or in any other manner deemed appropriate by the actuary. With respect to credibility, any value between 0 and 1 that the actuary deems appropriate for the block may be used.

ii. For claim durations beyond the elimination period, the valuation mortality rates and recovery rates shall be computed using the mortality rates from the 2023 GTLW Mortality Valuation Table (S_M) and recovery rates from the 2023 GTLW Recovery Valuation Table (S_R) multiplied by mortality experience adjustment factors (T_M) and recovery experience adjustment factors (T_R) that are calculated separately for three different duration groups for mortality and separately for three different duration groups for recovery.

Valuation Mortality Rate = T_M x S_M

Valuation Recovery Rate = T_R x S_R

The duration groups are defined as follows:

Group 1: duration > the satisfaction of the elimination period and duration <= 24 months
Group 2: duration > 24 months and duration <= 60 months
Group 3: duration > 60 months

a) S_M and S_R shall be the mortality rates and recovery rates respectively from the 2023 GTLW Mortality and Recovery Valuation Tables.

b) T_M shall be computed as $T_M = [Z_M \times F_M + (1 - Z_M)] \times (1 + M_M)$ and T_R shall be computed as $T_R = [Z_R \times F_R + (1 - Z_R)] \times (1 - M_R)$.

where

1) Z_M shall be a mortality credibility weighting factor, between 0 and 1, developed for each duration group according to the following specifications:

Group 1-3: $Z_M = Min\left(\sqrt{N_M / K_M}, 1\right)$ where N_M is the number of expected death counts determined by using claim mortality rates from the 2023 GTLW Mortality Valuation Table, and

2) K_M is a set of constants defined by duration group as follows for mortality:

Group 1: K_M = 800
Group 2: K_M = 800
Group 3: K_M = 800

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3) Z_R shall be a recovery credibility weighting factor, between 0 and 1, developed for each duration group according to the following specifications:

Group 1-3: $Z_R = Min\left(\sqrt{N_R/K_R}, 1\right)$ where N_R is the number of expected recovery counts determined by using claim recovery rates from the 2023 GTLW Recovery Valuation Table, and

4) K_R is a set of constants defined by duration group as follows for recoveries:

Group 1: K_R = 1,700 Group 3: K_R = 1,700
Group 2: K_R = 1,700

5) F_M shall be the ratio of the company's actual death counts to the expected death counts in the 2023 GTLW Mortality Valuation Table for each duration group specified above and F_R shall be the ratio of the company's actual recovery counts to the expected recovery counts in the 2023 GTLW Recovery Valuation Table for each duration group specified above.

If the actuary has reserve adequacy or other significant analysis that demonstrates in the development and use of company-specific experience (see Section VI.C. below) that an alternative measurement is deemed appropriate, such as:

I. Use of some other weighting of claims (for example, death benefit amount) that is not only appropriate for measuring actual to expected (A to E), but also is expected to generally produce reserves not less than those produced by using a claim count measurement.

II. Use of an increased mortality credibility factor Z_M if F_M is greater than 1 and / or use of an increased recovery credibility factor Z_R if F_R is less than 1 to give unfavorable company experience more weight.

6) M_M and M_R are the company experience margins for mortality and recovery respectively, determined for each duration group, according to the following formulas:

$$M_M = Min\left(15\%, Max\left(5\%, 3\% + 1.65 * \sqrt{A_M/C_M}\right)\right)$$

$$M_R = Min\left(15\%, Max\left(5\%, 3\% + 1.65 * \sqrt{A_R/C_R}\right)\right)$$

where A_M is a set of constants defined by duration group as follows for mortality:

Group 1: A_M = 1.0 Group 3: A_M = 1.0
Group 2: A_M = 1.0

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and A_R is a set of constants defined by duration group as follows for recoveries:

Group 1: $A_R = 2.0$ Group 3: $A_R = 2.0$
Group 2: $A_R = 2.0$

and C_M shall be the company's actual number of death counts by duration group.

and C_R shall be the company's actual number of recovery counts by duration group.

These are the minimum values for the definition of M_M and M_R prior to any reserve adequacy analysis. Adequacy tests and analysis of experience (for example, sharpness of fluctuations, trends over the period of the mortality rate study or recovery rate study, changing claims practices) may indicate that larger values of M_M or M_R may be more appropriate. If so, such values are deemed appropriate.

iii. The company shall not use mortality rates that are less than those produced by computing T_M as $T_M = 0.75$

C. Company-Specific Experience – Own Experience Measurement

In computing values F_M, F_R, T_M, and T_R to comply with section VI.B. above, the Appointed Actuary may consider the following:

i. Segment the company claim mortality experience and claim recovery experience into any major subgroups that may produce significantly different results (for example, market niches, claims operations, and unique benefit designs).

ii. Combine affiliated statutory entities and assumed reinsurance, where claim management is under a common structure, when considering company experience. It is also appropriate to evaluate experience separately when specific blocks of company business have distinct claim management practices or significantly different risk characteristics.

iii. Include all relevant experience the company is capable of providing for as many of the last five years as possible (not including the lag period described below). However, there are two situations where using other than a five-year period may be more appropriate. The first is when a company's experience in a longer period not only increases credibility but is still relevant and appropriate for the company's products and claim management practices. In this case, the period to be used is not to exceed ten years. The second is for a company that has had significant changes in product and/or claim management practices within the past five years that has diminished the relevance of the company's experience early in the five-year period. In this second situation, less than five years of experience may be used for any duration band for which there is compelling logic and when either the company's experience to be used is at least 90% credible, or the shorter experience period produces higher reserves than using five years.

iv. Recognize a suitable lag period to allow for a full resolution of claim status. For example, the lag period used in the 2019 Group Term Life Waiver Experience Study performed by the Society of Actuaries was 12 months. However, the

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Appointed Actuary may use a different lag period based on his or her company experience. For example, company experience indicates that all changes after the selected lag period are negligible.

v. Measure actual (A) to expected (E) deaths and A to E recoveries based on claim count (unless another weighting is deemed more appropriate, as mentioned in Section VI(B)(ii)(b)(5)), where the E is based on expected deaths and recoveries, respectively, from the 2023 GTLW Mortality Valuation Table and the 2023 GTLW Recovery Valuation Table. Claim count is also used in the measurement of credibility.

vi. Recognize where appropriate any flexibility built into the 2023 GTLW Mortality and Recovery Valuation Tables, such as not utilizing diagnosis-specific mortality rates and recovery rates when the information is deemed unreliable.

vii. Do not count as deaths or recoveries those claims that are closed due to settlement, or that have reached the end of the maximum benefit duration, or that are closed due to any other contractual limit.

viii. Use experience that is otherwise relevant in accordance with the professional judgment of the Appointed Actuary.

In the above paragraphs, the term "company" refers to a single company or a group of legally related companies subject to the same claim management.

D. Own Experience Measurement Exemption

Determine the number of claims that, according to the provisions of this Guideline, are subject to valuation using the 2023 GTLW Mortality and Recovery Valuation Tables. If, at the time of valuation, a company has fewer than 50 such open claims disabled within two years of the effective date of the valuation, and fewer than 200 such open claims disabled more than two years prior to the effective date of the valuation, the company is exempt from the requirement that the 2023 GTLW Mortality and Recovery Valuation Tables be modified by the company's own experience. Said company will use, based on the maximum values of M_M and M_R for any duration group according to Section VI(B)(ii)(b)(6) above, 115% of the 2023 GTLW Mortality Valuation Table for all duration groups to calculate claim mortality rates and 85% of the 2023 GTLW Recovery Valuation Table for all duration groups to calculate claim recovery rates in order to comply with the minimum valuation standard.

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Actuarial Guideline XLV

THE APPLICATION OF THE STANDARD NONFORFEITURE LAW FOR LIFE INSURANCE TO CERTAIN POLICIES HAVING INTERMEDIATE CASH BENEFITS

Scope

This Guideline applies to individual life insurance policies, other than variable and non-variable adjustable life policies and current assumption whole life policies, that provide for an endowment benefit, materially less than the policy face amount, at a specified intermediate duration during a longer period of life insurance protection. The payment of such endowment benefit does not alter or eliminate any premiums or benefits scheduled for the period subsequent to the endowment date, nor does the policy automatically terminate upon payment of the endowment benefit. Policies that offer a return of premium endowment benefit may be considered a special case of the policies subject to this Guideline.

Background

In recent years a new category of life insurance products has emerged in the life insurance marketplace. These products offer a cash benefit at a specified time, typically many years prior to the coverage expiry date of the policy, conditioned on the insured being alive and the policy being in force at that time. The cash benefit has often taken the form of an intermediate period endowment that is either built into the policy or is provided through a rider or an endorsement. When the amount of the cash benefit is based upon the premiums paid into the policy, the benefit is often referred to as a return of premium benefit.

The straightforward application of Sections 3 and 5c of the Standard Nonforfeiture Law For Life Insurance (the Law), considering guaranteed benefits and premiums (whether guaranteed or indeterminate) during the entire period death benefits are guaranteed available under the policy, subject only to the payment of required premiums, can result in negative or very low cash values at all durations for these products. This is caused by high premiums assumed applicable in the later durations. This application of the Law produces unacceptable results, as it fails to recognize that the cash benefit should be prefunded with the premiums that fall due prior to the time the benefit becomes available.

The intent of this Guideline is to provide guidance with respect to the required minimum cash values for some of the products described in the Scope section. However, other products within the scope designed to provide similar benefits, and having similar premium structures (for example products having a cash value at the end of an initial level premium period equal to the total premiums paid) would be expected to provide minimum cash values that are determined in a manner consistent with this Guideline. For products with multiple endowment benefits, the minimum cash values should be determined in accordance with the principles of this Guideline.

Text

A. The following methodology shall be used in the determination of minimum cash surrender values for policies subject to this Guideline in accordance with the requirements of the Law.

1. The endowment period shall be that period of time measured from the issue date of the policy to the date when the endowment benefit becomes payable (the endowment date) under the terms of the policy.

2. If the endowment benefit is added by rider to a policy, then for minimum cash value determination purposes the base policy and the endowment benefit are to be treated as integrated.

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3. Premiums under the policy may be provided through a scale of guaranteed rates for the term of the policy or through a scale of current rates that are subject to a scale of guaranteed maximum premiums; if rates are subject to a scale of guaranteed maximum premiums, the minimum cash values shall be the greater of those produced under this Guideline using the guaranteed maximum rates and current rate scale applicable at issue of the policy.

4. Any cash surrender value available under the policy in the event of default in a premium payment due on any policy anniversary during the endowment period shall be an amount not less than the excess, if any, of the present value, on the anniversary, of the endowment benefit and any future incremental death benefits during the endowment period which would have been provided for by the policy if there had been no default, over the sum of:

   (i) The then present value of the adjusted premiums as defined below corresponding to premiums which would have fallen due on and after the anniversary during the endowment period; and

   (ii) The amount of any indebtedness to the company on the policy.

5. Incremental death benefits are death benefits during the endowment period in excess of the lowest death benefit provided under the policy during the endowment period.

6. The adjusted premiums for the policy shall be calculated on an annual basis and shall be such uniform percentage of the respective premiums specified in the policy for each policy year during the endowment period, excluding amounts payable as extra premiums to cover impairments or special hazards and also excluding any uniform annual contract charge or policy fee specified in the policy in a statement of the method to be used in calculating the cash surrender value and paid-up nonforfeiture benefits, that the present value, at the date of issue of the policy, of all adjusted premiums shall be equal to the sum of:

   (i) The present value of the endowment benefit and any incremental death benefits provided for by the policy during the endowment period;

   (ii) One percent (1%) of the average amount of insurance (total death benefit under the policy, including any incremental death benefits) at the beginning of each of the first ten policy years; and

   (iii) One hundred twenty-five percent (125%) of the nonforfeiture net level premium as defined below, provided however, that no nonforfeiture net level premium shall be considered to exceed 4% of the average amount of insurance (total death benefit under the policy, including any incremental death benefits) at the beginning of each of the first ten policy years.

7. The nonforfeiture net level premium for the policy shall be equal to the present value, at the date of issue of the policy, of the endowment benefit and any incremental death benefits provided for by the policy during the endowment period, divided by the present value, at the date of issue of the policy, of an annuity of one per annum payable on the date of issue of the policy and on each anniversary of such policy on which a premium falls due prior to the endowment date.

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8. The mortality rates and interest rate used in the determination of the minimum cash values for the policy shall be those applicable under the Law considering during the entire period death benefits are guaranteed available under the policy, subject only to the payment of required premiums.

B. In no event can the cash surrender value under the policy at any duration be less than the greater of:

1. The minimum cash value calculated according to Section A of this Guideline; and

2. The minimum cash value at the same duration resulting from the application of the methods described in Sections 3 and 5c of the Law considering guaranteed benefits and premiums (whether guaranteed or indeterminate) during the entire period death benefits are guaranteed available under the policy, subject only to the payment of required premiums. In performing this calculation, no annual premium at any duration after the endowment period shall exceed the difference between the death benefit and the cash value at that duration.

C. The cash surrender values for the policy must also satisfy the consistency of progression of cash values test contained in Section 8 of the Law, considering guaranteed benefits and premiums (whether guaranteed or indeterminate) during the entire period death benefits are guaranteed available under the policy, subject only to the payment of required premiums.

D. For policies where the benefit is defined in more general terms as providing for a return of premiums paid or a portion of premiums paid, the procedures of Subsection 5c C of the Law and the requirements of Section A above shall be applied in the determination of a revised set of minimum cash values in the event the value of the endowment benefit of the policy changes due to a change made to the premium schedule provided at issue.

Applicability

This Guideline is effective for all policy forms filed on or after January 1, 2009, and affects all contracts issued on or after January 1, 2010.

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Actuarial Guideline XLVI

INTERPRETATION OF THE CALCULATION OF THE SEGMENT LENGTH WITH RESPECT TO THE LIFE INSURANCE POLICIES MODEL REGULATION UPON A CHANGE IN THE VALUATION MORTALITY RATES SUBSEQUENT TO ISSUE

I. Background

Some states have revised their regulation permitting the use of the 2001 CSO Preferred Class Structure Mortality Table so that at the company's option it might be used to value a policy on a plan which was previously approved for issue based on valuation using the 2001 CSO Mortality Table. A company making this election would be changing the valuation mortality rates. It is also the case that use of the 2001 CSO Preferred Class Structure Mortality Table is predicated upon the block of policies initially, and annually thereafter, satisfying certain requirements with respect to the present value of death benefits over certain future periods. If these requirements are not satisfied at some point in the future, the company must change to a table for which the requirements are satisfied. For example, this could mean changing from the super preferred nonsmoker table to the preferred nonsmoker table or maybe from the preferred smoker table to the smoker table. Although a non-elective change, this is also a change in the valuation mortality rates.

Section 4B of the Valuation of Life Insurance Policies Model Regulation defines the "Contract Segmentation Method" in which segments are to be calculated using the valuation mortality rates for deficiency reserves. Thus, potentially either of the two examples given above could trigger a recalculation of the valuation segments at the time the valuation mortality rates are changed. The purpose of this guideline is to prescribe which circumstances involving a change to the valuation mortality rates, require a recalculation of the segments and which do not.

The Valuation of Life Insurance Policies Model Regulation was adopted, in part, to stop the use of high net premiums late in the policy's life from unduly influencing the level of reserves early in the policy's life ("postfunding"). The contract segmentation method was the answer devised to control this. After the adoption of this regulation, companies incorporated the establishment of the segment lengths into the policy design process based on the valuation mortality expected to be used. Now it is seen that there are circumstances in which it may be necessary or desirable to change valuation mortality after issue. But if it triggers a segment recalculation then there could be unintended, undesirable results.

This guideline classifies the circumstances involved in changes to valuation mortality rates into two categories: those where deliberately designed postfunding is less likely so no segment recalculation is prescribed, and those where such postfunding is more possible so segment recalculation is required. In general, non-elective valuation mortality changes require no segment recalculation, while elective valuation mortality changes are divided into those on plans filed for approval before the adoption of this guideline and those filed after adoption. To preclude enhancing postfunding by changing valuation mortality after a plan is approved, recalculation of segments is required if the change is elected on plans filed after adoption of this guideline, but is not required for plans filed before.

II. Scope

This guideline is effective December 31, 2008.

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III. Text

A. For policies subject to a non-elective change in valuation mortality rates:

For policies which were the subject of a non-elective change in valuation mortality rates because the requirements for continued use of the prior rates were no longer satisfied, Section 4B of the Valuation of Life Insurance Policies Model Regulation shall be interpreted so that the segments need not be recalculated.

B. For policies subject to a company election to substitute the 2001 Preferred Class Structure Table for the 2001 CSO Mortality Table:

1. For policies issued on a policy form filed for approval prior to January 1, 2009, Section 4B of the Valuation of Life Insurance Policies Model Regulation shall be interpreted so that the segments need not be recalculated.

2. For policies issued on a policy form filed for approval after January 1, 2009, Section 4B of the Valuation of Life Insurance Policies Model Regulation shall be interpreted to require that the segments be recalculated using the new valuation mortality rates.

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Actuarial Guideline XLVII

THE APPLICATION OF COMPANY EXPERIENCE IN THE CALCULATION OF CLAIM RESERVES UNDER THE 2012 GROUP LONG-TERM DISABILITY VALUATION TABLE

I. Background

The 2012 Group Long-Term Disability (GLTD) Valuation Table, as included in the *Health Insurance Reserves Model Regulation* (#10), is the valuation standard to replace the Commissioner's Group Disability Table 1987 (CGDT87 Table) with a new one based on the GLTD 2008 Table. This table is referred to as the GLTD 2012 Valuation Table and can be found at the following location:

https://content.naic.org/sites/default/files/actuary-01-naic-2012-group-long-term-disability-valuation-table.xls

An actuarial guideline is more appropriate to handle the multiple segments of the 2012 GLTD Valuation Table, the computations of own experience and the application of credibility which are not normally found in model regulations.

II. Purpose

The purpose of this Actuarial Guideline is to provide an instruction for the use of the 2012 GLTD Valuation Table that is referenced in the *Health Insurance Reserves Model Regulation* (#10). This guideline pertains to Group Long-Term Disability claims consistent with the conditions defined in the model regulation, and governs the selection of claim termination rates for the purpose of calculating GLTD claim reserves. This guideline does not address reserve adequacy, which remains the concern of the insurer according to the terms expressed in the model regulation.

Although the various detailed formulas in this guideline do not directly address or define reserve adequacy, it is assumed that appropriate adequacy tests will be made periodically. Such adequacy testing is considered to be an additional tool for the actuary to make appropriate choices where leeway from any prescription made herein is allowed (A/E calculation, margin, etc.) so that the calculation of the reserve will generally be adequate and the actuary does not need to continually rely on other measures to achieve adequacy. In addition to the few times that leeway from prescription is mentioned below, nothing in this guideline should be assumed to prohibit the actuary from building a case and requesting permission from the state insurance commissioner for other appropriate variations. Many such situations, because they would apply to fully credible blocks of business and are intended for continual use, should be considered for approval by the commissioner for a period tied to the updates required by Section C.vi and not approved on an annual basis.

III. Text

A. When the insurer follows the instructions provided in this guideline, the selected claim termination rates automatically meet the minimum valuation standard defined in the model regulation.

B. Valuation Table Modifications

If not invoking the small company exception specified in Section D, a company must use a credibility-weighted combination of its own claim termination experience with the 2012 GLTD Valuation Table to create its specific valuation table.

i. For claims in Duration Group 1 (duration ≤ 3 months), termination rates may be developed as below consistent with other Duration Groups or in any other

manner deemed appropriate by the actuary. With respect to credibility, any value between 0 and 1.0 that the actuary deems appropriate for the block may be used.

ii. For claims beyond 3 months, the valuation termination rates shall be computed using the termination rates from the 2012 GLTD Valuation Table (S) multiplied by experience adjustment factors (T) that are calculated separately for four different duration groups.

Valuation Termination Rate = $T \times S$

The duration groups are defined as follows:

Group 2: duration > 3 months and duration ≤ 24 months
Group 3 duration > 24 months and duration ≤ 60 months
Group 4: duration > 60 months and duration ≤ 120 months
Group 5: duration > 120 months

a) S shall be the sum of recovery and death rates from the 2012 GLTD Valuation Table.

b) T shall be computed as $T = [Z \times F * (1 - M) + (1 - Z)]$.

1) Z shall be a credibility weighting factor, between 0 and 1, developed for each duration group according to the following specifications:

Groups 2–5: $Z = Min\left(\sqrt{N/K}, 1\right)$ N is the number of expected recovery and death counts from the 2012 GLTD Valuation Table.

2) K is a set of constants defined by duration group as follows:

Group 2: K = 3,300	Group 4: K = 2,100
Group 3: K = 2,500	Group 5: K = 1,700

3) F shall be the ratio of the company's actual total of recovery and death counts to the expected recovery and death counts for the 2012 GLTD Valuation Table for each duration group specified above.

If the actuary has reserve adequacy or other significant analysis that demonstrates in the development and use of Company Specific Experience (see Section C below) that an alternative measurement is deemed appropriate, such as:

I. Use of some other weighting of claims (gross benefit, net benefit, etc.) that is not only appropriate for measuring A/E, but also is expected to generally produce reserves not less than those produced by using a claim count measurement.

II. Use of an increased credibility factor Z if F is less than 1 to give the company experience more weight.

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Then, a basis other than claim count may be used.

4) M is the company experience margin, determined for each duration group according to the following formula:

$$M = Min\left(15\%, Max\left(5\%, 3\% + 1.65 * \sqrt{A/C}\right)\right)$$

This is the minimum value for the definition of M prior to any reserve adequacy analysis. Adequacy tests and analysis of experience (sharpness of fluctuations, trends over the period of the termination rate study, changing claims practices, etc.) may indicate that a larger value of M may be more appropriate. If so, such a value is deemed appropriate.

5) A is a set of constants defined by duration group as follows:

Group 2: A = 4.0	Group 4: A = 2.5
Group 3: A = 3.0	Group 5: A = 2.0

6) C shall be the company's actual number of total recovery and death counts by duration group.

iii. The company shall not use termination rates that produce total reserves for claims disabled for more than two years that are less than the reserves produced for these claims by computing T as $\underline{T}$ = 1.30. If the Company Specific Experience, determined in Section C below, for Duration Group 3 includes at least 5,000 claim terminations, the value of T for that Duration Group shall not be limited to ≤ 1.30

C. Company Specific Experience—Own Experience Measurement

In computing values F and S to comply with Section B above, the appointed actuary shall:

i. Segment the company claim termination experience into any major subgroups that may produce significantly different results (e.g., market niches, claims operations, unique benefit designs, etc.).

ii. Combine affiliated statutory entities and assumed reinsurance, where claim management is under a common structure, when considering company experience. It is also appropriate to evaluate experience separately when specific blocks of company business have distinct claim management practices or significantly different risk characteristics.

iii. Include all relevant experience the company is capable of providing for as many of the last five years as possible (not including the lag period described below). However, there are two situations where using other than a five-year period may be more appropriate. The first is when a company's experience in a longer period not only increases credibility but is still relevant and appropriate for the company's products and claim management practices. The second is for a company that has had significant changes in product and/or claim management practices within the past five years that has diminished the relevance of the company's experience early in the five-year period. In this second situation, less than five years of experience may be used for any duration band for which there

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is compelling logic and when either the company's experience to be used is at least 90% credible, or the shorter experience period produces higher reserves than using five years.

iv. Recognize a suitable lag period to allow for a full resolution of claim status. The lag period used in the 2008 GLTD Study was 12 months. However, the appointed actuary may use a different lag period based on his or her company experience. For example, company experience indicates that all changes after the selected lag period are negligible.

v. Measure actual (A) to expected (E) terminations based on claim count (unless another weighting is deemed more appropriate, as mentioned in Section B(ii)(b)4), where the E is based on monthly expected recoveries and deaths from the 2012 GLTD Valuation Table. Claim count is also used in the measurement of credibility.

vi. Update the minimum valuation basis in accordance with Section B above at least once every five years. In addition, the valuation basis also must be updated whenever the company's annual own experience study produces, in accordance with Section B, a value *T* that changes by more than 10% from the one used in the current valuation basis for any of the five duration groups.

vii. Recognize where appropriate any flexibility built into the 2012 GLTD Valuation Table, such as not utilizing diagnosis-specific termination rates when the information is deemed unreliable.

viii. Do not count as terminations those claims that are closed due to settlement (i.e., a lump sum replacing a series of potential future payments), or that have reached the end of the maximum benefit duration, or that are closed due to a contractual limit, such as a mental and nervous limit. For this purpose, a closure due to a change in definition of disability should be considered an actual termination and not a termination due to reaching the maximum benefit duration.

ix. Use experience that is otherwise relevant in accordance with the professional judgment of the appointed actuary.

x. Do not use experience that the commissioner has deemed inappropriate or likely to produce significantly inadequate reserves.

In the above paragraphs, the expression term "company" refers to a single company or a group of legally related companies subject to the same claim management.

D. Own Experience Measurement Exemption

If, at the time of valuation, a company has fewer than 50 open claims disabled within two years of the effective date of the valuation, and fewer than 200 open claims disabled more than two years prior to the effective date of the valuation, the carrier is exempt from the requirement that the 2012 GLTD Valuation Table be modified by the company's own experience. Open claims include only claims subject to valuation using the 2012 GLTD Valuation Table. Said company will use 100% of the 2012 Valuation Table for calculating claims termination rates in order to comply with the minimum valuation standard.

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Actuarial Guideline XLVIII
(*Applies to 2017 and Subsequent Year Valuations)*

ACTUARIAL OPINION AND MEMORANDUM REQUIREMENTS FOR THE REINSURANCE OF POLICIES REQUIRED TO BE VALUED UNDER SECTIONS 6 AND 7 OF THE NAIC VALUATION OF LIFE INSURANCE POLICIES MODEL REGULATION (MODEL #830)

Background

The NAIC Principle-Based Reserving Implementation (EX) Task Force ("PBRI Task Force") serves as the coordinating body for all NAIC technical groups involved with projects related to the Principle-Based Reserves (PBR) initiative for life and health policies. The PBRI Task Force was also charged with further assessing, and making recommendations regarding, the solvency implications of life insurance reserve financing mechanisms addressed in the June 6, 2013 NAIC White Paper of the Captives and Special Purpose Vehicle Use (E) Subgroup of the Financial Condition (E) Committee. Some of these reinsurance arrangements have been referred to as "XXX/AXXX Captive arrangements," although not all such arrangements actually involve reinsurers organized as captives. In this connotation, XXX denotes the reserves prescribed by Section 6 of the NAIC *Valuation of Life Insurance Policies Model Regulation* (Model #830) while AXXX denotes the reserves prescribed by Section 7 of Model #830, and by *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38). On June 30, 2014, the PBRI Task Force adopted a framework as found in Exhibits 1 and 2 of the June 4, 2014 report from Rector & Associates, Inc. (the "June 2014 Rector Report"). Exhibit 2 of the report included a charge to the Life Actuarial (A) Task Force (LATF) to develop a level of reserves (the "Required Level of Primary Security") that must be supported by certain defined assets ("Primary Security"). The level of reserves is to be calculated by a method referred to as the "Actuarial Method." Another charge to LATF was to promulgate an actuarial guideline specifying that, in order to comply with the NAIC *Actuarial Opinion and Memorandum Regulation*, Model 822 ("AOMR") as it relates to XXX/AXXX reinsurance arrangements, the opining actuary must issue a qualified opinion as to the ceding insurer's reserves if the ceding insurer or any insurer in its holding company system has engaged in a XXX/AXXX reserve financing arrangement that does not adhere to the Actuarial Method and Primary Security forms adopted by the NAIC. The initial version of *Actuarial Guideline XLVIII—Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation* (AG 48) was developed in response to that charge, with an effective date of January 1, 2015.

Coordination between this Actuarial Guideline and the NAIC Term and Universal Life Insurance Reserve Financing Model Regulation (Model #787)

Subsequently, on January 8, 2016, the NAIC adopted revisions to the *Credit for Reinsurance Model Law* (Model #785). Among other things, the revisions to Model #785 provide commissioners with the authority to enact, by regulation, additional requirements for ceding insurers to claim credit for reinsurance with respect to certain XXX/AXXX financing arrangements. On December 13, 2016, the NAIC adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (Model #787) as the regulation permitted by Model #785. LATF subsequently received a charge to redraft AG 48 to make it as consistent as possible with the provisions of Model #787. The current version of this actuarial guideline is the result.

The following is an overview of the interrelationship between this actuarial guideline and Model #787, and the regulatory strategy that led to the adoption of each:

1. The initial version of this actuarial guideline immediately established national standards for the use of XXX/AXXX financing arrangements in an attempt to quickly set minimum standards based on the framework adopted by the PBRI Task Force on June 30, 2014. This initial version applied to such reinsurance arrangements entered into on or after 1/1/2015.

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2. The revised statute (the NAIC *Credit for Reinsurance Model Law* (Model #785)) and a new regulation (the NAIC *Term and Universal Life Insurance Reserve Financing Model Regulation* (Model #787)) were then developed and adopted by the NAIC.

3. Except as noted in #4 below, this actuarial guideline will cease to be effective, on a state by state basis, as individual states enact Model #785 and adopt Model #787 to replace it.

4. Notwithstanding, it is anticipated that in a small number of states, Model #787 will need to be adopted on a "prospective" basis only (that is, it will only apply to ceded policies issued on or after the effective date thereof). In those cases, this actuarial guideline will remain as the authority for ceded policies subject to this actuarial guideline but to which Model #787, as adopted in a given state, does not apply. So although its role might diminish, this actuarial guideline will remain an essential part of the regulatory framework for a small number of states for many years to come.

5. To ensure uniformity of treatment between states, companies, and ceded policies (whether governed by this actuarial guideline or by Model #787) and to avoid confusion, this actuarial guideline is being updated, effective as of January 1, 2017, to make it as substantively identical to Model #787 as possible.

Authority, Avoidance, and Purpose

The requirements in this actuarial guideline derive authority from Section 3 of the AOMR, or, after the Operative Date of the *Valuation Manual*, from Section 1 of VM-30 of the *Valuation Manual*. Both Section 3 of the AOMR and Section 1 of VM-30 provide that the commissioner has the authority to specify specific methods of actuarial analysis and actuarial assumptions when, in the commissioner's judgment, these specifications are necessary for an acceptable opinion to be rendered relative to the adequacy of reserves and related items. As contained in the framework adopted by the PBRI Task Force on June 30, 2014, this actuarial guideline defines new terms, such as Primary Security and Required Level of Primary Security, specifies the Actuarial Method used to calculate the Required Level of Primary Security, and specifies other requirements that must be followed when reinsurance is involved in order for the appointed actuary to render an actuarial opinion that is not qualified.

No statute, regulation or guideline can anticipate every potential XXX/AXXX captive arrangement. Common sense and professional responsibility are needed to assure not only that the text of this actuarial guideline is strictly observed, but also that its purpose and intent are honored scrupulously. To that end, and to provide documentation to the appointed actuary as to the arrangements that are subject to review under this actuarial guideline, the appointed actuary may request from each ceding insurer, and may rely upon, the certification by the Chief Financial Officer or other responsible officer of each ceding insurer filed with the insurer's domiciliary regulator that the insurer has not engaged in any arrangement or series of arrangements involving XXX or AXXX reserves that are designed to exploit a perceived ambiguity in, or to violate the purpose and intent of, this actuarial guideline.

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The purpose and intent of this actuarial guideline is to establish uniform, national standards governing XXX or AXXX reserve financing arrangements[1] in conformity with the PBRI Task Force framework and, in connection with such arrangements, to ensure that Primary Security, in an amount at least equal to the Required Level of Primary Security, is held by or on behalf of the ceding insurer. As described further in Section 4.B., the provisions of this actuarial guideline are not intended to apply to policies that were issued prior to 1/1/2015 if those policies were included in a captive reserve financing arrangement as of 12/31/2014. Further, the requirements of this actuarial guideline should be viewed as minimum standards and are not a substitute for the diligent analysis of reserve financing arrangements by regulators. A regulator should impose requirements in addition to those set out in this actuarial guideline if the facts and circumstances warrant such action.

Text

1. Authority

Pursuant to Section 3 of the AOMR or, after the Operative Date of the *Valuation Manual*, to Section 1 of VM-30 of the *Valuation Manual*, the commissioner shall have the authority to specify specific methods of actuarial analysis and actuarial assumptions when, in the commissioner's judgment, these specifications are necessary for an acceptable opinion to be rendered relative to the adequacy of reserves and related items.

2. Scope

This actuarial guideline applies to reinsurance contracts that cede liabilities pertaining to Covered Policies as that term is defined in Section 4.

3. Exemptions

This actuarial guideline does not apply to the situations described in Subsections A through F.

A. Reinsurance of:

(1) Policies that satisfy the criteria for exemption set forth in Section 6F or Section 6G of Model #830; and which are issued before the later of:

(a) The effective date of Model #787 in the state of domicile of the ceding insurer, and

(b) The date on which the ceding insurer begins to apply the provisions of VM-20 to establish the ceded policies' statutory reserves, but in no event later than January 1, 2020;

(2) Portions of policies that satisfy the criteria for exemption set forth in Section 6E of Model #830 and which are issued before the later of:

[1] In general, reserve financing arrangements are those where the security/assets backing part or all of the reserves have one or more of the following characteristics: such security/assets (1) are issued by the ceding insurer or its affiliates; and/or (2) are not unconditionally available to satisfy the general account obligations of the ceding insurer; and/or (3) create a reimbursement, indemnification or other similar obligation on the part of the ceding insurer or any if its affiliates (other than a payment obligation under a derivative contract acquired in the normal course and used to support and hedge liabilities pertaining to the actual risks in the policies ceded pursuant to the reinsurance arrangement).

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(a) The effective date of Model #787 in the state of domicile of the ceding insurer, and

(b) The date on which the ceding insurer begins to apply the provisions of VM-20 to establish the ceded policies' statutory reserves, but in no event later than January 1, 2020;

(3) Any universal life policy that meets all of the following requirements:

(a) Secondary guarantee period, if any, is five (5) years or less;

(b) Specified premium for the secondary guarantee period is not less than the net level reserve premium for the secondary guarantee period based on the CSO valuation tables and valuation interest rate applicable to the issue year of the policy; and

(c) The initial surrender charge is not less than one hundred percent (100%) of the first year annualized specified premium for the secondary guarantee period;

(4) Credit life insurance;

(5) Any variable life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts; or

(6) Any group life insurance certificate unless the certificate provides for a stated or implied schedule of maximum gross premiums required in order to continue coverage in force for a period in excess of one year; or

B. Reinsurance ceded to an assuming insurer that meets the applicable requirements of Section 2D of Model #785; or

C. Reinsurance ceded to an assuming insurer that meets the applicable requirements of Sections 2A, 2B or 2C, of Model #785, and that, in addition:

(1) Prepares statutory financial statements in compliance with the NAIC *Accounting Practices and Procedures Manual*, without any departures from NAIC statutory accounting practices and procedures pertaining to the admissibility or valuation of assets or liabilities that increase the assuming insurer's reported surplus and are material enough that they need to be disclosed in the financial statement of the assuming insurer pursuant to *Statement of Statutory Accounting Principles No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures* ("SSAP No. 1"); and

(2) Is not in a Company Action Level Event, Regulatory Action Level Event, Authorized Control Level Event, or Mandatory Control Level Event as those terms are defined in the NAIC *Risk-Based Capital (RBC) for Insurers Model Act* (Model #312) when its RBC is calculated in accordance with the life risk-based capital report including overview and instructions for companies, as the same may be amended by the NAIC from time to time, without deviation; or

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D. Reinsurance ceded to an assuming insurer that meets the applicable requirements of Sections 2A, 2B or 2C, of Model #785, and that, in addition:

(1) Is not an affiliate, as that term is defined in Section 1A of the NAIC *Insurance Holding Company System Regulatory Model Act* (Model #440), of:

(a) The insurer ceding the business to the assuming insurer; or

(b) Any insurer that directly or indirectly ceded the business to that ceding insurer;

(2) Prepares statutory financial statements in compliance with the NAIC *Accounting Practices and Procedures Manual*;

(3) Is both:

(a) Licensed or accredited in at least 10 states (including its state of domicile), and

(b) Not licensed in any state as a captive, special purpose vehicle, special purpose financial captive, special purpose life reinsurance company, limited purpose subsidiary, or any other similar licensing regime; and

(4) Is not, or would not be, below 500% of the Authorized Control Level RBC as that term is defined in Model #312 when its risk-based capital (RBC) is calculated in accordance with the life risk-based capital report including overview and instructions for companies, as the same may be amended by the NAIC from time to time, without deviation, and without recognition of any departures from NAIC statutory accounting practices and procedures pertaining to the admission or valuation of assets or liabilities that increase the assuming insurer's reported surplus; or

E. Reinsurance ceded to an assuming insurer that meets the requirements of either Section 5B(4)(a) of Model #785, pertaining to certain certified reinsurers or Section 5B(4)(b) of Model #785, pertaining to reinsurers meeting certain threshold size and licensing requirements; or

F. Reinsurance not otherwise exempt under Subsections A through E if the commissioner, after consulting with the NAIC Financial Analysis Working Group (FAWG) or other group of regulators designated by the NAIC, as applicable, determines under all the facts and circumstances that all of the following apply:

(1) The risks are clearly outside of the intent and purpose of this actuarial guideline (as described in the Authority, Avoidance and Purpose section above);

(2) The risks are included within the scope of this actuarial guideline only as a technicality; and

(3) The application of this actuarial guideline to those risks is not necessary to provide appropriate protection to policyholders. The commissioner shall publicly disclose any decision made pursuant to this Section 3F to exempt a reinsurance

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treaty from this actuarial guideline, as well as the general basis therefor (including a summary description of the treaty).

Drafting Note: *The exemption set forth in Section 3F was added to address the possibility of unforeseen or unique transactions. This exemption exists because the NAIC recognizes that foreseeing every conceivable type of reinsurance transaction is impossible; that in rare instances unanticipated transactions might get caught up in this actuarial guideline purely as a technicality; and that regulatory relief in those instances may be appropriate. The example that was given at the time this exemption was developed pertained to bulk reinsurance treaties where the ceding insurer was exiting the type of business ceded. The exemption should not be used with respect to so-called "normal course" reinsurance transactions; rather, such transactions should either fit within one of the standard exemptions set forth in Sections 3A, B, C, D, or E or meet the substantive requirements of this actuarial guideline.*

4. Definitions

A. "Actuarial Method" means the methodology used to determine the Required Level of Primary Security, as described in Section 5.

B. "Covered Policies" means the following: Subject to the exemptions described in Section 3, Covered Policies are those policies, other than Grandfathered Policies, of the following policy types:

(1) Life insurance policies with guaranteed nonlevel gross premiums and/or guaranteed nonlevel benefits, except for flexible premium universal life insurance policies; or,

(2) Flexible premium universal life insurance policies with provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period.

Note*: Although "Covered Policies" is defined to include all the policies described in Subsections B1 and B2 above, it is noted that whether a given "Covered Policy" is subject to this actuarial guideline or, instead, to Model #787 should be determined under Section 8 (Sunset).*

C. "Grandfathered Policies" means policies of the types described in Subsections B1 and B2 above that were:

(1) Issued prior to January 1, 2015; and

(2) Ceded, as of December 31, 2014, as part of a reinsurance treaty that would not have met one of the exemptions set forth in Section 3 had that section then been in effect.

D. "Non-Covered Policies" means any policy that does not meet the definition of Covered Policies, including Grandfathered Policies.

E. "Required Level of Primary Security" means the dollar amount determined by applying the Actuarial Method to the risks ceded with respect to Covered Policies, but not more than the total reserve ceded.

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F. "Primary Security" means the following forms of security:

(1) Cash meeting the requirements of Section 3A of Model #785;

(2) Securities listed by the Securities Valuation Office meeting the requirements of Section 3B of Model #785, but excluding any synthetic letter of credit, contingent note, credit-linked note or other similar security that operates in a manner similar to a letter of credit, and excluding any securities issued by the ceding insurer or any of its affiliates; and

(3) For security held in connection with funds-withheld and modified coinsurance reinsurance treaties:

(a) Commercial loans in good standing of CM3 quality and higher;

(b) Policy Loans; and

(c) Derivatives acquired in the normal course and used to support and hedge liabilities pertaining to the actual risks in the policies ceded pursuant to the reinsurance treaty.

G. "Other Security" means any security acceptable to the commissioner other than security meeting the definition of Primary Security.

H. "*Valuation Manual*" means the valuation manual adopted by the NAIC as described in Section 11B(1) of the Standard Valuation Law, with all amendments adopted by the NAIC that are effective for the financial statement date on which credit for reinsurance is claimed.

I. "VM-20" means "Requirements for Principle-Based Reserves for Life Products," including all relevant definitions, from the *Valuation Manual*.

5. The Actuarial Method

A. Description of Actuarial Method

The Actuarial Method to establish the Required Level of Primary Security for each reinsurance treaty subject to this actuarial guideline shall be VM-20, applied on a treaty-by-treaty basis, including all relevant definitions, from the *Valuation Manual* as then in effect, applied as follows:

(1) For Covered Policies described in Section 4B(1) above, the Actuarial Method is the greater of the Deterministic Reserve or the Net Premium Reserve (NPR) regardless of whether the criteria for exemption testing can be met. However, if the Covered Policies do not meet the requirements of the Stochastic Reserve exclusion test in the *Valuation Manual*, then the Actuarial Method is the greatest of the Deterministic Reserve, the Stochastic Reserve, or the NPR. In addition, if such Covered Policies are reinsured in a reinsurance treaty that also contains Covered Policies described in Section 4B(2) above, the ceding insurer may elect to instead use paragraph 2 below as the Actuarial Method for the entire reinsurance agreement. Whether Paragraph 1 or 2 are used, the Actuarial Method must comply with any requirements or restrictions that the *Valuation Manual* imposes when aggregating these policy types for purposes of principle-based

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reserve calculations. The mortality basis for the NPR shall be the 2017 CSO Mortality Table.

(2) For Covered Policies described in Section 4B(2) above, the Actuarial Method is the greatest of the Deterministic Reserve, the Stochastic Reserve, or the NPR regardless of whether the criteria for exemption testing can be met. The mortality basis for the NPR shall be the 2017 CSO Mortality Table.

(3) Except as provided in Paragraph (4) below, the Actuarial Method is to be applied on a gross basis to all risks with respect to the Covered Policies as originally issued or assumed by the ceding insurer.

(4) If the reinsurance treaty cedes less than one hundred percent (100%) of the risk with respect to the Covered Policies then the Required Level of Primary Security may be reduced as follows:

(a) If a reinsurance treaty cedes only a quota share of some or all of the risks pertaining to the Covered Policies, the Required Level of Primary Security, as well as any adjustment under Subparagraph (c) below, may be reduced to a pro rata portion in accordance with the percentage of the risk ceded;

(b) If the reinsurance treaty in a non-exempt arrangement cedes only the risks pertaining to a secondary guarantee, the Required Level of Primary Security may be reduced by an amount determined by applying the Actuarial Method on a gross basis to all risks, other than risks related to the secondary guarantee, pertaining to the Covered Policies, except that for Covered Policies for which the ceding insurer did not elect to apply the provisions of VM-20 to establish statutory reserves, the Required Level of Primary Security may be reduced by the statutory reserve retained by the ceding insurer on those Covered Policies, where the retained reserve of those Covered Policies should be reflective of any reduction pursuant to the cession of mortality risk on a yearly renewable term basis in an exempt arrangement;

(c) If a portion of the Covered Policy risk is ceded to another reinsurer on a yearly renewable term basis in an exempt arrangement, the Required Level of Primary Security may be reduced by the amount resulting by applying the Actuarial Method including the reinsurance section of VM-20 to the portion of the Covered Policy risks ceded in the exempt arrangement, except that for Covered Policies issued prior to Jan 1, 2017, this adjustment is not to exceed [c_x/ (2 * number of reinsurance premiums per year)] where c_x is calculated using the same mortality table used in calculating the Net Premium Reserve; and

(d) For any other treaty ceding a portion of risk to a different reinsurer, including but not limited to stop loss, excess of loss and other non-proportional reinsurance treaties, there will be no reduction in the Required Level of Primary Security.

It is possible for any combination of Subparagraphs (a), (b), (c), and (d) above to apply. Such adjustments to the Required Level of Primary Security will be done in the sequence that accurately reflects the portion of the risk ceded via the treaty.

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The ceding insurer should document the rationale and steps taken to accomplish the adjustments to the Required Level of Primary Security due to the cession of less than one hundred percent (100%) of the risk.

The Adjustments for other reinsurance will be made only with respect to reinsurance treaties entered into directly by the ceding insurer. The ceding insurer will make no adjustment as a result of a retrocession treaty entered into by the assuming insurers.

(5) In no event will the Required Level of Primary Security resulting from application of the Actuarial Method exceed the amount of statutory reserves ceded.

(6) If the ceding insurer cedes risks with respect to Covered Policies, including any riders, in more than one reinsurance treaty subject to this actuarial guideline, in no event will the aggregate Required Level of Primary Security for those reinsurance treaties be less than the Required Level of Primary Security calculated using the Actuarial Method as if all risks ceded in those treaties were ceded in a single treaty subject to this actuarial guideline.

(7) If a reinsurance treaty subject to this actuarial guideline cedes risk on both Covered and Non-Covered Policies:

(a) The Actuarial Method shall be used to determine the Required Level of Primary Security for the Covered Policies; and

(b) Any Primary Security and/or Other Security used to meet any requirements pertaining to the Non-Covered Policies may not be used to satisfy any requirements related to the Required Level of Primary Security and/or Other Security for the Covered Policies.

B. Valuation Used for Purposes of Calculations

For the purposes of both calculating the Required Level of Primary Security pursuant to the Actuarial Method and determining the amount of Primary Security and Other Security, as applicable, held by or on behalf of the ceding insurer, the following shall apply:

(1) For assets, including any such assets held in trust, that would be admitted under the NAIC *Accounting Practices and Procedures Manual* if they were held by the ceding insurer, the valuations are to be determined according to statutory accounting procedures as if such assets were held in the ceding insurer's general account and without taking into consideration the effect of any prescribed or permitted practices; and

(2) For all other assets, the valuations are to be those that were assigned to the assets for the purpose of determining the amount of reserve credit taken. In addition, the asset spread tables and asset default cost tables required by VM-20 shall be included in the Actuarial Method if adopted by the NAIC's Life Actuarial (A) Task Force no later than the December 31 on or immediately preceding the valuation date for which the Required Level of Primary Security is being

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calculated. The tables of asset spreads and asset default costs shall be incorporated into the Actuarial Method in the manner specified in VM-20.

6. Required Actuarial Analysis and Actuarial Opinion and Memorandum Requirements

A. Required Actuarial Analysis

Before the due date of each actuarial opinion, as to each reinsurance treaty in which Covered Policies have been ceded, the appointed actuary of each ceding insurer must perform an analysis on a treaty by treaty basis, of such Covered Policies to determine whether, as of the immediately preceding December 31 (the valuation date):

(1) Funds consisting of Primary Security, in an amount at least equal to the Required Level of Primary Security, are held by or on behalf of the ceding insurer, as security under the reinsurance treaty within the meaning of Section 3 of Model #785, on a funds withheld, trust, or modified coinsurance basis; and

(2) Funds consisting of Other Security, in an amount at least equal to any portion of the statutory reserves as to which Primary Security is not held pursuant to Paragraph (1) above, are held by or on behalf of the ceding insurer as security under the reinsurance treaty within the meaning of Section 3 of Model #785; and

***Note**: For the sake of clarity, funds consisting of Primary Security pursuant to Paragraphs (1) may exceed the Required Level of Primary Security, and Other Security is only required under Paragraph (2) to the extent that there is any portion of the statutory reserves as to which Primary Security is not so held. For example, if a ceding insurer's statutory reserves equal $1 Billion, its Required Level of Primary Security is $600 Million, and it holds $1 Billion in Primary Security pursuant to Paragraph (1), no Other Security is required under Paragraph (2).*

(3) Any trust used to satisfy the requirements of this Section 6 complies with all of the conditions and qualifications of Section 11 of the NAIC *Credit for Reinsurance Model Regulation* (Model #786), except that:

(a) Funds consisting of Primary Security or Other Security held in trust, shall for the purposes identified in Section 5B, be valued according to the valuation rules set forth in Section 5B, as applicable; and

(b) There are no affiliate investment limitations with respect to any security held in such trust if such security is not needed to satisfy the requirements of Section 6A(1); and

(c) The reinsurance treaty must prohibit withdrawals or substitutions of trust assets that would leave the fair market value of the Primary Security within the trust (when aggregated with Primary Security outside the trust that is held by or on behalf of the ceding insurer in the manner required by Section 6A(1)) below 102% of the level required by Section 6A(1) at the time of the withdrawal or substitution.

B. Qualified Actuarial Opinion; Remediation

(1) The appointed actuary of the ceding insurer performing the analysis required by Section 6A above must issue a qualified actuarial opinion as described in Section 6.D. of the AOMR or Section 3A(10) of VM-30 of the *Valuation Manual*, as applicable, unless:

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(a) The requirements of Section 6A(1) and 6(A)(2) were fully satisfied as of the valuation date as to such reinsurance treaty; or

(b) Any deficiency has been eliminated before the due date of the Annual Statement to which the valuation date relates through the addition of Primary Security and/or Other Security, as the case may be, in such amount and in such form as would have caused the requirements of Section 6A(1) and 6A(2) to be fully satisfied as of the valuation date; or

(c) The ceding insurer has established a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held pursuant to Section 6A(1).

(2) In addition to the requirement set forth in Section 6B(1) above, the appointed actuary of the ceding insurer performing the analysis required by Section 6A above must issue a qualified actuarial option as described in Section 6.D. of the AOMR or Section 3A(10) of VM-30 of the *Valuation Manual*, as applicable, if the appointed actuary for any affiliated reinsurer of the ceding insurer issues a qualified actuarial opinion with respect to such affiliated reinsurer where (a) the affiliate reinsures Covered Policies of the ceding insurer and (b) the qualified actuarial opinion pertaining to the affiliated reinsurer results, in whole or in part, from the analysis required by this actuarial guideline.

***Note**: The remediation option set forth in Section 6B(1)(c) mirrors that set forth in Model #787. Under this option, a ceding company may choose to avoid the consequence (a qualified opinion under this actuarial guideline) by establishing a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held. For example, suppose a ceding insurer has established statutory reserves of $1 Billion and has Primary Security of $550 Million and Other Security of $450 Million. Suppose further that the actuary determines that the insurer's Required Level of Primary Security is $600 Million. Under Section 6B(1)(c), the insurer may avoid a qualified opinion by establishing a liability equal to $450 Million (the difference between the statutory reserve of $1 Billion and the $550 Million amount of Primary Security actually held).*

C. Additional Requirements for the Actuarial Opinion and Memorandum for Companies that have Covered Policies Requiring the Analysis Pursuant to this actuarial guideline

(1) In the statement of actuarial opinion, the appointed actuary of the ceding insurer must state whether (i) he has performed an analysis, as to each reinsurance arrangement under which Covered Policies have been ceded, of the security supporting the Covered Policies and whether funds consisting of Primary Security in an amount at least equal to the Required Level of Primary Security are held by or on behalf of the ceding insurer, as security under the reinsurance contract, on a funds withheld, trust, or modified coinsurance basis and (ii) funds consisting of Primary Security or Other Security in an amount equal to the statutory reserves are held by or on behalf of the ceding insurer as security under the reinsurance arrangement.

(2) In the actuarial memorandum as described by Section 7 of the AOMR or Section 3B of VM-30 of the *Valuation Manual*, as applicable, the appointed actuary of the ceding insurer must document the analysis and requirements applied by this

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actuarial guideline as to each reinsurance arrangement under which Covered Policies are ceded.

(3) In the event that a reinsurance treaty contains both (1) Covered Policies subject to this actuarial guideline rather than to Model #787, and (2) Covered Policies subject to Model #787 rather than to this actuarial guideline, the treaty shall be tested as a whole for purposes of a ceding insurer's compliance with both (a) the requirements of Section 6A(1) and Section 6A(2) of this actuarial guideline and (b) the requirements of Section 7A(3) and Section 7A(4) of Model #787; provided further, that:

(a) If funds consisting of Primary Security are held in amounts less than the Required Level of Primary Security, such funds consisting of Primary Security shall be allocated first to fulfill the Required Level of Primary Security for the Covered Policies subject to this actuarial guideline, with any remainder allocated to those Covered Policies subject to Model #787; and

(b) If funds consisting of Other Security are held in amounts less than the requirements of Section 6A(2), such funds consisting of Other Security shall be allocated first to fulfill the Other Security requirements for the Covered Policies subject to this actuarial guideline, and any remainder shall be allocated to those Covered Policies subject to Model #787.

7. Effective Date

This actuarial guideline shall become effective as of January 1, 2017 with respect to all Covered Policies. This actuarial guideline supersedes and replaces all previous versions thereof with respect to actuarial opinions rendered as to valuation periods ending on or after January 1, 2017.

Note*: For the avoidance of doubt, actuarial opinions issued with respect to the year ended December 31, 2016, shall be governed by the version of AG 48 in effect on December 31, 2016, as included in the Accounting Practices and Procedures Manual.*

8. Sunset Provision

This actuarial guideline shall cease to apply as to Covered Policies that are both (a) issued by ceding insurers domiciled in a jurisdiction that has in effect, as of December 31st[t] of the calendar year immediately preceding the year in which the actuarial opinion is to be filed, a regulation substantially similar to Model #787 adopted by the NAIC on December 13, 2016; and (b) subject to Model #787 as so adopted by the ceding insurer's jurisdiction of domicile. This Actuarial Guideline shall continue to apply, without interruption, to any and all Covered Policies not included in both (a) and (b) of the immediate preceding sentence.

Note*: It is anticipated that, for most states, this actuarial guideline will sunset pursuant to (a) and (b) of Section 8 and will continue only with respect to the limited number of states in which their version of Model #787 applies prospectively only, i.e., applies only to Covered Policies issued on or after the effective date of their version of Model #787. It is anticipated, however, that most states will be able to adopt a version of Model #787 that, like the Model itself, applies to all Covered Policies (subject to the applicable exemptions and grandfathering provisions) that are "in force" on or after the effective date, even if the policies were originally issued prior to that effective date. The goal of Section 8 is to ensure that* ***all*** *Covered Policies ceded in reinsurance transactions within the scope of this actuarial guideline continue to be subject to this actuarial guideline unless and until they become subject to Model #787.*

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Actuarial Guideline XLIX

THE APPLICATION OF THE LIFE ILLUSTRATIONS MODEL REGULATION TO POLICIES WITH INDEX-BASED INTEREST

Background

The *Life Insurance Illustrations Model Regulation* (#582) was adopted by the NAIC in 1995. Since that time there has been continued evolution in product design, including the introduction of benefits that are tied to an external index or indices. Although these policies are subject to Model #582, not all of their features are explicitly referenced in the model, resulting in a lack of uniform practice in its implementation. In the absence of uniform guidance, two illustrations that use the same index and crediting method often illustrated different credited rates. The lack of uniformity can be confusing to potential buyers and can cause uncertainty among illustration actuaries when certifying compliance with Model #582.

This guideline provides uniform guidance for policies with index-based interest. In particular, this guideline:

(1) Provides guidance in determining the maximum crediting rate for the illustrated scale and the earned interest rate for the disciplined current scale.

(2) Limits the policy loan leverage shown in an illustration.

(3) Requires additional consumer information (side-by-side illustration and additional disclosures) that will aid in consumer understanding.

Text

1. Effective Date

This Actuarial Guideline shall be effective as follows:

i. Sections 4 and 5 shall be effective for all new business and in force life insurance illustrations on policies sold on or after September 1, 2015.

ii. Effective March 1, 2017, Section 4 and Section 5 shall be effective for all in-force life insurance illustrations on policies within the scope of this Actuarial Guideline, regardless of the date the policy was sold.

iii. Sections 6 and 7 shall be effective for all new business and in force life insurance illustrations on policies sold on or after March 1, 2016.

iv. This actuarial guideline shall not apply for any new business or in force life insurance illustration on policies sold on or after December 14, 2020.

v. Notwithstanding part iv of this section, an insurer may choose to utilize AG 49-A guidance for new illustrations on policies sold prior to the effective date of AG 49-A provided that, 1) the insurer utilizes AG 49-A guidance for all new product illustrations subject to AG 49, and 2) the insurer does not revert back to the AG 49 guidance.

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2. Scope

This Actuarial Guideline shall apply to any life insurance illustration that meets both (i) and (ii) below:

i. The policy is subject to Model #582.

ii. Interest credits are linked to an external index or indices.

3. Definitions

A. **Alternate Scale**: A scale of non-guaranteed elements currently being illustrated such that:

i. The credited rate for each Index Account does not exceed the lesser of the maximum credited rate for the illustrated scale less 100 basis points and the credited rate for the Fixed Account. If the insurer does not offer a Fixed Account with the illustrated policy, the credited rate for each Index Account shall not exceed the average of the maximum credited rate for the illustrated scale and the guaranteed credited rate for that account. However, the credited rate for each Index Account shall never be less than the guaranteed credited rate for that account.

ii. If the illustration includes a loan, the illustrated rate credited to the loan balance does not exceed the illustrated loan charge.

iii. All other non-guaranteed elements are equal to the non-guaranteed elements for the illustrated scale.

B. **Benchmark Index Account**: An Index Account with the following features:

i. The interest calculation is based on the percent change in S&P 500® Index value only, over a one-year period using only the beginning and ending index values. (S&P 500® Index ticker: SPX)

ii. An annual cap is used in the interest calculation.

iii. The annual floor used in the interest calculation shall be 0%.

iv. The participation rate used in the interest calculation shall be 100%.

v. Interest is credited once per year.

vi. Account charges do not exceed the account charges for any corresponding Index Accounts within the policy in any policy year. If Index Accounts with different levels of account charges are offered with the illustrated policy, more than one Benchmark Index Account may be used in determining the maximum illustrated crediting rates for the policy's Index Accounts, subject to the requirements of paragraph 5 (D). However, for each Index Account within the policy, only one Benchmark Index Account shall apply. Any rate calculated in paragraph 4 (B) shall not apply for an Index Account if the account charges for the applicable Benchmark Index Account exceed the account charges for that Index Account in any policy year. Account charges include all charges applicable to an Index Account, whether deducted from policy values or from premiums or other amounts transferred into such Index Account.

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vii. Additional amounts credited are not less than the additional amounts credited for any corresponding Index Accounts within the policy in any policy year. Any rate calculated in paragraph 4 (B) shall not apply for an Index Account if the additional amounts credited for the applicable Benchmark Index Account are less than the additional amounts credited for that Index Account in any policy year. Additional amounts include all credits that increase policy values, including but not limited to experience refunds or bonuses**.**

viii. There are no limitations on the portion of account value allocated to the account.

C. **Fixed Account**: An account where the credited rate is not tied to an external index or indices.

D. **Index Account**: An account where the credited rate is tied to an external index or indices.

4. Illustrated Scale

The credited rate for the illustrated scale for each Index Account shall be limited as follows:

A. Calculate the geometric average annual credited rate for each applicable Benchmark Index Account for the 25-year period starting on 12/31 of the calendar year that is 66 years prior to the current calendar year (e.g., 12/31/1949 for 2015 illustrations) and for each 25-year period starting on each subsequent trading day thereafter, ending with the 25-year period that ends on 12/31 of the prior calendar year.

i. If the insurer offers an applicable Benchmark Index Account with the illustrated policy, the illustration actuary shall use the current annual cap for the applicable Benchmark Index Account in paragraph 4 (A).

ii. If the insurer does not offer an applicable Benchmark Index Account with the illustrated policy, the illustration actuary shall use actuarial judgment to determine a hypothetical, supportable current annual cap for a hypothetical, supportable Index Account that meets the definition of a Benchmark Index Account, and shall use that cap in paragraph 4 (A).

B. For each applicable Benchmark Index Account, the arithmetic mean of the geometric average annual credited rates calculated in paragraph 4 (A) shall be the maximum credited rate(s) for the illustrated scale.

C. For other Index Accounts using other equity, bond, and/or commodity indexes, and/or using other crediting methods, the illustration actuary shall use actuarial judgment to determine the maximum credited rate for the illustrated scale. The determination shall reflect the fundamental characteristics of the Index Account and the parameters shall have the appropriate relationship to the expected risk and return of the applicable Benchmark Index Account. In no event shall the credited rate for the illustrated scale exceed the applicable rate calculated in paragraph 4 (B).

D. At the beginning of each calendar year, the insurer shall be allowed up to three (3) months to update the credited rate for each Index Account in accordance with paragraphs 4 (B) and 4 (C).

5. Disciplined Current Scale

The earned interest rate for the disciplined current scale shall be limited as follows:

A. If an insurer engages in a hedging program for index-based interest, the assumed earned interest rate underlying the disciplined current scale shall not exceed 145% of the annual

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net investment earnings rate (gross portfolio earnings less provisions for investment expenses and default costs) of the general account assets (excluding hedges for index-based credits) allocated to support the policy.

B. If an insurer does not engage in a hedging program for index-based interest, the assumed earned interest rate underlying the disciplined current scale shall not exceed the annual net investment earnings rate of the general account assets allocated to support the policy.

C. These experience limitations shall be included when testing for self-support and lapse-support under Model #582, accounting for all benefits including illustrated bonuses.

D. If more than one Benchmark Index Account is used for an illustrated policy, each set of Index Accounts that correspond to each Benchmark Index Account must independently pass the self-support and lapse-support tests under Model #582, subject to the limitations in paragraphs 5 (A), 5 (B) and 5 (C). All experience assumptions that do not directly relate to the Index Accounts as to expenses, mortality, investment earnings rate of the general account assets, lapses, and election of any Fixed Account shall equal the assumptions used in the testing for the entire policy.

6. Policy Loans

If the illustration includes a loan, the illustrated rate credited to the loan balance shall not exceed the illustrated loan charge by more than 100 basis points.

7. Additional Standards

The basic illustration shall also include the following:

A. A ledger using the Alternate Scale shall be shown alongside the ledger using the illustrated scale with equal prominence.

B. A table showing the minimum and maximum of the geometric average annual credited rates calculated in paragraph 4 (A).

C. For each Index Account illustrated, a table showing actual historical index changes and corresponding hypothetical interest rates using current index parameters for the most recent 20-year period.

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Actuarial Guideline XLIX-A

THE APPLICATION OF THE LIFE ILLUSTRATIONS MODEL REGULATION TO POLICIES WITH INDEX-BASED INTEREST SOLD (On or After December 14, 2020)

Background

The *Life Insurance Illustrations Model Regulation* (#582) was adopted by the NAIC in 1995. Since that time there has been continued evolution in product design, including the introduction of benefits that are tied to an index or indices. Although these policies are subject to Model #582, not all of their features are explicitly referenced in the model, resulting in a lack of uniform practice in its implementation. In the absence of uniform guidance, two illustrations that use the same index and crediting method often illustrated different credited rates. The lack of uniformity can be confusing to potential buyers and can cause uncertainty among illustration actuaries when certifying compliance with Model #582.

~~In 2019, the NAIC decided that illustrations of products with multipliers, cap buy-ups, and other enhancements that are linked to an index or indices should not illustrate better than products without such features. This new requirement is intended to apply to illustrations on policies sold on or after the effective date of this guideline while the existing requirements continue to apply for inforce illustrations on policies sold before the effective date of this guideline.~~

This guideline provides uniform guidance for policies with index-based interest. In particular, this guideline:

(1) Provides guidance in determining the maximum crediting rate for the illustrated scale and the earned interest rate for the disciplined current scale.

(2) Limits the policy loan leverage shown in an illustration.

(3) Requires additional consumer information (side-by-side illustration and additional disclosures) that will aid in consumer understanding.

Text

1. Effective Date

   This Actuarial Guideline shall be effective for all new business and in force illustrations on policies sold on or after December 14, 2020.

2. Scope

   This Actuarial Guideline shall apply to any life insurance illustration that meets both (i) and (ii), below:

   i. The policy is subject to Model #582.

   ii. The policy offers Indexed Credits.

3. Definitions

   A. Alternate Scale: A scale of non-guaranteed elements currently being illustrated such that:

      i. The Annual Rate of Indexed Credits for each Index Account does not exceed the lesser of the maximum Annual Rate of Indexed Credits for the illustrated scale less

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100 basis points and the credited rate for the Fixed Account. If the insurer does not offer a Fixed Account with the illustrated policy, the Annual Rate of Indexed Credits for each Index Account shall not exceed the average of the maximum Annual Rate of Indexed Credits for the illustrated scale and the guaranteed Annual Rate of Indexed Credits for that account. However, the Annual Rate of Indexed Credits for each Index Account shall never be less than the guaranteed Annual Rate of Indexed Credits for that account.

ii. If the illustration includes a loan, the illustrated Policy Loan Interest Credited Rate shall not exceed the illustrated Policy Loan Interest Rate. For example, if the illustrated Policy Loan Interest Rate is 4%, the Policy Loan Interest Credited Rate shall not exceed 4%.

iii. All other non-guaranteed elements are equal to the non-guaranteed elements for the illustrated scale.

B. Annual Net Investment Earnings Rate: Gross portfolio annual earnings rate of the general account assets (excluding hedge assets for Indexed Credits), less provisions for investment expenses and default cost, allocated to support the policy. Charges of any kind cannot be used to increase the Annual Net Investment Earnings Rate.

C. Annual Rate of Indexed Credits: The total annualized Indexed Credits expressed as a percentage of the account value used to determine the Indexed Credits.

D. Benchmark Index Account: An Index Account with the following features:

i. The interest calculation is based on the percent change in S&P 500® Index value only, over a one-year period using only the beginning and ending index values. (S&P 500® Index ticker: SPX)

ii. An annual cap is used in the interest calculation.

iii. The annual floor used in the interest calculation shall be 0%.

iv. The participation rate used in the interest calculation shall be 100%.

v. Interest is credited once per year.

vi. The Hedge Budget used to determine the cap in 3 (D) (ii) does not exceed the Annual Net Investment Earnings Rate. Charges of any kind cannot be used to increase the annual cap.

vii. There are no enhancements or similar features that provide additional Indexed Credits in excess of the interest provided by 3 (D) (i) through 3 (D) (v), including but not limited to experience refunds, multipliers, or bonuses.

viii. There are no limitations on the portion of account value allocated to the account.

ix. A single Benchmark Index Account will be determined for each policy. This can be either an Index Account offered with the illustrated policy or determined according to Section 4 (A) (ii) for purposes of complying with this guideline. A policy shall have no more than one Benchmark Index Account.

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E. Fixed Account: An account where there are no Indexed Credits.

F. Hedge Budget: For each Index Account, the total annualized amount assumed to be used to generate the Indexed Credits of the account, expressed as a percent of the account value in the Index Account. This total annualized amount should be consistent with the hedging program of the company.

G. Index Account: An account where some or all of the amounts credited are Indexed Credits.

H. Indexed Credits: Any interest credit, multiplier, factor, bonus, charge reduction, or other enhancement to policy values that is linked to an index or indices. Amounts credited to the policy resulting from a floor greater than zero on an account with any interest credit, multiplier, factor, bonus, charge reduction, or other enhancement to policy values that is linked to an index or indices are included.

I. Loan Balance: Any outstanding policy loan and loan interest, as defined in the policy.

J. Policy Loan Interest Rate: The current annual interest rate as defined in the policy that is charged on any Loan Balance. This does not include any other policy charges.

K. Policy Loan Interest Credited Rate: The annualized interest rate credited that applies to the portion of the account value backing the Loan Balance:

i. For the portion of the account value in the Fixed Account that is backing the Loan Balance, the Policy Loan Interest Credited Rate is the applicable annual interest crediting rate.

ii. For the portion of the account value in an Index Account that is backing the Loan Balance, the Policy Loan Interest Credited Rate is the Annual Rate of Indexed Credits, net of any applicable Supplemental Hedge Budget, for that account.

L. Supplemental Hedge Budget: For each Index Account, the Hedge Budget minus the minimum of the Annual Net Investment Earnings Rate and the Hedge Budget that is used in the determination of the Benchmark Index Account. The Supplemental Hedge Budget will never be less than zero. This amount should be consistent with the hedging program of the company.

4. Illustrated Scale

The total Annual Rate of Indexed Credits for the illustrated scale for each Index Account shall be limited as follows:

A. Calculate the geometric average annual credited rate for the Benchmark Index Account for the 25-year period starting on 12/31 of the calendar year that is 66 years prior to the current calendar year (e.g., 12/31/1949 for 2015 illustrations) and for each 25-year period starting on each subsequent trading day thereafter, ending with the 25- year period that ends on 12/31 of the prior calendar year.

i. If the insurer offers a Benchmark Index Account with the illustrated policy, the illustration actuary shall use the current annual cap for the Benchmark Index Account in 4 (A).

ii. If the insurer does not offer a Benchmark Index Account with the illustrated policy, the illustration actuary shall use actuarial judgment to determine a hypothetical,

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supportable current annual cap for a hypothetical, supportable Index Account that meets the definition of the Benchmark Index Account, and shall use that cap in 4 (A).

B. For the Benchmark Index Account the Annual Rate of Indexed Credits shall not exceed the minimum of (i) and (ii):

i. The arithmetic mean of the geometric average annual credited rates calculated in 4 (A).

ii. 145% of the Annual Net Investment Earnings Rate.

C. For any other Index Account that is not the Benchmark Index Account in 3 (D), the Annual Rate of Indexed Credits illustrated as a percentage of the account value in the Index Account prior to the deduction of any charges used to fund a Supplemental Hedge Budget shall not exceed the minimum of (i) and (ii) for policies sold prior to May 1, 2023, and shall not exceed the minimum of (i), (ii), and (iii) for policies sold on or after May 1, 2023:

i. The Annual Rate of Indexed Credits for the Benchmark Index Account calculated in 4 (B) plus the Supplemental Hedge Budget for the Index Account.

ii. The Annual Rate of Indexed Credits reflecting the fundamental characteristics of the Index Account and the appropriate relationship to the expected risk and return of the Benchmark Index Account. The illustration actuary shall use actuarial judgment to determine this value using lookback methodology consistent with 4 (A) and 4 (B) (i) where appropriate.

iii. The lesser of (1) and (2) multiplied by the Annual Rate of Index Credits for the Benchmark Index Account, calculated in 4 (B), divided by (2); plus, the Supplemental Hedge Budget for the Index Account:

1. Hedge Budget of the Index Account.

2. Hedge Budget of the Benchmark Index Account.

D. For the purposes of compliance with Section 6 (C) of Model #582, the Supplemental Hedge Budget is subtracted from the Annual Rate of Indexed Credits before comparing to the earned interest rate underlying the disciplined current scale.

At the beginning of each calendar year, the insurer shall be allowed up to three (3) months to update the credited rate for each Index Account in accordance with 4 (B) and 4 (C).

5. Disciplined Current Scale

The earned interest rate for the disciplined current scale shall be limited as follows:

A. If an insurer engages in a hedging program for Indexed Credits in an account, the assumed earned interest rate underlying the disciplined current scale for that account, inclusive of all general account assets, both hedge and non-hedge assets, that support the policy, net of default costs and investment expenses (including the amount spent to generate the Indexed Credits of the policy) shall not exceed the lesser of (i) and (ii):

i. The Annual Net Investment Earnings Rate, plus 45% of the lesser of (1) and (2):

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1. Hedge Budget minus any annual floor, to the extent that the floor is supported by the Hedge Budget.

2. The minimum of the Annual Net Investment Earnings Rate and the Hedge Budget that is used in the determination of the Benchmark Index Account.

ii. The Annual Rate of Indexed Credits plus the Annual Net Investment Earnings Rate minus the Hedge Budget.

These rates should be adjusted for timing differences in the hedge cash flows to ensure that fixed interest is not earned on the Hedge Budget minus any annual floor, to the extent that the floor is supported by the Hedge Budget.

Guidance Note: The above approach does not stipulate any required methodology as long as it produces a consistent limit on the assumed earned interest rate underlying the disciplined current scale.

For a policy with multiple Index Accounts, a maximum rate in 5 (A) should be calculated for each account. All accounts, fixed and indexed, within a policy can be tested in aggregate.

B. If an insurer does not engage in a hedging program for Indexed Credits, the assumed earned interest rate underlying the disciplined current scale shall not exceed the Annual Net Investment Earnings Rate.

C. These experience limitations shall be included when testing for self-support and lapse-support under Model #582, accounting for all illustrated benefits including any illustrated benefits and bonuses that impact the policy's account value.

6. Policy Loans

If the illustration includes a loan, the illustrated Policy Loan Interest Credited Rate shall not exceed the illustrated.

Policy Loan Interest Rate by more than 50 basis points. For example, if the illustrated Policy Loan Interest Rate is 4.00%, the Policy Loan Interest Credited Rate shall not exceed 4.50%.

7. Additional Standards

The basic illustration shall also include the following:

A. A ledger using the Alternate Scale shall be shown alongside the ledger using the illustrated scale with equal prominence.

B. A table showing the minimum and maximum of the geometric average annual credited rates calculated in 4 (A).

C. For each Index Account illustrated, a table showing actual historical index changes and corresponding hypothetical Indexed Credits using current index parameters for the most recent 20-year period.

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Actuarial Guideline L

2013 INDIVIDUAL DISABILITY INCOME VALUATION TABLE ACTUARIAL GUIDELINE

A. Background

The 2013 IDI Valuation Table, as included in the *Health Insurance Reserves Model Regulation* (#10), is the valuation standard to replace the 1985 Commissioner's Individual Disability Tables (85CIDA/85CIDC). The link below brings one to the 2013 IDI Valuation Table workbook and instructions:

https://content.naic.org/sites/default/files/actuary-01-2013-idi-valuation-table-workbook-and-instructions-version-1-3.zip

An actuarial guideline is more appropriate to handle the multiple segments of the 2013 IDI Valuation Table, the computations of own experience, the application of credibility, and successor updates to the table, which are not normally found in model regulations.

B. Purpose

The purpose of this actuarial guideline is to provide instructions for the use of the 2013 IDI Valuation Table that is referenced in the *Health Insurance Reserves Model Regulation* (#10). This guideline pertains to IDI claims consistent with the conditions defined in the model regulation and governs the selection of claim termination rates for the purpose of calculating IDI claim reserves. This guideline does not address reserve adequacy, which remains the concern of the insurer according to the terms expressed in the model regulation.

Although the various detailed formulas in this guideline do not address or define reserve adequacy directly, it is assumed that appropriate adequacy tests will be made periodically. Such adequacy testing is considered to be an additional tool for the actuary to make appropriate choices in cases in which leeway from any prescription made herein is allowed (A/E calculation, margin, etc.) so that the calculation of the reserve generally will be adequate and the actuary does not need to continually rely on other measures to achieve adequacy. In addition to the instances in which leeway from prescription is mentioned below, nothing in this guideline should be assumed to prohibit the actuary from building a case and requesting permission from the state insurance commissioner for other appropriate variations. Many such situations, because they would apply to fully credible blocks of business and are intended for continual use, should be considered for approval by the commissioner for a period tied to the updates required by section C.vi. of this guideline and not approved on an annual basis.

When the insurer follows the instructions provided in this guideline, the selected claim termination rates meet the minimum valuation standard defined in the model regulation.

C. Valuation Table Modifications

If not invoking the own experience measurement exemption exception specified in section E of this guideline, a company should use a credibility weighted combination of its own claim termination experience with the 2013 IDI Valuation Table to create its specific valuation table for the purpose of calculating disabled life reserve (DLR).

For claims in duration group 1 (months 1 to 12 following disability incurral) or greater, the valuation termination rates are computed using the termination rates from the 2013 IDI Valuation Table (S) multiplied by experience adjustment factors (T) that are calculated separately for four different duration groups.

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Valuation Termination Rate = T x S

The duration groups are defined as follows:

Group 1: duration 1 to 12 months
Group 2: duration > 12 months and duration <= 24 months
Group 3 duration > 24 months and duration <= 60 months
Group 4: duration > 60 months and duration <= 120 months
Group 5: duration > 120 months

S is the claim termination rates from the 2013 IDI Valuation Table; and

T is computed as $T = [Z \text{ x } F * (1\text{-}M) + (1 - Z)]$.

Z is a credibility weighting factor, between 0 and 1, developed for each duration group according to the following specifications:

Group 1-5: $Z = Min\left(\sqrt{N/K}, 1\right)$ N is the number of expected claimant termination counts from the 2013 IDI Valuation Table.

K is a set of constants defined by duration group as follows:

Group 1 and 2: K = 3,300
Group 3: K = 2,500
Group 4: K = 2,100
Group 5: K = 1,700

F is the ratio of the company's actual total of termination counts to the expected termination counts for the 2013 IDI Valuation Table for each duration group specified above;

The A/E ratio (F) is to be determined based on monthly indemnity. If the actuary has reserve adequacy or other significant analysis that demonstrates that some other weighting of claims (claim or claimant counts, gross benefit, net benefit, etc.) is appropriate for measuring A/E, and also is expected to produce reserves not less than those produced by using a monthly indemnity measurement, such alternative measurement is deemed appropriate. If the actuary cannot produce A/E ratios based on monthly indemnity and only based on claim count or claimant count, an adjustment factor on 0.962 should be multiplied by the A/E ratios in each duration segment to convert them to an indemnity basis. The 0.962 factor is based on the observed relationship for indemnity- versus count-based claim termination experience in the IDI Valuation Table.

M is the company experience margin, determined for each duration group 2 or greater according to the following formula:

$$M = Min\left(15\%, Max\left(5\%, 3\% + 1.65 * \sqrt{A/C}\right)\right)$$

This is the minimum value for the definition of M prior to any reserve adequacy analysis. Adequacy tests and analysis of experience (sharpness of fluctuations, trends over the period of the termination rate study, changing claims practices, etc.) may indicate that a larger value of M may be more appropriate. If so, such a value is deemed appropriate. For duration group 1 (1 to 12 months), M is 5 percent, the same as the 2013 IDI Valuation Table margin for duration 1.

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A is a set of constants defined by duration group as follows:

Group 1 and 2: $A = 4.0$
Group 3: $A = 3.0$
Group 4: $A = 2.5$
Group 5: $A = 2.0$

C is the company's actual number of total claimant termination counts by duration group. If an actuary cannot directly determine claimant termination counts, he or she may approximate it using the average number of claims per claimant for their block of claims.

The company should not use termination rates that produce total reserves for claims disabled for more than two years that are less than the reserves produced for these claims by computing T as T = 1.30.

D. Company-Specific Experience—Own Company Experience Measurement

In computing values F and S to comply with section B of this guideline, the appointed actuary should:

1. Segment the company claim termination experience into any major subgroup that may produce significantly different results (e.g., market niches, risk management practices, unique benefit designs, etc.);

2. Combine affiliated statutory entities and assumed reinsurance, in which claim management is under a common structure, when considering company experience. It also is appropriate to evaluate experience separately when specific blocks of company business have distinct risk management practices or significantly different risk characteristics;

3. Include all relevant experience the company is capable of providing for as many of the last five years (not including the lag period described below) as is appropriate;

4. Include a suitable lag period. Some claims may close retroactively, and others initially thought to be closed may reopen retroactively. Therefore, based on company experience, a suitable lag period is needed. The appointed actuary may use a lag period of up to 12 months if company experience shows it is appropriate. The five-year period mentioned above does not include the lag period;

5. Measure A/E based on monthly indemnity consistent with the development of the 2013 IDI Valuation Table. The A/E ratio is defined as the ratio of actual claim termination experience to the expected claim termination experience, according to the 2013 IDI Valuation Table with margin (by disability duration grouping). The A/E ratio is referred to as the variable F in section B, paragraph 4 of this guideline. For companies that can develop A/E studies only based on claim termination counts, an adjustment factor of 0.962 should be multiplied by their A/E ratio for each claim duration to convert it to an indemnity basis. The 0.962 factor was developed based on the relationship of the indemnity-based A/E to count-based A/E for the industry table;

6. In calculating expected claim terminations based on the 2013 IDI Valuation Table, companies should use all variables and modifiers with two exceptions:

    a. If a company has not maintained appropriate diagnosis codes on historical claim records, the company may set the diagnosis CTR modifier to 1.00.

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b. If a company has not maintained appropriate occupation codes on historical claim records to identify occupations and assign them to the five occupation classes of the 2013 IDI Valuation Table consistent with definitions of these occupation classes, the company may assign claims to Occ Classes 1, 2, 3, and 4 based on the way the company has assigned claims to the 85CIDA occupation classes.

7. Assign credibility based on claimant termination counts, and not monthly indemnity terminated. Companies should use claimant termination counts and not claim termination counts in determining the number of terminations for their own company experience credibility. Each company will need to make appropriate adjustments based on its average number of claims per claimant if it is not able to determine claimant termination counts directly and can only directly measure claim termination counts. For example, on average, if a company has 1.5 open claims per claimant and if it had 100 claim terminations in a duration segment over its five-year study period, it would divide 100 by 1.5 and use 67 claimant terminations when determining credibility;

8. Update the minimum valuation basis in accordance with section B of this guideline at least once every five years. In addition, the valuation basis also should be updated whenever the company's annual own experience study produces, in accordance with section B, a value T that changes by more than 10 percent from the one used in the current valuation basis for any of the five duration groups. All claims valued using the 2013 IDI Valuation Table share the same company experience factors. When the company experience factors are updated, the new factors apply to all claims valued using the 2013 table, including claims incurred prior to the update of the experience factors;

9. Do not count as terminations those claims that are closed due to settlement (i.e., a lump sum replacing a series of potential future payments); that have reached the end of the maximum benefit duration; or that are closed due to a contractual limitation, such as a mental disorder limitation. For this purpose, a termination due to a change in definition of disability is not considered a termination due to reaching the maximum benefit duration. Terminations of residual or partial disability claims count as total disability terminations. Changes in the definition of disability do not count as a termination unless the claim actually terminates. If a claim closes when the definition of disability changes, that is counted as a claim termination;

10. Use experience that is otherwise relevant in accordance with the professional judgment of the appointed actuary;

11. Do not use experience that the commissioner has deemed inappropriate or likely to produce significantly inadequate reserves; and

12. In the above paragraphs, the term "company" refers to a single company or a group of legally related companies subject to the same claim management.

E. Own Experience Measurement Exemption

If, at the time of valuation, a company has fewer than 50 open claimants disabled within two years of the effective date of the valuation, and fewer than 200 open claimants disabled more than two years prior to the effective date of the valuation, the insurer is exempt from the requirement that the 2013 IDI Valuation Table be modified by the company's own experience. Said company should use 100 percent of the 2013 IDI Valuation Table for calculating claims termination rates in order to comply with the minimum valuation standard. This exemption is determined at the statutory company level and not at any segmented level that might be used in determining the own experience modifier.

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Actuarial Guideline LI

THE APPLICATION OF ASSET ADEQUACY TESTING TO LONG-TERM CARE INSURANCE RESERVES

Background

The *Health Insurance Reserves Model Regulation (#010)* and the *NAIC Valuation Manual (VM-25)* contain requirements for the calculation of long-term care insurance (LTC) reserves. Regulators have observed a lack of uniform practice in the implementation of tests of reserve adequacy and reasonableness of LTC reserves. The reserve adequacy testing required by Model #10 and VM-25 does not provide regulators comfort as to the reserve adequacy of companies with material blocks of LTC business. As such, regulators must rely upon asset adequacy analysis required by the *NAIC Valuation Manual* (*VM-30*) to evaluate the solvency position of companies with sizable blocks of LTC business. This Guideline is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for the asset adequacy testing applied to a company's LTC block of contracts. In particular, this Guideline:

(1) Specifies that the appropriate form of asset adequacy analysis may be in the form of a gross premium valuation or in a more robust form, such as cash-flow testing, with Actuarial Standards of Practice providing guidance in this area;

(2) Clarifies the type of adequacy testing methods that must be used for aggregation with other blocks of business to be allowed for asset adequacy analysis purposes;

(3) Requires a uniform approach to supporting acceptable assumptions regarding future LTC premium rate increases;

(4) Provides requirements for documentation of assumptions associated with all key LTC risks; and

(5) Provides requirements for documentation of standalone LTC asset adequacy testing results.

Note: It is anticipated that the requirements contained in this Guideline will be incorporated into the *NAIC Valuation Manual* (VM-30) at a future date, effective for a future valuation year. This Guideline will cease to apply to annual statutory financial statements at the time the corresponding VM-30 requirements become effective.

Text

1. **Effective Date**

This Guideline shall be effective for reserves reported with the December 31, 2017, and subsequent annual statutory financial statements.

2. **Authority**

Pursuant to Section 1, paragraph 3, of *VM-30* of the *NAIC Valuation Manual*, the commissioner shall have the authority to specify specific methods of actuarial analysis and actuarial assumptions when, in the commissioner's judgment, these specifications are necessary for an acceptable opinion to be rendered relative to the adequacy of reserves and related items.

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3. Scope

This Guideline shall apply to a company with over 10,000 inforce lives covered by long-term care insurance contracts as of the valuation date. All long-term care insurance contracts, whether directly written or assumed through reinsurance are included. Accelerated death benefit products or other combination products where the substantial risk of the product is associated with life insurance or an annuity are not subject to this Guideline.

4. Asset Adequacy Analysis of LTC Business

A. As stated in Actuarial Standard of Practice (ASOP) No. 22, multiple asset adequacy analysis methods, including cash-flow testing and gross premium valuation, are available to actuaries for this analysis.

The method of analysis used for LTC shall conform with ASOP No. 22 in recognition of the typical significant asset and liability-related risks associated with LTC.

B. Asset adequacy analysis specific to all inforce LTC business, and without consideration of results for other block of business within the company, must be performed for valuations associated with the December 31, 2017, and subsequent annual statutory financial statements. The analysis shall comply with applicable Actuarial Standards of Practice, including standards regarding identification of key risks. Material assumptions associated with the LTC business shall be determined testing moderately adverse deviations in actuarial assumptions.

C. When determining whether additional reserves are necessary:

1. A reserve deficiency in the LTC block may be aggregated with sufficiencies in the company's other blocks of business for the purposes of developing an actuarial opinion, if cash-flow testing is used for both the LTC business and for all significant blocks of non-LTC business within a company. If a reserve deficiency in the LTC block is not offset with sufficiencies in the company's other blocks of business, then additional reserves shall be established as required by section 2.C.2. of *VM-30*.

2. If cash-flow testing is not used for testing of the LTC business, then a reserve deficiency revealed from another method, e.g., a gross premium valuation, utilized for purposes of asset adequacy analysis of the LTC block under this Guideline shall not be offset with sufficiencies in the company's other blocks of business. The additional reserves under this Guideline shall be established based only upon the adequacy of the reserves in the LTC block.

D. When determining the effect of investment returns or the time value of money:

1. In the case where cash-flow testing is used, the company must allocate investment income to the LTC block of business consistently with the way investment income generated by the General Account is managed. If, however, a segment of the General Account is used to manage the investment risk for LTC business, the investment income generated by assets from that segment should be appropriately represented within the asset adequacy analysis.

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2. In the case where a gross premium valuation method is used or asset cash flows are not explicitly modeled, the discount rate used by the actuary must reflect consideration of the yield on current assets held to support the liability as well as future yields on assets purchased with future premium income and reinvestments or anticipated divesture of existing assets.

E. The analysis shall only anticipate premium rate increases based upon a rate increase plan that is documented, is supported by and has been approved by management, is highly likely to be undertaken, and contains rate increase requests and timelines by jurisdiction. The assumptions used in the analysis should reflect a reasonable estimate of regulatory approved amounts and implementation timelines.

5. **Documentation Required**

The documentation requirements below are to be incorporated as a separate section of the appointed actuary's Actuarial Memorandum required by the *VM-30* or in a special Actuarial Memorandum containing LTC-specific information and shall be submitted to the commissioner of the company's state of domicile. The separate section of the companywide Actuarial Memorandum or the special Actuarial Memorandum shall be available to other state insurance commissioners in which the company is licensed upon request to the company. The confidentiality provisions regarding the Actuarial Memorandum contained in *VM-30* are applicable to the separate section of the Actuarial Memorandum and to the special Memorandum.

A. Results of the asset adequacy analysis of the LTC business shall be reported and documented in the separate section of the Actuarial Memorandum or the special Memorandum, as appropriate.

B. Assumptions on mortality shall be documented to state the reference standard valuation table, if applicable, and explicitly cite adjustments, select factors, and mortality improvement factors, where applicable. If a reference standard valuation table is not used in setting the mortality assumption, then a table of rates and comparison of the applied rates to rates from an unmodified standard mortality table for sample issue ages shall be provided. A summary of experience or other actuarial support of assumptions used shall be documented.

C. Assumptions on voluntary lapse shall be documented in table format by duration band and by other factors such as gender, marital status, with versus without inflation rider, and length of benefit period impacting the lapse assumption, where applicable. A summary of experience or other support of assumptions shall be documented.

D. Assumptions on morbidity shall be documented and actuarial support of the assumption shall be provided. If an outside source is used as the basis for morbidity assumptions, then the rationale for the applicability of that source and any adjustments to the factors from that source shall be documented.

E. Assumptions on investment returns and interest rates shall be documented. If a simplified approach is applied, such as implicit reflection of projected investment returns through the use of discount rates in a gross premium valuation as contemplated in Section 4.D.2., then justification shall be provided.

F. Any rate increases already approved shall be documented by jurisdiction with approved implementation timelines. Assumptions on future rate increases shall be documented by policy form or policy grouping. Such documentation should adequately describe the way in which future rate increase assumptions are developed. Unless the appointed actuary has operational responsibility for carrying out the rate increase plan specified in Section 4.E.,

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the Memorandum shall contain a signed and dated reliance statement from the person with operational responsibility for carrying out such actions that the rate increase plan(s) provided to the appointed actuary appropriately reflects management's plan.

G. Documentation of any other material assumptions shall be provided.

H. Documentation shall be provided for assumptions that have significantly changed from the prior year's analysis.

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Actuarial Guideline LII

VARIABLE ANNUITY EARLY ADOPTION

Background

Beginning in 2015, the NAIC commissioned a study of the reserve and RBC framework for Variable Annuity products. The study concluded that the existing requirements resulted in non-economic volatility, providing incentive for companies to engage in the use of financial planning techniques that the NAIC deemed inappropriate. Considerable effort was spent to develop and test updates to the reserve and RBC framework to address these issues. That revised framework was adopted by the NAIC during 2018, and the changes to NAIC models, the NAIC *Valuation Manual*, and the NAIC *Life Risk-Based Capital Forecasting & Instructions* have been developed and adopted by the NAIC on August 2, 2019. By the provisions of the SVL (Model 820), the changes to the *Valuation Manual* will be effective on January 1, 2020, and will impact subsequent financial statements.

During the discussion of the framework by the Variable Annuities Issues (E) Working Group, the question was raised whether companies would have the option to 'early adopt'; that is, to apply the new framework for the reserve and RBC values used for the December 31, 2019, financial statements. Since the new framework has been determined to provide improved financial measurement of the company's liability and risk, there was agreement that optional application of the new framework for the December 31, 2019, financial statements would be appropriate.

Guideline

A company may elect to apply the VM-21 requirements from the 2020 NAIC *Valuation Manual* as the *Valuation Manual* requirements for the valuation on December 31, 2019. For such election, the phase-in provision of *Valuation Manual* VM-21 Section 2.B. may not be elected. Any company electing early adoption of VM-21 shall also:

1. Apply the provisions of *Actuarial Guideline XLIII—CARVM for Variable Annuities* as amended for 2020 to the December 31, 2019, valuation of contracts within the scope of that guideline;

2. Apply the Life RBC instructions for 2020 in the calculation of C-3 RBC in LR027 for 2019;

3. Follow the documentation and certification requirements of VM-31 from the 2020 *Valuation Manual* for the Variable Annuity Business. In the VA Summary, clearly indicate the use of the new requirements in the section on change in methods from prior year; and

4. Notify the commissioner of the state of domicile of such elections.

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Actuarial Guideline LIII

APPLICATION OF THE VALUATION MANUAL FOR TESTING THE ADEQUACY OF LIFE INSURER RESERVES

Background

The *NAIC Valuation Manual (VM-30)* contains actuarial opinion and supporting actuarial memorandum requirements, including requirements for asset adequacy analysis. Regulators have observed a lack of uniform practice in the implementation of asset adequacy analysis. The variety of practice in incorporating the risk of complex assets into testing does not provide regulators comfort as to reserve adequacy. Examples of complex assets are structured securities, including asset-backed securities and collateralized loan obligations, as well as assets originated by the company or affiliated or contracted entity. An initial increase of this activity has been noted in support of general account annuity blocks; however, recent activity was noted in other life insurer blocks.

This Guideline is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for asset adequacy analysis performed by life insurers. In particular, this Guideline:

(1) Helps identify reserve adequacy and claims-paying ability in moderately adverse conditions, including conditions negatively impacting cash flows from complex assets.

(2) Clarifies elements to consider in establishing margins on asset-related assumptions.

(3) Ensures recognition that higher expected gross returns from assets are, to some extent, associated with higher risk, and that assumptions fit reasonably within the risk-return spectrum.

(4) Requires sensitivity testing regarding complex assets supporting life insurer business.

(5) Identifies expectations in practice regarding the valuation of complex assets within asset adequacy analysis.

(6) Reflects that while complex assets tend to have higher uncertainty regarding timing and amount of cash flows than more traditional investments, because complex assets are difficult to classify, and the regulatory concern is regarding the projected net yields and cash flows from those assets, the focus of the analysis requirements will be on assets categorized as high-yielding.

(7) Requires additional documentation of investment fee income relationships with affiliated entities or entities close to the company.

Text

1. **Effective Date**

This Guideline shall be effective for asset adequacy analysis of the reserves reported in the December 31, 2022, Annual Statement and for the asset adequacy analysis of the reserves reported in all subsequent Annual Statements.

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Guidance Note: It is anticipated that the requirements contained in this Guideline will be incorporated into VM-30 at a future date, effective for a future valuation year. Requirements in the Guideline will cease to apply to annual statutory financial statements when the corresponding or replacement VM-30 requirements become effective.

2. **Scope**

This Guideline shall apply to all life insurers with:

A. Over $5 billion of general account actuarial reserves (from Exhibits 5, 6, 7 and 8 of the annual statement) and non-unitized separate account assets, or

B. Over $100 million of general account actuarial reserves (from Exhibits 5, 6, 7 and 8 of the annual statement) and non-unitized separate account assets and over 5% of supporting assets (selected for asset adequacy analysis) in the category of Projected High Net Yield Assets, as defined in Section 3.F.

Actuarial reserve amounts are included in the amounts in A and B whether directly written or assumed through reinsurance and are determined before any reinsurance ceded credit.

This Guideline applies to assets supporting liabilities tested in the asset adequacy analysis except it does not apply to unitized separate account assets or policy/contract loans.

3. **Definitions**

A. Equity-Like Instruments – Assets that include the following:

i. Any assets that, for purposes of risk-based capital C-1 reporting, are in the category of common stock, i.e., have a 30% or higher risk-based capital charge.

ii. Any assets that are captured on Schedule A or Schedule BA of the annual statement.

iii. Bond funds.

B. Fair Value – The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, consistent with methodology of fair value, as reported in the Annual Statement.

C. Net Market Spread – For each asset grouping, shall mean the spread over comparable Treasury bonds that equates the fair value as of the valuation date with modeled cash flows, less the default assumption used in asset adequacy analysis.

Market conventions and other approximations are acceptable for the purposes of this definition.

D. Investment Grade Net Spread Benchmark – The applicable spread found in Appendix I using the weighted average life (WAL) of the associated non-Equity-Like Instrument.

E. Guideline Excess Spread – The net spread derived by subtracting the Investment Grade Net Spread Benchmark from the Net Market Spread for non-Equity-Like Instruments. Investment expenses shall be excluded from this calculation.

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F. Projected High Net Yield Assets – Currently held or reinvestment assets that are either:

i. An Equity-Like Instrument assumed to have higher value at projection year 10 or later than under an assumption of annual total returns, before the deduction of investment expenses, of 4% for the first 10 projection years after the valuation date followed by 5% for projection year 11 and after. Aggregation shall be done at a level of granularity that is consistent with or more granular than how the assets are grouped, i.e., compressed, in the asset adequacy analysis model, or

ii. Assets other than Equity-Like Instruments where the assumed Guideline Excess Spread is higher than zero. In addition:

(a) Aggregation of the comparison between the assumed Net Market Spread from each asset and the Investment Grade Net Spread Benchmark shall be done at a level of granularity that is consistent with or more granular than how the assets are grouped, i.e., compressed, in the asset adequacy analysis model.

(b) For applicable assets that do not have an explicit WAL or term to maturity, the appointed actuary shall disclose the method used to determine the appropriate WAL used for comparing to the Investment Grade Net Spread Benchmark.

(c) For purposes of the comparison between the assumed Net Market Spread from each asset and the Investment Grade Net Spread Benchmark, investment expenses shall be excluded.

iii. The following asset types can be excluded from the scope of requirements in sections 4.A.ii. through 5.:

(a) Cash or cash equivalents

(b) Treasuries and agency bonds

(c) Public non-convertible, fixed-rate corporate bonds with no or immaterial callability

4. Asset Adequacy Considerations and Documentation Expectations

A. Net Return and Risk Documentation

i. For all assets, either currently held or in assumed reinvestments, provide:

(a) Identification of the assumed gross asset yield and the key components (for example, default and investment expenses) deducted to arrive at the assumed net asset yield.

(b) Explanation of any future reinvestment strategy assumptions that materially differ from current practices.

ii. For Projected High Net Yield Assets, either currently held or in assumed reinvestments, provide:

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(a) A detailed explanation describing the relationship between the expected gross returns from these assets and the risk. It shall also include, for the aspect of any higher expected gross returns not assumed to be associated with higher risk, an explanation of how overperforming assets with expected returns lying outside the risk-return spectrum can be assumed to persist and be available for reinvestments throughout the projection period in moderately adverse conditions.

(b) Commentary on how assumptions on assets with risk factors leading to substantial volatility of returns, as identified through sensitivity testing or other means, contain an appropriate margin to reflect the uncertainty in the timing and amounts of asset cash flows.

(c) Identification of the extent to which Projected High Net Yield Assets are supporting major product categories, e.g., individual fixed annuities and pension risk transfers.

(d) Explanation of rationale for materially changing or not changing complex-asset-based assumptions from the prior year's analysis.

B. Model Rigor – Where significant risks associated with complex, Projected High Net Yield Assets are not adequately captured with traditional modeling techniques, more rigorous modeling of those risks should occur.

i. Where necessary to adequately reflect the risk:

(a) Multi-scenario testing of those risks specific to complex assets should be performed. For example, investments that may provide a higher expected return in part due to limited information, niche skill sets, or other factors may require unique scenarios (for instance to adequately capture credit or liquidity risk) to fully encompass potential sources of loss.

(b) Asset cash flows should be appropriately projected to reflect anticipated liquidity under adverse conditions. If such model aspects are not developed, sufficient additional conservatism to reflect this risk shall be applied.

(c) To the extent that the process for modeling or otherwise evaluating the risks is complex, and the potential for disconnect between reality and modeling increases, an additional margin to assumption(s) should be applied. Any such margin shall be applied in the direction of asset adequacy analysis results being less favorable.

(d) The full distribution of risk associated with complex assets should be considered.

ii. An appointed actuary may use simplifications, approximations, and modeling efficiency techniques if the appointed actuary can demonstrate that the use of such techniques does not make asset adequacy analysis results more favorable. These techniques may be less appropriate if the amount of complex, high-yielding assets becomes a higher percentage of total assets.

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Guidance Note: Actuarial Standards of Practice (ASOPs), including ASOP No. 7 and No. 56 contain additional guidance on the use of models in the analysis of cash flows.

C. Fair Value Determination – In asset adequacy analysis, when an asset is projected to be available for sale, a fair value of that asset is established, based on the projected market conditions. Fair Value should only be determined internally (by the insurance or investment management company) when the market-based value of the asset or similar asset cannot be obtained or expected to be obtained in a projected scenario.

i. When the Fair Value of a material portion of supporting assets is determined internally, the actuarial memorandum shall contain a step-by-step description of the approach used to calculate the Fair Value of such assets.

ii. Provide the total Fair Value of assets that have values determined internally.

iii. When the Fair Value of a material portion of assets is determined internally, a sensitivity test should be performed (and the impact on asset adequacy analysis results presented) assuming a haircut to internally derived Fair Values that the appointed actuary deems reasonable given the commensurate level of anticipated uncertainty.

D. Non-Publicly Traded Assets – For non-publicly traded assets originated by the company, within the company's group, or within an entity closely tied to a company's group (inclusive of the company's investment manager), provide the following:

i. Documentation of practices to help ensure accurate valuation of those assets.

ii. The total Fair VGuideline Excess Spreadalue of such assets.

iii. To the extent the contractual agreement affects the investment income revenue streams included in the asset adequacy analysis, disclose in detail applicable contractual agreements and revenue sharing, e.g., performance fees, between the entity responsible for providing investment or other types of services and the insurer.

Also, assumed net cash flows from assets should be net of all explicit or implicit fees or expenses, such as origination fees, as well as reflective of other asset-related risks including credit risk, illiquidity risk, and other market risks.

E. Investments Expenses (Fees) – Assumed investment expenses, whether paid to an external asset manager or to internal investment management staff, as well as additional expenses that are directly attributable to the specific investments, should be commensurate with the expected expenses in light of the complexity of the assets.

F. Reinsurance Modeling – Related to reinsurance, relevant communications and disclosures, for instance commentary on collectability and counterparty risk, should be presented in the memorandum.

Guidance Note: Section 4.F. is consistent with the standard laid out in ASOP No. 11 – Reinsurance Involving Life Insurance, Annuities, or Health Benefit Plans in Financial Reports.

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G. Borrowing – Please identify if any borrowing is modeled besides to address very short-term liquidity needs. Also, verify borrowing and reinvestment rates to ensure that projections are not materially benefiting from arbitrage advantages.

5. **Sensitivity Tests and Attribution Analysis related to Assumptions on Projected High Net Yield Assets**

A. Sensitivity Testing

i. Perform and disclose, separately for (a) and (b), the asset adequacy analysis results from the following sensitivity tests:

(a) For reinvestment assets other than Equity-Like Instruments, assume the Net Market Spreads (before deduction of investment expenses) for Projected High Net Yield Assets do not exceed the Investment Grade Net Spread Benchmark and apply the test to a baseline of a level Treasury rate scenario.

For the purposes of limiting the Net Market Spreads at the Investment Grade Net Spread Benchmark, Projected High Net Yield Assets may be aggregated together but shall not include any assets that are not Projected High Net Yield Assets.

(b) For reinvestment assets that are Equity-Like Instruments, assume annual total returns, before the deduction of investment expenses, of 4% for the first 10 projection years after the valuation date followed by 5% for projection year 11 and after.

ii. Strict technical compliance for each asset may not be practical for reasons such as model limitations. Professional judgment should be applied to produce sensitivity testing results that are consistent with the spirit of the test. A variety of alternative methods may be acceptable. Appropriate explanation and justification should be provided for the method that was employed.

iii. Sensitivity testing for the purpose of this Guideline does not reflect commentary on moderately adverse conditions, but the volatility and impact demonstrated from the testing should be contemplated in Section 4.A.ii.(b) considerations.

B. For Projected High Net Yield Assets for non-Equity-Like Instruments, either currently held or in assumed reinvestments, perform and disclose the following attribution analysis steps at the asset type level associated with the templates in Section 6:

i. State the assumed Guideline Excess Spread.

ii. Estimate the proportion of the Guideline Excess Spread attributable to the following factors:

(a) Credit risk

(b) Illiquidity risk

(c) Deviations of current spreads from long-term spreads defined in Appendix 1

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(d) Volatility and other risks (identify and describe these risks in detail)

iii. Provide commentary on the results of Section 5.B.ii. Also, where judgment is applied, provide supporting rationale of how the expected return in excess of the Investment Grade Net Spread Benchmark is estimated.

Guidance Note: A best-efforts approach is expected for the year-end 2022 attribution analysis.

6. **Reporting, Review, and Templates**

Guidance Note: The NAIC Valuation Analysis (E) Working Group (VAWG) shall serve as a resource in the targeted review of asset adequacy analysis related to modeling of business supported with Projected High Net Yield Assets. VAWG shall provide periodic reports identifying outliers and concerns regarding the analysis to help inform regulators on the effectiveness of this Guideline in meeting the seven objectives stated in the Background section.

A. The documentation, sensitivity test results, and attribution analysis referenced above are to be incorporated as a separate, easily identifiable section of the actuarial memorandum required by VM-30 or as a standalone document, with a due date of April 1 following the applicable valuation date. The domiciliary commissioner may approve a later due date for companies seeking a hardship extension. The separate section or standalone document shall be available to other state insurance commissioners in which the company is licensed upon request to the company. The confidentiality and information provisions in state adoptions of NAIC Model 820 regarding the actuarial memorandum are applicable to the separate section or standalone document required by this Guideline.

B. The following sample templates adopted by the Life Actuarial (A) Task Force (LATF) are available on the LATF web page (https://content.naic.org/cmte_a_latf.htm) under the "Documents" tab:

i. Asset summary.

ii. Components of net asset yield for various asset classes, with separate tables to be provided for initial assets and reinvestment assets.

iii. Sensitivity test aspects for Projected High Net Yield Assets that are fixed-income.

iv. Sensitivity test results for Projected High Net Yield Assets.

v. Attribution analysis, with separate tables to be provided for initial assets and reinvestment assets for Projected High Net Yield Assets.

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Appendix I – Investment Grade Net Spread Benchmark

WAL (Weighted Avg Life)	Investment Grade Net Spread Benchmark (in bps)
1-10	170
11-20	175
21-30	185

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Actuarial Guideline LIV

NONFORFEITURE REQUIREMENTS FOR INDEX-LINKED VARIABLE ANNUITY PRODUCTS

Background

The purpose of this guideline is to specify the conditions under which an Index-Linked Variable Annuity (ILVA) is consistent with the definition of a variable annuity and exempt from Model 805 and specify nonforfeiture requirements consistent with variable annuities.

A number of insurers have developed and are issuing annuity products with credits based on the performance of an index with caps on returns, participation rates, spreads or margins, or other crediting elements, that include a risk of negative index returns subject to limitations on the loss, such as a floor or a buffer. These products are not unitized and do not invest directly in the assets whose performance forms the basis for the credits.

There is no established terminology for these annuity products. These products go by several names, including structured annuities, registered index-linked annuities (RILA), or index-linked variable annuities, among others. This guideline refers to these products as index-linked variable annuities (ILVA).

Variable annuities are exempted from the scope of NAIC Model 805, *Standard Nonforfeiture Law for Individual* Deferred Annuities*;* however*,* NAIC Model 805 does not define the term "variable annuity".

NAIC Model 250, *Variable Annuity Model Regulation*, defines variable annuities as “contracts that provide for annuity benefits that vary according to the investment experience of a separate account.” Section 7B of NAIC Model 250 provides that "to the extent that a variable annuity contract provides benefits that do not vary in accordance with the investment performance of a separate account" the contract shall satisfy the requirements of the NAIC Model 805.

The application of the NAIC Model 250 to a traditional variable annuity with unitized values is straightforward. The unitized feature provides an automatic linkage between annuity values and the investment experience of a separate account. Daily values (market values of the separate account assets) are the basis of all the benefits, including surrender values.

The fact that ILVA accounts are not unitized means they do not have values determined directly by the market prices of the underlying assets. Therefore, this guideline sets forth principles and requirements for determining values, including death benefit, withdrawal amount, annuitization amount or surrender values, such that an ILVA is considered a variable annuity and thereby exempt from Model 805. An ILVA that does not comply with the principles and requirements of this guideline is not considered a variable annuity and therefore is subject to Model 805.

Drafting Note: This guideline interprets the term “variable annuity” for purposes of exemption from Model 805. It is not intended to modify the definition of a variable annuity under Model 250 or other Model Regulations.

Scope

This guideline applies to any index-linked annuity exempt from the NAIC Model 805 on the basis that it is a variable annuity and includes index-linked crediting features that are built into policies or contracts (with or without unitized subaccounts) or added to such by rider, endorsement, or amendment.

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Principles

This guideline is based on the following principles:

1. Interim Values defined in the contract provide equity between the contract holder and the insurance company.

2. Interim Values are consistent with the value of the Hypothetical Portfolio over the Index Strategy Term.

Definitions

"Derivative Asset Proxy" means a package of hypothetical derivative assets established at the beginning of an Index Strategy Term that is designed to replicate credits provided by an Index Strategy at the end of an Index Strategy Term.

"Fixed Income Asset Proxy" is a hypothetical fixed income asset.

"Hypothetical Portfolio" means a hypothetical portfolio composed of a Fixed Income Asset Proxy and a Derivative Asset Proxy.

"Index" means a benchmark designed to track the performance of a defined portfolio of securities.

"Index Strategy" means a method used to determine index credits with specified index or indices and cap, buffer, participation rate, spread, margin or other index crediting elements.

"Index Strategy Base" means the notional amount used to determine index credits that does not change throughout the Index Strategy Term except for withdrawals, transfers, deposits, loans, and any explicit charges.

"Index Strategy Term" means the period of time from the term start date to the term end date over which an index changes and the index credit is determined.

"Interim Value" means the Strategy Value at any time other than the start date and end date of an Index Strategy Term.

"Strategy Value" means the value, attributable to an Index Strategy, used in determining values including death benefit, withdrawal amount, annuitization amount or surrender values.

"Trading Cost" means the additional cost of liquidating the derivative assets in the Derivative Asset Proxy or actual derivative assets supporting the Index Strategy that is not accounted for in the Derivative Asset Proxy calculation.

Text

The Index Strategy Base must equal the Strategy Value at the Index Strategy Term start date.

The Fixed Income Asset Proxy is assumed to be a hypothetical fixed income asset with a yield that results in:

i. At the beginning of the Index Strategy Term, the book value of the Fixed Income Asset Proxy equal to the Index Strategy Base less the Derivative Asset Proxy value; and

ii. At the end of the Index Strategy Term, the book value of the Fixed Income Asset Proxy, assuming no change in yield, projected to equal the Index Strategy Base.

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Drafting Note: This guideline defines the conditions under which an index-linked variable annuity is exempt from Model 805 on the basis that it is a variable annuity. A variable annuity provides daily values (analogous to Interim Values in this guideline) based on the market value of separate account assets. In order to more closely align an ILVA to a variable annuity, Interim Values should be consistent with the market value of hypothetical assets supporting the ILVA (i.e., Hypothetical Portfolio). The market value of the assets may be determined by a fair value methodology or by applying an MVA to the book value. A state may want to consider whether including or excluding an MVA is appropriate. In making a determination regarding whether including or excluding an MVA is appropriate and, if applicable, what an acceptable MVA formula is, the state should consider whether the Interim Values provide reasonable equity between the contract holder and the insurance company.

The value of the package of derivative assets is determinable daily. Assumptions used to determine the market value of the Derivative Asset Proxy including implied volatilities, risk-free rates, and dividend yields must be consistent with the observable market prices of derivative assets, whenever possible.

Interim Values must be materially consistent with the value of the Hypothetical Portfolio over the Index Strategy Term less a provision for the cost attributable to reasonably expected or actual Trading Costs at the time the Interim Value is calculated.

If a contract provides Interim Values determined using a methodology other than a Hypothetical Portfolio methodology as described in this guideline, the company must demonstrate that the contractually defined Interim Values will be materially consistent over the Index Strategy Term with the Interim Values that would be produced using the Hypothetical Portfolio methodology for each combination of Index Strategy and Index Strategy Term under a reasonable number of realistic economic scenarios that include index changes that test crediting constraints and recognize initial option pricing market conditions.

The company must provide an actuarial memorandum with each ILVA product filing that includes the following:

1. Actuarial certifications must be included with each ILVA product filing and must include the following:

    a. Interim Values defined in the contract provide equity between the contract holder and the insurance company;

    b. The assumptions used to determine the market value of the Derivative Asset Proxy including implied volatilities, risk-free rates, dividend yields, and other parameters required to value the derivatives are consistent with the observable market prices of derivative assets over the Index Strategy Term, whenever possible. Valuation techniques include the standard Black-Scholes method, Monte-Carlo Simulation techniques, and other market consistent option valuation techniques for more complex options;

    c. The contractually defined Interim Values are materially consistent with the Interim Values that would be produced using the Hypothetical Portfolio methodology for each combination of Index Strategy and Index Strategy Term over the Index Strategy Term less a provision for the Trading Costs at the time the Interim Value is calculated; and

    d. Any Trading Costs represent reasonably expected or actual costs at the time the Interim Value is calculated.

2. If the Interim Values are determined using a methodology other than the Hypothetical Portfolio methodology described in this guideline, the actuary shall describe the testing performed to verify that the values are materially consistent with the Hypothetical Portfolio

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methodology. The actuary should define any parameters or assumptions used in determining material consistency and provide a summary of the results of the testing.

3. Descriptions of:

   a. The value of the Fixed Income Asset Proxy;

   b. The market value adjustment formula, if any;

   c. The market value of the Derivative Asset Proxy including any Trading Costs; and

   d. All formulas, methodologies and assumptions used to calculate these values for each Index Strategy and Index Strategy Term as well as the sources for all assumptions.

ILVA nonforfeiture benefits for Index Strategies subject to this guideline must comply with Section 7 of Model 250 not including Section 7.B with net investment return consistent with the requirements for determining Interim Values in this guideline.

Effective Date

This guideline applies to all contracts (including associated riders, endorsements, or amendments) issued on or after July 1, 2024.

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ACTUARIAL GUIDELINES – APPENDICES

Appendix C-1

Provides maximum reserve valuation and maximum life policy nonforfeiture interest rates for new issues, new purchases or changes in fund (as defined) under Section 4217, 4218, and 4221(k) of the New York Insurance Law as amended in 1982, 1983, 1985, 1986, 1987, 1988, 1990 and 1994. This information is provided for informational purposes and to aid compliance with the New York law.

Appendix C-2

Includes interpretations from the former Emerging Actuarial Issues (E) Working Group adopted by the Financial Condition (E) Committee. The Financial Analysis (E) Working Group and the Valuation Analysis (E) Working Group follow these interpretations when performing reviews of the reserving methodologies under *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38).

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Appendix C-1

APPENDIX TO GUIDELINES

This information can be found on the New York State Department of Financial Services website:
https://www.dfs.ny.gov/apps_and_licensing/life_insurers/max_reserve_life

NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES

Maximum Reserve Valuation and Maximum Life Policy Nonforfeiture Interest Rates

The maximum reserve valuation and nonforfeiture interest rates, prescribed by Sections 4217 and 4221(k) of the New York Insurance Law, are specified in "Table A through Table H Rates" noted below. Such rates vary from year to year based on Moody's corporate bond yield averages for 12 and 36 months ending on June 30, and weighting factors prescribed by Section 4217. The Moody's averages are provided for years 1981 to present in the attached Appendix.

Notice Regarding Payout Annuity Valuation Interest Rate Changes

Pursuant to Section 4217(g) of the New York State Insurance Law, the maximum valuation interest rates for payout annuities with premium determination dates on or after January 1, 2019, are prescribed in Section 103.5 of 11 NYCRR 103 (Insurance Regulation No. 213).

Payout Annuity Maximum Valuation Interest Rates for Premiums Received after 2019:

For the policies, contracts, certificates, and benefits with premium determination dates on or after January 1, 2020, the maximum valuation interest rates prescribed by Section 103.5 of Regulation 213 are specified in the following file: 2024 Payout Annuity MVIR (XLSX)

Payout Annuity Maximum Valuation Interest Rates for Premiums Received during 2019:

For the policies, contracts, certificates, and benefits with premium determination dates on or after January 1, 2019, and prior to January 1, 2020, the maximum valuation interest rates prescribed in Section 103.5(c)(2) of Regulation 213 and Section 103.5(c)(3) of Regulation 213 are specified in the following file: 2019 Payout Annuity MVIR (XLSX).

Clarification on Fixed Annuity Reserves Interest Rates

We note that there has been some concern over the appropriate maximum valuation interest rate for flexible premium deferred annuities (FPDA). Section 4217(c)(4)(D)(iii) of the New York Insurance Law does not allow the use of the additional .05 weighting factor for annuities that guarantee interest rates on future considerations received more than twelve months beyond the valuation date. Accordingly, for flexible premium deferred annuities the weighting factors shown in Section 4217(c)(4)(D)(iii)(I) or 4217(c)(4)(D)(iii)(II) should be used. For convenience, maximum valuation interest rates for such FPDAs are shown in Table D (issue year basis) and Table G (change in fund basis). The rates shown in Table E and Table H are not appropriate for FPDAs.

- General Information
- Table A through Table H Rates
- Appendix (Moody's Averages)

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KATHY HOCHUL
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ADRIENNE A. HARRIS
Acting Superintendent

August 3, 2023

TO: ALL AUTHORIZED LIFE INSURANCE COMPANIES, ACCREDITED LIFE REINSURERS, FRATERNAL BENEFIT SOCIETIES AND CHARITABLE ANNUITY SOCIETIES

SUBJECT: MAXIMUM RESERVE VALUATION AND MAXIMUM LIFE POLICY NONFORFEITURE INTEREST RATES

Attached hereto is an outline providing maximum reserve valuation and maximum life policy non-forfeiture interest rates for new issues, new purchases or changes in fund (as defined) for years 1982 through 2023 (and other years where shown), under Sections 4217, 4218 and 4221(k) of the New York Insurance Law, as amended in 1982, 1983, 1985, 1986, 1987, 1988, 1990, and 1994.

The maximum valuation and non-forfeiture interest rates, prescribed by Sections 4217 and 4221(k) of the New York Insurance Law for future years, will vary from year to year depending on Moody's corporate bond yield averages.

The maximum valuation interest rates for issues, purchases and changes-in-fund of years 1982 through 2023 (and other years where shown) are outlined below. The maximum valuation and non-forfeiture interest rates for Ordinary Life Insurance are shown in Category A of page 1, except for Single Premium Life Insurance, as defined in Section 4217(c)(4)(B)(vi), the maximum valuation interest rates for which are shown in Category B on pages 2-5.

Please refer to Sections 4217 and 4221 of NY Insurance Law, Regulation 147, Regulation 151, and Regulation 213 for definitions and explanations of valuation interest rate, guarantee duration, plan type and product category. This notice is to be used for informational purposes, as an aid in complying with the law.

Should any person have any question or comment in regard to this information, please contact Matthew Ryan of the Life Bureau at (518) 474-7929 or Matthew.Ryan@dfs.ny.gov.

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A. ORDINARY LIFE INSURANCE (Except as covered in B)

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate	Maximum Nonforfeiture Interest Rate*
1979-1981	10 years or less	4.50%	5.50%
	More than 10 years, up to 20	4.50	5.50
	More than 20 years	4.50	5.50
1982	10 years or less	6.75%	8.50%
	More than 10 years, up to 20	6.25	7.75
	More than 20 years	5.50	7.00
1983-1986	10 years or less	7.25%	9.00%
	More than 10 years, up to 20	6.75	8.50
	More than 20 years	6.00	7.50
1987	10 years or less	6.50%	8.25%
	More than 10 years, up to 20	6.00	7.50
	More than 20 years	5.50	7.00
1988-1992	10 years or less	6.00%	7.50%
	More than 10 years, up to 20	6.00	7.50
	More than 20 years	5.50	7.00
1993	10 years or less	6.00%	7.50%
	More than 10 years, up to 20	6.00	7.50
	More than 20 years	5.00	6.25
1994	10 years or less	5.50%	7.00%
	More than 10 years, up to 20	5.25	6.50
	More than 20 years	5.00	6.25
1995-1998	10 years or less	5.50%	7.00%
	More than 10 years, up to 20	5.25	6.50
	More than 20 years	4.50	5.75
1999-2005	10 years or less	5.00%	6.25%
	More than 10 years, up to 20	4.75	6.00
	More than 20 years	4.50	5.75
2006-2012	10 years or less	4.50%	5.75%
	More than 10 years, up to 20	4.25	5.25
	More than 20 years	4.00	5.00
2013-2020	10 years or less	3.75%	4.75%
	More than 10 years, up to 20	3.75	4.75
	More than 20 years	3.50	4.50

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A. (cont.) ORDINARY LIFE INSURANCE (Except as covered in B)

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate	Maximum Nonforfeiture Interest Rate*
2021-2024	10 years or less	3.25%	4.00%
	More than 10 years, up to 20	3.25	4.00
	More than 20 years	3.00	3.75

*Per New York Insurance Law section 4221(k)(9)(B)(i), at the option of the company, calculations for all policies issued in a particular calendar year may be made on the basis of a rate of interest not exceeding the nonforfeiture interest rate per New York Insurance Law section 4221(k)(10) for policies issued in the immediately preceding calendar year.

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B. Single Premium Life Insurance of the kind referred to in Section 4217(c)(4)(B)(vi) of the New York Insurance Laws (as amended by Chapter 302 of the laws of 1987).

		Maximum Reserve Valuation Interest Rate	
Issue Year	Guarantee Duration	Issue Year Basis	Change-in-Fund Basis
1982	10 years or less	10.00%	10.50%
	More than 10 years, up to 20	7.25	10.00
	More than 20 years	6.25	8.75
1983	10 years or less	8.75%	9.25%
	More than 10 years, up to 20	7.00	8.75
	More than 20 years	6.25	7.75
1984	10 years or less	8.50%	9.25%
	More than 10 years, up to 20	7.00	8.50
	More than 20 years	6.25	7.50
1985	10 years or less	8.50%	9.00%
	More than 10 years, up to 20	7.00	8.50
	More than 20 years	6.25	7.50
1986	10 years or less	7.25%	7.75%
	More than 10 years, up to 20	6.50	7.25
	More than 20 years	5.75	6.50
1987	10 years or less	6.50%	6.75%
	More than 10 years, up to 20	6.00	6.50
	More than 20 years	5.50	6.00
1988	10 years or less	7.00%	7.50%
	More than 10 years, up to 20	6.25	7.00
	More than 20 years	5.75	6.25
1989	10 years or less	7.00%	7.25%
	More than 10 years, up to 20	6.25	7.00
	More than 20 years	5.50	6.25
1990	10 years or less	6.50%	7.00%
	More than 10 years, up to 20	6.25	6.50
	More than 20 years	5.50	6.00
1991	10 years or less	6.75%	7.00%
	More than 10 years, up to 20	6.25	6.75
	More than 20 years	5.50	6.00
1992	10 years or less	6.25%	6.50%
	More than 10 years, up to 20	6.00	6.25
	More than 20 years	5.25	5.75

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B. (cont.) Single Premium Life Insurance of the kind referred to in Section 4217(c)(4)(B)(vi) of the New York Insurance Laws (as amended by Chapter 302 of the laws of 1987).

		Maximum Reserve Valuation Interest Rate	
Issue Year	Guarantee Duration	Issue Year Basis	Change-in-Fund Basis
1993	10 years or less	5.75%	6.00%
	More than 10 years, up to 20	5.50	5.75
	More than 20 years	5.00	5.25
1994	10 years or less	5.50%	5.75%
	More than 10 years, up to 20	5.25	5.50
	More than 20 years	4.75	5.00
1995	10 years or less	6.00%	6.25%
	More than 10 years, up to 20	5.50	6.00
	More than 20 years	5.00	5.50
1996	10 years or less	5.50%	5.75%
	More than 10 years, up to 20	5.25	5.50
	More than 20 years	4.75	5.00
1997	10 years or less	5.50%	5.75%
	More than 10 years, up to 20	5.25	5.50
	More than 20 years	5.00	5.25
1998	10 years or less	5.25%	5.50%
	More than 10 years, up to 20	5.00	5.25
	More than 20 years	4.75	4.75
1999	10 years or less	5.25%	5.50%
	More than 10 years, up to 20	5.00	5.25
	More than 20 years	4.50	4.75
2000	10 years or less	5.75%	6.00%
	More than 10 years, up to 20	5.25	5.75
	More than 20 years	4.75	5.25
2001	10 years or less	5.50%	5.75%
	More than 10 years, up to 20	5.25	5.50
	More than 20 years	4.75	5.00
2002	10 years or less	5.50%	5.75%
	More than 10 years, up to 20	5.25	5.50
	More than 20 years	4.75	5.00
2003	10 years or less	5.00%	5.25%
	More than 10 years, up to 20	4.75	5.00
	More than 20 years	4.50	4.75

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B. (cont.) Single Premium Life Insurance of the kind referred to in Section 4217(c)(4)(B)(vi) of the New York Insurance Laws (as amended by Chapter 302 of the laws of 1987).

		Maximum Reserve Valuation Interest Rate	
Issue Year	Guarantee Duration	Issue Year Basis	Change-in-Fund Basis
2004	10 years or less	4.75%	5.00%
	More than 10 years, up to 20	4.75	4.75
	More than 20 years	4.25	4.50
2005	10 years or less	4.50%	4.75%
	More than 10 years, up to 20	4.50	4.50
	More than 20 years	4.00	4.25
2006	10 years or less	4.50%	4.75%
	More than 10 years, up to 20	4.50	4.50
	More than 20 years	4.25	4.25
2007	10 years or less	4.75%	4.75%
	More than 10 years, up to 20	4.50	4.75
	More than 20 years	4.25	4.25
2008	10 years or less	4.75%	5.00%
	More than 10 years, up to 20	4.50	4.75
	More than 20 years	4.25	4.50
2009	10 years or less	5.00%	5.25%
	More than 10 years, up to 20	4.75	5.00
	More than 20 years	4.25	4.75
2010	10 years or less	4.50%	4.75%
	More than 10 years, up to 20	4.50	4.50
	More than 20 years	4.00	4.25
2011	10 years or less	4.25%	4.50%
	More than 10 years, up to 20	4.25	4.25
	More than 20 years	4.00	4.00
2012	10 years or less	3.75%	4.00%
	More than 10 years, up to 20	3.75	3.75
	More than 20 years	3.50	3.75
2013	10 years or less	3.75%	3.75%
	More than 10 years, up to 20	3.50	3.75
	More than 20 years	3.50	3.50
2014	10 years or less	4.00%	4.00%
	More than 10 years, up to 20	3.75	4.00
	More than 20 years	3.50	3.75

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B. (cont.) Single Premium Life Insurance of the kind referred to in Section 4217(c)(4)(B)(vi) of the New York Insurance Laws (as amended by Chapter 302 of the laws of 1987).

		Maximum Reserve Valuation Interest Rate	
Issue Year	Guarantee Duration	Issue Year Basis	Change-in-Fund Basis
2015	10 years or less	3.75%	3.75%
	More than 10 years, up to 20	3.50	3.75
	More than 20 years	3.50	3.50
2016	10 years or less	3.75%	3.75%
	More than 10 years, up to 20	3.75	3.75
	More than 20 years	3.50	3.75
2017	10 years or less	3.50%	3.75%
	More than 10 years, up to 20	3.50	3.50
	More than 20 years	3.50	3.50
2018	10 years or less	3.50%	3.75%
	More than 10 years, up to 20	3.50	3.50
	More than 20 years	3.50	3.50
2019	10 years or less	3.75%	3.75%
	More than 10 years, up to 20	3.50	3.75
	More than 20 years	3.50	3.50
2020	10 years or less	3.25%	3.25%
	More than 10 years, up to 20	3.25	3.25
	More than 20 years	3.25	3.25
2021	10 years or less	3.00%	3.00%
	More than 10 years, up to 20	3.00	3.00
	More than 20 years	3.00	3.00
2022	10 years or less	3.25%	3.25%
	More than 10 years, up to 20	3.25	3.25
	More than 20 years	3.00	3.25
2023	10 years or less	4.25%	4.25%
	More than 10 years, up to 20	3.50	4.25
	More than 20 years	3.25	4.00

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C. Single Premium Immediate Annuities and annuity benefits arising from life insurance policies and annuity and guaranteed interest contracts with cash settlements options.

Issues of or Purchases During	Maximum Reserve Valuation Interest Rate
1982	13.25%
1983-1984	11.25
1985	11.00
1986	9.25
1987	8.00
1988	8.75
1989	8.75
1990	8.25
1991	8.25
1992	7.75
1993	7.00
1994	6.50
1995	7.25
1996-1997	6.75
1998-1999	6.25
2000	7.00
2001	6.75
2002	6.50
2003	6.00
2004	5.50
2005-2006	5.25
2007-2008	5.50
2009	6.00

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C. (cont.) Single Premium Immediate Annuities and annuity benefits arising from life insurance policies and annuity and guaranteed interest contracts with cash settlements options.

Issues of or Purchases During	Maximum Reserve Valuation Interest Rate
2010	5.25
2011	5.00
2012	4.25
2013	4.00
2014	4.50
2015-2016	4.00
2017-2018	3.75
2019	4.00

For Single Premium Immediate Annuities and annuity benefits arising from life insurance policies and annuity and guaranteed interest contracts with cash settlement options issued on or after January 1, 2020, the maximum valuation interest rates are prescribed by Section 103.5 of 11 NYCRR 103 (Insurance Regulation 213). These maximum valuation interest rates may be found on the Department's website here:

https://www.dfs.ny.gov/apps_and_licensing/life_insurers/max_reserve_life

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D. Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
1982	5 years or less	13.25%	10.50%	9.25%
	More than 5 years, up to 10	12.50	10.50	9.25
	More than 10 years, up to 20	8.50	7.25	6.75
	More than 20 years	6.75	6.00	6.00
1983	5 years or less	11.25%	9.25%	8.25%
	More than 5 years, up to 10	10.75	9.25	8.25
	More than 10 years, up to 20	8.25	7.00	6.75
	More than 20 years	6.75	5.75	5.75
1984	5 years or less	11.25%	9.25%	8.00%
	More than 5 years, up to 10	10.75	9.25	8.00
	More than 10 years, up to 20	8.25	7.00	6.75
	More than 20 years	6.75	5.75	5.75
1985	5 years or less	11.00%	9.00%	8.00%
	More than 5 years, up to 10	10.50	9.00	8.00
	More than 10 years, up to 20	8.25	7.00	6.50
	More than 20 years	6.50	5.75	5.75
1986	5 years or less	9.25%	7.75%	6.75%
	More than 5 years, up to 10	8.75	7.75	6.75
	More than 10 years, up to 20	7.50	6.50	6.00
	More than 20 years	6.00	5.50	5.50
1987	5 years or less	8.00%	6.75%	6.25%
	More than 5 years, up to 10	7.75	6.75	6.25
	More than 10 years, up to 20	7.00	6.00	5.75
	More than 20 years	5.75	5.25	5.25
1988	5 years or less	8.75%	7.50%	6.75%
	More than 5 years, up to 10	8.50	7.50	6.75
	More than 10 years, up to 20	7.25	6.25	6.00
	More than 20 years	6.00	5.25	5.25
1989	5 years or less	8.75%	7.25%	6.50%
	More than 5 years, up to 10	8.25	7.25	6.50
	More than 10 years, up to 20	7.25	6.25	6.00
	More than 20 years	6.00	5.25	5.25
1990	5 years or less	8.25%	7.00%	6.25%
	More than 5 years, up to 10	8.00	7.00	6.25
	More than 10 years, up to 20	7.00	6.25	5.75
	More than 20 years	5.75	5.25	5.25

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D. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
1991	5 years or less	8.25%	7.00%	6.25%
	More than 5 years, up to 10	8.00	7.00	6.25
	More than 10 years, up to 20	7.00	6.25	5.75
	More than 20 years	5.75	5.25	5.25
1992	5 years or less	7.75%	6.50%	6.00%
	More than 5 years, up to 10	7.50	6.50	6.00
	More than 10 years, up to 20	6.75	6.00	5.75
	More than 20 years	5.75	5.00	5.00
1993	5 years or less	7.00%	6.00%	5.50%
	More than 5 years, up to 10	6.75	6.00	5.50
	More than 10 years, up to 20	6.25	5.50	5.25
	More than 20 years	5.25	4.75	4.75
1994	5 years or less	6.50%	5.75%	5.25%
	More than 5 years, up to 10	6.50	5.75	5.25
	More than 10 years, up to 20	6.00	5.25	5.00
	More than 20 years	5.00	4.50	4.50
1995	5 years or less	7.25%	6.25%	5.75%
	More than 5 years, up to 10	7.00	6.25	5.75
	More than 10 years, up to 20	6.25	5.50	5.25
	More than 20 years	5.25	4.75	4.75
1996	5 years or less	6.75%	5.75%	5.25%
	More than 5 years, up to 10	6.50	5.75	5.25
	More than 10 years, up to 20	6.00	5.25	5.00
	More than 20 years	5.00	4.50	4.50
1997	5 years or less	6.75%	5.75%	5.25%
	More than 5 years, up to 10	6.50	5.75	5.25
	More than 10 years, up to 20	6.00	5.25	5.25
	More than 20 years	5.25	4.75	4.75
1998	5 years or less	6.25%	5.50%	5.00%
	More than 5 years, up to 10	6.00	5.50	5.00
	More than 10 years, up to 20	5.75	5.00	4.75
	More than 20 years	4.75	4.50	4.50
1999	5 years or less	6.25%	5.50%	5.00%
	More than 5 years, up to 10	6.00	5.50	5.00
	More than 10 years, up to 20	5.50	5.00	4.75
	More than 20 years	4.75	4.50	4.50

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D. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
2000	5 years or less	7.00%	6.00%	5.50%
	More than 5 years, up to 10	6.75	6.00	5.50
	More than 10 years, up to 20	5.75	5.25	5.00
	More than 20 years	5.00	4.50	4.50
2001	5 years or less	6.75%	5.75%	5.25%
	More than 5 years, up to 10	6.50	5.75	5.25
	More than 10 years, up to 20	6.00	5.25	5.00
	More than 20 years	5.00	4.50	4.50
2002	5 years or less	6.50%	5.75%	5.25%
	More than 5 years, up to 10	6.25	5.75	5.25
	More than 10 years, up to 20	6.00	5.25	5.00
	More than 20 years	5.00	4.50	4.50
2003	5 years or less	6.00%	5.25%	4.75%
	More than 5 years, up to 10	5.75	5.25	4.75
	More than 10 years, up to 20	5.50	4.75	4.75
	More than 20 years	4.75	4.25	4.25
2004	5 years or less	5.50%	5.00%	4.75%
	More than 5 years, up to 10	5.50	5.00	4.75
	More than 10 years, up to 20	5.00	4.75	4.50
	More than 20 years	4.50	4.25	4.25
2005	5 years or less	5.25%	4.75%	4.50%
	More than 5 years, up to 10	5.00	4.75	4.50
	More than 10 years, up to 20	4.75	4.50	4.25
	More than 20 years	4.25	4.00	4.00
2006	5 years or less	5.25%	4.75%	4.50%
	More than 5 years, up to 10	5.25	4.75	4.50
	More than 10 years, up to 20	4.75	4.50	4.25
	More than 20 years	4.25	4.00	4.00
2007	5 years or less	5.50%	4.75%	4.50%
	More than 5 years, up to 10	5.25	4.75	4.50
	More than 10 years, up to 20	4.75	4.50	4.25
	More than 20 years	4.25	4.00	4.00
2008	5 years or less	5.50%	5.00%	4.50%
	More than 5 years, up to 10	5.50	5.00	4.50
	More than 10 years, up to 20	5.00	4.50	4.25
	More than 20 years	4.25	4.00	4.00

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D. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
2009	5 years or less	6.00%	5.25%	5.00%
	More than 5 years, up to 10	5.75	5.25	5.00
	More than 10 years, up to 20	5.25	4.75	4.50
	More than 20 years	4.50	4.25	4.25
2010	5 years or less	5.25%	4.75%	4.25%
	More than 5 years, up to 10	5.00	4.75	4.25
	More than 10 years, up to 20	4.75	4.25	4.25
	More than 20 years	4.25	4.00	4.00
2011	5 years or less	5.00%	4.50%	4.25%
	More than 5 years, up to 10	4.75	4.50	4.25
	More than 10 years, up to 20	4.50	4.25	4.00
	More than 20 years	4.00	3.75	3.75
2012	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, up to 10	4.25	4.00	3.75
	More than 10 years, up to 20	4.00	3.75	3.75
	More than 20 years	3.75	3.50	3.50
2013	5 years or less	4.00%	3.75%	3.50%
	More than 5 years, up to 10	3.75	3.75	3.50
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.50	3.50
2014	5 years or less	4.50%	4.00%	3.75%
	More than 5 years, up to 10	4.25	4.00	3.75
	More than 10years, up to 20	4.00	3.75	3.75
2015	5 years or less	4.00%	3.75%	3.50%
	More than 5 years, up to 10	4.00	3.75	3.50
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.50	3.50
2016	5 years or less	4.00%	3.75%	3.75%
	More than 5 years, up to 10	4.00	3.75	3.75
	More than 10 years, up to 20	4.00	3.75	3.75
	More than 20 years	3.75	3.50	3.50

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D. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
2017	5 years or less	3.75%	3.75%	3.50%
	More than 5 years, up to 10	3.75	3.75	3.50
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.25	3.25
2018	5 years or less	3.75%	3.75%	3.50%
	More than 5 years, up to 10	3.75	3.75	3.50
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.25	3.25
2019	5 years or less	4.00%	3.75%	3.75%
	More than 5 years, up to 10	4.00	3.75	3.75
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.50	3.50
2020	5 years or less	3.25%	3.25%	3.25%
	More than 5 years, up to 10	3.25	3.25	3.25
	More than 10 years, up to 20	3.25	3.25	3.25
	More than 20 years	3.25	3.00	3.00
2021	5 years or less	3.00%	3.00%	3.00%
	More than 5 years, up to 10	3.00	3.00	3.00
	More than 10 years, up to 20	3.00	3.00	3.00
	More than 20 years	3.00	3.00	3.00
2022	5 years or less	3.50%	3.25%	3.25%
	More than 5 years, up to 10	3.50	3.25	3.25
	More than 10 years, up to 20	3.25	3.25	3.00
	More than 20 years	3.00	3.00	3.00
2023	5 years or less	4.75%	4.25%	4.00%
	More than 5 years, up to 10	4.50	4.25	4.00
	More than 10 years, up to 20	3.50	3.50	3.50
	More than 20 years	3.50	3.25	3.25

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E. Other Annuities and Guaranteed Interest Contracts, with cash settlement options but without interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
1982	5 years or less	13.75%	11.25%	10.00%
	More than 5 years, up to 10	13.25	11.25	10.00
	More than 10 years, up to 20	8.75	7.50	7.25
	More than 20 years	7.25	6.25	6.25
1983	5 years or less	11.75%	9.75%	8.75%
	More than 5 years, up to 10	11.25	9.75	8.75
	More than 10 years, up to 20	8.75	7.50	7.00
	More than 20 years	7.00	6.25	6.25
1984	5 years or less	11.75%	9.75%	8.50%
	More than 5 years, up to 10	11.25	9.75	8.50
	More than 10 years, up to 20	8.75	7.50	7.00
	More than 20 years	7.00	6.25	6.25
1985	5 years or less	11.50%	9.50%	8.50%
	More than 5 years, up to 10	11.00	9.50	8.50
	More than 10 years, up to 20	8.50	7.50	7.00
	More than 20 years	7.00	6.25	6.25
1986	5 years or less	9.50%	8.00%	7.25%
	More than 5 years, up to 10	9.25	8.00	7.25
	More than 10 years, up to 20	7.75	6.75	6.50
	More than 20 years	6.50	5.75	5.75
1987	5 years or less	8.50%	7.25%	6.50%
	More than 5 years, up to 10	8.00	7.25	6.50
	More than 10 years, up to 20	7.25	6.50	6.00
	More than 20 years	6.00	5.50	5.50
1988	5 years or less	9.25%	7.75%	7.00%
	More than 5 years, up to 10	8.75	7.75	7.00
	More than 10 years, up to 20	7.50	6.50	6.25
	More than 20 years	6.25	5.75	5.75
1989	5 years or less	9.00%	7.50%	7.00%
	More than 5 years, up to 10	8.75	7.50	7.00
	More than 10 years, up to 20	7.50	6.50	6.25
	More than 20 years	6.25	5.50	5.50
1990	5 years or less	8.50%	7.25%	6.50%
	More than 5 years, up to 10	8.25	7.25	6.50
	More than 10 years, up to 20	7.50	6.50	6.25
	More than 20 years	6.25	5.50	5.50

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E. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options but without interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
1991	5 years or less	8.75%	7.25%	6.75%
	More than 5 years, up to 10	8.25	7.25	6.75
	More than 10 years, up to 20	7.50	6.50	6.25
	More than 20 years	6.25	5.50	5.50
1992	5 years or less	8.00%	6.75%	6.25%
	More than 5 years, up to 10	7.75	6.75	6.25
	More than 10 years, up to 20	7.00	6.25	6.00
	More than 20 years	6.00	5.25	5.25
1993	5 years or less	7.25%	6.25%	5.75%
	More than 5 years, up to 10	7.00	6.25	5.75
	More than 10 years, up to 20	6.50	5.75	5.50
	More than 20 years	5.50	5.00	5.00
1994	5 years or less	6.75%	6.00%	5.50%
	More than 5 years, up to 10	6.50	6.00	5.50
	More than 10 years, up to 20	6.25	5.50	5.25
	More than 20 years	5.25	4.75	4.75
1995	5 years or less	7.50%	6.50%	6.00%
	More than 5 years, up to 10	7.25	6.50	6.00
	More than 10 years, up to 20	6.50	5.75	5.50
	More than 20 years	5.50	5.00	5.00
1996	5 years or less	6.75%	6.00%	5.50%
	More than 5 years, up to 10	6.75	6.00	5.50
	More than 10 years, up to 20	6.25	5.50	5.25
	More than 20 years	5.25	4.75	4.75
1997	5 years or less	7.00%	6.00%	5.50%
	More than 5 years, up to 10	6.75	6.00	5.50
	More than 10 years, up to 20	6.25	5.50	5.25
	More than 20 years	5.25	5.00	5.00
1998	5 years or less	6.50%	5.75%	5.25%
	More than 5 years, up to 10	6.25	5.75	5.25
	More than 10 years, up to 20	6.00	5.25	5.00
	More than 20 years	5.00	4.75	4.75
1999	5 years or less	6.25%	5.50%	5.25%
	More than 5 years, up to 10	6.25	5.50	5.25
	More than 10 years, up to 20	5.75	5.25	5.00
	More than 20 years	5.00	4.50	4.50

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E. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options but without interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
2000	5 years or less	7.25%	6.25%	5.75%
	More than 5 years, up to 10	7.00	6.25	5.75
	More than 10 years, up to 20	6.00	5.50	5.25
	More than 20 years	5.25	4.75	4.75
2001	5 years or less	7.00%	6.00%	5.50%
	More than 5 years, up to 10	6.75	6.00	5.50
	More than 10 years, up to 20	6.25	5.50	5.25
	More than 20 years	5.25	4.75	4.75
2002	5 years or less	6.75%	6.00%	5.50%
	More than 5 years, up to 10	6.50	6.00	5.50
	More than 10 years, up to 20	6.00	5.50	5.25
	More than 20 years	5.25	4.75	4.75
2003	5 years or less	6.25%	5.50%	5.00%
	More than 5 years, up to 10	6.00	5.50	5.00
	More than 10 years, up to 20	5.50	5.00	4.75
	More than 20 years	4.75	4.50	4.50
2004	5 years or less	5.75%	5.00%	4.75%
	More than 5 years, up to 10	5.50	5.00	4.75
	More than 10 years, up to 20	5.25	4.75	4.75
	More than 20 years	4.75	4.25	4.25
2005	5 years or less	5.25%	4.75%	4.50%
	More than 5 years, up to 10	5.25	4.75	4.50
	More than 10 years, up to 20	5.00	4.50	4.50
	More than 20 years	4.50	4.00	4.00
2006	5 years or less	5.50%	4.75%	4.50%
	More than 5 years, up to 10	5.25	4.75	4.50
	More than 10 years, up to 20	5.00	4.50	4.50
	More than 20 years	4.50	4.25	4.25
2007	5 years or less	5.50%	5.00%	4.75%
	More than 5 years, up to 10	5.50	5.00	4.75
	More than 10 years, up to 20	5.00	4.50	4.50
	More than 20 years	4.50	4.25	4.25
2008	5 years or less	5.75%	5.00%	4.75%
	More than 5 years, up to 10	5.50	5.00	4.75
	More than 10 years, up to 20	5.00	4.75	4.50
	More than 20 years	4.50	4.25	4.25

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E. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options but without interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
2009	5 years or less	6.25%	5.50%	5.00%
	More than 5 years, up to 10	6.00	5.50	5.00
	More than 10 years, up to 20	5.25	4.75	4.75
	More than 20 years	4.75	4.25	4.25
2010	5 years or less	5.25%	4.75%	4.50%
	More than 5 years, up to 10	5.25	4.75	4.50
	More than 10 years, up to 20	5.00	4.50	4.25
	More than 20 years	4.25	4.00	4.00
2011	5 years or less	5.00%	4.50%	4.25%
	More than 5 years, up to 10	5.00	4.50	4.25
	More than 10 years, up to 20	4.75	4.25	4.25
	More than 20 years	4.25	4.00	4.00
2012	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, up to 10	4.25	4.00	3.75
	More than 10 years, up to 20	4.00	3.75	3.75
	More than 20 years	3.75	3.50	3.50
2013	5 years or less	4.00%	3.75%	3.75%
	More than 5 years, up to 10	4.00	3.75	3.75
	More than 10 years, up to 20	3.75	3.75	3.50
	More than 20 years	3.50	3.50	3.50
2014	5 years or less	4.50%	4.00%	4.00%
	More than 5 years, up to 10	4.50	4.00	4.00
	More than 10 years, up to 20	4.00	3.75	3.75
	More than 20 years	3.75	3.50	3.50
2015	5 years or less	4.00%	3.75%	3.75%
	More than 5 years, up to 10	4.00	3.75	3.75
	More than 10 years, up to 20	3.75	3.75	3.50
	More than 20 years	3.50	3.50	3.50
2016	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, up to 10	4.00	4.00	3.75
	More than 10 years, up to 20	4.00	3.75	3.75
	More than 20 years	3.75	3.50	3.50

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E. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options but without interest rate guarantees on future considerations, valued on the "Issue Year" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Issue Year	Guarantee Duration	A	B	C
2017	5 years or less	4.00%	3.75%	3.50%
	More than 5 years, up to 10	3.75	3.75	3.50
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.50	3.50
2018	5 years or less	4.00%	3.75%	3.50%
	More than 5 years, up to 10	3.75	3.75	3.50
	More than 10 years, up to 20	3.75	3.50	3.50
	More than 20 years	3.50	3.50	3.50
2019	5 years or less	4.00%	3.75%	3.75%
	More than 5 years, up to 10	4.00	3.75	3.75
	More than 10 years, up to 20	3.75	3.75	3.50
	More than 20 years	3.50	3.50	3.50
2020	5 years or less	3.25%	3.25%	3.25%
	More than 5 years, up to 10	3.25	3.25	3.25
	More than 10 years, up to 20	3.25	3.25	3.25
	More than 20 years	3.25	3.25	3.25
2021	5 years or less	3.00%	3.00%	3.00%
	More than 5 years, up to 10	3.00	3.00	3.00
	More than 10 years, up to 20	3.00	3.00	3.00
	More than 20 years	3.00	3.00	3.00
2022	5 years or less	3.50%	3.25%	3.25%
	More than 5 years, up to 10	3.50	3.25	3.25
	More than 10 years, up to 20	3.25	3.25	3.25
	More than 20 years	3.25	3.00	3.00
2023	5 years or less	4.75%	4.50%	4.25%
	More than 5 years, up to 10	4.75	4.50	4.25
	More than 10 years, up to 20	3.50	3.50	3.50
	More than 20 years	3.50	3.25	3.25

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F. Other Annuities and Guaranteed Interest Contracts, without cash settlement options, valued on the "Issue Year" basis.

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A
1982	5 years or less	13.25%
	More than 5 years, up to 10	12.50
	More than 10 years, up to 20	11.25
	More than 20 years	8.75
1983	5 years or less	11.25%
	More than 5 years, up to 10	10.75
	More than 10 years, up to 20	9.75
	More than 20 years	7.75
1984	5 years or less	11.25%
	More than 5 years, up to 10	10.75
	More than 10 years, up to 20	9.75
	More than 20 years	7.50
1985	5 years or less	11.00%
	More than 5 years, up to 10	10.50
	More than 10 years, up to 20	9.50
	More than 20 years	7.50
1986	5 years or less	9.25%
	More than 5 years, up to 10	8.75
	More than 10 years, up to 20	8.00
	More than 20 years	6.50
1987	5 years or less	8.00%
	More than 5 years, up to 10	7.75
	More than 10 years, up to 20	7.25
	More than 20 years	6.00
1988	5 years or less	8.75%
	More than 5 years, up to 10	8.50
	More than 10 years, up to 20	7.75
	More than 20 years	6.25
1989	5 years or less	8.75%
	More than 5 years, up to 10	8.25
	More than 10 years, up to 20	7.50
	More than 20 years	6.25
1990	5 years or less	8.25%
	More than 5 years, up to 10	8.00
	More than 10 years, up to 20	7.25
	More than 20 years	6.00

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F. (cont.) Other Annuities and Guaranteed Interest Contracts, without cash settlement options, valued on the "Issue Year" basis.

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A
1991	5 years or less	8.25%
	More than 5 years, up to 10	8.00
	More than 10 years, up to 20	7.25
	More than 20 years	6.00
1992	5 years or less	7.75%
	More than 5 years, up to 10	7.50
	More than 10 years, up to 20	6.75
	More than 20 years	5.75
1993	5 years or less	7.00%
	More than 5 years, up to 10	6.75
	More than 10 years, up to 20	6.25
	More than 20 years	5.25
1994	5 years or less	6.50%
	More than 5 years, up to 10	6.50
	More than 10 years, up to 20	6.00
	More than 20 years	5.00
1995	5 years or less	7.25%
	More than 5 years, up to 10	7.00
	More than 10 years, up to 20	6.50
	More than 20 years	5.50
1996	5 years or less	6.75%
	More than 5 years, up to 10	6.50
	More than 10 years, up to 20	6.00
	More than 20 years	5.00
1997	5 years or less	6.75%
	More than 5 years, up to 10	6.50
	More than 10 years, up to 20	6.00
	More than 20 years	5.25
1998	5 years or less	6.25%
	More than 5 years, up to 10	6.00
	More than 10 years, up to 20	5.75
	More than 20 years	4.75
1999	5 years or less	6.25%
	More than 5 years, up to 10	6.00
	More than 10 years, up to 20	5.50
	More than 20 years	4.75

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F. (cont.) Other Annuities and Guaranteed Interest Contracts, without cash settlement options, valued on the "Issue Year" basis.

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A
2000	5 years or less	7.00%
	More than 5 years, up to 10	6.75
	More than 10 years, up to 20	6.25
	More than 20 years	5.25
2001	5 years or less	6.75%
	More than 5 years, up to 10	6.50
	More than 10 years, up to 20	6.00
	More than 20 years	5.00
2002	5 years or less	6.50%
	More than 5 years, up to 10	6.25
	More than 10 years, up to 20	6.00
	More than 20 years	5.00
2003	5 years or less	6.00%
	More than 5 years, up to 10	5.75
	More than 10 years, up to 20	5.50
	More than 20 years	4.75
2004	5 years or less	5.50%
	More than 5 years, up to 10	5.50
	More than 10 years, up to 20	5.00
	More than 20 years	4.50
2005	5 years or less	5.25%
	More than 5 years, up to 10	5.00
	More than 10 years, up to 20	4.75
	More than 20 years	4.25
2006	5 years or less	5.25%
	More than 5 years, up to 10	5.25
	More than 10 years, up to 20	4.75
	More than 20 years	4.25
2007	5 years or less	5.50%
	More than 5 years, up to 10	5.25
	More than 10 years, up to 20	5.00
	More than 20 years	4.25
2008	5 years or less	5.50%
	More than 5 years, up to 10	5.50
	More than 10 years, up to 20	5.00
	More than 20 years	4.50

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F. (cont.) Other Annuities and Guaranteed Interest Contracts, without cash settlement options, valued on the "Issue Year" basis.

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A
2009	5 years or less	6.00%
	More than 5 years, up to 10	5.75
	More than 10 years, up to 20	5.50
	More than 20 years	4.75
2010	5 years or less	5.25%
	More than 5 years, up to 10	5.00
	More than 10 years, up to 20	4.75
	More than 20 years	4.25
2011	5 years or less	5.00%
	More than 5 years, up to 10	4.75
	More than 10 years, up to 20	4.50
	More than 20 years	4.00
2012	5 years or less	4.25%
	More than 5 years, up to 10	4.25
	More than 10 years, up to 20	4.00
	More than 20 years	3.75
2013	5 years or less	4.00%
	More than 5 years, up to 10	3.75
	More than 10 years, up to 20	3.75
	More than 20 years	3.50
2014	5 years or less	4.50%
	More than 5 years, up to 10	4.25
	More than 10 years, up to 20	4.00
	More than 20 years	3.75
2015	5 years or less	4.00%
	More than 5 years, up to 10	4.00
	More than 10 years, up to 20	3.75
	More than 20 years	3.50
2016	5 years or less	4.00%
	More than 5 years, up to 10	4.00
	More than 10 years, up to 20	4.00
	More than 20 years	3.75
2017	5 years or less	3.75%
	More than 5 years, up to 10	3.75
	More than 10 years, up to 20	3.75
	More than 20 years	3.50

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F. (cont.) Other Annuities and Guaranteed Interest Contracts, without cash settlement options, valued on the "Issue Year" basis.

Issue Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A
2018	5 years or less	3.75%
	More than 5 years, up to 10	3.75
	More than 10 years, up to 20	3.75
	More than 20 years	3.50
2019	5 years or less	4.00%
	More than 5 years, up to 10	4.00
	More than 10 years, up to 20	3.75
	More than 20 years	3.50
2020	5 years or less	3.25%
	More than 5 years, up to 10	3.25
	More than 10 years, up to 20	3.25
	More than 20 years	3.25
2021	5 years or less	3.00%
	More than 5 years, up to 10	3.00
	More than 10 years, up to 20	3.00
	More than 20 years	3.00
2022	5 years or less	3.50%
	More than 5 years, up to 10	3.50
	More than 10 years, up to 20	3.25
	More than 20 years	3.25
2023	5 years or less	4.75%
	More than 5 years, up to 10	4.50
	More than 10 years, up to 20	4.50
	More than 20 years	4.00

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G. Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
1982	5 years or less	15.00%	13.75%	10.00%
	More than 5 years, up to 10	14.50	13.75	10.00
	More than 10 years, up to 20	13.25	12.50	9.25
	More than 20 years	10.50	10.50	8.00
1983	5 years or less	12.75%	11.75%	8.75%
	More than 5 years, up to 10	12.25	11.75	8.75
	More than 10 years, up to 20	11.25	10.75	8.25
	More than 20 years	9.25	9.25	7.25
1984	5 years or less	12.75%	11.75%	8.50%
	More than 5 years, up to 10	12.25	11.75	8.50
	More than 10 years, up to 20	11.25	10.75	8.00
	More than 20 years	9.25	9.25	7.00
1985	5 years or less	12.50%	11.50%	8.50%
	More than 5 years, up to 10	12.00	11.50	8.50
	More than 10 years, up to 20	11.00	10.50	8.00
	More than 20 years	9.00	9.00	7.00
1986	5 years or less	10.25%	9.50%	7.25%
	More than 5 years, up to 10	10.00	9.50	7.25
	More than 10 years, up to 20	9.25	8.75	6.75
	More than 20 years	7.75	7.75	6.00
1987	5 years or less	9.00%	8.50%	6.50%
	More than 5 years, up to 10	8.75	8.50	6.50
	More than 10 years, up to 20	8.00	7.75	6.25
	More than 20 years	6.75	6.75	5.50
1988	5 years or less	10.00%	9.25%	7.00%
	More than 5 years, up to 10	9.50	9.25	7.00
	More than 10 years, up to 20	8.75	8.50	6.75
	More than 20 years	7.50	7.50	6.00
1989	5 years or less	9.75%	9.00%	7.00%
	More than 5 years, up to 10	9.50	9.00	7.00
	More than 10 years, up to 20	8.75	8.25	6.50
	More than 20 years	7.25	7.25	5.75
1990	5 years or less	9.25%	8.50%	6.50%
	More than 5 years, up to 10	8.75	8.50	6.50
	More than 10 years, up to 20	8.25	8.00	6.25
	More than 20 years	7.00	7.00	5.50

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G. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
1991	5 years or less	9.25%	8.75%	6.75%
	More than 5 years, up to 10	9.00	8.75	6.75
	More than 10 years, up to 20	8.25	8.00	6.25
	More than 20 years	7.00	7.00	5.75
1992	5 years or less	8.50%	8.00%	6.25%
	More than 5 years, up to 10	8.25	8.00	6.25
	More than 10 years, up to 20	7.75	7.50	6.00
	More than 20 years	6.50	6.50	5.25
1993	5 years or less	7.75%	7.25%	5.75%
	More than 5 years, up to 10	7.50	7.25	5.75
	More than 10 years, up to 20	7.00	6.75	5.50
	More than 20 years	6.00	6.00	5.00
1994	5 years or less	7.25%	6.75%	5.50%
	More than 5 years, up to 10	7.00	6.75	5.50
	More than 10 years, up to 20	6.50	6.50	5.25
	More than 20 years	5.75	5.75	4.75
1995	5 years or less	8.25%	7.50%	6.00%
	More than 5 years, up to 10	8.00	7.50	6.00
	More than 10 years, up to 20	7.25	7.00	5.75
	More than 20 years	6.25	6.25	5.25
1996	5 years or less	7.25%	6.75%	5.50%
	More than 5 years, up to 10	7.00	6.75	5.50
	More than 10 years, up to 20	6.75	6.50	5.25
	More than 20 years	5.75	5.75	4.75
1997	5 years or less	7.50%	7.00%	5.50%
	More than 5 years, up to 10	7.25	7.00	5.50
	More than 10 years, up to 20	6.75	6.50	5.25
	More than 20 years	5.75	5.75	5.00
1998	5 years or less	7.00%	6.50%	5.25%
	More than 5 years, up to 10	6.75	6.50	5.25
	More than 10 years, up to 20	6.25	6.00	5.00
	More than 20 years	5.50	5.50	4.75

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G. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
1999	5 years or less	6.75%	6.25%	5.25%
	More than 5 years, up to 10	6.50	6.25	5.25
	More than 10 years, up to 20	6.25	6.00	5.00
	More than 20 years	5.50	5.50	4.50
2000	5 years or less	7.75%	7.25%	5.75%
	More than 5 years, up to 10	7.50	7.25	5.75
	More than 10 years, up to 20	7.00	6.75	5.50
	More than 20 years	6.00	6.00	5.00
2001	5 years or less	7.50%	7.00%	5.50%
	More than 5 years, up to 10	7.25	7.00	5.50
	More than 10 years, up to 20	6.75	6.50	5.25
	More than 20 years	5.75	5.75	5.00
2002	5 years or less	7.25%	6.75%	5.50%
	More than 5 years, up to 10	7.00	6.75	5.50
	More than 10 years, up to 20	6.50	6.25	5.25
	More than 20 years	5.75	5.75	4.75
2003	5 years or less	6.50%	6.25%	5.00%
	More than 5 years, up to 10	6.25	6.25	5.00
	More than 10 years, up to 20	6.00	5.75	4.75
	More than 20 years	5.25	5.25	4.50
2004	5 years or less	6.00%	5.75%	4.75%
	More than 5 years, up to 10	6.00	5.75	4.75
	More than 10 years, up to 20	5.50	5.50	4.75
	More than 20 years	5.00	5.00	4.25
2005	5 years or less	5.75%	5.25%	4.50%
	More than 5 years, up to 10	5.50	5.25	4.50
	More than 10 years, up to 20	5.25	5.00	4.50
	More than 20 years	4.75	4.75	4.00
2006	5 years or less	5.75%	5.50%	4.50%
	More than 5 years, up to 10	5.50	5.50	4.50
	More than 10 years, up to 20	5.25	5.25	4.50
	More than 20 years	4.75	4.75	4.25
2007	5 years or less	5.75%	5.50%	4.75%
	More than 5 years, up to 10	5.75	5.50	4.75
	More than 10 years, up to 20	5.50	5.25	4.50
	More than 20 years	4.75	4.75	4.25

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G. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
2008	5 years or less	6.00%	5.75%	4.75%
	More than 5 years, up to 10	6.00	5.75	4.75
	More than 10 years, up to 20	5.50	5.50	4.50
	More than 20 years	5.00	5.00	4.25
2009	5 years or less	6.50%	6.25%	5.00%
	More than 5 years, up to 10	6.50	6.25	5.00
	More than 10 years, up to 20	6.00	5.75	5.00
	More than 20 years	5.25	5.25	4.50
2010	5 years or less	5.50%	5.25%	4.50%
	More than 5 years, up to 10	5.50	5.25	4.50
	More than 10 years, up to 20	5.25	5.00	4.25
	More than 20 years	4.75	4.75	4.00
2011	5 years or less	5.25%	5.00%	4.25%
	More than 5 years, up to 10	5.25	5.00	4.25
	More than 10 years, up to 20	5.00	4.75	4.25
	More than 20 years	4.50	4.50	4.00
2012	5 years or less	4.50%	4.25%	3.75%
	More than 5 years, up to 10	4.50	4.25	3.75
	More than 10 years, up to 20	4.25	4.25	3.75
	More than 20 years	4.00	4.00	3.50
2013	5 years or less	4.00%	4.00%	3.75%
	More than 5 years, up to 10	4.00	4.00	3.75
	More than 10 years, up to 20	4.00	3.75	3.50
	More than 20 years	3.75	3.75	3.50
2014	5 years or less	4.75%	4.50%	4.00%
	More than 5 years, up to 10	4.50	4.50	4.0
	More than 10 years, up to 20	4.50	4.25	3.75
	More than 20 years	4.00	4.00	3.75
2015	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, up to 10	4.00	4.00	3.75
	More than 10 years, up to 20	4.00	4.00	3.50
	More than 20 years	3.75	3.75	3.50
2016	5 years or less	4.25%	4.25%	3.75%
	More than 5 years, up to 10	4.25	4.25	3.75
	More than 10 years, up to 20	4.00	4.00	3.75
	More than 20 years	3.75	3.75	3.50

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G. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and with interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
2017	5 years or less	4.00%	4.00%	3.50%
	More than 5 years, less than 10	4.00	4.00	3.50
	More than 10 years, less than 20	3.75	3.75	3.50
	More than 20 years	3.75	3.75	3.50
2018	5 years or less	4.00%	4.00%	3.50%
	More than 5 years, less than 10	4.00	4.00	3.50
	More than 10 years, less than 20	3.75	3.75	3.50
	More than 20 years	3.75	3.75	3.50
2019	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, less than 10	4.25	4.00	3.75
	More than 10 years, less than 20	4.00	4.00	3.75
	More than 20 years	3.75	3.75	3.50
2020	5 years or less	3.25%	3.25%	3.25%
	More than 5 years, less than 10	3.25	3.25	3.25
	More than 10 years, less than 20	3.25	3.25	3.25
	More than 20 years	3.25	3.25	3.25
2021	5 years or less	3.00%	3.00%	3.00%
	More than 5 years, less than 10	3.00	3.00	3.00
	More than 10 years, less than 20	3.00	3.00	3.00
	More than 20 years	3.00	3.00	3.00
2022	5 years or less	3.50%	3.50%	3.25%
	More than 5 years, less than 10	3.50	3.50	3.25
	More than 10 years, less than 20	3.50	3.50	3.25
	More than 20 years	3.25	3.25	3.25
2023	5 years or less	5.00%	4.75%	4.25%
	More than 5 years, less than 10	5.00	4.75	4.25
	More than 10 years, less than 20	4.75	4.50	4.00
	More than 20 years	4.25	4.25	3.75

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H. Other Annuities and Guaranteed Interest Contracts, with cash settlement options and without interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

Change in Fund During Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A	B	C
1982	5 years or less	15.75%	14.50%	10.50%
	More than 5 years, up to 10	15.00	14.50	10.50
	More than 10 years, up to 20	13.75	13.25	10.00
	More than 20 years	11.25	11.25	8.75
1983	5 years or less	13.50%	12.25%	9.25%
	More than 5 years, up to 10	12.75	12.25	9.25
	More than 10 years, up to 20	11.75	11.25	8.75
	More than 20 years	9.75	9.75	7.75
1984	5 years or less	13.25%	12.25%	9.25%
	More than 5 years, up to 10	12.75	12.25	9.25
	More than 10 years, up to 20	11.75	11.25	8.50
	More than 20 years	9.75	9.75	7.50
1985	5 years or less	13.00%	12.00%	9.00%
	More than 5 years, up to 10	12.50	12.00	9.00
	More than 10 years, up to 20	11.50	11.00	8.50
	More than 20 years	9.50	9.50	7.50
1986	5 years or less	10.75%	10.00%	7.75%
	More than 5 years, up to 10	10.25	10.00	7.75
	More than 10 years, up to 20	9.50	9.25	7.25
	More than 20 years	8.00	8.00	6.50
1987	5 years or less	9.50%	8.75%	6.75%
	More than 5 years, up to 10	9.00	8.75	6.75
	More than 10 years, up to 20	8.50	8.00	6.50
	More than 20 years	7.25	7.25	6.00
1988	5 years or less	10.25%	9.50%	7.50%
	More than 5 years, up to 10	10.00	9.50	7.50
	More than 10 years, up to 20	9.25	8.75	7.00
	More than 20 years	7.75	7.75	6.25
1989	5 years or less	10.00%	9.50%	7.25%
	More than 5 years, up to 10	9.75	9.50	7.25
	More than 10 years, up to 20	9.00	8.75	7.00
	More than 20 years	7.50	7.50	6.25

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H. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and without interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
1990	5 years or less	9.50%	8.75%	7.00%
	More than 5 years, up to 10	9.25	8.75	7.00
	More than 10 years, up to 20	8.50	8.25	6.50
	More than 20 years	7.25	7.25	6.00
1991	5 years or less	9.75%	9.00%	7.00%
	More than 5 years, up to 10	9.25	9.00	7.00
	More than 10 years, up to 20	8.75	8.25	6.75
	More than 20 years	7.25	7.25	6.00
1992	5 years or less	9.00%	8.25%	6.50%
	More than 5 years, up to 10	8.50	8.25	6.50
	More than 10 years, up to 20	8.00	7.75	6.25
	More than 20 years	6.75	6.75	5.75
1993	5 years or less	8.25%	7.50%	6.00%
	More than 5 years, up to 10	7.75	7.50	6.00
	More than 10 years, up to 20	7.25	7.00	5.75
	More than 20 years	6.25	6.25	5.25
1994	5 years or less	7.50%	7.00%	5.75%
	More than 5 years, up to 10	7.25	7.00	5.75
	More than 10 years, up to 20	6.75	6.50	5.50
	More than 20 years	6.00	6.00	5.00
1995	5 years or less	8.50%	8.00%	6.25%
	More than 5 years, up to 10	8.25	8.00	6.25
	More than 10 years, up to 20	7.50	7.25	6.00
	More than 20 years	6.50	6.50	5.50
1996	5 years or less	7.50%	7.00%	5.75%
	More than 5 years, up to 10	7.25	7.00	5.75
	More than 10 years, up to 20	6.75	6.75	5.50
	More than 20 years	6.00	6.00	5.00
1997	5 years or less	7.75%	7.25%	5.75%
	More than 5 years, up to 10	7.50	7.25	5.75
	More than 10 years, up to 20	7.00	6.75	5.50
	More than 20 years	6.00	6.00	5.25
1998	5 years or less	7.00%	6.75%	5.50%
	More than 5 years, up to 10	7.00	6.75	5.50
	More than 10 years, up to 20	6.50	6.25	5.25
	More than 20 years	5.75	5.75	4.75

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H. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and without interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

Change in Fund During Year	Guarantee Duration	Maximum Reserve Valuation Interest Rate Plan Type A	B	C
1999	5 years or less	7.00%	6.50%	5.50%
	More than 5 years, up to 10	6.75	6.50	5.50
	More than 10 years, up to 20	6.25	6.25	5.25
	More than 20 years	5.50	5.50	4.75
2000	5 years or less	8.00%	7.50%	6.00%
	More than 5 years, up to 10	7.75	7.50	6.00
	More than 10 years, up to 20	7.25	7.00	5.75
	More than 20 years	6.25	6.25	5.25
2001	5 years or less	7.75%	7.25%	5.75%
	More than 5 years, up to 10	7.50	7.25	5.75
	More than 10 years, up to 20	7.00	6.75	5.50
	More than 20 years	6.00	6.00	5.00
2002	5 years or less	7.50%	7.00%	5.75%
	More than 5 years, up to 10	7.25	7.00	5.75
	More than 10 years, up to 20	6.75	6.50	5.50
	More than 20 years	6.00	6.00	5.00
2003	5 years or less	6.75%	6.25%	5.25%
	More than 5 years, up to 10	6.50	6.25	5.25
	More than 10 years, up to 20	6.25	6.00	5.00
	More than 20 years	5.50	5.50	4.75
2004	5 years or less	6.25%	6.00%	5.00%
	More than 5 years, up to 10	6.00	6.00	5.00
	More than 10 years, up to 20	5.75	5.50	4.75
	More than 20 years	5.00	5.00	4.50
2005	5 years or less	5.75%	5.50%	4.75%
	More than 5 years, up to 10	5.75	5.50	4.75
	More than 10 years, up to 20	5.25	5.25	4.50
	More than 20 years	4.75	4.75	4.25
2006	5 years or less	5.75%	5.50%	4.75%
	More than 5 years, up to 10	5.75	5.50	4.75
	More than 10 years, up to 20	5.50	5.25	4.50
	More than 20 years	4.75	4.75	4.25
2007	5 years or less	6.00%	5.75%	4.75%
	More than 5 years, up to 10	5.75	5.75	4.75
	More than 10 years, up to 20	5.50	5.50	4.75
	More than 20 years	5.00	5.00	4.25

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H. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and without interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
2008	5 years or less	6.25%	6.00%	5.00%
	More than 5 years, up to 10	6.00	6.00	5.00
	More than 10 years, up to 20	5.75	5.50	4.75
	More than 20 years	5.00	5.00	4.50
2009	5 years or less	6.75%	6.50%	5.25%
	More than 5 years, up to 10	6.50	6.50	5.25
	More than 10 years, up to 20	6.25	6.00	5.00
	More than 20 years	5.50	5.50	4.75
2010	5 years or less	5.75%	5.50%	4.75%
	More than 5 years, up to 10	5.50	5.50	4.75
	More than 10 years, up to 20	5.25	5.25	4.50
	More than 20 years	4.75	4.75	4.25
2011	5 years or less	5.25%	5.25%	4.50%
	More than 5 years, up to 10	5.25	5.25	4.50
	More than 10 years, up to 20	5.00	5.00	4.25
	More than 20 years	4.50	4.50	4.00
2012	5 years or less	4.50%	4.50%	4.00%
	More than 5 years, up to 10	4.50	4.50	4.00
	More than 10 years, up to 20	4.25	4.25	3.75
	More than 20 years	4.00	4.00	3.75
2013	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, up to 10	4.00	4.00	3.75
	More than 10 years, up to 20	4.00	4.00	3.75
	More than 20 years	3.75	3.75	3.50
2014	5 years or less	4.75%	4.50%	4.00%
	More than 5 years, up to 10	4.75	7.50	4.00
	More than 10 years, up to 20	4.50	4.50	4.00
	More than 20 years	4.00	4.00	3.75
2015	5 years or less	4.25%	4.00%	3.75%
	More than 5 years, up to 10	4.25	4.00	3.75
	More than 10 years, up to 20	4.00	4.00	3.75
	More than 20 years	3.75	3.75	3.50
2016	5 years or less	4.50%	4.25%	3.75%
	More than 5 years, up to 10	4.25	4.25	3.75
	More than 10 years, up to 20	4.25	4.00	3.75
	More than 20 years	4.00	4.00	3.75

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H. (cont.) Other Annuities and Guaranteed Interest Contracts, with cash settlement options and without interest rate guarantees on future considerations, valued on the "Change-in-Fund" basis.

		Maximum Reserve Valuation Interest Rate		
		Plan Type		
Change in Fund During Year	Guarantee Duration	A	B	C
2017	5 years or less	4.00%	4.00%	3.75%
	More than 5 years, less than 10	4.00	4.00	3.75
	More than 10 years, less than 20	4.00	3.75	3.50
	More than 20 years	3.75	3.75	3.50
2018	5 years or less	4.00%	4.00%	3.75%
	More than 5 years, less than 10	4.00	4.00	3.75
	More than 10 years, less than 20	4.00	3.75	3.50
	More than 20 years	3.75	3.75	3.50
2019	5 years or less	4.25%	4.25%	3.75%
	More than 5 years, less than 10	4.25	4.25	3.75
	More than 10 years, less than 20	4.00	4.00	3.75
	More than 20 years	3.75	3.75	3.50
2020	5 years or less	3.25%	3.25%	3.25%
	More than 5 years, less than 10	3.25	3.25	3.25
	More than 10 years, less than 20	3.25	3.25	3.25
	More than 20 years	3.25	3.25	3.25
2021	5 years or less	3.00%	3.00%	3.00%
	More than 5 years, less than 10	3.00	3.00	3.00
	More than 10 years, less than 20	3.00	3.00	3.00
	More than 20 years	3.00	3.00	3.00
2022	5 years or less	3.50%	3.50%	3.25%
	More than 5 years, less than 10	3.50	3.50	3.25
	More than 10 years, less than 20	3.50	3.50	3.25
	More than 20 years	3.25	3.25	3.25
2023	5 years or less	5.25%	5.00%	4.25%
	More than 5 years, less than 10	5.00	5.00	4.25
	More than 10 years, less than 20	4.75	4.75	4.25
	More than 20 years	4.50	4.50	4.00

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APPENDIX

The maximum reserve valuation interest rates are based on reference interest rates, which are averages of corporate bond earnings published by Moody's Investors Service, Inc., and weighting factors prescribed by Section 4217, which defines running averages of the published monthly yield rates for 12-month and 36-month periods.

The following table shows the 12-month and 36-month yield averages for recent years:

TABLE 1

For Period Ending June 30 of Year	12-Month Running Average (1)	36-Month Running Average (2)	Lesser of Two Averages (3)
1981	13.71%	11.57%	11.57%
1982	15.70%	13.64%	13.64%
1983	13.39%	14.26%	13.39%
1984	13.22%	14.10%	13.22%
1985	13.01%	13.21%	13.01%
1986	10.75%	12.33%	10.75%
1987	9.40%	11.05%	9.40%
1988	10.32%	10.15%	10.15%
1989	10.09%	9.93%	9.93%
1990	9.52%	9.97%	9.52%
1991	9.63%	9.74%	9.63%
1992	8.88%	9.34%	8.88%
1993	8.13%	8.88%	8.13%
1994	7.52%	8.18%	7.52%
1995	8.42%	8.03%	8.03%
1996	7.55%	7.83%	7.55%
1997	7.74%	7.90%	7.74%
1998	7.11%	7.47%	7.11%
1999	6.96%	7.27%	6.96%
2000	7.93%	7.33%	7.33%
2001	7.72%	7.54%	7.54%
2002	7.44%	7.70%	7.44%
2003	6.71%	7.29%	6.71%
2004	6.26%	6.80%	6.26%

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TABLE 1
(cont.)

For Period Ending June 30 of Year	12-Month Running Average (1)	36-Month Running Average (2)	Lesser of Two Averages (3)
2005	5.78%	6.25%	5.78%
2006	5.87%	5.97%	5.87%
2007	6.00%	5.88%	5.88%
2008	6.21%	6.02%	6.02%
2009	6.79%	6.33%	6.33%
2010	5.75%	6.25%	5.75%
2011	5.37%	5.97%	5.37%
2012	4.55%	5.22%	4.55%
2013	4.15%	4.69%	4.15%
2014	4.72%	4.48%	4.48%
2015	4.19%	4.36%	4.19%
2016	4.39%	4.44%	4.19%
2017	4.05%	4.21%	4.05%
2018	4.05%	4.17%	4.05%
2019	4.31%	4.14%	4.14%
2020	3.35%	3.90%	3.35%
2021	2.96%	3.54%	2.96%
2022	3.52%	3.28%	3.28%
2023	5.16%	3.88%	3.88%

The maximum nonforfeiture interest rate for Life Insurance, under Section 4221(k), for a particular issue year, is equal to 125% of the maximum reserve valuation interest rate for the same issue year, rounded to the nearer 1/4%.

Should the computed maximum reserve valuation interest rate for Life Insurance (other than Single Premium Life Insurance covered in Category B on pages 2-4) for a particular issue year be different from the actual maximum reserve valuation interest rate for the next previous issue year by less than 1/2%, then the maximum reserve valuation interest rate for such particular issue year will be the same as that for such next previous issue year.

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Appendix C-2

Interpretations of the Emerging Actuarial Issues (E) Working Group

Introduction

The former Emerging Actuarial Issues (E) Working Group (EAIWG) and the current Valuation Analysis (E) Working Group (VAWG) respond to questions of application, interpretation and clarification with respect to *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38). Following an abbreviated public comment and review period of no less than seven days, the Working Group will adopt by consensus formal interpretations on issues presented before it. These interpretations will then be reported to the Financial Condition (E) Committee, which, after adopting, will direct the Financial Analysis (E) Working Group to follow the interpretations in performing its reviews of the reserving methodologies under AG 38. These interpretations will not become effective until formally adopted by the Financial Condition (E) Committee. In no event shall a consensus opinion of the former EAIWG or current VAWG supersede or otherwise conflict with AG 38.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 01

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(b)

Issue / Question

1. The Guideline does not seem to preclude a company from using the Alternative Reserve Methodology for yearend 2012, thus avoiding the Primary Reserve Methodology calculations, even if in prior valuations their total reserve held was not at least as great as the total reserve determined in accordance with the November 1, 2011 Life Actuarial (A) Task Force (LATF) statement. In other words, at yearend 2012 a company can switch to any alternative reserve methodology as long as the total reserve held is at least as great as the total reserve determined in accordance with the November 1, 2011, LATF statement using the required lapses and mortality. Is that a correct interpretation?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Yes. The requirements as written provide for use of either 8D(a) or 8D(b) for the 12/31/12 valuation.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 02

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(b)

Issue / Question

1. If a company uses the Alternative Reserve Methodology for yearend 2012, can they switch to the Primary Reserve Methodology for future valuations? What, if anything, should be reported in Exhibit 5A-Changes in Basis of Valuation for yearend 2012 or in future years as a result of these AG 38 revisions and any switch to the Primary Reserve Methodology or to the Alternative Reserve Methodology?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. A company, pursuant to the requirements of AG 38, 8D, may switch between the Primary Reserve Methodology and the Alternative Reserve Methodology.

3. For 12/31/12 or subsequent reserve valuations any change to or from the Primary or Alternative reserve methodologies should be reported in Exhibit 5A.

4. The company should check with their domestic state whether approval is required for any subsequent change to or from the Primary or Alternative reserve methodologies for reserves after 12/31/12.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 03

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(b)

Issue / Question

1. The Alternative Reserve Methodology calls for deficiency reserve mortality to be based on the VM-20 deterministic reserve mortality. Since XXX calls for segments to be based on deficiency reserve mortality this could affect segment lengths. However, at least the spirit of AG46, which came out when the 2001 CSO Preferred Risk tables came out, seems to allow for segments to continue to be based on the mortality table in use when the policy was issued. Does AG46 apply here and thus the original mortality basis for the segment lengths can continue to be used?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. The original mortality basis for determining the segment length can continue to be used. 8D is not intended to be more restrictive in determination of segments.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 04

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D

Issue / Question

1. The Guideline states "The requirements of this Section 8D apply to a company on December 31, 2012, and on any subsequent valuation date if (1) on the applicable date, the in force face amount (direct plus assumed) of universal life insurance to which this Section 8D would otherwise apply exceeds 2% of the company's face amount of individual permanent life insurance in force…" Does the referenced individual permanent life insurance exclude term insurance?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Yes. Term is excluded.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 05

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D

Issue / Question

1. Subsection 8Da states that the Primary Reserve is determined by adding any excess of (2) over (1), where (1) is the reserve according to the methodology and assumptions used to calculate the reserves reported as of December 31, 2011. In the following three scenarios, what is the basis for the determination of (1)? Assume that scenarios 1 and 2 involve universal life with secondary guarantees (ULSG) policies issued between July 1, 2005 and December 31, 2006, with a higher set of cost of insurance (COI) charges being triggered if the shadow account value ever becomes 0 after issue:

a. Issue 1) Reserves have always been calculated using the wrong methodology for determining the ratio in the fourth step of Section 8B. In applying Section 8D, would the reserves for 8Da1 be based on the correct methodology or on the methodology actually used by the company for year-end 2011?

b. Issue 2) A policy has a negative account value but has not lapsed due to the secondary guarantee. The shadow account value eventually drops to 0 and then becomes negative, and the policyholder pays a premium during the grace period intended on keeping the policy in force. The company invokes the higher secondary guarantee charges to calculate the shadow account value, but the policyholder argues that the lower shadow account COI charges apply due to the premium being paid during the state required grace period; i.e. that during the grace period the policyholder has the opportunity to pay a premium based on the lower COI charges rather than based on the much higher set of COI charges. This is litigated, and a ruling is made that the higher COI rates cannot be charged unless the shadow account value has not been positive for a period of time greater than the grace period. Based on this ruling, the assumption in the AG38 calculation that the higher set of COI charges would be triggered at the end of the first policy year would not be valid. Would the reserves for 8Da1 continue to be based on the assumption that the higher COI charges would be triggered after the first policy year, or would they be modified to reflect the lower COI charges?

c. Issue 3) Policies with multiple sets of COI charges have only been issued in 2012. What is the basis for the value of (1)?

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2. Issue 1) The reserves determined by the company under 8D(a)(1) are intended to be consistent with the methodology used by the company for the 12/31/2011 valuation. If a calculation error has been made in applying the 2011 methodology, this error should not be repeated in applying this methodology for the 2012 year-end valuation.

3. Issue 2) Where a valid court decision has interpreted the provisions of a policy, those interpretations should be reflected in future reserve calculations. In effect, the court ruled that the company made a mistake in applying certain policy provisions. Therefore, the 2012 reserve calculations should incorporate the correct view of the affected policies' provisions as determined by the court. As in 1) above, any error in the 2011 reserve calculations due to this company mistake should not be perpetuated in the 2012 reserve calculations.

4. Issue 3) In this case, the value of (1) would be based on the company's methodology for reserving these policies for 2012 quarterly reporting.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 06

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(b)

Issue / Question

1. Is the report documenting the special 2012 sensitivity test described at the end of Section 8D required to be a stand-alone document or can it be included in the required Section 8D Actuarial Memorandum?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Considering the special nature of the 2012 sensitivity test, the documentation should be contained either in a stand-alone document or included as a separate appendix in the Actuarial Memorandum.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 07

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(b)

Issue / Question

1. If all of a company's universal life with secondary guarantees (ULSG) policies subject to Section 8D are the same identical policies that are subject to Section 8C, are they still required to perform the separate Section 8C stand-alone asset adequacy analysis or does the Section 8D Primary Reserve Methodology calculation suffice?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Such policies are still required to perform the separate Section 8C stand-alone asset adequacy analysis. Section 8D, second paragraph, clarifies that Section 8D is "in addition to any testing that may be required under Section 8C."

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 08

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(a)

Issue / Question

1. For companies using the Primary Reserve Methodology, is it expected that the full deterministic reserve calculations will be performed every quarter or just annually?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. This methodology would be used at least annually, with appropriate approximations used as permitted pursuant to quarterly statutory reporting requirements.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 09

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(a)

Issue / Question

1. If the deterministic reserve "wins" for the Primary Reserve Methodology calculation, what impact should that have on tax reserves?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. This question involves determination of values under the requirements of the Internal Revenue Code. The NAIC has no comment on how those values should be determined.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 10

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(a)(2)

Issue / Question

1. In relation to the Valuation Manual, Item 2. under the Primary Reserve Methodology section references "…or in any version subsequently adopted by the NAIC…." Please clarify exactly what constitutes "adopted by the NAIC." Does it have to be adopted by Executive/Plenary or just the A Committee or just Life Actuarial (A) Task Force (LATF)? "version" includes amendments that have been adopted, correct?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Adopted by the NAIC means the Valuation Manual and any amendments adopted through Executive & Plenary as of the 7/1 preceding the year-end valuation date.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 11

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation

Issue / Question

1. My question is on section 8E, regarding when a product would fall under method 1 or method 2. If you have a shadow account product that has either a single set of charges, or multiple sets of charges, and the product meets the crediting rate limitations defined in method 1, is there anything that could cause the product to be deemed to be subject to method 2? To put it another way, when I read section 8E, it seems that any shadow account product meeting the interest crediting limits would fall under method 1. This is because all shadow accounts have either a single set of charges or multiple sets of charges, so all shadow account products that meet the interest crediting limitation would fall under policy design 1 or policy design 3. Is this a correct interpretation, or if not, why?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. This interpretation is not completely correct. In drafting the revisions to AG 38, regulators were aware of the possibility that all existing and future product designs might not fit the three generic product designs noted in AG 38, independent of the crediting rate limitation. Method II was intended to provide a default reserve methodology for these other product designs, together with the more generic product designs containing interest crediting guarantees higher than the company-selected interest index plus 3 percent. The considerations in satisfying the actuarial opinion requirements contained in Section 8E should enable the opining actuary to determine the appropriate reserving methodology for a particular universal life with secondary guarantees (ULSG) product design.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 12

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D(b)

Issue / Question

1. Section 8D(b), Alternate Methodology, requires the company to determine its deficiency reserve under Model 830 using mortality and lapse assumptions according to the same requirements for determining the deterministic reserve in the Valuation Manual. Does this require the company to determine its Triple-X segments (under the segmentation method) using the qx and lapse rates of the VM, or simply use these qx and lapse rates in calculating the deficiency reserve once the segments are determined using the company's current approach for determining such segments?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. The original mortality basis for determining the segment length can continue to be used. 8D is not intended to be more restrictive in determination of segments.

Note: This response is similar to that for question Actuarial INT 03.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 13

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation

Issue / Question

1. Given all of the focus that the Guideline places on what premiums to use for these universal life with secondary guarantees (ULSG) reserve calculations, we are having unexpected difficulty finding published guidance on what premiums to assume in the deterministic reserve calculations for the Primary Reserve Methodology. Does such guidance exist and if so, where can we find it?

2. This question specifically asks for published guidance, but if none exists, perhaps the Working Group could provide such guidance or at least common practices/approaches they are aware of. Guidance is needed to create consistency amongst how companies are approaching this step of the calculation.

Interpretation of Emerging Actuarial Issues (E) Working Group

3. For 8D(a)(2) reserve calculations, the company should use the expected premium to be paid by the policyholder, determined either policy-by-policy or by appropriate policy groupings. The Valuation Manual adopted by the A Committee on 8/17/12 provides requirements regarding premiums for the deterministic reserve calculation. Such requirements include those in Section 4(A), Section 7(B), and Sections 9(A) and 9(D).

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 14

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E

Issue / Question

1. In the case of a Method I type product that is currently being sold and will continue to be sold unmodified after 12/31/12, the company would have to do a standalone asset adequacy analysis under Section 8C for issues 1/1/07 through 12/31/12 but they would not have to do a standalone asset adequacy analysis for issues after 12/31/12 even though it is the same product. Correct?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Yes. It is a correct interpretation that the stand-alone asset adequacy analysis in 8C does not include policies issued after 12/31/12.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 15

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E(II)

Issue / Question

1. The minimum schedule of premiums required to be identified/tested for in Method II is something that is expected to be needed to be done separately for every age/sex cell, correct?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Yes. The schedule of minimum gross premiums should be based on all appropriate attributes unique to the policy being valued.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 16

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E

Issue / Question

1. If all of a company's currently approved universal life with secondary guarantees (ULSG) policy forms fall under the same Method I policy design, pass the Index Test, and meet the minimum premium requirements, can a single Actuarial Opinion and a single Company Representation be submitted that lists each policy form or does a separate Actuarial Opinion and a separate Company Representation need to be submitted for each form?

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2. This is up to the state of domicile. Some groupings may make sense but any special qualification or language needed should result in a separate opinion and representation.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 17

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E(II)

Issue / Question

1. Is the greatest deficiency reserve test to be performed on a seriatim or product level basis? What if we see mixed results (For example, 70% pattern 1 and 30% pattern 2)

Interpretation of Emerging Actuarial Issues (E) Working Group

2. The test should be performed on a seriatim basis, except to the extent it may be practical to group policies with identical attributes. It is possible that several combination premium patterns will be identified as having broad applicability. Regardless, each policy should assume a premium pattern that produces the greatest deficiency reserve as of the issue date consistent with good faith testing and review.

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Actuarial INT 18

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E(II)

Issue / Question

1. For the combination premium patterns, what does it mean "...to have access to better charges and credits...."? Can this be ignored it if the product only has one set of charges?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Better charges and credits can be understood as lower charges and/or higher credits that may be triggered based on the magnitude of the premium paid, the shadow account or other measures generally dependent on policyholder behavior. For example, a higher interest rate might apply to amounts above or below some defined premium dollar limit in particular policy years or based simply on the level of the shadow account. Higher or lower premium payments could lead directly to the most favorable interest rate (or weighted average interest rate) accessible within product design constraints. Better charges and credits would generally lead to lower minimum gross premiums and potentially greater deficiency reserves. For purposes of this question this requirement cannot be ignored, particularly if there are multiple sets of credits in addition to the assumed single set of charges.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 19

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E(II)

Issue / Question

1. When testing combination premium patterns, do premium patterns that break segments need to be considered?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. It is not necessary to reverse engineer premium patterns solely to create unfavorable segment breaks. However, segment breaks that result from premium patterns consistent with the applicability of favorable charges and credits must be considered.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 20

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 20, 2012

Date Adopted by Financial Condition (E) Committee

December 1, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E(II)

Issue / Question

1. Do patterns with dump-in premiums need to be tested? If so, how should the dump-in premium be reflected in the determination of the uniform percentage (i.e., do you include the dump-in premium in determining the k percentage).

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Premium patterns that involve dump-in premiums must be considered, and testing may be appropriate. In the absence of more definitive guidance, the uniform percentage should be determined in accordance with Actuarial Guideline 21.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 21

Date Adopted by Emerging Actuarial Issues (E) Working Group

January 30, 2013

Date Adopted by Financial Condition (E) Committee

February 20, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D (a)(2a)

Issue / Question

1. Should the VM-20 deterministic reserve starting asset requirement related to the 2% collar be applied before or after the Primary Reserve Methodology caps on starting and reinvestment assets are applied?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. Subsection a.2.a) (I) of Section 8D requires the determination of one of two portfolios of existing assets to support the initial reserve estimate for the block. Once this initial asset portfolio is determined, the deterministic gross premium reserve is determined using as the discount rates the net investment returns generated by the future projected cash flows calculated using the selected initial portfolio and future net reinvestment rates established according to subsection a.2.a) (II) of Section 8D.

3. If the resulting reserve falls within the +/- 2% collar (referenced in VM-20) relative to the initial reserve estimate (and corresponding level of initial assets), the calculated reserve is the final reserve. If the calculated reserve breaches the +/- 2% collar, the actuary must either provide a detailed rationale as to why the calculated reserve is appropriate or redo the reserve calculation assuming revised initial reserve and asset levels.

4. In performing the additional reserve calculation(s), use the same asset portfolio (adjusted upward or downward as below based on the results of the deterministic reserve calculation), either that of subsection a.2.a) (I) (i) or a.2.a) (I) (ii), as chosen for the initial reserve calculation.

5. If the initial or subsequently determined reserve is greater than the prior reserve estimate and the asset portfolio used in the deterministic reserve calculation is:

   a. as described in subsection a.2.a)(I)(i), then the prior asset portfolio shall be adjusted upward using assets as described in subsection a.2.a)(I)(i) to the extent such assets remain available in the company's portfolio after which such assets shall be adjusted upward as needed using assets as described in subsection a.2.a)(I)(ii). The recommended method for adjusting the prior asset portfolio upward is to do so in a pro rata fashion. Any other method proposed for adjusting the prior asset portfolio upward must be clearly documented in the Actuarial Memorandum and shall not involve changing the asset composition of the prior asset portfolio but shall constitute only additions to that portfolio.

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b. as described in subsection a.2.a)(I)(ii), then the prior asset portfolio shall be adjusted upward as needed in a pro rata fashion using assets as described in subsection a.2.a)(I)(ii).

6. Regardless of which portfolio is chosen for the initial deterministic reserve calculation, if the initial or subsequently determined, reserve is less than the prior reserve estimate, then the prior asset portfolio shall be adjusted downward as needed in a pro rata fashion.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 22

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E/8D

Issue / Question

1. Consider the following: A universal life policy with a secondary guarantee requires that a shadow account be maintained at a positive level for the secondary guarantee to remain in effect. Once the shadow account value goes down to zero, the secondary guarantee terminates and cannot be reactivated. There is only one set of charges and credits that apply to the shadow account. In determining reserves for this policy under section 8E, would the assumption be made that the secondary guarantee terminates at the end of the first policy year since, if only the minimum premium is paid, the shadow account value would be zero at the end of the first policy year?

2. If the policy was written before 2012, would it be subject to section 8D?

Interpretation of Emerging Actuarial Issues (E) Working Group

3. For issues in or after January 1, 2013, 8E would be applicable. But the policy, as described, would not fit into Method I because the minimum premium derived according to Method I would not satisfy the secondary guarantee requirements. Calculation of the reserve using Method I requires that the minimum premium keep the secondary guarantee in effect. Therefore, it must be reserved according to Method II.

4. For issues between July 1, 2005 and December 31, 2012 (inclusive), any regulatory response regarding applicability of Section 8D would require analysis of the policy form and dialog with the valuation actuary.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 23

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E

Issue / Question

1. Under 8E, Method I, Policy Design #1 applies for policies containing a secondary guarantee that uses a shadow account with a single set of charges and credits. For those policies, the minimum gross premium for any policy year is the premium that, when paid into a policy with a zero shadow account value at the beginning of the policy year, produces a zero shadow account value at the end of the policy year, using the guaranteed shadow account charges and credits specified under the secondary guarantee. Presumably, this will result in a yearly renewable term (YRT)-like pattern for the minimum premium.

2. The actuarial opinion required by 8E includes the statement "the minimum gross premiums determined under Policy Design # ___ are not inconsistent with the minimum premiums, charges and credits that are expected to apply under the policy." What is meant by "expected to apply"?

3. Since it is not likely that the policyholder will fund the policy using the YRT-like pattern that is the minimum premium, it does not seem as if "expected to apply" means "expected to be paid." It appears that "expected to apply" should be interpreted to mean that the YRT-type pattern will either fund the secondary guarantee or it is less than the minimum amount necessary to fund the guarantee.

Interpretation of Emerging Actuarial Issues (E) Working Group

4. The phrase "expected to apply" is intended to mean that the minimum premiums determined ($0-to-$0) are based on charges/credits generally consistent with those expected to apply to premium scales likely to be received from policyholders. For example, high premium loads at later durations would not be expected to apply for products with charges and credits that encourage a limited-pay or single-pay premium pattern. Other design features that should give the opining actuary pause, and could draw regulatory scrutiny, include negative charges and credits or unusual patterns of charges and credits. In addition, the actuary should not favorably opine on a product for Method I reserves with variables resulting in minimum gross premiums that would be inconsistent with the premiums a reasonable person would pay to limit advance funding. If the actuary is unable to opine favorably, the reserves should be calculated under Method II.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 24

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 19, 2012

Date Adopted by Financial Condition (E) Committee

December 20, 2012

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation

Issue / Question

1. A shadow account has a product design feature where the premium load is expressed as a fixed percentage of premium up to the target premium, and the target premium is reasonably consistent with level premium funding of the lifetime guarantee. In effect, there is a fixed dollar cap on the annual premium charge. The literal form of the charge is simply a specified percentage of premiums up the target premium and 0% thereafter. This will always mathematically produce the same result as the capped charge described above. Please clarify that a fixed dollar cap for the premium load, regardless of how the cap is expressed, does not make such a product incompatible with Policy Design # 1.

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2. A flat percentage of premium charge, subject to an annual maximum, would be compatible with Policy Design (PD) #1 provided the actuary is able to issue an unqualified actuarial opinion. The specified percentage rate subject to an annual maximum may be construed as a single rate even though an alternative expression of this charge could be viewed as involving a second rate equal to zero. However, it should be noted that the actuary might be unable to opine favorably in the case of designs with credit/charge structures that encourage limited-pay premium schedules.

3. The above interpretation does not extend to designs using a flat percentage load for premiums up to a break point and a different (non 0%) load for premiums above that. Such a design should be considered as PD#3, as would any design with tiered interest rate credits or other tiered credits/charges.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 25

Date Adopted by Emerging Actuarial Issues (E) Working Group

January 30, 2013

Date Adopted by Financial Condition (E) Committee

February 20, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E

Issue / Question

1. Does the exemption for UL policies with short guarantee periods (see below) still apply in Section 8E of AG38?

2. This language is from the XXX model reg (Model 830)

> 3.A.(2) This regulation shall not apply to any universal life policy that meets all the following requirements:
>
> (a) Secondary guarantee period, if any, is five (5) years or less;
>
> (b) Specified premium for the secondary guarantee period is not less than the net level reserve premium for the secondary guarantee period based on the CSO valuation tables as defined in Section 4F and the applicable valuation interest rate; and
>
> (c) The initial surrender charge is not less than 100 percent of the first year annualized specified premium for the secondary guarantee period.

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3. Yes.

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Actuarial INT 26

Date Adopted by Emerging Actuarial Issues (E) Working Group

February 12, 2013

Date Adopted by Financial Condition (E) Committee

April 8, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D

Issue / Question

1. Section 8D(a) references the deterministic reserve calculation in the VM20 valuation manual in the definition of the Primary Reserve Methodology. As part of the asset assumptions used in the deterministic reserve calculation, page 82 of the VM20 manual describes the derivation of the Illustrative Current Market Benchmark Spreads. We have reviewed the JP Morgan US Liquid Index data referenced, and the final published values appear to be derived from the underlying data for the index as opposed to referencing published table views. Does the Working Group agree that using an updated table would be preferred? Would the Working Group consider publishing an updated table as of 9/30 or providing additional details on how the table values (shown on page 89) were derived? The values for Table G (page 90) for the below investment grade bonds were taken directly from the source index so they are easy to replicate.

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2. For the 12/31/12 AG 38, 8D valuation it may be assumed that the 9/30/09 Tables H & I approximate both Tables F & G and Tables H & I as of 12/31/12. This assumption is based on benchmarking with current spread information from other sources as of 12/31/12. It is understood that strict technical compliance for each and every asset may not be possible due to modeling limitations. Professional judgment should be used to produce results that comply with the spirit of this standard, i.e., no lessening of conservatism. For example, if a company has access to current data sources and can reconstruct Tables F and G as of 12/31/12 then this would be an acceptable approach. In any event, appropriate explanation and justification should be provided for the methodology that was employed and the results that were obtained. The NAIC intends to provide updated tables for future year end AG 38, 8D, valuations.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 27

Date Adopted by Emerging Actuarial Issues (E) Working Group

February 12, 2013

Date Adopted by Financial Condition (E) Committee

April 8, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D

Issue / Question

1. If the modified VM-20 deterministic reserve ends up being the minimum reserve held in the AG 38 8D calculation, can a reinsurance reserve credit also be calculated under the guidance of VM-20 (in particular for YRT reinsurance)?

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2. The Section 8D reserve methodology (VM-20 deterministic) applies for calculating the company's aggregate gross reserve before reinsurance. AG 38, 8D, does not address how the credit for reinsurance is determined. The approach to determine the credit for YRT reinsurance shall be documented in the stand-alone Actuarial Memorandum required by AG 38, Section 8D(c).

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Actuarial INT 28

Date Adopted by Emerging Actuarial Issues (E) Working Group

February 12, 2013

Date Adopted by Financial Condition (E) Committee

April 8, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation

Issue / Question

1. A product has a shadow account product design feature where, in addition to the fixed charges and credits associated with the policy, there is a shadow account premium charge in the event that the policyholder underfunds the policy. This premium charge is expressed as a fixed percentage of the premium shortfall when compared to a given level premium.

2. Please clarify whether a shadow account charge expressed as a fixed percentage of the premium shortfall is regarded as "multiple sets of charges" or as a "single set of charges" and thus whether such a product is compatible with Policy Design # 1 or Policy Design # 3.

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3. This charge and treatment as Policy Design 1 does not appear consistent with the type of charge and treatment addressed by adopted INT 24 (formerly referred to as Pending Submission 6 prior to its adoption).

4. INT 24 deals with a single charge that all policyholders will incur which stops after a certain level of premiums have been paid. The charge described here is not incurred by all policyholders and provides the potential for a reserve premium being subject to the full impact of this charge whereas the premiums actually expected to be paid would not incur this charge.

5. More information is needed to fully assess the applicable Policy Design but based on the information provided Policy Design 3 appears appropriate.

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Actuarial INT 29

Date Adopted by Emerging Actuarial Issues (E) Working Group

April 4, 2013

Date Adopted by Financial Condition (E) Committee

April 8, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E I) 3 Actuarial Opinion and Company Representation section

Issue / Question

1. A company currently issues a ULSG product that is clearly a Policy Design #3. Two hypothetical examples of the charge/credit structure are shown in Tables 1 and 2 below. Under either structure, the policy form:

- Is clearly Policy Design #3
- Does not run afoul of the "Index plus 3%" of 8E

2. The purpose of the bifurcated cost of insurance charge structure in Table 1 or bifurcated premium charge structure in Table 2 is to optimize management of policyholder premium paying pattern behavior. The exact insurance charge for any given policy under the Table 1 design is either COI 1 or COI 2, where the rate is determined by comparing the actual fund value to a pre-defined fund value. If the actual fund value is in excess of the pre-defined fund value, COI 1 is used, otherwise COI 2 is used. Similarly, the exact premium charge amount for any given policy under the Table 2 design is PremPct1 for amounts paid up to a target amount plus PremPct2 for amounts paid in excess of the target amount.

3. The company's approach to establishing statutory reserves has always been to determine AG XXXVIII Step 1 minimum premiums based on the lowest charges from Table 1 (or Table 2). The actuary concludes that everything in the reserving practices of the company with respect to this policy form is in compliance with the letter and spirit of AG XXXVIII, and except for the third statement in the Actuarial Opinion (of Section E), the actuary feels s/he could sign such an attestation. The third statement declares "the minimum gross premiums determined under Policy Design #3 are not inconsistent with the minimum premiums, charges and credits that are expected to apply".

4. What is the actuary expected to do in such a situation?

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	TABLE 1					TABLE 2			
	COI_1	COI_2	Interest	Prem Load		COI	Interest	Up to Target PremPct1	In excess PremPct2
45	0.000066	0.000231	3.75%	15%	45	0.000149	4.00%	15%	5%
46	0.000108	0.000378	3.75%	15%	46	0.000243	4.00%	15%	5%
47	0.000146	0.000511	3.75%	15%	47	0.000329	4.00%	15%	5%
48	0.000180	0.000630	3.75%	15%	48	0.000405	4.00%	15%	5%
49	0.000212	0.000742	3.75%	15%	49	0.000477	4.00%	15%	5%
50	0.000242	0.000847	3.75%	15%	50	0.000545	4.00%	15%	5%
51	0.000276	0.000966	3.75%	15%	51	0.000621	4.00%	15%	5%
52	0.000316	0.001106	3.75%	15%	52	0.000711	4.00%	15%	5%
53	0.000364	0.001274	3.75%	15%	53	0.000819	4.00%	15%	5%
54	0.000422	0.001477	3.75%	15%	54	0.000950	4.00%	15%	5%
55	0.000486	0.001701	3.75%	15%	55	0.001094	4.00%	15%	5%
56	0.000556	0.001946	3.75%	15%	56	0.001251	4.00%	15%	5%
57	0.000632	0.002212	3.75%	15%	57	0.001422	4.00%	15%	5%
58	0.000712	0.002492	3.75%	15%	58	0.001602	4.00%	15%	5%
59	0.000796	0.002786	3.75%	15%	59	0.001791	4.00%	15%	5%
60	0.000882	0.003087	3.75%	15%	60	0.001985	4.00%	15%	5%
61	0.000972	0.003402	3.75%	15%	61	0.002187	4.00%	15%	5%
62	0.001070	0.003745	3.75%	15%	62	0.002408	4.00%	15%	5%
63	0.001180	0.004130	3.75%	15%	63	0.002655	4.00%	15%	5%
64	0.001310	0.004585	3.75%	15%	64	0.002948	4.00%	15%	5%
65	0.001470	0.005145	3.75%	15%	65	0.003308	4.00%	15%	5%

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5. As indicated in INT 23, the actuary who is unable to opine favorably would be required to calculate reserves in accordance with Method II.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 30

Date Adopted by Emerging Actuarial Issues (E) Working Group

June 6, 2013

Date Adopted by Financial Condition (E) Committee

July 17, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E

Issue / Question

1. Does Section 8E apply to the following.... (a) a 10 year secondary guarantee of the cumulative minimum premium variety where there is no interest credited to the premiums, and premiums are expected to be level (b) same question as above except the secondary guarantee period is 15 years.

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2. Yes. Section 8E applies to both, for policies issued on or after 1/1/2013.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 31

Date Adopted by Emerging Actuarial Issues (E) Working Group

August 23, 2013

Date Adopted by Financial Condition (E) Committee

August 26, 2013

Reference

1. Subsection 8D states in the second paragraph that: "This section does not apply if the minimum gross premiums for the policies are determined by applying the set of charges and credits that produces the lowest premiums, …"

2. Interpretation ACT INT 02 states that a company may switch between the Primary Reserve Methodology and the Alternative Reserve Methodology.

Issue / Question

3. Can a company use the Alternative Reserve Methodology found in sub-section 8D of AG38 for a policy with multiple sets of interest credits or charges if the reserves have previously been calculated using the lowest minimum gross premiums?

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4. The applicability language in the second paragraph of AG 38, Section 8D, should not be interpreted to preclude a company from using AG 38, Section 8D(b), "Alternative Reserve Methodology", pursuant to the requirements of 8D(b) and any applicable interpretations adopted by the NAIC.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 32

Date Adopted by Emerging Actuarial Issues (E) Working Group

August 23, 2013

Date Adopted by Financial Condition (E) Committee

August 26, 2013

Reference

Regulation XXX; *Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation*, Section 8D

Issue / Question

1. The company states that reserves equal to the deterministic reserve required in the valuation manual of the valuation law (model 820) are lower than produced under the above methodology, but states that it would hold reserves per the valuation manual if that produced greater reserves in aggregate for the block. If tested for each policy, the reserve required per the valuation manual would in some cases be higher than as calculated based on regulation XXX. Can the valuation manual floor be applied in aggregate rather than for each policy?

Interpretation of Emerging Actuarial Issues (E) Working Group

2. The deterministic reserve as required by Actuarial Guideline 38 8D(a) should be applied in the aggregate versus policy by policy.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 33

Date Adopted by Emerging Actuarial Issues (E) Working Group

August 23, 2013

Date Adopted by Financial Condition (E) Committee

August 26, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 7 and Steps 1, 2, and 8 of Section 8E

Issue / Question

1. Does the language "This result may be negative." occurring twice in Step 3 of Section 8E of Actuarial Guideline 38 (AG 38) apply only to the Method II reserve approach in AG 38 or to both Method I and Method II reserve approaches? Step 3 of Section 8E of AG 38 provides for the determination of the amount of actual premium payments (or shadow account) greater than or less than the minimum gross premiums (or shadow account based on minimum premiums), as defined in Section 8E.

2. The issue regarding the referenced language relates to the interpretation of Step 3 as it applies particularly to (i) cumulative premium secondary guarantee designs with a "premium catch-up provision" or (ii) shadow account secondary guarantee designs where, if the shadow account is below the level necessary to maintain the secondary guarantee, there is a "catch-up provision" where the shadow account may be reinstated prior to the end of the secondary guarantee period.

3. In addition to Section 8E of AG 38, it appears that Section 7 of AG 38 applies in this situation. For Section 8E Method I reserve calculations, the language of Section 7 appears to deal with any deficiency indicated in Step 3 of Section 8E satisfactorily since that deficiency is measured relative to the guarantees (cumulative premium or shadow account). In this case, the value of the numerator in Step 3 of Section 8E would be zero and the floor basic and deficiency reserve would be set at the minimums defined in Section 7.

4. However, for Section 8E Method II reserve calculations, for purposes of applying Section 8E, the deficiency in Step 3 is measured relative to the premium defined in Step 1 which is the schedule of minimum gross premiums that create the greatest deficiency reserve rather than the schedule of minimum gross premiums based on the policy guarantees. This is inconsistent with the requirements and intent of Section 7 and therefore would allow for the ratio in Step 4 of Section 8E to be negative.

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5. The recommended response is essentially correct. The phrase, "This result may be negative" applies only to Method II policies in Section 8E, Step 3. This phrase does not apply to the Step 3 amount for Method I policies given the requirements of AG 38, Section 7. Method I policies that would otherwise have a negative Step 3 amount were it not for Section 7 are those policies that are underfunded but provide for a catch up provision as addressed by Section 7. The Step 2 basic and deficiency reserves for such policies, used to calculate the "reserve floor" in Step 8 (c), must be adjusted as provided by Section 7 prior to calculating the "reserve floor" in Step 8 (c).

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 34

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 22, 2013

Date Adopted by Financial Condition (E) Committee

December 17, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D.a.2(a)

Issue / Question

1. Section 8D directs companies to use "…the same requirements for determining the deterministic reserve in the version of the valuation manual specified…but with two modifications…" In determining future Treasury yield rates used in calculating the sale price of any asset existing on the valuation date, this language in Section 8D of AG38 can be interpreted in one of two ways:

   a. Assuming a level series of future Treasury yield curves for all future years of the model projection period. In this case, any gains or losses arising from the sale of existing assets during the projection period would be determined using a level Treasury yield curve scenario prospectively, and a spread applicable to the asset, as determined on the valuation date.

   b. Assuming the series of future Treasury yield curves is that described under Scenario 12 from the prescribed set of interest rate scenarios used in the stochastic exclusion test in VM-20. To these Treasury rates is added a spread to determine the yield rate to be used on the sale of an existing asset during the model projection period.

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2. It is recommended that the approach outlined in paragraph 1.a. be the interpretation of the relevant language of Actuarial Guideline 38 Section 8D.a.2(a).

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 35

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 13, 2013

Date Adopted by Financial Condition (E) Committee

December 17, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D.A.2(a)(I)

Issue / Question

1. Section 8.D.A.2(a)(I) states, "net investment returns based on a portfolio of A-rated corporate bonds purchased in the year of issue of the policies based on yields available in the year of issue of those bonds" shall be calculated.

2. A possible interpretation of this language is that a company may be permitted to determine this hypothetical portfolio book yield for each year using their actual A-rated bonds purchased in that year, i.e. their own A-rated bonds. Is this approach acceptable?

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3. It was the intent of this provision that a company use a hypothetical portfolio composed of A-rated corporate bonds with yields commensurate with the A-rated corporate bond yields available in the year of issue. If the yields associated with the company's actual A-rated bonds purchased in the year of issue are commensurate with A-rated corporate bond yields available in the year of issue, then the company's approach is acceptable. If the yields associated with the company's bonds are significantly higher than A-rated corporate bond yields available in the year of issue, then the approach is unacceptable.

4. If such an approach was used, the appointed actuary should address this question in the memorandum. Reasonable approaches for comparison to a company's assets include using a published index of A-rated corporate bond yields such as Moody's at an appropriate point in the year of issue or an average over the course of the year. Another reasonable approach would be to use a Treasury yield curve at an appropriate point in the year of issue or an average over the course of the year plus an appropriate published spread of A-rated corporate bond yields over Treasuries. An appropriate point in time would be June 30 of that year if the business was sold uniformly throughout the year. If the comparison does not show the yields from company's assets to be commensurate with the published index or adjusted yield curve rate, then (a) the sample size of the company's own A-rated portfolio relative to the total portfolio backing the liabilities, and (b) the year to year consistency of asset allocation become major items to be addressed in the memorandum.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 36

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 13, 2013

Date Adopted by Financial Condition (E) Committee

December 17, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D.a

Issue / Question

1. Section 8D.a. applies to a company's aggregate gross reserve before reinsurance. The reserve calculation requires a projection of future year-by-year cash flows, which includes such items as investment earnings and general insurance expenses. If a company has ceded 100% of the business to an authorized reinsurer by use of coinsurance, the assets and net liabilities are no longer on the ceding company's books. Additionally, the administration is also generally transferred to the reinsurer. In such circumstances, the projection of future cash flows is "hypothetical" in that one must assume a starting asset portfolio, future investment strategy, future general insurance expenses, and so on. Furthermore, the ceding company generally does not have the data or systems to determine the reserves and must rely on the assuming company.

2. Since the assuming company is required to calculate the reserves on both direct and assumed business, may the ceding company use the reserves as reported by the reinsurer in the reinsurer's annual statement?

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3. Under 100% coinsurance agreements with an authorized reinsurer, the ceding company is permitted to report reserves equal to those calculated by the reinsurer in the reinsurer's Exhibit 5/Schedule S.

4. Note that this interpretation was not being requested for coinsurance with funds withheld, modified coinsurance, or agreements where the reinsurer is unauthorized.

5. The Working Group recommends the above interpretation as guidance for yearend 2013, provided there is no conflict with the accounting requirements in the *Accounting Practices and Procedures Manual*. The issue/question will be submitted to the Life Actuarial (A) Task Force for broader consideration and possible amendment to the valuation manual.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 37

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 13, 2013

Date Adopted by Financial Condition (E) Committee

December 17, 2013

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Sections 8B and 8C

Issue / Question

1. Step 4 of Section 8E says "…determine the minimum amount of shadow account required to fully fund the guarantee." Should this determination take into account actual history, or is this a purely theoretical value?

2. Consider a hypothetical policy valued on its 5th anniversary. It has a shadow fund value of $12,000. Premiums of $2,500 were paid on each anniversary. If the policyholder paid an additional $63,000 (net of premium loads) on the valuation date, the guarantee would be fully funded. However, due to the product design, if the $12,000 shadow fund value resulted from a single premium of $10,000 at issue, the guarantee would be fully funded by payment of an additional $60,000 (net) at the valuation date. Is the "minimum amount" $75,000 or $72,000?

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3. Step 4 of Section 8E states that the determination is to be made as of "the valuation date for the policy being valued…", indicative of a seriatim calculation that considers the actual circumstances of the policy. If on the valuation date a specific set of charges and credits are applicable for future shadow account calculations, such charges and credits should be used in the determination regardless of any more favorable charges and credits that may have been available as of the issue date.

4. Given the information that the policyholder has no control over the future charges and credits to be applied in fully funding the guarantee, it is presumed that a single set of charges/credits (with no caps or floors) is operative as of the valuation date. While an unqualified response is not possible in the absence of a full understanding of the policy design, the minimum amount appears to be $75,000 rather than $72,000.

5. Also, per AG38, Section 8E, the actuary must ensure that the methodology is compatible with the intent that the funding ratio (Step 3 result divided by the Step 4 result) measures the level of prefunding.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 38

Date Adopted by Emerging Actuarial Issues (E) Working Group

August 14, 2014

Date Adopted by Financial Condition (E) Committee

August 18, 2014

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D

Issue / Question

1. Actuarial INT 27 clarifies that AG38, Section 8D, addresses the gross reserve requirements and required documentation regarding reinsurance. In reviewing the AG 38, Section 8D Actuarial Memorandum and reinsurance information, it appears that guidance is needed to address situations where the YRT reinsurance agreement reserve credit taken may be significantly different than the reserve an assuming company has set up. Such a significant difference can be due to a larger credit being calculated under VM-20 assumptions versus that set up by an assuming company. Additionally, in some cases the higher gross reserve required under the AG 38, Section 8D modified deterministic reserve, was not reported in the statutory blank prior to the reinsurance credit being taken.

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2. The reserve established pursuant to AG 38, Section 8D (AG38-8D), should be reported on a gross basis prior to any adjustment for reinsurance. In addition, the reserve credit for reinsurance on policies subject to AG38-8D should be calculated using current statutory requirements and mortality and interest applicable under the AG38-8D.a.1. calculation.

3. Since AG38-8D does not address credit for reinsurance and only addresses calculation of the gross reserve, any determination of such credit would be outside of AG38-8D and, therefore, based on current statutory requirements and accepted practices. For example, for the calculation of the ceding credit to be posted in the statutory statement, current accounting guidance (including SSAP No. 61R, paragraph 37) should be followed. And for asset adequacy analysis, both for general testing of aggregate reserves and for the standalone analysis required by AG38-8C, currently accepted actuarial practice should be followed. AG38-8D does not incorporate VM-20 directly into either of these.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 39

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 14, 2014
Revised November 2, 2015

Date Adopted by Financial Condition (E) Committee

November 18, 2014
Revised November 21, 2015

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D. a.2.a)(I), Section 7.D. of VM-20

Issue / Question

1. Subsection a.2. of Section 8D provides for two exceptions to the usual deterministic reserve requirements of VM-20 in calculating the gross premium reserve in Section 8D.a.2. One of these exceptions, in subsection a.2.a)(I), relates to net investment earnings on starting assets and limits those earnings to "…the lesser of (i) the actual portfolio net investment returns and (ii) the net investment returns based on a portfolio of A-rated corporate bonds…".

2. The language of Section 8D.a.2.a)(I) is not prescriptive as to the process for determining this net investment earnings comparison. One option is to compare actual portfolio yields to hypothetical portfolio yields as of a single point in time, most logically the valuation date. Another option is to develop both an actual and hypothetical portfolio as of the valuation date and project future asset cash flows and net investment returns prospectively and then use the lesser earning portfolio net investment return in each future year. Other prospective-type approaches to determining the Section 8D.a.2.a)(I) lesser net investment return portfolio are also possible. These lesser returns are then combined, in some fashion, with the net reinvestment return prescribed in Section 8D.a.2.a)(II) to develop the final path of discount rates used in the final Section 8D.a.2.c) reserve calculation.

3. In determining an appropriate interpretation of the language of Section 8D.a.2.a)(I) an important question to ask is: Is a prospective-type interpretation and approach illustrated above, or something similar, consistent with the determination of a single starting asset portfolio as described in Section 7.D. ofVM-20? The objective of the requirement in Section 8D.a.2.a)(I) is to impose a restriction on the determination of the starting asset portfolio required under VM-20 for the deterministic reserve calculation, not to anticipate the use of multiple portfolios prospectively. The use of future year-by-year net investment returns from multiple portfolios (actual and hypothetical) would appear to be inconsistent with the starting asset portfolio requirement of VM-20.

4. The issues at hand are twofold:

   a. Does a prospective future net investment return comparison interpretation of the language of Section 8D.a.2.a)(I) create an inconsistency with the language of Section 7.D. of VM-20 with respect to the requirements for utilizing a single starting asset portfolio in the deterministic reserve calculation?

   b. Given the multitude of possible approaches that might be used, does a prospective future net investment return comparison interpretation of the language of Section 8D.a.2.a)(I)

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lead to the creation of a non-level playing field beyond the range of approaches available in interpreting Section 8D.a.2.a)(I) in a manner that is consistent with VM-20?

Interpretation of Emerging Actuarial Issues (E) Working Group

5. For 12/31/2014 and later Section 8D submissions, for purposes of determining the starting asset portfolio, the language of Section 8D.a.2.a)(I) is interpreted such that the actual/hypothetical starting asset portfolio net investment return comparison is made as of the valuation date and not prospectively. Examples of how the comparison may be made include (i) a comparison of the weighted average hypothetical portfolio versus actual portfolio net investment returns as of the valuation date or (ii) a historical issue-year-by-issue-year hypothetical versus actual portfolio net investment return comparison, perhaps resulting in a starting asset portfolio as of the valuation date that is a hybrid of the company's actual portfolio assets for certain issue years and a hypothetical asset portfolio for other issue years.

6. For purposes of this comparison for 12/31/16 and later, the actual portfolio net investment return is adjusted by the current amortization of IMR allocated to the portfolio. This adjustment is made only for the comparison of portfolio yields to determine the appropriate portfolio to use in the development of the deterministic reserve. The reserve amount is then determined following the procedure defined in VM-20.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 40

Date Adopted by Emerging Actuarial Issues (E) Working Group

November 14, 2014

Date Adopted by Financial Condition (E) Committee

November 18, 2014

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D.a.2.c) and Section 7.C.4. of VM-20

Issue / Question

1. Subsection a.2.c) of Section 8D provides for the calculation of gross premium Primary Reserve to be performed using the path of net investment returns determined in Section 8D.a.2.b) "…to discount the cash flows applicable to those policies.", i.e. those policies subject to Section 8D. The cash flows referenced in Section 8D.a.2.c) are to include, as per Section 4.A.3. of VM-20, death and cash surrender benefits. For the ULSG policy types subject to the requirements of Section 8D, if the interest rate credited to the policy account value is a non-guaranteed element (NGE), the value of the benefits be directly impacted by the net investment earnings of the assets used to back the reserves held in support of the risks assumed under the policies. In addition, lapse rates for these ULSG policy types also may vary depending on the net investment earnings of the assets used to back the reserves held in support of the risks assumed under the policies.

2. Section 7.C. of VM-20, covering NGE cash flows, requires, in subsection 4. that:

   a. "Projected levels of NGE in the cash flow model must be consistent with the experience assumptions used in each scenario. Policyholder behavior assumptions in the model must be consistent with the NGE assumed in the model."

   b. There is only a single (level) interest rate scenario applicable for the Section 8D.a.2. reserve gross premium reserve calculation so the issue centers on whether the NGE and policyholder behavior assumptions are "consistent" with the experience assumptions and NGE respectively.

Interpretation of Emerging Actuarial Issues (E) Working Group

3. This interpretation permits the delinking of the liability cash flows used in the Section 8D.a.2.c) gross premium reserve calculation from the net investment returns determined as in Section 8D.a.2.b) provided the actuary can provide justification that the impact of such delinkage on the Section 8D.a.2. reserve calculation is consistent with the requirements of Section 7.C.4 and Section 2G of VM-20.

4. The information required to support the delinked approach would need to present reasonable justification and reflect the consistency of the assumptions used with the particular company's anticipated experience and ULSG product structures. The information provided should be adequate to support the assertion that the requirements of Section 2.G. and Section 7.C.4. of VM-20 have been achieved.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 41

Date Adopted by Emerging Actuarial Issues (E) Working Group

December 11, 2014

Date Adopted by Financial Condition (E) Committee

December 12, 2014

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8D. a.2.a)(I)

Issue / Question

1. Section 8D directs companies to test: "The company's aggregate gross reserve before reinsurance for the business subject to this Section 8D to be reported in the December 31, 2012, and subsequent annual statutory financial statements of the company will be the aggregate reserve under 1 below, plus any excess of the aggregate reserve determined as defined in 2 below, over 1".

2. Furthermore Section 8D requires that for existing assets: "The projected net investment earnings from the starting assets shall be the lesser of (i) the actual portfolio net investment returns and (ii) net investment returns based on a portfolio of A-rated corporate bonds purchased in the year of issue of the policies based on yields available in the year of issue for those bonds."

3. Is it required to test reinsurance assumed?

    a. Some companies only test at the direct writer level (using hypothetical portfolios) while other companies test the reinsurance assumed against actual assets.

4. Is it appropriate to use hypothetical portfolios for testing?

    a. Assuming a company where the reserves are 100% ceded (all but an insignificant amount was coinsurance) and no assets remain. May the company test on the basis of a hypothetical portfolio of A rated bonds described above? While this may be the only interpretation available, there is no connection between the assets and the liabilities or any company investment policy.

    b. When the existing asset yield is below that of the hypothetical portfolio, is it required to take a hair-cut on the yields of the existing assets or is it acceptable to use a hypothetical portfolio of just one bond per issue year instead?

Interpretation of Emerging Actuarial Issues (E) Working Group

5. Do the requirements of AG38-8D apply to applicable reinsurance assumed?

    a. Yes. It is required to apply the requirements of AG38-8D to include reinsurance assumed on risks that are within its scope. AG38-8D(a) includes the company's "aggregate gross reserve before reinsurance…". This is interpreted, for applicable business, to be the company's direct written business plus coinsurance reinsurance assumed and prior to any

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reinsurance ceded. Only this interpretation is consistent with the scope of AG38-8D and the reporting of reserves in Exhibit 5 of the annual statement.

6. Is it appropriate to use hypothetical portfolios for testing?

   a. There are two types of hypothetical portfolios possible for this question.

      i. The first type of hypothetical portfolio is required by AG-38, 8D(a)(2)(a)(I)(ii). This citation provides for a derivation of a hypothetical "portfolio of A rated corporate bonds purchased in the year of issue of the policies based on yields available in the year of issue for those bonds."

      ii. There may be a second type of hypothetical portfolio to use in place of the actual portfolio pursuant to AG38, 8D(a)(2)(a)(I)(i) if that actual portfolio is incomplete or unavailable for a company that has ceded some or all of the risk through coinsurance. In this case the company may coordinate with and make use of the reserve calculations of the assuming reinsurer, as provided in VM-20 Section 8.A.1. However, the ceding company, in calculating the pre-reinsurance ceded reserve or gross reserve required by AG-38 Section 8D, must assure that such modeling and assumptions are appropriate as provided by the first paragraph of VM-20 Section 8.D.2 and as provided by VM-20 Section 8.D.2.b.

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Interpretation of the Emerging Actuarial Issues (E) Working Group

Actuarial INT 42

Date Adopted by Emerging Actuarial Issues (E) Working Group

May 14, 2015

Date Adopted by Financial Condition (E) Committee

August 17, 2015

Reference

Actuarial Guideline 38—The Application of the Valuation of Life Insurance Policies Model Regulation, Section 8E

Issue / Question

1. A universal life policy contains a secondary guarantee based on the value of a shadow account. As long as the shadow account is positive, the policy is guaranteed not to lapse, even if the cash surrender value is not positive. The shadow account value accumulates with interest from one period to another, with deductions for COI charges. The interest credited to the shadow account is calculated as follows:

- 10% interest is credited to the shadow account up to a threshold amount.
- 0% interest is credited to the any excess of the shadow account over the threshold amount.
- The threshold amount is equal to the accumulation of the level premium that would keep the shadow account positive throughout the secondary guarantee period, assuming 10% interest is credited.

2. The shadow account is not larger than the threshold amount on the valuation date. For purposes of the fourth step in sections 8B and 8C of the Guideline, what interest rate should be used to determine the shadow account value that would fully fund the secondary guarantee?

Interpretation of Emerging Actuarial Issues (E) Working Group

3. This interpretation is qualified for issues within the scope of AG 38, Section 8E, only and applies to those section 8E products issued on and after 1/1/16. The intent of the ratio in AG 38 8E Step 4 is to measure the level of pre-funding and to specify its use to establish reserves in its application to the Net Single Premium. The objective is to provide for reserves equal to the appropriate portion of the Net Single Premium represented by pre-funding as of the valuation date. The ratio is a practical convention for this objective.

4. For shadow account secondary guarantee product designs with multiple charges/multiple credits where consistency of charges and credits in the numerator and denominator of the ratio is difficult to achieve, reasonable efforts must be made to establish a ratio which, on an aggregate basis, carries out the objective above.

5. Otherwise, reasonable efforts should be made to produce a conservative estimate of the present value of future benefits on a statutory basis which, in the aggregate, carries out the objective above. Such conservative estimate, when divided by the Net Single Premium calculated in AG 38 8E, Step 5, produces the ratio.

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6. For any shadow account secondary guarantee product designs with multiple charges/multiple credits the denominator of the ratio shall be limited to be no larger than the Net Single Premium as calculated in AG 38 8E, Step 5.

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Appendix D
GAAP Cross-Reference to SAP
as of December 2023

Introduction

As expressed in the Statement of Concepts, statutory accounting principles (SAP) utilize the framework established by Generally Accepted Accounting Principles (GAAP). Appendix D includes GAAP pronouncements that have been considered or are pending consideration in the development of SAP.

The NAIC Codification of Statutory Accounting Principles Working Group addressed all GAAP pronouncements included in Category A, Category B and Category C issued through 1996 during the initial drafting of the SSAPs, as well as the AICPA Accounting Interpretations included in Category D. This working group is now called the Statutory Accounting Principles (E) Working Group (SAPWG).

- Category A – FASB Statements and Interpretations, APB Opinions, and AICPA Accounting Research Bulletins
- Category B – FASB Technical Bulletins, Board-Directed FASB Staff Positions, AICPA Industry Audit and Accounting Guides, and AICPA Statements of Position
- Category C – Consensus positions of the FASB Emerging Issues Task Force (EITF) and AICPA Practice Bulletins
- Category D – AICPA Accounting Interpretations

Subsequent to the NAIC codification of statutory accounting principles, as documented in the Policy Statement on the Maintenance of Statutory Accounting Principles (included in Appendix F), the SAPWG continued to review new GAAP guidance for applicability to SAP. Beginning January 1, 1999, the Emerging Accounting Issues (E) Working Group (EAIWG) was formed and began addressing FASB EITF opinions issued subsequent to 1996. The positions of the EAIWG are documented in an interpretation (INT) as indicated by reference in the applicable column of the GAAP Cross-Reference to SAP chart. Appendix B includes the full text of EAIWG INTs issued before December 31, 2015. In October 2010, the SAPWG undertook a project to incorporate authoritative guidance related to specific topics in one location. This means that guidance within INTs has been incorporated into the applicable SSAPs, where possible. Appendix D now references the applicable SSAP, not the nullified INT. Therefore, completely superseded SSAPs and nullified INTs are removed from the Manual and retained in *Appendix H – Superseded SSAPs and Nullified Interpretations*, which is posted for public reference on the SAPWG web page at *https://content.naic.org/cmte_e_app_sapwg.htm*. Under this approach, only current guidance is included in the Manual, while preserving the historical reference of previous authoritative SSAPs and INTs for accounting purposes.

In addition to the GAAP Cross Reference to SSAP, Appendix D includes a Nonapplicable GAAP Pronouncements supplement which contains a listing of GAAP pronouncements that have been considered in the development of SAP and deemed not applicable.

In June 2009, the FASB issued *FASB Statement 168, FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles (FAS 168)*, effective for interim and annual periods ending after Sept. 15, 2009. FAS 168 (Topic 105 of the FASB Codification) identified the sources of accounting principles and the framework for selecting the principles used in the preparation of the financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States. Pursuant to this standard:

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- FASB Accounting Standards Codification was established as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities. (SEC guidance included within the FASB Codification is provided for convenience and relates only to SEC entities.)

- Accounting Standards Updates issued after the effective date of FAS 168 are not considered authoritative in their own right. Such standards serve only to update the FASB Codification, provide background information, and provide the bases of conclusions on the changes to the FASB Codification.

- Effective September 15, 2009, all non-SEC accounting and reporting standards were superseded. Additionally, all nongrandfathered, non-SEC accounting literature not included in the Codification was deemed nonauthoritative. As of September 15, 2009, AICPA Statements of Position are no longer reviewed as part of the statutory maintenance process as they are no longer considered authoritative GAAP literature. If the AICPA were to address an issue that affects the FASB Codification, an accounting standard update (ASU) would be issued and reviewed for applicability to statutory accounting.

As a result of FAS 168, Appendix D – GAAP Cross Reference to SAP has been revised to include reference of FASB Accounting Standards Updates, as well as the Accounting Standards Codification Reference (Topic and Subtopic) for pre-codification GAAP guidance. Pre-codification GAAP guidance that has been superseded as a result of exclusion from the GAAP Codification has been identified within Appendix D. Users of the NAIC *Accounting Practices and Procedures Manual* shall continue to refer to the FASB pre-codification standards, and the applicable references to such standards, to determine the GAAP guidance that has been adopted, adopted with modification or rejected for statutory accounting.

To assist users in tracing pre-codification GAAP standards to the FASB Codification, Appendix D – GAAP Cross-Reference to SAP includes the Topic and Subtopic for all pre-codification GAAP standards that have been included in the FASB Codification. This FASB Codification reference does not reflect GAAP guidance adopted for statutory accounting. Only the guidance detailed in specific SSAPs or INTs shall be utilized in determining the GAAP guidance adopted, adopted with modification or rejected for statutory accounting. Items noted with "Not Explicitly Included in Codification" are no longer included in the FASB Cross Reference tool.

Information Provided in Appendix D – GAAP Cross-Reference to SSAP:

- Status – This column includes the SAPWG status of review. A "pending" status indicates that the SAPWG has not completed deliberation of the GAAP pronouncement. Items noted as "Not Board-Directed or SEC Update" will not be reviewed by the SAPWG unless specifically requested for review.

- Disposition – This column represents the general conclusion of the SAPWG/EAIWG for the stated GAAP pronouncement. This information is included in Appendix D as a reference tool, however, the guidance in the specific SSAP or INT shall be the authoritative source in determining the GAAP guidance adopted, adopted with modification or rejected for statutory accounting.

- Statutory Reference – This column provides the statutory accounting source addressing the GAAP pronouncement.

- Accounting Standards Codification Topic and Subtopic – This column provides a reference guide to trace pre-codification GAAP standards to the new FASB Codification.

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In addition to the "GAAP Cross Reference to SSAP," Appendix D includes the "FASB Codification to Pre-Codification GAAP" supplement. This supplement serves as a reference tool in tracing the FASB Codification to pre-codification GAAP standards that have been reviewed or are pending review as part of the current NAIC statutory accounting maintenance process. This supplement does not indicate which GAAP standards have been adopted, adopted with modification or rejected for statutory accounting. Pre-codification GAAP guidance not captured as part of the statutory accounting maintenance process, but that has been incorporated in the FASB Codification, has not been referenced within this supplement. Future consideration will occur on whether this pre-codification GAAP guidance will be reviewed for statutory accounting. Pre-codification GAAP included in the FASB codification, but not referenced within this supplement includes: FASB Derivative Implementation Group Issues; EITF Appendix D Topics; FASB Statement No. 138 Examples; FASB Staff Implementation Guides; AICPA Technical Inquiry Service and Audit and Accounting Guides. (The Audit and Accounting Guides (AAG) related to insurance have been reviewed for statutory accounting and are referenced in this supplement – HCO: Health Care Organizations, LHI: Life and Health Insurance and PLI: Property and Liability Insurance Companies. This supplement also does not include reference to the SEC standards incorporated within the FASB Codification: SEC Financial Reporting Releases; SEC Interpretive Releases; SEC Staff Accounting Bulletins; and SEC Regulation S-X.

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Category B - FASB Technical Bulletins, FASB Staff Positions, AICPA Industry Audit and Accounting Guides, and AICPA Statements of Position D-51

Category C - Consensus positions of the FASB Emerging Issues Task Force and AICPA Practice Bulletins D-74

Category D - AICPA Accounting Interpretations D-120

Nonapplicable GAAP Pronouncements D-122

FASB Codification Cross Reference to GAAP Pronouncements D-134

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ACCOUNTING STANDARDS UPDATES

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2009-01	Topic 105—Generally Accepted Accounting Principles—Amendments based on—Statement of Financial Accounting Standards No. 168—The *FASB Accounting Standards Codification*™ and the Hierarchy of Generally Accepted Accounting Principles	Complete	Adopt (Adopted FAS 168)	Preamble	Not Explicitly Included in Codification.
2009-02	Omnibus Update—Amendments to Various Topics for Technical Corrections	Complete	N/A	App D – NA GAAP	Not Explicitly Included in Codification.
2009-03	SEC Update—Amendments to Various Topics Containing SEC Staff Accounting Bulletins (SEC Update)	SEC Update			Not Explicitly Included in Codification.
2009-04	Accounting for Redeemable Equity Instruments—Amendment to Section 480-10-S99 (SEC Update)	SEC Update			Not Explicitly Included in Codification.
2009-05	Fair Value Measurements and Disclosures (Topic 820)—Measuring Liabilities at Fair Value	Pending			820 825
2009-06	Income Taxes (Topic 740)—Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities	Pending			740
2009-07	Accounting for Various Topics—Technical Corrections to SEC Paragraphs (SEC Update)	SEC Update			Not Explicitly Included in Codification.
2009-08	Earnings per Share—Amendments to Section 260-10-S99 (SEC Update)	SEC Update			260
2009-09	Accounting for Investments—Equity Method and Joint Ventures and Accounting for Equity-Based Payments to Non-Employees—Amendments to Sections 323-10-S99 and 505-50-S99 (SEC Update)	SEC Update			Not Explicitly Included in Codification.
2009-10	Financial Services—Broker and Dealers: Investments—Other—Amendment to Subtopic 940-325 (SEC Update)	SEC Update			Not Explicitly Included in Codification.
2009-11	Extractive Activities—Oil and Gas—Amendment to Section 932-10-S99 (SEC Update)	SEC Update			932

[1] To assist users in tracing pre-codification GAAP standards to the FASB Codification, the FASB Codification Topic and Subtopic for all pre-codification GAAP standards has been included in this Appendix. This FASB Codification reference does not reflect GAAP guidance adopted for statutory accounting. The Accounting Practices and Procedures Manual (E) Subgroup was formed to assess changes necessary to reflect the new GAAP Codification within statutory accounting principles. Until this process is complete, or as otherwise noted in specific SSAPs or Interpretations, users of the *NAIC Accounting Practices and Procedures Manual* shall continue to refer to the FASB pre-codification standards, and the applicable references to such standards, to determine the GAAP guidance that has been adopted, adopted with modification, or rejected for statutory accounting.

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2009-12	Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)	Complete	Adopt	100R	820
2009-13	Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements	Complete	N/A Nullifies INT 04-18	App D - NA GAAP	605
2009-14	Software (Topic 985): Certain Revenue Arrangements That Include Software Elements	Complete	Adopt/M	16R	985
2009-15	Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing	Complete	N/A	App D - NA GAAP	470
2009-16	Transfers and Servicing (Topic 860): Accounting for Transfers of Financial Assets (FAS 166)	Complete	Adopt/M	103R	Not Explicitly Included in Codification.
2009-17	Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities (FAS 167)	Complete	Reject	25	Not Explicitly Included in Codification.
2010-01	Equity (Topic 505): Accounting for Distributions to Shareholders with Components of Stock and Cash	Complete	N/A	App D - NA GAAP	505
2010-02	Consolidation (Topic 810): Accounting and Reporting for Decreases in Ownership of a Subsidiary—A Scope Clarification	Complete	Reject	25	805 810 845
2010-03	Extractive Activities—Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures	Complete	N/A	App D - NA GAAP	932
2010-04	Accounting for Various Topics: Technical Corrections to SEC Paragraphs	SEC Update			Not Explicitly Included in Codification.
2010-05	Compensation—Stock Compensation (Topic 718): Escrowed Share Arrangements and the Presumption of Compensation (SEC Update)	SEC Update			Not Explicitly Included in Codification.
2010-06	Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements	Complete	Adopt/M	92, 100R, 102	715 820
2010-07	Not-for-Profit Entities (Topic 958): Not-for-Profit Entities: Mergers and Acquisitions	Pending			Not Explicitly Included in Codification.
2010-08	Technical Corrections to Various Topics	Complete	Adopt para. 815-20-25-15 Reject all others	86	Various
2010-09	Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements	Complete	Reject	9	855

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ACCOUNTING STANDARDS UPDATES

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2010-10	Consolidation (Topic 810): Amendments for Certain Investment Funds	Complete	Reject	25	810
2010-11	Derivatives and Hedging (Topic 815): Scope Exception Related to Embedded Credit Derivatives	Complete	Adopt/M Paragraph 815-10-50k Reject all others	27, 86	815
2010-12	Income Taxes (Topic 740): Accounting for Certain Tax Effects of the 2010 Health Care Reform Acts	SEC Update			740
2010-13	Compensation—Stock Compensation (Topic 718): Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Currency of the Market in Which the Underlying Equity Security Trades	Complete	Adopt/M	104R	718
2010-14	Accounting for Extractive Activities—Oil & Gas: Amendments to Paragraph 932-10-S99-1 (SEC Update)	SEC Update			932
2010-15	Financial Services—Insurance (Topic 944): How Investments Held through Separate Accounts Affect an Insurer's Consolidation Analysis of Those Investments	Pending			944
2010-16	Entertainment—Casinos (Topic 924): Accruals for Casino Jackpot Liabilities	Complete	N/A	App D - NA GAAP	924
2010-17	Revenue Recognition—Milestone Method (Topic 605): Milestone Method of Revenue Recognition	Complete	N/A	App D - NA GAAP	605
2010-18	Receivables (Topic 310): Effect of a Loan Modification When the Loan Is Part of a Pool That Is Accounted for as a Single Asset	Pending			310
2010-19	Foreign Currency (Topic 830): Foreign Currency Issues: Multiple Foreign Currency Exchange Rates	SEC Update			830
2010-20	Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses	Complete	Adopt/M for mortgage loans Reject all others	36, 37	310
2010-21	Accounting for Technical Amendments to Various SEC Rules and Schedules: Amendments to SEC Paragraphs Pursuant to Release No. 33-9026: Technical Amendments to Rules, Forms, Schedules and Codification of Financial Reporting Policies (SEC Update)	SEC Update			Various
2010-22	Accounting for Various Topics—Technical Corrections to SEC Paragraphs (SEC Update)	SEC Update			Various
2010-23	Health Care Entities (Topic 954): Measuring Charity Care for Disclosure	Complete	Adopt/M	54R	954

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2010-24	Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries	Complete	N/A	App D - NA GAAP	954
2010-25	Plan Accounting—Defined Contribution Pension Plans (Topic 962): Reporting Loans to Participants by Defined Contribution Pension Plans	Complete	N/A	App D - NA GAAP	310 962
2010-26	Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts	Complete	Reject	71	944
2010-27	Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers	Complete	N/A	App D - NA GAAP	720
2010-28	Intangibles—Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts	Complete	Reject	68, 90	350
2010-29	Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations	Pending			805 958
2011-01	Receivables (Topic 310): Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20	Complete	See ASU 2011-02	36	310
2011-02	Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring	Complete	Adopt/M Paragraphs 310-40-15-13 through 18 and 310-40-15-20 Reject all others	36	310
2011-03	Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements	Complete	Adopt	103R	860
2011-04	Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs	Pending			715 805 820
2011-05	Comprehensive Income (Topic 220): Presentation of Comprehensive Income	Complete	N/A	App D - NA GAAP	205 220
2011-06	Other Expenses (Topic 720): Fees Paid to the Federal Government by Health Insurers	Complete	Adopt/M	106	405 720
2011-07	Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities	Complete	N/A	App D - NA GAAP	954
2011-08	Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment	Complete	Reject	68, 90	350
2011-09	Compensation—Retirement Benefits—Multiemployer Plans (Subtopic 715-80): Disclosures about an Employer's Participation in a Multiemployer Plan	Complete	Adopt	92, 102	715

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ACCOUNTING STANDARDS UPDATES

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2011-10	Property, Plant, and Equipment (Topic 360): Derecognition of in Substance Real Estate—A Scope Clarification	Complete	Reject	97	360
2011-11	Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities	Complete	Reject	64	210 270
2011-12	Comprehensive Income (Topic 220)–Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05	Complete	N/A	App D - NA GAAP	220
2012-01	Health Care Entities (Topic 954)–Continuing Care Retirement Communities— Refundable Advance Fees	Complete	N/A	App D - NA GAAP	954
2012-02	Intangibles—Goodwill and Other (Topic 350)–Testing Indefinite-Lived Intangible Assets for Impairment	Complete	Reject	68, 90	350
2012-03	Technical Amendments and Corrections to SEC Sections–Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 114, Technical Amendments Pursuant to SEC Release No. 33-9250, and Corrections Related to FASB Accounting Standards Update 2010-22	SEC Update			Not Explicitly Included in Codification.
2012-04	Technical Corrections and Improvements	Complete	N/A	App D - NA GAAP	Various
2012-05	Statement of Cash Flows (Topic 230)–Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows	Complete	Adopt/M	69	230 958
2012-06	Business Combinations (Topic 805)–Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution	Pending			805
2012-07	Entertainment—Films (Topic 926)–Accounting for Fair Value Information That Arises after the Measurement Date and Its Inclusion in the Impairment Analysis of Unamortized Film Costs	Complete	N/A	App D - NA GAAP	926
2013-01	Clarifying the Scope of Disclosures About Offsetting Assets and Liabilities	Complete	Reject	64	210
2013-02	Comprehensive Income – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income	Complete	N/A	App D - NA GAAP	220 270
2013-03	Financial Instruments: Clarifying the Scope and Applicability of a Particular Disclosure to Nonpublic Entities	Complete	Reject	100R	825
2013-04	Liabilities: Obligations Resulting from Joint and Several Liability Arrangements for which the Total Amount is Fixed at the Reporting Date (Topic 405)	Complete	Adopt/M	5R	405

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2013-05	Foreign Currency Matters: Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity (Topic 830)	Complete	Adopt/M	23	805 810 830
2013-06	Not-for-Profit Entities: Services Received from Personnel of an Affiliate (Topic 958)	Complete	Reject	25	954 958
2013-07	Presentation of Financial Statements: Liquidation Basis of Accounting (Topic 205)	Complete	N/A	App D - NA GAAP	205 960 962 965
2013-08	Investment Companies: Amendments to the Scope, Measurement, and Disclosure Requirements (Topic 946)	Complete	Reject	App D NA GAAP	230 323 810 820 946
2013-09	Fair Value Measurements: Deferral of the Effective Date of Certain Disclosures for Nonpublic Employee Benefit Plans in Update No. 2011-04	Pending			820
2013-10	Derivatives and Hedging (Topic 815) Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes	Complete	Adopt	86	815
2013-11	Income Taxes (Topic 740) Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists	Complete	Reject	101	740
2013-12	Definition of a Public Business Entity, An Addition to the Master Glossary	Complete	N/A	App D - NA GAAP	Glossary
2014-01	Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects	Complete	Adopt/M	93	323
2014-02	Intangibles—Goodwill and Other (Topic 350): Accounting for Goodwill	Complete	Reject	68, 90	350
2014-03	Derivatives and Hedging (Topic 815): Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps—Simplified Hedge Accounting Approach (PCC)	Complete	Reject	86	815 825
2014-04	Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure	Complete	Adopt/M	37	270 310
2014-05	Service Concession Arrangements (Topic 853)	Complete	Adopt/M	22R	853
2014-06	Technical Corrections and Improvements Related to Glossary Terms	Complete	N/A	App D – NA GAAP	Glossary
2014-07	Consolidation (Topic 810): Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements (PCC)	Complete	Reject	25	810

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2014-08	Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity	Complete	Adopt/M	24	205 360
2014-09	Revenue from Contracts with Customers (Topic 606)	Complete	Reject	47	Various
2014-10	Development Stage Entities (Topic 915), Elimination of Certain Financial Reporting Requirements, Including an Amendment to Variable Interest Entities Guidance in Topic 810, Consolidation	Complete	N/A	App D - NA GAAP	275 925
2014-11	Transfers and Servicing (Topic 860), Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures	Pending			860
2014-12	Compensation—Stock Compensation (Topic 718), Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period	Complete	Adopt	104R	718
2014-13	Consolidation (Topic 810)—Measuring the Financial Assets and the Financial Liabilities of a Consolidated Collateralized Financing Entity	Complete	N/A	App D - NA GAAP	805 810 820
2014-14	Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40)—Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure	Complete	Adopt	37	310
2014-15	Presentation of Financial Statements—Going Concern (Subtopic 205-40)—Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern	Complete	Adopt	1	205
2014-16	Derivatives and Hedging (Topic 815)—Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity	Complete	Reject	86	815
2014-17	Business Combinations (Topic 805)—Pushdown Accounting	Pending			805
2014-18	Business Combinations (Topic 805): Accounting for Identifiable Intangible Assets in a Business Combination (a consensus of the Private Company Council)	Pending			805
2015-01	Income Statement—Extraordinary and Unusual Items (Subtopic 225-20)—Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items	Complete	Adopt/M	24	225
2015-02	Consolidation (Topic 810)—Amendments to the Consolidation Analysis	Complete	Reject	25	810
2015-03	Interest—Imputation of Interest (Subtopic 835-30)—Simplifying the Presentation of Debt Issuance Costs	Complete	Reject	15	835
2015-04	Compensation—Retirement Benefits (Topic 715)—Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets	Complete	Adopt/M	92, 102	715

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2015-05	Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40)—Customer's Accounting for Fees Paid in a Cloud Computing Arrangement	Complete	Adopt	16R	350
2015-06	Earnings Per Share (Topic 260)—Effects on Historical Earnings per Unit of Master Limited Partnership Dropdown Transactions	Complete	Reject	App D - NA GAAP	260
2015-07	Fair Value Measurement (Topic 820)—Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)	Complete	Adopt	100R	820
2015-08	Business Combination (Topic 805)—Pushdown Accounting, Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115	Complete	Reject	App D - NA GAAP	805
2015-09	Financial Services—Insurance (Topic 944)—Disclosures about Short-Duration Contracts	Complete	Reject	55, 65	944
2015-10	Technical Corrections and Improvements	Complete	Reject	App D - NA GAAP	
2015-11	Inventory (Topic 330)–Simplifying the Measurement of Inventory	Complete	Reject	App D - NA GAAP	330
2015-12	Plan Accounting: Defined Benefit Pension Plans (Topic 960); Defined Contribution Pension Plans (Topic 962); Health and Welfare Benefit Plans (Topic 965)—I. Fully Benefit-Responsive Investment Contracts; II. Plan Investment Disclosures; III. Measurement Date Practical Expedient (consensuses of the FASB Emerging Issues Task Force)	Complete	Reject	App D - NA GAAP	960 962 965
2015-13	Derivatives and Hedging (Topic 815)—Application of the Normal Purchases and Normal Sales Scope Exception to Certain Electricity Contracts within Nodal Energy Markets (a consensus of the FASB Emerging Issues Task Force)	Complete	Reject	App D - NA GAAP	815
2015-14	Revenue from Contracts with Customers (Topic 606)—Deferral of the Effective Date	Complete	Reject	47	606
2015-15	Interest—Imputation of Interest (Subtopic 835-30)—Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements—Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting	Complete	Reject	15	835
2015-16	Business Combinations (Topic 805)—Simplifying the Accounting for Measurement-Period Adjustments	Pending			805
2015-17	Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes	Complete	Reject	101	740
2016-01	Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities	Complete	Reject	26R, 30R, 32, 43R, 100R	825
2016-02	Leases (Topic 842)	Complete	Reject	22R	840 842

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2016-03	Intangibles—Goodwill and Other (Topic 350), Business Combinations (Topic 805), Consolidation (Topic 810), Derivatives and Hedging (Topic 815): Effective Date and Transition Guidance (a consensus of the Private Company Council)	Complete	Reject	3, 68, 86	350 805 815
2016-04	Liabilities—Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products (a consensus of the Emerging Issues Task Force)	Complete	N/A	App D - NA GAAP	405
2016-05	Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships (a consensus of the Emerging Issues Task Force)	Complete	Adopt/M	86	815
2016-06	Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments (a consensus of the Emerging Issues Task Force)	Complete	Reject	86	815
2016-07	Investments—Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting	Complete	Adopt/M	30R, 48, 97	323
2016-08	Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)	Complete	Reject	47	606
2016-09	Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting	Complete	Adopt/M	104R	718
2016-10	Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing	Complete	Reject	47	606
2016-11	Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting (SEC Update)	Complete	N/A	App D - NA GAAP	605
2016-12	Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients	Complete	Reject	47	606
2016-13	Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	Complete	Reject	2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, 105R INT 06-07	326
2016-14	Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities	Complete	Reject	App D - NA GAAP	958

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2016-15	Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)	Complete	Adopt	69	320
2016-16	Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory	Complete	Reject	101	740
2016-17	Consolidation (Topic 810): Interests Held through Related Parties That Are under Common Control	Complete	Reject	25	810
2016-18	Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force)	Complete	Adopt	1, 69	230
2016-19	Technical Corrections and Improvements	Complete	Adopt/M	5R, 92, 102, 103R	Various
2016-20	Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers	Complete	Reject	47	606
2017-01	Business Combinations (Topic 805): Clarifying the Definition of a Business	Pending			805
2017-02	Not-for-Profit Entities – Consolidation (Subtopic 958-810): Clarifying When a Not-for-Profit Entity That Is a General Partner or a Limited Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity	Complete	Reject	App D - NA GAAP	958
2017-03	Accounting Changes and Error Corrections (Topic 250) and Investments—Equity Method and Joint Ventures (Topic 323): SEC Update	Complete	Reject	App D - NA GAAP	250 323 326 606 842
2017-04	Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment	Complete	Reject	68, 90	350 985
2017-05	Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets	Pending			310 323 350 360 606 610 805 810 845 860 970
2017-06	Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting (a consensus of the Emerging Issues Task Force)	Complete	Reject	App D - NA GAAP	960 962 965
2017-07	Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost	Complete	Reject	92, 102	220 330 715 958 980

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2017-08	Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities	Complete	Reject	26R	310 342 346
2017-09	Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting	Complete	Adopt/M	104R	718
2017-10	Service Concession Arrangements (Topic 853): Determining the Customer of the Operation Services (a consensus of the FASB Emerging Issues Task Force)	Complete	Adopt	22R	853
2017-11	Earnings Per Share (Topic 260); Distinguishing Liabilities from Equity (Topic 480); Derivatives and Hedging (Topic 815): (Part I) Accounting for Certain Financial Instruments with Down Round Features, (Part II) Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests with a Scope Exception	Complete	Reject	5R, 72, 86	260 480 505 815
2017-12	Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities	Complete	Adopt/M	86	220 320 815 954
2017-13	Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842), Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017, EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments	Complete	Reject	App D - NA GAAP	605 606 842
2017-14	Income Statement—Reporting Comprehensive Income (Topic 220), Revenue Recognition (Topic 605), and Revenue from Contracts with Customers (Topic 606) (SEC Update)	Complete	Reject	App D - NA GAAP	220 605 606
2017-15	Codification Improvements to Topic 995, U.S. Steamship Entities: Elimination of Topic 995	Complete	Reject	App D - NA GAAP	740 995
2018-01	Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842	Complete	Reject	22R	842
2018-02	Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income	Complete	Reject	App D - NA GAAP	220
2018-03	Technical Corrections and Improvements to Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities	Complete	Reject	26R, 30R, 32, 43R, 86, 100R	825
2018-04	Investments—Debt Securities (Topic 320) and Regulated Operations (Topic 980): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 117 and SEC Release No. 33-9273 (SEC Update)	Complete	Reject	App D - NA GAAP	320 980

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2018-05	Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 (SEC Update)	Complete	Reject	App D - NA GAAP	740
2018-06	Codification Improvements to Topic 942, Financial Services—Depository and Lending	Complete	Reject	App D - NA GAAP	942
2018-07	Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting	Complete	Adopt/M	95, 104R	718
2018-08	Not-For-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made	Complete	Reject	App D - NA GAAP	958
2018-09	Codification Improvements	Complete	Reject	App D - NA GAAP	Various
2018-10	Codification Improvements to Topic 842, Leases	Complete	Reject	22R	842
2018-11	Leases (Topic 842): Targeted Improvements	Complete	Reject	22R	842
2018-12	Financial Services—Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts	Complete	Reject	Preamble 50, 51R, 52, 54R, 55, 56, 71, 86	944
2018-13	Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement	Complete	Adopt/M	100R	820
2018-14	Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans	Complete	Adopt/M	92, 102	715
2018-15	Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract (a consensus of the FASB Emerging Issues Task Force)	Complete	Adopt/M	16R	350
2018-16	Derivatives and Hedging (Topic 815): Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes	Complete	Adopt	86	815
2018-17	Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities	Complete	Reject	25	810
2018-18	Collaborative Arrangements (Topic 808): Clarifying the Interaction between Topic 808 and Topic 606	Complete	Reject	47	808

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2018-19	Codification Improvements to Topic 326, Financial Instruments—Credit Losses	Complete	Reject	2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, 105R	326
2018-20	Leases (Topic 842): Narrow-Scope Improvements for Lessors	Complete	Reject	22R	842
2019-01	Leases (Topic 842): Codification Improvements	Complete	Reject	22R	842 942
2019-02	Entertainment—Films—Other Assets—Film Costs (Subtopic 926-20) and Entertainment—Broadcasters—Intangibles—Goodwill and Other (Subtopic 920-350): Improvements to Accounting for Costs of Films and License Agreements for Program Materials (a consensus of the FASB Emerging Issues Task Force)	Complete	Reject	App D - NA GAAP	920 926
2019-03	Not-for-Profit Entities (Topic 958): Updating the Definition of Collections	Complete	Reject	App D - NA GAAP	360 958
2019-04	Codification Improvements to Topic 326, Financial Instruments—Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments	Complete	Reject	2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, 105R	310 320 321 323 326 815 825 830 942 948
2019-05	Financial Instruments—Credit Losses (Topic 326): Targeted Transition Relief	Complete	Reject	100R	326
2019-06	Intangibles—Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958): Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities	Complete	Reject	68, 97	323 350 805 958

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2019-07	Codification Updates to SEC Sections: Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10532, Disclosure Update and Simplification, and Nos. 33-10231 and 33-10442, Investment Company Reporting Modernization, and Miscellaneous Updates	Complete	Reject	App D – NA GAAP	205 210 220 235 270 470 505 810 932 942 944 946 942 962 970 974
2019-08	Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer	Complete	Adopted/M	47, 95, 104R	260 470 606 718 845
2019-09	Financial Services—Insurance (Topic 944): Effective Date	Complete	Reject	App D - NA GAAP	944
2019-10	Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates	Complete	Reject	2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, 105R	326 350 815 842
2019-11	Codification Improvements to Topic 326, Financial Instruments—Credit Losses	Complete	Reject	2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, 105R	320 326 805
2019-12	Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes	Pending			323 718 740
2020-01	Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815)—Clarifying the Interactions between Topic 321, Topic 323, and Topic 815	Complete	Reject	48, 86, 97	321 323 815 825

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2020-02	Financial Instruments—Credit Losses (Topic 326) and Leases (Topic 842)—Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 119 and Update to SEC Section on Effective Date Related to Accounting Standards Update No. 2016-02, Leases (Topic 842)	Complete	Reject	App D - NA GAAP	326 842
2020-03	Codification Improvements to Financial Instruments	Complete	Reject	2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, 105R	326 470 820 825 860 942
2020-04	Reference Rate Reform (Topic 848)—Facilitation of the Effects of Reference Rate Reform on Financial Reporting	Complete	Adopted/M	App B – INT 20-01	848
2020-05	Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842)—Effective Dates for Certain Entities	Complete	Reject	App D - NA GAAP	606 842
2020-06	Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40)—Accounting for Convertible Instruments and Contracts in an Entity's Own Equity	Complete	Reject	5R, 72, 86	260 470 505 718 740 815 820 825 835 848
2020-07	Not-for-Profit Entities (Topic 958)—Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets	Complete	Reject	App D - NA GAAP	820 958
2020-08	Codification Improvements to Subtopic 310-20, Receivables—Nonrefundable Fees and Other Costs	Complete	Reject	26R	310
2020-09	Debt (Topic 470)—Amendments to SEC Paragraphs Pursuant to SEC Release No. 33-10762	Complete	Reject	App D – NA GAAP	270 460 505

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2020-10	Codification Improvements	Complete	Reject	App D - NA GAAP	105 205 220 250 260 270 310 460 715 740 830 835 852 942 946 958 965 970
2020-11	Financial Services—Insurance (Topic 944): Effective Date and Early Application	Complete	Reject	App D - NA GAAP	944
2021-01	Reference Rate Reform (Topic 848): Scope	Complete	Adopted/M	App B - INT 20-01	848
2021-02	Franchisors—Revenue from Contracts with Customers (Subtopic 952-606): Practical Expedient	Complete	Reject	47	606 952
2021-03	Intangibles—Goodwill and Other (Topic 350): Accounting Alternative for Evaluating Triggering Events	Complete	Reject	68	323 350 805 958
2021-04	Earnings Per Share (Topic 260), Debt—Modifications and Extinguishments (Subtopic 470-50), Compensation—Stock Compensation (Topic 718), and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40): Issuer's Accounting for Certain Modifications or Exchanges of Freestanding Equity-Classified Written Call Options (a consensus of the FASB Emerging Issues Task Force)	Complete	Reject	72	260 470 505 718 815
2021-05	Leases (Topic 842): Lessors—Certain Leases with Variable Lease Payments	Complete	Reject	22R	255 310 450 805 810 840 842 860 970

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2021-06	Presentation of Financial Statements (Topic 205), Financial Services—Depository and Lending (Topic 942), and Financial Services— Investment Companies (Topic 946)—Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10786, Amendments to Financial Disclosures about Acquired and Disposed Businesses, and No. 33-10835, Update of Statistical Disclosures for Bank and Savings and Loan Registrants	Complete	Reject	App D - NA GAAP	205 942 946
2021-07	Compensation—Stock Compensation (Topic 718)—Determining the Current Price of an Underlying Share	Complete	Adopted/M	104R	718
2021-08	Business Combinations (Topic 805)—Accounting for Contract Assets and Contract Liabilities from Contracts with Customers	Complete	Reject	47, 68	805
2021-09	Leases (Topic 842)—Discount Rate for Lessees That Are Not Public Business Entities	Complete	Reject	22R	842
2021-10	Government Assistance (Topic 832)—Disclosures by Business Entities about Government Assistance	Complete	Reject	24	832
2022-01	Derivatives and Hedging (Topic 815): Fair Value Hedging—Portfolio Layer Method	Complete	Adopted/M	86	310 320 326 815 860 948
2022-02	Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures	Complete	Reject	36	270 310 320 326 360 470 842 942 958 978
2022-03	Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions	Complete	Adopt/M	100R	820 940
2022-04	Liabilities—Supplier Finance Programs (Subtopic 405-50): Disclosure of Supplier Finance Program Obligations	Complete	Reject	105R	270 405
2022-05	Financial Services—Insurance (Topic 944): Transition for Sold Contracts	Complete	Reject	50 51R 52 56 71 86	944
2022-06	Reference Rate Reform (Topic 848): Deferral of the Sunset Date of Topic 848	Complete	Reject	INT 20-01	848
2023-01	Leases (Topic 842): Common Control Arrangements	Pending			842

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2023-02	Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method (a consensus of the Emerging Issues Task Force)	Pending			270 323 740 810
2023-03	Presentation of Financial Statements (Topic 205), Income Statement—Reporting Comprehensive Income (Topic 220), Distinguishing Liabilities from Equity (Topic 480), Equity (Topic 505), and Compensation—Stock Compensation (Topic 718): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 120, SEC Staff Announcement at the March 24, 2022 EITF Meeting, and Staff Accounting Bulletin Topic 6.B, Accounting Series Release 280—General Revision of Regulation S-X: Income or Loss Applicable to Common Stock (SEC Update)	Pending			220 480 505 718
2023-04	Liabilities (Topic 405): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 121 (SEC Update)	Pending			405
2023-05	Business Combinations—Joint Venture Formations (Subtopic 805-60): Recognition and Initial Measurement	Pending			205 350 450 730 740 805 808 810 815 842 845 958
2023-06	Disclosure Improvements: Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative	Pending			105 230 250 260 270 440 470 505 815 860 932 946 974
2023-07	Segment Reporting (Topic 280): Improvements to Reportable Segment Disclosures	Pending			270 280
2023-08	Intangibles—Goodwill and Other—Crypto Assets (Subtopic 350-60): Accounting for and Disclosure of Crypto Assets	Pending			230 270 350 958

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ACCOUNTING STANDARDS UPDATES

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.[1]
2023-09	Income Taxes (Topic 740): Improvements to Income Tax Disclosures	Pending			230 740

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 01	Disclosure of Foreign Currency Translation Information	Superseded by FAS 8 & FAS 52			
FAS 02	Accounting for Research and Development Costs	Complete	Adopt	17	730-10
FAS 03	Reporting Accounting Changes in Interim Financial Statements—An Amendment of APB Opinion No. 28	Superseded by FAS 154 Complete	N/A	App D - NA GAAP	
FAS 04	Reporting Gains and Losses from Extinguishment of Debt—An Amendment of APB Opinion No. 30	Superseded by FAS 145 Complete	Reject	15	
FAS 05	Accounting for Contingencies	Complete	Adopt Adopt paragraph 15	5R 72	310-10 360-10 440-10 450-10 450-20 450-30 460-10 505-10 720-20 730-20 944-20 944-40 944-60
FAS 06	Classification of Short-Term Obligations Expected to Be Refinanced—An Amendment of ARB No. 43, Chapter 3A	Complete	N/A	App D - NA GAAP	210-10 470-10
FAS 07	Accounting and Reporting by Development Stage Enterprises	Complete	Reject	17	915-10 915-205 915-210 915-215 915-225 915-230 915-235 915-340 915-605 915-810 980-10
FAS 08	Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements	Superseded by FAS 52			
FAS 09	Accounting for Income Taxes: Oil and Gas Producing Companies—An Amendment of APB Opinions 11 and 23	Superseded by FAS 19			

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 10	Extension of "Grandfather" Provisions for Business Combinations—An Amendment of APB Opinion No. 16	Superseded by FAS 141 Complete	Reject	68	
FAS 11	Accounting for Contingencies: Transition Method—An Amendment of FASB Statement No. 5	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification. See FAS 5
FAS 12	Accounting for Certain Marketable Securities	Superseded by FAS 115			
FAS 13	Accounting for Leases Reject except certain guidance on operating leases, leveraged leases, and sale leaseback transactions	Superseded by ASU 2016-02 Complete	Adopt paragraph 15, 16(b, c, d), 19 (a, b), 23(b, c), 36, 37, 39(c), 42-47 Reject all others N/A	22 22R	360-10 410-20 440-10 450-10 460-10 470-10 840-10 840-20 840-30 840-40 958-810 980-840
FAS 14	Financial Reporting for Segments of a Business Enterprise	Superseded by FAS 131 Complete	N/A	App D - NA GAAP	
FAS 15	Accounting by Debtors and Creditors for Troubled Debt Restructurings	Complete	Adopt/M	36	310-40 450-20 470-60
FAS 16	Prior Period Adjustments	Complete	Reject	3	250-10 270-10 450-20
FAS 17	Accounting for Leases: Initial Direct Costs—An Amendment of FASB Statement No. 13	Superseded by FAS 91			
FAS 18	Financial Reporting for Segments of a Business Enterprise: Interim Financial Statements—An Amendment of FASB Statement No. 14	Superseded by FAS 131 Complete	N/A	App D - NA GAAP	

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 19	Financial Accounting and Reporting by Oil and Gas Producing Companies	Complete	N/A	App D - NA GAAP	932-10 932-235 932-270 932-360 932-470 932-720 932-740
FAS 20	Accounting for Forward Exchange Contracts—An Amendment of FASB Statement No. 8	Superseded by FAS 52			
FAS 21	Suspension of the Reporting of Earnings per Share and Segment Information by Nonpublic Enterprises—An Amendment of APB Opinion No. 15 and FASB Statement No. 14	Superseded by FAS 131 Complete	N/A	App D - NA GAAP	
FAS 22	Changes In the Provisions of Lease Agreements Resulting from Refundings of Tax-Exempt Debt—An Amendment of FASB Statement No. 13	Superceded by ASU 2016-02 Complete	Reject N/A	22 22R	840-30
FAS 23	Inception of the Lease—An Amendment of FASB Statement No. 13	Superceded by ASU 2016-02 Complete	Adopt paragraph 10 - Reject all others N/A	22 22R	840-10
FAS 24	Reporting Segment Information in Financial Statements That Are Presented in Another Enterprise's Financial Report—An Amendment of FASB Statement No. 14	Superseded by FAS 131 Complete	N/A	App D - NA GAAP	
FAS 25	Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies—An Amendment of FASB Statement No. 19	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification See FAS 19
FAS 26	Profit Recognition on Sales-Type Leases of Real Estate—An Amendment of FASB Statement No. 13	Superseded by FAS 98			

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 27	Classification of Renewals or Extensions of Existing Sales-Type or Direct Financing Leases—An Amendment of FASB Statement No. 13	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	Not Directly Included in Codification Included as amendments to FAS 13
FAS 28	Accounting for Sales with Leasebacks—An Amendment of FASB Statement No. 13	Superceded By ASU 2016-02 Complete	 Adopt/M N/A	 22 22R	840-40
FAS 29	Determining Contingent Rentals—An Amendment of FASB Statement No. 13	Complete	Adopt paragraphs 8 & 11 - Reject all others	22	840-10
FAS 30	Disclosure of Information about Major Customers—An Amendment of FASB Statement No. 14	Superseded by FAS 131 Complete	 N/A	 App D - NA GAAP	
FAS 31	Accounting for Tax Benefits Related to U. K. Tax Legislation Concerning Stock Relief	Superseded by FAS 96 & FAS 109			
FAS 32	Specialized Accounting and Reporting Principles and Practices in AICPA Statements of Position and Guides on Accounting and Auditing Matters—An Amendment of APB Opinion No. 20	Superseded by FAS 111			
FAS 33	Financial Reporting and Changing Prices	Superseded by FAS 89			
FAS 34	Capitalization of Interest Cost	Complete	Adopt	44	360-10 835-20
FAS 35	Accounting and Reporting by Defined Benefit Pension Plans	Complete	N/A	App D - NA GAAP	460-10 960-10 960-20 960-30 960-205 960-310 960-325 960-360 962-10 965-10
FAS 36	Disclosure of Pension Information—An Amendment of APB Opinion No. 8	Superseded by FAS 87			

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 37	Balance Sheet Classification of Deferred Income Taxes—An Amendment of APB Opinion No. 11	Complete	N/A	App D - NA GAAP	740-10
FAS 38	Accounting for Preacquisition Contingencies of Purchased Enterprises—An Amendment of APB Opinion No. 16	Superseded by FAS 141 Complete	Reject	68	
FAS 39	Financial Reporting and Changing Prices: Specialized Assets—Mining and Oil and Gas—A Supplement to FASB Statement No. 33	Superseded by FAS 89			
FAS 40	Financial Reporting and Changing Prices: Specialized Assets—Timberlands and Growing Timber—A Supplement to FASB Statement No. 33	Superseded by FAS 89			
FAS 41	Financial Reporting and Changing Prices: Specialized Assets—Income-Producing Real Estate—A Supplement to FASB Statement No. 33	Superseded by FAS 89			
FAS 42	Determining Materiality for Capitalization of Interest Cost—An Amendment of FASB Statement No. 34	Complete	Adopt	44	835-20
FAS 43	Accounting for Compensated Absences	Complete	Adopt	11	420-10 710-10
FAS 44	Accounting for Intangible Assets of Motor Carriers—An Amendment of Chapter 5 of ARB No. 43 and an Interpretation of APB Opinions 17 and 30	Superseded by FAS 145 Complete	N/A	App D - NA GAAP	
FAS 45	Accounting for Franchise Fee Revenue	Complete	N/A	App D - NA GAAP	850-10 952-10 952-340 952-440 952-605 952-720
FAS 46	Financial Reporting and Changing Prices: Motion Picture Films	Superseded by FAS 89			
FAS 47	Disclosure of Long-Term Obligations	Complete	N/A	App D - NA GAAP	440-10 470-10
FAS 48	Revenue Recognition When Right of Return Exists	Complete	N/A	App D - NA GAAP	450-10 460-10 605-15
FAS 49	Accounting for Product Financing Arrangements	Complete	N/A	App D - NA GAAP	470-40

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 50	Financial Reporting in the Record and Music Industry	Complete	N/A	App D - NA GAAP	928-10 928-340 928-405 928-430 928-440 928-605 928-720
FAS 51	Financial Reporting by Cable Television Companies	Complete	N/A	App D - NA GAAP	922-10 922-350 922-360 922-430 922-605 922-720 922-835
FAS 52	Foreign Currency Translation	Complete	Reject	23, 31	205-10 440-10 815-20 830-10 830-20 830-30
FAS 53	Financial Reporting by Producers and Distributors of Motion Picture Films	Superseded by FAS 139 Complete	 N/A	 App D - NA GAAP	
FAS 54	Financial Reporting and Changing Prices: Investment Companies—An Amendment of FASB Statement No. 33	Superseded by FAS 89			
FAS 55	Determining whether a Convertible Security is a Common Stock Equivalent—An Amendment of APB Opinion No. 15	Superseded by FAS 111			
FAS 56	Designation of AICPA Guide and Statement of Position (SOP) 81-1 on Contractor Accounting and SOP 81-2 Concerning Hospital-Related Organizations as Preferable for Purposes of Applying APB Opinion 20—An Aamendment of FASB Statement No. 32	Superseded by FAS 111			
FAS 57	Related Party Disclosures	Complete	Adopt/M	25	850-10 958-20 958-810
FAS 58	Capitalization of Interest Cost in Financial Statements That Include Investments Accounted for by the Equity Method—An Amendment of FASB Statement No. 34	Complete	Adopt	44	835-20
FAS 59	Deferral of the Effective Date of Certain Accounting Requirements for Pension Plans of State and Local Governmental Units—An Amendment of FASB Statement No. 35	Superseded by FAS 75			

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 60	Accounting and Reporting by Insurance Enterprises	Complete	Reject paragraph 52 Reject	40R 50, 51R, 52, 53, 54R, 57, 59, 71	325-10 944-10 944-20 944-30 944-40 944-50 944-60 944-80 944-310 944-325 944-360 944-505 944-605 944-740 944-805
FAS 61	Accounting for Title Plant	Complete	Adopt/M	57	950-350
FAS 62	Capitalization of Interest Cost in Situations Involving Certain Tax-Exempt Borrowings and Certain Gifts and Grants—An Amendment of FASB Statement No. 34	Complete	Adopt/M	44	835-20
FAS 63	Financial Reporting by Broadcasters	Complete	N/A	App D - NA GAAP	920-10 920-350 920-405 920-440 920-845
FAS 64	Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements—An Amendment of FASB Statement No. 4	Superseded by FAS 145 Complete	 Reject	 15	
FAS 65	Accounting for Certain Mortgage Banking Activities	Complete	N/A	App D - NA GAAP	310-10 440-10 860-50 948-10 948-310 948-340 948-605 948-720 958-320
FAS 66	Accounting for Sales of Real Estate	Complete	Adopt/M	40R	360-20 440-10 460-10 605-10 840-10 976-10 976-310 976-330 976-605 976-705

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FASB STATEMENTS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 67	Accounting for Costs and Initial Rental Operations of Real Estate Projects	Complete	Adopt	40R	970-10 970-340 970-360 970-605 970-720
FAS 68	Research and Development Arrangements	Complete	N/A	App D - NA GAAP	440-10 730-20
FAS 69	Disclosures about Oil and Gas Producing Activities—An Amendment of FASB Statements 19, 25, 33, and 39	Complete	N/A	App D - NA GAAP	932-235
FAS 70	Financial Reporting and Changing Prices: Foreign Currency Translation—An Amendment of FASB Statement No. 33	Superseded by FAS 89			
FAS 71	Accounting for the Effects of Certain Types of Regulation	Complete	N/A	App D - NA GAAP	840-30 980-10 980-250 980-340 980-350 980-405 980-410 980-450 980-470 980-605 980-710 980-810 980-835 980-840
FAS 72	Accounting for Certain Acquisitions of Banking or Thrift Institutions—An Amendment of APB Opinion No. 17, an Interpretation of APB Opinions 16 and 17, and an Amendment of FASB Interpretation No. 9	Superseded by FAS 141R Complete	N/A	App D - NA GAAP	
FAS 73	Reporting a Change in Accounting for Railroad Track Structures—An Amendment of APB Opinion No. 20	Superseded by FAS 154 Complete	N/A	App D - NA GAAP	
FAS 74	Accounting for Special Termination Benefits Paid to Employees	Superseded by FAS 88			
FAS 75	Deferral of the Effective Date of Certain Accounting Requirements for Pension Plans of State and Local Governmental Units—An Amendment of FASB Statement No. 35	Superseded by FAS 135 Complete	N/A	App D - NA GAAP	

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 76	Extinguishment of Debt—An Amendment of APB Opinion No. 26	Superseded by FAS 125 & FAS 140			
FAS 77	Reporting by Transferors for Transfers of Receivables with Recourse	Superseded by FAS 125 & FAS 140			
FAS 78	Classification of Obligations That Are Callable by the Creditor—An Amendment of ARB No. 43, Chapter 3A	Complete	N/A	App D - NA GAAP	470-10
FAS 79	Elimination of Certain Disclosures for Business Combinations by Nonpublic Enterprises—An Amendment of APB Opinion No. 16	Superseded by FAS 141 Complete	 Reject	 68	
FAS 80	Accounting for Futures Contracts	Superseded by FAS 133 Complete	 Reject	 31	
FAS 81	Disclosure of Postretirement Health Care and Life Insurance Benefits	Superseded by FAS 106			
FAS 82	Financial Reporting and Changing Prices: Elimination of Certain Disclosures—An Amendment of FASB Statement No. 33	Superseded by FAS 89			
FAS 83	Designation of AICPA Guides and Statement of Position on Accounting by Brokers and Dealers in Securities, by Employee Benefit Plans, and by Banks as Preferable for Purposes of Applying APB Opinion 20—An Amendment of FASB Statement No. 32 and APB Opinion No. 30 and a Rescission of FASB Interpretation No. 10	Superseded by FAS 111			
FAS 84	Induced Conversions of Convertible Debt—An Amendment of APB Opinion No. 26	Complete	Adopt	15	470-20
FAS 85	Yield Test for Determining whether a Convertible Security Is a Common Stock Equivalent—An Amendment of APB Opinion No. 15	Superseded by FAS 128 Complete	 N/A	 App D - NA GAAP	
FAS 86	Accounting for the Costs of Computer Software to Be Sold, Leased or Otherwise Marketed	Complete	Adopt/M	17	730-10 985-20 985-330 985-705

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 87	Employers' Accounting for Pensions	Complete	Adopt/M	8, 89, 92, 102	420-10 715-10 715-20 715-30 715-80 805-20 835-20 958-715 960-10 962-10 965-10 980-715
FAS 88	Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits	Complete	Adopt/M Adopt paragraph 15	8, 89, 92, 102 11	710-10 712-10 715-30 715-60 958-10 958-715
FAS 89	Financial Reporting and Changing Prices	Complete	N/A	App D - NA GAAP	255-10
FAS 90	Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs—an Amendment of FASB Statement No. 71	Complete	N/A	App D - NA GAAP	980-360 980-835
FAS 91	Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases—An Amendment of FASB Statements No. 13, 60, and 65 and a Rescission of FASB Statement No. 17	Complete	Reject	26R, 37, 43R	310-20 440-10 840-30
FAS 92	Regulated Enterprises—Accounting for Phase-In Plans—An Amendment of FASB Statement No. 71	Complete	N/A	App D - NA GAAP	360-10 980-340
FAS 93	Recognition of Depreciation by Not-for-Profit Organizations	Complete	N/A	App D - NA GAAP	958-360 958-720
FAS 94	Consolidation of All Majority-Owned Subsidiaries—An Amendment of ARB No. 51, with Related Amendments of APB Opinion No. 18 and ARB No. 43, Chapter 12	Complete	Reject	3	810-10 840-10
FAS 95	Statement of Cash Flows	Complete	Reject	69	230-10 310-10 815-10 815-20 830-230 942-230
FAS 96	Accounting for Income Taxes	Superseded by FAS 109			

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 97	Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments	Complete	Reject	50, 51R, 52, 71	944-20 944-30 944-40 944-60 944-605 944-825
FAS 98	Accounting for Leases: Sale-Leaseback Transactions Involving Real Estate, Sales-Type Leases of Real Estate, Definition of the Lease Term, and Initial Direct Costs of Direct Financing Leases—An Amendment of FASB Statements No. 13, 66, and 91 and a Rescission of FASB Statement No. 26 and Technical Bulletin No. 79-11	Superseded by ASU 2016-02 Complete	 Adopt paragraphs 1-13, 17-22 (a, b, d & e) Adopt/M paragraphs 22j, 27, 30, and 31 Reject all others N/A	 22 22R	840-40 980-840
FAS 99	Deferral of the Effective Date of Recognition of Depreciation by Not-for-Profit Organizations—An Amendment of FASB Statement No. 93	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification. See FAS 99
FAS 100	Accounting for Income Taxes—Deferral of the Effective Date of FASB Statement No. 96—An Amendment of FASB Statement No. 96	Superseded by FAS 103, FAS 108 & FAS 109			
FAS 101	Regulated Enterprises—Accounting for the Discontinuation of Application of FASB Statement No. 71	Complete	N/A	App D - NA GAAP	980-20
FAS 102	Statement of Cash Flows—Exemption of Certain Enterprises and Classification of Cash Flows from Certain Securities Acquired for Resale—An Amendment of FASB Statement No. 95	Complete	Reject	69	230-10 310-10 960-205 962-205 970-230
FAS 103	Accounting for Income Taxes—Deferral of the Effective Date of FASB Statement No. 96—An Amendment of FASB Statement No. 96	Superseded by FAS 108 & FAS 109			
FAS 104	Statement of Cash Flows—Net Reporting of Certain Cash Receipts and Cash Payments and Classification of Cash Flows From Hedging Transactions—An Amendment of FASB Statement No. 95	Complete	Reject	69	Not Directly Included in Codification. Included as amendments to FAS 95

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 105	Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk	Superseded by FAS 133 Complete	 Adopt/M	 27, 31	
FAS 106	Employers' Accounting for Postretirement Benefits Other Than Pensions	Complete	Adopt/M	14, 92	420-10 710-10 715-10 715-20 715-30 715-60 715-70 715-80 805-20 958-715 980-715
FAS 107	Disclosures about Fair Value of Financial Instruments	Complete	Adopt	100R	310-10 825-10 942-470 958-320
FAS 108	Accounting for Income Taxes—Deferral of the Effective Date of FASB Statement No. 96	Superseded by FAS 109			
FAS 109	Accounting for Income Taxes	Superseded by ASU 2016-02 Complete	 Adopt paragraphs 256-258 Adopt/M N/A	 22 10, 10R, 101 22R	225-20 272-10 450-10 718-740 740-10 740-20 740-30 805-740 830-20 830-740 840-30 852-740 942-740 944-740 946-740 958-720 980-740 995-740
FAS 110	Reporting by Defined Benefit Pension Plans of Investment Contracts—An Amendment of FASB Statement No. 35	Complete	N/A	App D - NA GAAP	960-325
FAS 111	Rescission of FASB Statement No. 32 and Technical Corrections	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Technical Amendments to Various Standards

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 112	Employers' Accounting for Postemployment Benefits—An Amendment of FASB Statements No. 5 and 43	Complete	Adopt	11	420-10 712-10
FAS 113	Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts	Complete	Adopt/M	61R, 62R	450-10 944-20 944-30 944-40 944-210 944-310 944-340 944-405 944-605 944-825
FAS 114	Accounting by Creditors for Impairment of a Loan—An Amendment of FASB Statements No 5 and 15	Complete	Adopt FAS 5 amendments and para-graphs 35 and 36 of CON 6 Adopt paragraphs 9, 22, and 25 Reject paragraphs 6d, 13 & 21 Adopt/M	5R 36 37	310-10 310-30 310-40
FAS 115	Accounting for Certain Investments in Debt and Equity Securities	Complete	Reject	26R, 30R, 32, 43R	320-10 942-320
FAS 116	Accounting for Contributions Received and Contributions Made	Complete	Adopt	67	440-10 605-10 720-25 835-10 958-10 958-30 958-205 958-310 958-320 958-325 958-360 958-450 958-605
FAS 117	Statements of Not-for-Financial-Profit Organizations	Complete	N/A	App D - NA GAAP	954-225 958-205 958-210 958-225 958-230 958-320 958-720

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FASB STATEMENTS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 118	Accounting by Creditors for Impairment of a Loan-Income Recognition and Disclosures	Complete	Adopt for troubled debt re-structuring Adopt/M	36 37	310-10 310-40
FAS 119	Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments	Superseded by FAS 133 Complete	Adopt/M	31, 100R	
FAS 120	Accounting and Reporting by Mutual Life Insurance Enterprises and by Insurance Enterprises for Certain Long-Duration Participating Contracts	Complete	Reject	50, 51R, 52	944-20
FAS 121	Accounting for Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of	Superseded by FAS 144 Complete	Adopt/M Adopt paragraphs 12,14a & 14b Reject, paragraphs 13,14c & d	40R 68	
FAS 122	Accounting for Mortgage Servicing Rights	Superseded by FAS 125 & FAS 140			
FAS 123	Accounting for Stock-Based Compensation	Superseded by FAS 123(R) Complete	Reject	13	
FAS 123(R)	Share-Based Payment	Complete	Adopt/M	104R	260-10 505-60 718-10 718-20 718-30 718-50 718-740 815-10
FAS 124	Accounting for Certain Investments Held by Not-For-Profit Organizations	Complete	N/A	App D - NA GAAP	954-320 958-205 958-320 958-325

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FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 125	Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities	Superseded by FAS 140 Complete	 Reject paragraph 83 Adopt 9-13 15-17,23-25 27-30,66-71 Reject paragraph 14 Adopt/M For Securiti-zations Adopt/M	 42 45 33 18	
FAS 126	Exemption from Certain Required Disclosures about Financial Instruments for Certain Nonpublic Entities	Complete	Reject	100R	825-10
FAS 127	Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125	Superseded by FAS 140 Complete	 Reject	 18	
FAS 128	Earnings per Share	Complete	N/A	App D - NA GAAP	205-20 250-10 260-10
FAS 129	Disclosure of Information about Capital Structure	Complete	Adopt paragraphs 6, 7 and 9, rejecting all others	72	470-10 505-10
FAS 130	Reporting Comprehensive Income	Complete	N/A	App D - NA GAAP	205-10 220-10 323-10 505-10 715-30 965-205
FAS 131	Disclosures about Segments of an Enterprise and Related Information	Complete	N/A	App D - NA GAAP	280-10

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 132	Employers' Disclosures about Pensions and Other Postretirement Benefits an amendment of FASB Statements No. 87, 88 and 106	Superseded by FAS 132(R) Complete	 Adopt/M	 8, 11, 14, 89	230-10
FAS 132(R)	Employers' Disclosures about Pensions and Other Postretirement Benefits—An Amendment of FASB Statements No. 87, 88 and 106	Complete	Adopt/M Adopt paragraphs 5(a), 5(b), 5(h), 5(q), and 8(m) as modified by FAS 158.	14, 89, 92, 102 11	450-20 715-20 715-70 715-80 958-715
FAS 133	Accounting for Derivative Instruments and Hedging Activities	Complete	Adopt/M Adopt/M regarding short sales	86 103R	220-10 310-10 440-10 815-10 815-15 815-20 815-25 815-30 815-35 960-325
FAS 134	Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise an amendment of FASB Statement No. 65	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included as amendments to FAS 65
FAS 135	Rescission of FASB Statement No. 75 and Technical Corrections	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Technical Amendments to Various Standards
FAS 136	Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others	Complete	N/A	App D - NA GAAP	958-20 958-30 958-205 958-225 958-605
FAS 137	Accounting for Derivative Instruments and Hedging Activities—Deferral of the Effective Date of FASB Statement No. 133	Complete	Reject	86	Not Explicitly Included in Codification. See FAS 133

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 138	Accounting for Certain Derivative Instruments and Certain Hedging Activities—An Amendment of FASB Statement No. 133	Complete	Adopt/M	86	815-10 815-20 815-25 815-30
FAS 139	Rescission of FASB Statement No. 53 and amendments to FASB Statements No. 63, 89 and 121	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included as amendments to FAS 63, FAS 89 and FAS 121
FAS 140	Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, A Replacement of FASB Statement 125	Superseded by FAS 166 Complete	 Adopt/M	 91R, 103R	310-10 320-10 405-20 460-10 470-50 815-20 840-30 860-10 860-20 860-30 860-50
FAS 141	Business Combinations – June 2001	Superseded by FAS 141 revised in 12/07 Complete	 Reject	 68	
FAS 141 (Revised)	Business Combinations – December 2007	Pending			805-10 805-20 805-30 805-40 805-50 805-740 958-805
FAS 142	Goodwill and Other Intangible Assets	Complete	Reject	68	205-20 280-10 323-10 350-10 350-20 350-30
FAS 143	Accounting for Asset Retirement Obligations	Complete	N/A	App D - NA GAAP	360-10 410-20 450-20 835-20 840-10 840-40 980-410

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 144	Accounting for the Impairment or Disposal of Long-Lived Assets	Complete	Reject paragraphs 44.a.-44.c.	24	205-10 205-20 225-20 360-10 840-20 840-30 855-10 958-225 958-360
FAS 145	Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections	Superseded by ASU 2016-02 Complete	 Adopt paragraph 9.c.c. Reject all others N/A	 22 22R	470-50
FAS 146	Accounting for Costs Associated with Exit or Disposal Activities	Superseded by ASU 2016-02 Complete	 Adopt paragraphs 420-10-25-11 through 13 and 420-10-30-8 All others rejected N/A	 22 24 22R	280-10 420-10 450-20 712-10 715-30 840-10 912-275 958-225
FAS 147	Acquisitions of Certain Financial Institutions—An Amendment of FASB Statements No. 72 and 144 and FASB Interpretation No. 9	Superseded by FAS 141(R) Complete	 N/A	 App D - NA GAAP	
FAS 148	Accounting for Stock-Based Compensation—Transition and Disclosure—An Amendment of FASB Statement No. 123	Superseded by FAS 123(R) Complete	 Reject	 13	
FAS 149	Amendment of Statement 133 on Derivative Instruments and Hedging Activities	Complete	Paragraphs 4 and 25 adopted. Reject all others.	86	815-10

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 150	Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity	Complete	Adopted as referenced in SSAP No. 104R only. All other rejected as not applicable.	104R	260-10 460-10 480-10 835-10
FAS 151	Inventory Costs—An Amendment of ARB No. 43, Chapter 4	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included as amendments to ARB 43, Chp 4
FAS 152	Accounting for Real Estate Time-Sharing Transactions—An Amendment of FASB Statements No. 66 and 67	Complete	Adopt	40R	Not Directly Included in Codification. Included as amendments to FAS 66 and FAS 67
FAS 153	Exchanges of Nonmonetary Assets—An Amendment of APB Opinion No. 29	Complete	Adopt/M	90, INT 00-26	Not Directly Included in Codification. Included as amendments to APB 29
FAS 154	Accounting Changes and Error Corrections—A Replacement of APB Opinion No. 20 and FASB Statement No. 3	Complete	Reject	3	250-10 835-20
FAS 155	Accounting for Certain Hybrid Financial Instruments—An Amendment of FASB Statements No. 133 and 140	Pending			815-15
FAS 156	Accounting for Servicing of Financial Assets—An Amendment of FASB Statement No. 140	Complete	Adopt/M	91R, 103R	860-50
FAS 157	Fair Value Measurements	Complete	Adopt/M	100R	250-10 270-10 815-10 820-10
FAS 158	Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—An Amendment of FASB Statements No. 87, 88, 106 and 132(R)	Complete	Adopt/M Paragraphs 1-7, 16-17, Appendices D and E. Adopt/M Paragraphs 1-7, 16-17, Appendices C and E.	92 102	715-20 715-30 715-60 958-715

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB STATEMENTS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FAS 159	The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of FASB Statement No. 115	Complete	Reject	App D - NA GAAP	470-20 825-10 954-825
FAS 160	Noncontrolling Interests in Consolidated Financial Statements—An Amendment of ARB No. 51	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification.
FAS 161	Disclosures about Derivative Instruments and Hedging Activities—An Amendment of FASB Statement No. 133	Pending			815-10
FAS 162	The Hierarchy of Generally Accepted Accounting Principles	Replaced by FAS 168 Complete	Adopt/M	Preamble	
FAS 163	Accounting for Financial Guarantee Insurance Contracts—An Interpretation of FASB Statement No. 60	Pending			944-20 944-40 944-310 944-605
FAS 164	Not-for-Profit Entities: Mergers and Acquisitions—Including an Amendment of FASB Statement No. 142	Pending			740-10 805-10 805-50 954-805 954-810 958-805 958-810
FAS 165	Subsequent Events	Complete	Adopt/M	9	855-10
FAS 166	Accounting for Transfers of Financial Assets—An Amendment of FASB Statement No. 140	Complete (ASU 2009-16)	Adopt/M	103R	860-10
FAS 167	Amendments to FASB Interpretation No. 46(R)	Pending (ASU 2009-17)			810-10
FAS 168	The *FASB Accounting Standards Codification™* and the Hierarchy of Generally Accepted Accounting Principles—A Replacement of FASB Statement No. 162	Complete	Adopt	Preamble	105-10

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB INTERPRETATIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FIN 01 (APB 20)	Accounting Changes Related to the Cost of Inventory	Complete	N/A	App D - NA GAAP	250-10 330-10
FIN 02 (APB 21)	Imputing Interest on Debt Arrangements Made under the Federal Bankruptcy Act	Superseded by FAS 15			
FIN 03 (APB 8)	Accounting for the Cost of Pension Plans subject to the Employee Retirement Income Security Act of 1974	Superseded by FAS 87			
FIN 04 (FASB 2)	Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method	Superseded by FAS 141R Complete	Reject	68	
FIN 05 (FASB 2)	Applicability of FASB Statement No. 2 to Development Stage Enterprises	Superseded by FAS 7			
FIN 06 (FASB 2)	Applicability of FASB Statement No. 2 to Computer Software	Complete	Adopt	17	730-10 985-20
FIN 07 (FASB 7)	Applying FASB Statement No. 7 in Financial Statements of Established Operating Enterprises	Complete	Reject	17	915-10 915-810
FIN 08 (FASB 6)	Classification of a Short-Term Obligation Repaid Prior to Being Replaced by a Long-Term Security	Complete	N/A	App D - NA GAAP	470-10
FIN 09 (APB 16 & 17)	Applying APB Opinions No. 16 and 17 When a Savings and Loan Association or a Similar Institution is Acquired in a Business Combination Accounted for by the Purchase Method	Superseded by FAS 141R Complete	N/A	App D - NA GAAP	
FIN 10 (FASB 12	Application of FASB Statement No. 12 to Personal Financial Statements	Superseded by FAS 83			
FIN 11 (FASB 12)	Changes in Market Value after the Balance Sheet Date	Superseded by FAS 115			
FIN 12 (FASB 12)	Accounting for Previously Established Allowance Accounts	Superseded by FAS 115			
FIN 13 (FASB 12)	Consolidation of a Parent and Its Subsidiaries Having Different Balance Sheet Dates	Superseded by FAS 115			
FIN 14 (FASB 5)	Reasonable Estimation of the Amount of a Loss	Complete	Adopt/M	5R	450-20
FIN 15 (FASB 8)	Translation of Unamortized Policy Acquisition Costs by a Stock Life Insurance Company	Superseded by FAS 52			
FIN 16 (FASB 12)	Clarification of Definitions and Accounting for Marketable Equity Securities That Become Nonmarketable	Superseded by FAS 115			
FIN 17 (FASB 8)	Applying the Lower of Cost or Market Rule in Translated Financial Statements	Superseded by FAS 52			
FIN 18 (APB 28)	Accounting for Income Taxes in Interim Periods	Complete	Reject	10, 10R, 101	225-20 740-270

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB INTERPRETATIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FIN 19 (FASB 13)	Lessee Guarantee of the Residual Value of Leased Property	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	460-10 840-10
FIN 20 (APB 20)	Reporting Accounting Changes under AICPA Statements of Position	Superseded by FAS 154 Complete	 Reject	 3	
FIN 21 (FASB 13)	Accounting for Leases in a Business Combination	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	840-10 840-30 958-805
FIN 22 (APB 11 & 23)	Applicability of Indefinite Reversal Criteria to Timing Differences	Superseded by FAS 96 & FAS 109			
FIN 23 (FASB 13)	Leases of Certain Property Owned by a Governmental Unit or Authority	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	840-10
FIN 24 (FASB 13)	Leases Involving Only Part of a Building	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	840-10
FIN 25 (APB 2, 4, 11, & 16)	Accounting for an Unused Investment Tax Credit	Superseded by FAS 96 & FAS 109			
FIN 26 (FASB 13)	Accounting for Purchase of a Leased Asset by the Lessee during the Term of the Lease	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	840-30

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB INTERPRETATIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FIN 27 (FASB 13 & APB 30)	Accounting for a Loss on a Sublease	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	Glossary Term
FIN 28 (APB 15 & 25)	Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans	Superseded by FAS 123(R) Complete	 Adopt N/A	 13 104R	
FIN 29 (APB 23 & 24)	Reporting Tax Benefits Realized on Disposition of Investments in Certain Subsidiaries and Other Investees	Superseded by FAS 96 & FAS 109			
FIN 30 (APB 29)	Accounting for Involuntary Conversions of Nonmonetary Assets to Monetary Assets	Complete	Adopt/M	28, 95	450-10 605-40 740-10
FIN 31 (APB 15 & FASB 28)	Treatment of Stock Compensation Plans in EPS Computations	Superseded by FAS 128 Complete	 N/A	 App D - NA GAAP	
FIN 32 (APB 2, 4 & 11)	Application of Percentage Limitations in Recognizing Investment Tax Credit	Superseded by FAS 96 & FAS 109			
FIN 33 (FASB 34)	Applying FASB Statement No. 34 to Oil and Gas Producing Operations Accounted for by the Full Cost Method	Complete	N/A	App D - NA GAAP	932-835
FIN 34 (FASB 5)	Disclosure of Indirect Guarantees of Indebtedness of Others	Superseded by FIN 45 Complete	 Adopt	 5R	
FIN 35 (APB 18)	Criteria for Applying the Equity Method of Accounting for Investments in Common Stock	Complete	Adopt	46, 88, 97	323-10
FIN 36 (FASB 19)	Accounting for Exploratory Wells in Progress at the End of a Period	Complete	N/A	App D - NA GAAP	932-360
FIN 37 (FASB 52)	Accounting for Translation Adjustments upon Sale of Part of an Investment in a Foreign Entity	Complete	Reject	23	830-30
FIN 38 (APB 25)	Determining the Measurement Date for Stock Option, Purchase and Award Plans Involving Junior Stock	Superseded by FAS 123(R) Complete	 Adopt N/A	 13 104R	

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
FASB INTERPRETATIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FIN 39 (APB 10 & FASB 105)	Offsetting of Amounts Related to Certain Contracts	Complete	Adopt/M	64	210-20 450-30 815-10
FIN 40 (FASB 12, 60, 97 & 113)	Applicability of Generally Accepted Accounting Principles to Mutual Life Insurance and Other Enterprises	Complete	Reject	51R, 52	Not Directly Included in Codification. Issue Addressed in FAS 168 and APB 22
FIN 41 (APB 10 and FIN 39)	Offsetting of Amounts Related to Certain Repurchase and Reverse Repurchase Agreements	Complete	Reject	64, 103R	210-20 860-30
FIN 42 (FASB 116)	Accounting for Transfers of Assets in Which a Not-for-Profit Organization is Granted Variance Power	Superseded by FAS 136 Complete	 N/A	 App D - NA GAAP	
FIN 43	Real Estate Sales	Complete	Adopt/M	40R, 77	360-20 978-10
FIN 44 (APB 25)	Accounting for Certain Transactions involving Stock Compensation	Superseded by FAS 123(R)	N/A	104R	
FIN 45 (FASB 5, 57 & 107)	Guarantor's Accounting and Disclosure requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others	Complete	Adopt/M	5R	460-10 840-10 850-10
FIN 46 (ARB 51) FIN 46(R)	Consolidation of Variable Interest Entities Consolidation of Variable Interest Entities	Superseded by FIN 46(R) Complete Pending	 Reject	 3	 323-10 712-10 715-30 715-60 810-10 860-10 954-810 958-810
FIN 47 (FASB 143)	Accounting for Conditional Asset Retirement Obligations	Complete	N/A	App D - NA GAAP	410-20 450-20
FIN 48 (FASB 109)	Accounting for Uncertainty in Income Taxes	Complete	Reject	101	740-10 740-270 805-740 835-10

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
APB OPINIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
APB 1	New Depreciation Guidelines and Rules	Superseded by FAS 96 and 109			
APB 2	Accounting for the "Investment Credit"	Complete	Adopt/M paragraphs 9-15, Reject all others	10, 10R, 101	740-10
APB 3	The Statement of Source and Application of Funds	Superseded by APB 19			
APB 4	Accounting for the "Investment Credit" (Amending No. 2)	Complete	Reject	10, 10R, 101	740-10
APB 5	Reporting of Leases in Financial Statements of Lessee	Superseded by FAS 13			
APB 6	Status of Accounting Research Bulletins	Complete	Adopt /M Paragraph 12 Reject all others Reject paragraph 16	72 28, 95	Not Directly Included in Codification. Included as amendments to ARB 43
APB 7	Accounting for Leases in Financial Statements of Lessors	Superseded by FAS 13			
APB 8	Accounting for the Cost of Pension Plans	Superseded by FAS 87			
APB 9	Reporting the Results of Operations	Complete	Reject paragraphs 1-19 and 26-27 Adopt paragraph 28 Paragraphs 20-25 and 29 superseded by APB 20 & 30 and FAS 16	3 72	225-10 225-20 250-10 505-10

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
APB OPINIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
APB 10	Omnibus Opinion—1966	Complete	Adopt paragraphs 10 & 11 Reject paragraph 12 Adopt/M paragraphs 1,7 &13 Adopt paragraph 6 All other paragraphs rejected	72 64 10, 10R, 101	210-20 605-10 740-10
APB 11	Accounting for Income Taxes	Superseded by FAS 96 & 109			
APB 12	Omnibus Opinion—1967	Complete	Adopt paragraphs 4 & 5 Adopt/M paragraphs 9 & 10 Adopt/M paragraphs 2 and 3 Adopt paragraphs 6, 6A and 7 Adopt/M paragraphs 6 - 8 Adopt paragraphs 16 & 17 Paragraphs 11-15 superseded	19 72 5R 11 14 15	210-10 310-10 360-10 505-10 710-10 715-20 835-30
APB 13	Amending Paragraph 6 of APB Opinion No. 9, Application to Commercial Banks	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included as amendments to APB 9

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
APB OPINIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
APB 14	Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants	Complete	Adopt	15	470-20 505-10
APB 15	Earnings Per Share	Superseded by FAS 128 Complete	N/A	App D - NA GAAP	
APB 16	Business Combinations	Superseded by FAS 141 Complete	Reject	68	
APB 17	Intangible Assets	Superseded by FAS 142 Complete	Reject	68	
APB 18	The Equity Method of Accounting for Investments in Common Stock	Complete	Reject	46, 88, 97	225-20 250-10 260-10 323-10 325-20 460-10 810-10 850-10 958-20 958-810 970-810
APB 19	Reporting Changes in Financial Position	Superseded by FAS 95			
APB 20	Accounting Changes	Superseded by FAS 154 Complete	Reject	3	
APB 21	Interest on Receivables and Payables	Complete	Adopt/M	15	310-10 470-10 740-10 835-30
APB 22	Disclosure of Accounting Policies	Complete	Adopt	1	235-10

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
APB OPINIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
APB 23	Accounting for Income Taxes—Special Areas	Complete	Adopt paragraphs 1-3, 5-9, 12-13, 15-18 Reject paragraphs 19-23, 25, 31-33	10R	
			Adopt paragraphs 1-3, 5-9, 12-13, 15-18 Reject paragraphs 19-25, 31-33	101	740-30 942-740
APB 24	Accounting for Income Taxes—Investments in Common Stock Accounted for by the Equity Method (Other than Subsidiaries and Corporate Joint Ventures)	Superseded by FAS 96 & 109			
APB 25	Accounting for Stock Issued to Employees	Superseded by FAS 123(R)			
		Complete	Adopt/M	13	
			N/A	104R	
APB 26	Early Extinguishment of Debt	Complete	Adopt/M	15	470-50 850-10
APB 27	Accounting for Lease Transactions by Manufacturer or Dealer Lessors	Superseded by FAS 13			
APB 28	Interim Financial Reporting	Complete	Adopt paragraphs 19 & 20 Reject all others	10, 10R, 101	225-20 250-10 270-10 450-10 740-270
APB 29	Accounting for Nonmonetary Transactions	Complete Amended by FAS 153	Adopt/M	28, 95	605-40 610-30 845-10
APB 30	Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions	Complete	Reject	24	225-20 830-10
APB 31	Disclosure of Lease Commitments by Lessees	Superseded by FAS 13			

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
ACCOUNTING RESEARCH BULLETINS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
ARB 43	Restatement and Revision of Accounting Research Bulletins:				
	Chapter 1	Complete	Reject	72	310-10 505-10 605-10 850-10
	Chapter 2A	Complete	Adopt	1	205-10
	Chapter 2B	Deleted by APB 9			
	Chapter 3A	Complete	Reject	20	210-10 310-10 340-10 470-10 958-210
	Chapter 3B	Replaced by APB 10			
	Chapter 4	Complete	N/A	App D - NA GAAP	330-10 440-10 450-20
	Chapter 5	Deleted by FAS 142			
	Chapter 6	Deleted by FAS 5			
	Chapter 7A	Complete	Adopt/M	72	852-20
	Chapter 7B	Complete	Adopt paragraphs 1-4 and paragraphs 10-16 Adopt paragraphs 1-9	72 28, 95	505-20
	Chapter 7C	Deleted by ARB 48			
	Chapter 8	Deleted by APB 9			
	Chapter 9A	Complete	Reject	19	Not Explicitly Included in Codification.
	Chapter 9B	Replaced by APB 6			
	Chapter 9C	Complete	Reject	19	360-10
	Chapter 10A	Complete	Reject	40R	720-30
	Chapter 10B	Deleted by APB 11			

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
ACCOUNTING RESEARCH BULLETINS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
ARB 43 continued	Chapter 11	Complete	Reject	20	912-10 912-20 912-210 912-225 912-275 912-310 912-330 912-405 912-605
	Chapter 12	Complete	Reject	23	Not Directly Included in Codification. Issue Addressed in FAS 133
	Chapter 13A	Deleted by APB 8			
	Chapter 13B	Deleted by FAS 123(R)			
		Complete	Adopt/M N/A	13 104R	
	Chapter 14	Deleted by APB 5			
	Chapter 15	Deleted by APB 26			
ARB 44	Declining-Balance Depreciation	Superseded by ARB 44 (Rev.)			
ARB 44 (Rev.)	Declining-Balance Depreciation	Superseded by FAS 96 & 109			
ARB 45	Long-Term Construction-Type Contracts	Complete	N/A	App D - NA GAAP	440-10 605-35
ARB 46	Discontinuance of Dating Earned Surplus	Complete	Adopt/M	72	Not Directly Included in Codification. Included as amendments to ARB 43, Chapter 7a
ARB 47	Accounting for Costs of Pension Plans	Superseded by APB 8			
ARB 48	Business Combinations	Superseded by APB 16			
ARB 49	Earnings per Share	Superseded by APB 9			
ARB 50	Contingencies	Superseded by FAS 5			

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PRE-CODIFICATION STANDARDS - CATEGORY A GAAP
ACCOUNTING RESEARCH BULLETINS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
ARB 51	Consolidated Financial Statements	Complete	Reject	3	505-10 810-10 850-10 860-10 958-810 970-810

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PRE-CODIFICATION STANDARDS – CATEGORY B GAAP
FASB TECHNICAL BULLETINS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
TB79-1 (Revised)	Purpose and Scope of FASB Technical Bulletins and Procedures for Issuance	Complete	N/A	App D - NA GAAP	Not Included in Codification. No Longer Applicable or Relevant.
TB79-2	Computer Software Costs	Superseded by FAS 86			
TB79-3	Subjective Acceleration Clauses in Long-Term Debt Agreements	Complete	N/A	App D - NA GAAP	470-10
TB79-4	Segment Reporting of Puerto Rican Operations	Complete	N/A	App D - NA GAAP	280-10
TB79-5	Meaning of the Term "Customer" as it Applies to Health Care Facilities under FASB Statement No. 14	Complete	N/A	App D - NA GAAP	954-280
TB79-6	Valuation Allowances Following Debt Restructuring	Superseded by FAS 114			
TB79-7	Recoveries of a Previous Writedown under a Troubled Debt Restructuring Involving a Modification of Terms	Superseded by FAS 114			
TB79-8	Applicability of FASB Statements 21 and 33 to Certain Brokers and Dealers in Securities	Superseded by FAS 131 Complete	N/A	App D - NA GAAP	
TB79-9	Accounting in Interim Periods for Changes in Income Tax Rates	Complete	Reject	10, 10R, 101	740-270
TB79-10	Fiscal Funding Clauses in Lease Agreements	Superseded by ASU 2016-02 Complete	Reject N/A	22 22R	840-10
TB79-11	Effect of a Penalty on the Term of a Lease	Superseded by FAS 98			
TB79-12	Interest Rate used in Calculating the Present Value of Minimum Lease Payments	Superseded by ASU 2016-02 Complete	Reject N/A	22 22R	Glossary Terms

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PRE-CODIFICATION STANDARDS – CATEGORY B GAAP
FASB TECHNICAL BULLETINS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
TB79-13	Applicability of FASB Statement No. 13 to Current Value Financial Statements	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	840-10
TB79-14	Upward Adjustment of Guaranteed Residual Values	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	840-30
TB79-15	Accounting for Loss on a Sublease Not Involving the Disposal of a Segment	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	840-20 840-30
TB79-16 (Revised)	Effect of a Change in Income Tax Rate on the Accounting for Leveraged Leases	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	840-30
TB79-17	Reporting Cumulative Effect Adjustment from Retroactive Application of FASB Statement No. 13	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	Not Explicitly Included in Codification. See FAS 13
TB79-18	Transition Requirement of Certain FASB Amendments and Interpretations of FASB Statement No. 13	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	Not Explicitly Included in Codification. See FAS 13
TB79-19	Investor's Accounting for Unrealized Losses on Marketable Securities Owned by an Equity Method Investee	Complete	Reject	46, 88, 97	Not Directly Included in Codification. Included within FAS 115 and FAS 133
TB80-1	Early Extinguishment of Debt through Exchange for Common or Preferred Stock	Complete	Adopt/M	15	470-50
TB80-2	Classification of Debt Restructurings by Debtors and Creditors	Complete	Adopt	36	310-40 470-60

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PRE-CODIFICATION STANDARDS – CATEGORY B GAAP
FASB TECHNICAL BULLETINS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
TB81-1	Disclosure of Interest Rate Futures Contracts and Forward and Standby Contracts	Superseded by FAS 80			
TB81-2	Accounting for Unused Investment Tax Credits Acquired in a Business Combination Accounted for by the Purchase Method	Superseded by FAS 96 & FAS 109			
TB81-3	Multi-Employer Pension Plan Amendments Act of 1980	Superseded by FAS 111			
TB81-4	Classification as Monetary or Non-monetary Items	Superseded by FAS 89			
TB81-5	Offsetting Interest Cost to Be Capitalized with Interest Income	Superseded by FAS 62			
TB81-6	Applicability of Statement 15 to Debtors in Bankruptcy Situations	Complete	Adopt	36	470-60
TB82-1	Disclosure of the Sale or Purchase of Tax Benefits through Tax Leases	Complete	Adopt	10, 10R, 101	Not Directly Included in Codification. Included within FAS 109, APB 22 and APB 30
TB82-2	Accounting for the Conversion of Stock Options into Incentive Stock Options as a Result of the Economic Recovery Tax Act of 1981	Superseded by FAS 123 and 123(R) Complete	N/A	App D - NA GAAP	
TB83-1	Accounting for the Reduction in the Tax Basis of an Asset Caused by the Investment Tax Credit	Superseded by FAS 96 & FAS 109			
TB84-1	Accounting for Stock Issued to Acquire the Results of a Research and Development Arrangement	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within FAS 141R
TB84-2	Accounting for the Effects of the Tax Reform Act of 1984 on Deferred Income Taxes Relating to Domestic International Sales Corporations	Superseded by FAS 96 & FAS 109			
TB84-3	Accounting for the Effects of the Tax Reform Act of 1984 on Deferred Income Taxes of Stock Life Insurance Enterprises	Superseded by FAS 96 & FAS 109			
TB84-4	In-Substance Defeasance of Debt	Superseded by FAS 125 & FAS 140			
TB85-1	Accounting for the Receipt of Federal Home Loan Mortgage Corporation Participating Preferred Stock	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within APB 29

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PRE-CODIFICATION STANDARDS – CATEGORY B GAAP
FASB TECHNICAL BULLETINS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
TB85-2	Accounting for Collateralized Mortgage Obligations (CMOs)	Superseded by FAS 125 & FAS 140			
TB85-3	Accounting for Operating Leases with Scheduled Rent Increases	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	840-20
TB85-4	Accounting for Purchases of Life Insurance	Complete	Adopt/M	21R	325-30
TB85-5	Issues Relating to Accounting for Business Combinations, Including Costs of Closing Duplicate Facilities of an Acquirer, Stock Transactions between Companies under Common Control, Downstream Mergers, Identical Common Shares for a Pooling of Interests, and Pooling of Interests by Mutual and Cooperative Enterprises	Superseded by FAS 141R Complete	 Reject	 68	
TB85-6	Accounting for a Purchase of Treasury Shares at a Price Significantly in Excess of the Current Market Price of the Shares and the Income Statement Classification of Costs Incurred in Defending Against a Takeover Attempt	Complete	Reject	72	225-20 505-30
TB86-1	Accounting for Certain Effects of the Tax Reform Act of 1986	Superseded by FAS 96 & FAS 109			
TB86-2	Accounting for an Interest in the Residual Value of a Leased Asset Acquired by a Third Party or Retained by a Lessor That Sells the Related Minimum Rental Payments	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	360-10 840-30
TB87-1	Accounting for a Change in Method of Accounting for Certain Postretirement Benefits	Superseded by FAS 106			
TB87-2	Computation of a Loss on an Abandonment	Complete	N/A	App D - NA GAAP	980-360 980-740
TB87-3	Accounting for Mortgage Servicing Fees and Rights	Complete	N/A	App D - NA GAAP	860-50

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PRE-CODIFICATION STANDARDS – CATEGORY B GAAP
FASB TECHNICAL BULLETINS

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
TB88-1	Issues Relating to Accounting for Leases: Time Pattern of the Physical Use of the Property in an Operating Lease, Lease Incentives in an Operating Lease, Applicability of Leveraged Lease Accounting to Existing Assets of the Lessor, Money-Over-Money Lease Transactions, and Wrap Lease Transactions	Superseded by ASU 2016-02 Complete	 Adopt paragraphs 1—12 Reject all others N/A	 22 22R	840-10 840-20 840-30 840-40
TB88-2	Definition of a Right of Setoff	Superseded by FIN 39			
TB90-1	Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts	Complete	N/A	App D - NA GAAP	460-10 605-20
TB94-1	Application of Statement 115 to Debt Securities Restructured in a Troubled Debt Restructuring	Complete	Reject	36	320-10
TB97-1	Accounting under Statement 123 for Certain Employee Stock Purchase Plans with a Look-Back Option (Amended with FAS 123(R) - not superseded.)	Complete	Adopt/M	104R	718-50
TB01-1	Effective Date for Certain Financial Institutions of Certain Provisions of Statement 140 Related to the Isolation of Transferred Financial Assets	Complete	Reject	91R, 103R	Glossary Terms

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP FAS 13-1	Accounting for Rental Costs Incurred during a Construction Period	Not Board Directed			840-20
FSP FAS 13-2	Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	Not Directly Included in Codification. Included within FAS 13
FSP FAS 19-1	Accounting for Suspended Well Costs	Complete	N/A	App D - NA GAAP	932-360
FSP FAS 97-1	FSP FAS 97-1—Situations in Which Paragraphs 17(b) and 20 of FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments, Permit or Require Accrual of an Unearned Revenue Liability	Not Board Directed			944-605
FSP FAS 106-1	Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003	Superseded by FSP FAS 106-2			
FSP FAS 106-2	Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003	Complete	Adopt/M	INT 04-17	715-60 740-10
FSP FAS 107-1 and APB 28-1	Interim Disclosures about Fair Value of Financial Instruments	Complete	Adopt	100R	Not Explicitly Included in Codification.
FSP FAS 109-1	Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004	Complete	Adopt	101	740-10
FSP FAS 109-2	Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004	Complete	Reject	App D - NA GAAP	Not Explicitly Included in Codification. See FAS 109

[2] On December 5, 2009, the Statutory Accounting Principles (E) Working Group adopted revisions to the NAIC *Accounting Practices and Procedures Manual* to refer to the FASB Accounting Standards Codification as prescribed in *FAS 168, FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles* (FAS 168). With the issuance of FAS 168, and the establishment of the FASB Codification, the previous GAAP hierarchy established in *FAS 162, The Hierarchy of Generally Accepted Accounting Principles* (FAS 162) has been eliminated. As a result of FAS 168, the FASB Accounting Standards Codification is the source of authoritative accounting principles recognized by the FASB. (SEC guidance included within the codification is provided for convenience and relates only to SEC entities.) Pursuant to previous decisions by the Statutory Accounting Principles (E) Working Group, FASB Staff Positions (FSPs) issued after May 9, 2008, will be reviewed as part of the statutory accounting maintenance review process. FSPs issued prior to May 9, 2008, will be reviewed as part of the maintenance process if considered to be "Board-directed". (Board-directed FSPs were issued to provide narrow and limited revisions to the FASB statements or FASB interpretations formerly provided in FASB Technical Bulletins.) FSPs that were not considered "Board-directed" were considered to provide application guidance similar to that found in FASB Staff Implementation Guides and Staff Announcements and were previously classified (pre-FAS 162) as NAIC Level 5 guidance. Due to this Level 5 classification, these FSPs were not reviewed as part of the statutory accounting maintenance review process.

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP FAS 115-1 and FAS 124-1	The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments	Complete	Adopt/M	26R, 32, 34 INT 06-07	320-10 325-20 958-325
FSP FAS 115-2 and 124-2	Recognition and Presentation of Other-Than-Temporary Impairments	Pending			320-10
FSP FAS 117-1	Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds	Complete	N/A	App D - NA GAAP	958-205
FSP FAS 123(R)-1	Classification and Measurement of Freestanding Financial Instruments Originally Issued in Exchange for Employee Services under FASB Statement No. 123(R)	Complete	Adopt/M	104R	718-10
FSP FAS 123(R)-2	Practical Accommodation to the Application of Grant Date as Defined in FASB Statement No. 123(R)	Not Board Directed Complete	Adopt/M	104R	718-10
FSP FAS 123(R)–3	Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards	Not Board Directed Complete	Rejected	104R	Not Explicitly Included in Codification. See FAS 123R
FSP FAS 123(R)-4	Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event	Complete	Adopt/M	104R	718-10
FSP FAS 123(R)-5	Amendment of FASB Staff Position FAS 123(R)-1	Complete	Adopt/M	104R	Not Directly Included in Codification. Included within FAS 123R-1
FSP FAS 123(R)-6	Technical Corrections of FASB Statement No. 123(R)	Complete	Adopt/M	104R	Not Directly Included in Codification. Included within FAS 123R
FSP FAS 126-1	Applicability of Certain Disclosure and Interim Reporting Requirements for Obligors for Conduit Debt Securities	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within APB 28, FAS 69, FAS 109, FAS 126, FAS 131, FAS 132R and 141R

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP FAS 129-1	Disclosure Requirements under FASB Statement No. 129 Relating to Contingently Convertible Securities	Not Board Directed			470-10 505-10 815-10
FSP FAS 132(R)-1	Employers' Disclosures about Postretirement Benefit Plan Assets	Complete	Revisions to paragraph 5d of FAS 132 adopted. Reject all others.	92, 102	Not Explicitly Included in Codification.
FSP FAS 133-1 and FIN 45-4	Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45; and Clarification of the Effective Date of FASB Statement No. 161	Complete	Adopt	86, 5R	Not Explicitly Included in Codification.
FSP FAS 140-1	Accounting for Accrued Interest Receivable Related to Securitized and Sold Receivables under FASB Statement No. 140	Not Board Directed			860-20
FSP FAS 140-2	Clarification of the Application of Paragraphs 40(b) and 40(c) of FASB Statement No. 140	Not Board Directed			Not Explicitly Included in Codification.
FSP FAS 140-3	Accounting for Transfers of Financial Assets and Repurchase Financing Transactions	Complete	Adopt	91R, 103R	860-10
FSP FAS 140-4 and FIN 46(R)-8	Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities	Superseded by ASU 2009-17			*810-10*
FSP FAS 141-1 & 142-1	Interaction of FASB Statements No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets, and EITF Issue No. 04-2, Whether Mineral Rights Are Tangible or Intangible Assets	Superseded by FAS 141R Complete	Reject	68	
FSP FAS 141R-1	Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies	Pending			805-10 805-20 805-30
FSP FAS 142-2	Application of FASB Statement No. 142 to Oil- and Gas-Producing Entities	Not Board Directed			932-350
FSP FAS 142-3	Determination of the Useful Life of Intangible Assets	Complete	Reject	68	275-10 350-30
FSP FAS 143-1	Accounting for Electronic Equipment Waste Obligations	Complete	N/A	App D - NA GAAP	410-20 720-40
FSP FAS 144-1	Determination of Cost Basis for Foreclosed Assets under FASB Statement No. 15 and the Measurement of Cumulative Losses Previously Recognized under Paragraph 37 of FASB Statement No. 144	Not Board Directed			310-40
FSP FAS 146-1	Determining Whether a One-Time Termination Benefit Offered in Connection with an Exit or Disposal Activity Is, in Substance, an Enhancement to an Ongoing Benefit Arrangement	Not Board Directed			420-10 715-30

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP FAS 150-1	Issuer's Accounting for Freestanding Financial Instruments Composed of More Than One Option or Forward Contract Embodying Obligations under FASB Statement No. 150	Not Board Directed			480-10
FSP FAS 150-2	Accounting for Mandatorily Redeemable Shares Requiring Redemption by Payment of an Amount that Differs from the Book Value of Those Shares under FASB Statement No. 150	Not Board Directed			480-10
FSP FAS 150-3	Effective Date, Disclosures, and Transition for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests under FASB Statement No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity	Complete	N/A	App D - NA GAAP	480-10
FSP FAS 150-4	Issuers' Accounting for Employee Stock Ownership Plans under FASB Statement No. 150	Not Board Directed			480-10
FSP FAS 150-5	Issuer's Accounting under FASB Statement No. 150 for Freestanding Warrants and Other Similar Instruments on Shares that are Redeemable	Complete	N/A	App D - NA GAAP	480-10
FSP FAS 157-1	Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13	Complete	Adopt/M	100R	Not Directly Included in Codification. Included within FAS 157 and FAS 13
FSP FAS 157-2	Effective Date of FASB Statement No. 157	Complete	Reject	100R	Not Explicitly Included in Codification.
FSP FAS 157-3	Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active	Superseded by FSP FAS 157-4 Complete	 Reject	 100R	Not Explicitly Included in Codification.
FSP FAS 157-4	Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly	Complete	Adopt/M	100R	Not Explicitly Included in Codification.
FSP FAS 158-1	Conforming Amendments to the Illustrations in FASB Statements No. 87, No. 88, and No. 106 and to the Related Staff Implementation Guides	Not Board Directed Complete	 Adopt/M	 92, 102	Not Directly Included in Codification. Included within FAS 87, FAS 88 and FAS 106

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP FIN 39-1	Amendment of FASB Interpretation No. 39	Complete	Reject	64, 86	Not Directly Included in Codification. Included within FIN 39
FSP FIN 45-1	Accounting for Intellectual Property Infringement Indemnifications under FASB Interpretation No. 45	Not Board Directed			460-10
FSP FIN 45-2	Whether FASB Interpretation No. 45 Provides Support for Subsequently Accounting for a Guarantor's Liability at Fair Value	Not Board Directed			460-10
FSP FIN 45-3	Application of FASB Interpretation No. 45 to Minimum Revenue Guarantees Granted to a Business or Its Owners	Complete	Adopt/M	5R	460-10 954-460
FSP FIN 46(R)-1	Reporting Variable Interests in Specified Assets of Variable Interest Entities as Separate Variable Interest Entities under Paragraph 13 of FASB Interpretation No. 46 (revised December 2003)	Not Board Directed			810-10
FSP FIN 46(R)-2	Calculation of Expected Losses under FASB Interpretation No. 46 (revised December 2003)	Not Board Directed			810-10
FSP FIN 46(R)-3	Evaluating Whether, as a Group, the Holders of the Equity Investment at Risk Lack the Direct or Indirect Ability to Make Decisions about an Entity's Activities through Voting Rights or Similar Rights under FASB Interpretation No. 46 (revised December 2003)	Not Board Directed			810-10 952-810
FSP FIN 46(R)-4	Technical Correction of FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities, Relating to Its Effects on Question No. 12 of EITF Issue No. 96-21, “Implementation Issues in Accounting for Leasing Transactions involving Special-Purpose Entities”	Pending			
FSP FIN 46(R)-5	Implicit Variable Interests under FASB Interpretation No. 46 (revised December 2003)	Pending			810-10
FSP FIN 46(R)-6	Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R)	Not Board Directed			810-10
FSP FIN 46(R)-7	Application of FASB Interpretation No. 46(R) to Investment Companies	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within FIN 46R
FSP FIN 48-1	Definition of Settlement in FASB Interpretation No. 48	Pending			740-10

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP FIN 48-2	Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises	Complete	Reject	101	Not Explicitly Included in Codification. See FIN 48
FSP FIN 48-3	Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises	Complete	Reject	101	Not Explicitly Included in Codification.
FSP APB 14-1	Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)	Pending			470-20 815-15 825-10
FSP APB 18-1	Accounting by an Investor for Its Proportionate Share of Accumulated Other Comprehensive Income of an Investee Accounted for under the Equity Method in Accordance with APB Opinion No. 18 upon a Loss of Significant Influence	Complete	Reject	88, 97	323-10 323-30
FSP FTB 85-4-1	Accounting for Life Settlement Contracts by Third-Party Investors	Pending			325-30
FSP EITF 85-24-1	Application of EITF Issue No. 85-24 When Cash for the Right to Future Distribution Fees for Shares Previously Sold is Received from Third Parties	Complete	N/A	App D - NA GAAP	946-605
FSP EITF 99-20-1	Amendments to the Impairment Guidance of EITF Issue No. 99-20	Complete	Adopt	43R	Not Explicitly Included in Codification.
FSP EITF 00-19-1	Application of EITF Issue No. 00-19 to Freestanding Financial Instruments Originally Issued as Employee Compensation	Superseded by FSP FAS 123(R)-1			
FSP EITF 00-19-2	Accounting for Registration Payment Arrangements	Complete	Adopt/M	5R	470-20 815-10 815-40 825-20
FSP EITF 03-1-1	Effective Date of Paragraphs 10–20 of EITF Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments	Superseded by FSP FAS 115-1/124-1 Complete	 Reject	 INT 06-07	
FSP EITF 03-6-1	Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities	Complete	Reject	104R	260-10
FSP AAG INV-1 and SOP 94-4-1	Reporting of Fully Benefit-Responsive Investment Contracts Held by Certain Investment Companies Subject to the AICPA Investment Company Guide and Defined-Contribution Health and Welfare and Pension Plans	Complete	N/A	App D - NA GAAP	946-205 946-210
FSP AUG AIR-1	Accounting for Planned Major Maintenance Activities	Complete	N/A	App D - NA GAAP	340-10 360-10 908-360
FSP SOP 78-9-1	Interaction of AICPA Statement of Position 78-9 and EITF Issue No. 04-5	Complete	N/A	App D - NA GAAP	970-810

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
FASB STAFF POSITIONS[2]

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
FSP SOP 90-7-1	An Amendment of AICPA Statement of Position 90-7	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within SOP 90-1
FSP SOP 94-3-1 and AAG HCO-1	Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations	Complete	N/A	App D - NA GAAP	958-810
FSP SOP 94-6-1	Terms of Loan Products That May Give Rise to a Concentration of Credit Risk	Not Board Directed			310-10 825-10
FSP SOP 07-1-1	Effective Date of AICPA Statement of Position 07-1	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within SOP 07-1

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA INDUSTRY AUDIT & ACCOUNTING GUIDES

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
	Audits of Stock Life Insurance Companies	Complete	Reject	51R, 52	944 – Financial Services - Insurance
	Audits of Property and Liability Insurance Companies	Complete	Reject	65	944 – Financial Services - Insurance
	Audits of Health Care Organizations	Complete	Reject	73	954 – Health Care Entities

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
14,040	Confirmation of Insurance Policies in Force	Withdrawn Complete	N/A	App D - NA GAAP	
14,060	Auditing Property and Liability Reinsurance	Withdrawn Complete	N/A	App D - NA GAAP	
14,070	Auditing Life Reinsurance	Withdrawn Complete	N/A	App D - NA GAAP	
74-6	Withdrawn 1985				
74-8	Superseded 1996	Complete	N/A	App D - NA GAAP	
74-11	Superseded 1987				
74-12	Withdrawn 1985				
75-1	Withdrawn 1981				
75-2	Accounting Practices of Real Estate Investment Trusts	Complete	N/A	App D - NA GAAP	974-10 974-605 974-835
75-3	Superseded 1986				
75-4	Superseded 1986				
75-5	Withdrawn 1985				
75-6	Withdrawn 1985				
76-1	Withdrawn 1985				
76-2	Withdrawn 1985				
76-3	Accounting Practices for Certain Employee Stock Ownership Plans	Complete	N/A	App D - NA GAAP	Grandfathered 105-10-70-2c
77-1	Superseded 1987				
77-2	Superseded 1986				
78-1	Superseded 1990				
78-2	Superseded 1993				
78-3	Withdrawn 1985				
78-4	Withdrawn 1985				
78-5	Withdrawn 1985				
78-6	Withdrawn 1985				
78-7	Superseded 1986				
78-8	Withdrawn 1981				
78-9	Accounting for Investments in Real Estate Ventures	Complete	Reject	48	320-10 323-30 970-323 970-605 970-810 970-835

[3] As of September 15, 2009, AICPA Statements of Position are no longer reviewed as part of the statutory maintenance process as they are no longer considered authoritative GAAP literature. If the AICPA were to address an issue that affects the FASB Codification, an accounting standard update (ASU) would be issued and reviewed for applicability to statutory accounting. Therefore, this table will no longer be updated after SOP 09-1.

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
78-10	Superseded 1996	Complete	N/A	App D - NA GAAP	
79-1	Superseded 1987				
79-2	Withdrawn 1985				
79-3	Withdrawn 1985				
79-4	Withdrawn 1985				
80-1	Withdrawn 1985				
80-2	Superseded l986				
80-3	Withdrawn 1985				
81-1	Accounting for Performance of Construction-Type and Certain Production-Type Contracts	Complete	N/A	App D - NA GAAP	210-10 460-10 605-35 910-20 912-20
81-2	Superseded 1990				
82-1	Accounting and Financial Reporting for Personal Financial Statements	Complete	N/A	App D - NA GAAP	274-10
83-1	Reporting by Banks of Investment Securities Gains or Losses	Superseded Complete	N/A	App D - NA GAAP	
85-1	Superseded 1990				
85-2	Superseded 1991				
85-3	Accounting by Agricultural Producers and Agricultural Cooperatives	Complete	N/A	App D - NA GAAP	905-10 905-205 905-310 905-325 905-330 905-360 905-405 905-605
86-1	Superseded 1991				
87-1	Superseded 1990				
87-2	Accounting for Joint Costs of Informational Materials and Activities of Not-For-Profit Organizations That Include a Fund-Raising Appeal	Superseded Complete	N/A	App D - NA GAAP	
88-1	Accounting for Developmental and Preoperating Costs, Purchases and Exchanges of Take-off and Landing Slots, and Airframe Modifications	Complete	N/A	App D - NA GAAP	908-350 908-360 908-720 908-845
88-2	Superseded 1991				
89-1	Superseded 1997				
89-2	Reports on Audited Financial Statements of Investment Companies	Withdrawn Complete	N/A	App D - NA GAAP	

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
89-3	Questions Concerning Accountants' Services on Prospective Financial Statements	Withdrawn Complete	N/A	App D - NA GAAP	
89-4	Superseded 1997				
89-5	Superseded 1996				
89-6	Superseded 1992				
89-7	Report on the Internal Control Structure in Audits of Investment Companies	Withdrawn Complete	N/A	App D - NA GAAP	
90-1	Accountants' Services on Prospective Financial Statements for Internal Use Only and Partial Presentations	Withdrawn Complete	N/A	App D - NA GAAP	
90-2	Report on Internal Control Structure in Audits of Futures Commission Merchants	Withdrawn Complete	N/A	App D - NA GAAP	
90-3	Definition of Term Substantially the Same for Holders of Debt Instruments, as Used in Certain Audit Guides and a Statement of Position	Complete	Adopt	18, 45, 91R, 103R	860-10
90-4	Superseded 1992				
90-5	Superseded 1996				
90-6	Superseded 1996				
90-7	Financial Reporting by Entities in Reorganization Under the Bankruptcy Code	Complete	N/A	App D - NA GAAP	210-10 852-10 852-20 852-740
90-8	Financial Accounting and Reporting by Continuing Care Retirement Communities	Superseded Complete	N/A	App D - NA GAAP	
90-9	Superseded 1992				
90-10	Superseded 1995				
90-11	Disclosure of Certain Information by Financial Institutions About Debt Securities Held as Assets	Superseded Complete	Adopt	26R	
91-1	Software Revenue Recognition	Superseded Complete	N/A	App D - NA GAAP	
92-1	Accounting for Real Estate Syndication Income	Complete	Adopt	40R	970-605
92-2	Questions and Answers on the Term Reasonably Objective Basis and Other Issues Affecting Prospective Financial Statements	Withdrawn Complete	N/A	App D - NA GAAP	
92-3	Accounting for Foreclosed Assets	Superseded Complete	Adopt	40R	

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
92-4	Auditing Insurance Entities Loss Reserves	Withdrawn Complete	 Reject	 55	
92-5	Accounting for Foreign Property and Liability Reinsurance	Complete	Reject	62R	944-605
92-6	Accounting and Reporting by Health and Welfare Benefit Plans	Complete	N/A	App D - NA GAAP	962-325 965-10 965-20 965-30 965-40 965-205 965-310 965-320 965-325 965-360
92-7	Superseded 1994				
92-8	Auditing Property/Casualty Insurance Entities Statutory Financial Statements—Applying Certain Requirements of the NAIC Annual Statement Instructions	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
92-9	Audits of Not-for-Profit Organizations Receiving Federal Awards	Superseded Complete	 N/A	 App D - NA GAAP	
93-1	Financial Accounting and Reporting for High-Yield Debt Securities by Investment Companies	Complete	N/A	App D - NA GAAP	450-20 946-320
93-2	Determination, Disclosure, and Financial Statement Presentation of Income, Capital Gain, and Return of Capital Distributions by Investment Companies	Superseded Complete	 N/A	 App D - NA GAAP	
93-3	Rescission of Accounting Principles Board Statements	Complete	N/A	App D - NA GAAP	255-10
93-4	Foreign Currency Accounting and Financial Statement Presentation for Investment Companies	Complete	N/A	App D - NA GAAP	946-830
93-5	Reporting on Required Supplementary Information Accompanying Compiled or Reviewed Financial Statements of Common Interest Realty Associations	Withdrawn Complete	 N/A	 App D - NA GAAP	
93-6	Employers' Accounting for Employee Stock Ownership Plans	Complete	Adopt/M Reject paragraphs 28-34, 37, 44 & 53.b. Adopt/M paragraphs 13 & 25	12 15	460-10 718-40 718-740

PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
93-7	Reporting on Advertising Costs	Complete	Reject	29	340-20 720-35 958-720
93-8	The Auditor's Consideration of Regulatory Risk-Based Capital for Life Insurance Enterprises	Withdrawn Complete	N/A	App D - NA GAAP	
94-1	Inquiries of State Insurance Regulators	Withdrawn Complete	N/A	App D - NA GAAP	
94-2	The Application of the Requirements of Accounting Research Bulletins, Opinions of the Accounting Principles Board, and Statements and Interpretations of the Financial Accounting Standards Board to Not-for-Profit Organizations	Superseded Complete	N/A	App D - NA GAAP	
94-3	Reporting of Related Entities by Not-for-Profit Organizations	Complete	N/A	App D - NA GAAP	954-810 958-810 958-840
94-4	Reporting of Investment Contracts Held by Health and Welfare Benefit Plans and Defined-Contribution Pension Plans	Complete	N/A	App D - NA GAAP	962-10 962-205 962-325 965-325
94-5	Disclosures of Certain Matters in the Financial Statements of Insurance Enterprises	Complete	Adopt	1	944-10 944-20 944-40 944-505
94-6	Disclosures of Certain Significant Risks and Uncertainties	Complete	Adopt	1	205-20 275-10 330-10 360-10 410-30 450-20 460-10 605-35 740-10 958-205 958-605 985-20
95-1	Accounting for Certain Insurance Activities of Mutual Life Insurance Enterprises	Complete	Reject	51R, 52	944-20 944-30 944-40 944-50 944-605
95-2	Financial Reporting by Nonpublic Investment Partnerships	Complete	N/A	App D - NA GAAP	946-20 946-210 946-225
95-3	Accounting for Certain Distribution Costs of Investment Companies	Complete	N/A	App D - NA GAAP	946-20

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
95-4	Letters for State Insurance Regulators to Comply with the NAIC Model Audit Rule	Withdrawn Complete	 N/A	 App D - NA GAAP	
95-5	Auditor's Reporting on Statutory Financial Statements of Insurance Enterprises	Withdrawn Complete	 N/A	 App D - NA GAAP	
96-1	Environmental Remediation Liabilities	Complete	Adopt	67	410-30 440-10 450-20
97-1	Accounting by Participating Mortgage Loan Borrowers	Complete	Adopt	40R	310-30 470-30 835-20
97-2	Software Revenue Recognition	Complete	Adopt/M paragraphs 6-91	16R 81	450-10 605-35 730-10 730-20 985-20 985-605
97-3	Accounting by Insurance and Other Enterprises for Insurance-Related Assessments	Complete	Reject Adopt/M	35 35R	310-10 405-30 450-20
98-1	Accounting for the Costs of Computer Software Developed or Obtained for Internal Use	Complete	Adopt/M Paragraphs 11-42 & 93	16R	350-10 350-40 350-50 730-10 985-20
98-2	Accounting for Costs of Activities of Not-for-Profit Organizations and State and Governmental Entities that Include Fund Raising	Complete	N/A	App D - NA GAAP	958-720
98-3	Audits of States, Local Governments, and Not-for-Profit Organizations Receiving Federal Awards	Superseded Complete	 N/A	 App D - NA GAAP	
98-4	Deferral of the Effective Date of a Provision of SOP 97-2, Software Revenue Recognition	Complete	Reject	16R	Not Directly Included in Codification. Included within SOP 97-2
98-5	Reporting on the Costs of Start-Up Activities	Complete	Adopt	76	720-15
98-6	Reporting on Management's Assessment Pursuant to the Life Insurance Ethical Market Conduct Program of the Insurance Marketplace Standards Association	Withdrawn Complete	 N/A	 App D - NA GAAP	

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
98-7	Deposit Accounting: Accounting for Insurance and Reinsurance Contracts That Do Not Transfer Insurance Risk	Complete	Adopt paragraphs 10-12 & 19b. Reject 13-17, 19a & 19c.	62R	340-30 450-10 835-10
98-8	Engagements to Perform Year 2000 Agreed-Upon Procedures Attestation Engagements Pursuant to Rule 17a-5 of the Securities Exchange Act of 1934, Rule 17Ad-18 of the Securities Exchange Act of 1934, and Advisories No. 17-98 and No. 42-98 of the Commodity Futures Trading Commission	Withdrawn Complete	N/A	App D - NA GAAP	
98-9	Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions	Complete	Adopt/M paragraphs 6-8	16R	Not Directly Included in Codification. Included within SOP 97-2
99-1	Guidance to Practitioners in Conducting and Reporting on an Agreed-Upon Procedures Engagement to Assist Management in Evaluating the Effectiveness of its Corporate Compliance Program	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
99-2	Accounting for and Reporting of Postretirement Medical Benefit (401(h)) Features of Defined Benefit Pension Plans	Complete	N/A	App D - NA GAAP	960-20 960-30 960-205 965-10 965-205
99-3	Accounting for and Reporting of Certain Defined Contribution Plan Investments and Other Disclosure Matters	Complete	N/A	App D - NA GAAP	962-10 962-325 965-325
00-1	Auditing Health Care Third-Party Revenues and Related Receivables	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
00-2	Accounting by Producers or Distributors of Films	Complete	N/A	App D - NA GAAP	210-10 430-10 460-10 855-10 926-10 926-20 926-230 926-330 926-405 926-430 926-605 926-705 926-720 926-835 926-845 926-855
00-3	Accounting by Insurance Enterprises for Demutualizations and Formations of Mutual Insurance Holding Companies and for Certain Long-Duration Participating Contracts	Pending			944-805
01-1	Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to Include Commodity Pools	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within SOP 95-2
01-2	Accounting and Reporting by Health and Welfare Benefit Plans	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within EBP AAG and SOP 92-6
01-3	Performing Agreed-Upon Procedures Engagements That Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
01-4	Reporting Pursuant to the Association for Investment Management and Research Performance Presentation Standards	Withdrawn Complete	 N/A	 App D - NA GAAP	
01-5	Amendments to Specific AICPA Pronouncements for Changes Related to the NAIC Codification	Complete	Adopt	1	Not Directly Included in Codification. Included within SOP 94-5

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
01-6	Accounting by Certain Entities (Including Entities With Trade Receivables) That Lend to or Finance the Activities of Others	Complete	N/A Adopt/M guidance on short sales	App D - NA GAAP 103R	310-10 310-20 460-10 605-20 825-10 835-30 860-20 860-50 942-10 942-210 942-305 942-310 942-320 942-325 942-360 942-405 942-470 942-505 942-825 944-320 948-10
02-1	Performing Agreed-Upon Procedures Engagements That Address Annual Claims Payment Reports as Required by the New Jersey Administrative Code	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
02-2	Accounting for Derivative Instruments and Hedging Activities by Not-for-Profit Health Care Organizations, and Clarification of the Performance Indicator	Complete	N/A	App D - NA GAAP	954-815
03-1	Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts	Complete	Rejected	56	944-20 944-30 944-40 944-80 944-320 944-605
03-2	Attest Engagements on Greenhouse Gas Emissions Information	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
03-3	Accounting for Certain Loans or Debt Securities Acquired in a Transfer	Considered for 43R only Pending	Paragraphs 5, 7 and 9 adopted for 43R only.	43R	310-10 310-30 835-10
03-4	Reporting Financial Highlights and Schedule of Investments by Nonregistered Investment Partnerships: An Amendment to the Audit and Accounting Guide Audits of Investment Companies and AICPA Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within SOP 95-2

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PRE-CODIFICATION STANDARDS - CATEGORY B GAAP
AICPA STATEMENTS OF POSITION[3]

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
03-5	Financial Highlights of Separate Accounts: An Amendment to the Audit and Accounting Guide Audits of Investment Companies	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included within INV AAG
04-1	Auditing the Statement of Social Insurance	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
04-2	Accounting for Real Estate Time-Sharing Transactions	Complete	N/A	App D - NA GAAP	978-10 978-230 978-250 978-310 978-330 978-340 978-605 978-720 978-810 978-840
05-1	Statement of Position 05-1 Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection With Modifications or Exchanges of Insurance Contracts	Complete	Rejected	71	944-30
06-1	Statement of Position 06-1 Reporting Pursuant to the Global Investment Performance Standards	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
07-1	Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies	Complete	N/A	App D - NA GAAP	946-10 946-323 946-810
07-2	Attestation Engagements That Address Specified Compliance of Control Objectives and Related Controls at Entities That Provide Services to Investment Companies, Investment Advisers, or Other Service Providers	Complete	N/A	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP
09-1	Performing Agreed-Upon Procedures Engagements That Address the Completeness, Accuracy, or Consistency of XBRL-Tagged Data	Complete	Reject	App D - NA GAAP	Not Included in Codification. Auditing and Attestation SOP

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
84-1	1984 Tax Reform Act: Deferred Income Taxes of Stock Life Insurance Companies	Resolved by FAS 109			
84-2	Tax Reform Act of 1984: Deferred Income Taxes Relating to Domestic International Sales Corporations	Resolved by FAS 109			
84-3	Convertible Debt "Sweeteners"	Nullified by FAS 84			
84-4	Acquisition, Development and Construction Loans	Resolved by PB 1			810-10 815-15
84-5	Sale of Marketable Securities with a Put Option	Complete	Reject	18, 91R, 103R	460-10 860-20
84-6	Termination of Defined Benefit Pension Plans	Nullified by FAS 88			
84-7	Termination of Interest Rate Swaps	Partially nullified and Partially resolved by FAS 133 Complete	 Adopt	 31	
84-8	Variable Stock Purchase Warrants Given by Suppliers to Customers	Resolved by FAS 123(R) Complete	 N/A	 104R	
84-9	Deposit Float of Banks	Superseded by PB 1 and AAG BSI Complete	 N/A	 App D - NA GAAP	.
84-10	LIFO Conformity of Companies Relying on Insilco Tax Court Decision	No EITF Consensus			
84-11	Offsetting Installment Note Receivables and Bank Debt ("Note Monetization")	Resolved by FIN 39			
84-12	Operating Leases with Scheduled Rent Increases	Nullified by FTB 85-3			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
84-13	Purchase of Stock Options and Stock Appreciation Rights in a Leveraged Buyout	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	Adopt Nullified	13 104R	
84-14	Deferred Interest Rate Setting	Nullified by FAS 133 Complete	Reject	31	
84-15	Grantor Trusts Consolidation	No EITF Consensus			
84-16	Earnings-per-Share Cash-Yield Test for Zero Coupon Bonds	Resolved by FAS 85			
84-17	Profit Recognition on Sales of Real Estate with Graduated Payment Mortgages or Insured Mortgages	Complete	Adopt	40R	360-20
84-18	Stock Option Pyramiding	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	Adopt Nullified	13 104R	
84-19	Mortgage Loan Payment Modifications	Complete	Adopt	37	310-20
84-20	GNMA Dollar Rolls	Complete	Adopt	45	815-10 860-10
84-21	Sale of a Loan with a Partial Participation Retained	Resolved by FAS 125 & FAS 140			
84-22	Prior Years' Earnings per Share following a Savings and Loan Association Conversion and Pooling	Resolved by FAS 141			
84-23	Leveraged Buyout Holding Company Debt	No EITF Consensus			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
84-24	LIFO Accounting Issues	No EITF Consensus			
84-25	Offsetting Nonrecourse Debt with Sales-Type of Direct Financing Lease Receivables	Resolved by FTB 86-2			
84-26	Defeasance of Special-Purpose Borrowings	Resolved by FAS 125 & FAS 140			
84-27	Deferred Taxes on Subsidiary Stock Sales	Resolved by FAS 109			
84-28	Impairment of Long-Lived Assets	Resolved by FAS 121 and FAS 144			
84-29	Gain and Loss Recognition on Exchanges of Productive Assets and the Effect of Boot	Resolved by EITF 86-29			
84-30	Sales of Loans to Special-Purpose Entities	Resolved by FIN 46 & FIN 46 (R)			
84-31	Equity Certificates of Deposit	Resolved by FAS 133			
84-32	(Not Used)				
84-33	Acquisition of a Tax Loss Carryforward—Temporary Parent-Subsidiary Relationship	Resolved by FAS 144			
84-34	Permanent Discount Restricted Stock Purchase Plans	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	N/A	104R	
84-35	Business Combinations: Sale of Duplicate Facilities and Accrual of Liabilities	No EITF Consensus			
84-36	Interest Rate Swap Transactions	Nullified by FAS 133 Complete	Adopt	31	
84-37	Sale-Leaseback Transaction with Repurchase Option	No EITF Consensus			840-40

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
84-38	Identical Common Shares for a Pooling of Interests	Nullified by FTB 85-5			
84-39	Transfers of Monetary and Nonmonetary Assets among Individuals and Entities under Common Control	No longer technically helpful			
84-40	Long-Term Debt Repayable by a Capital Stock Transaction	Nullified by FIN 46, FIN 46 (R) & FAS 150 Complete	Reject	15	
84-41	Consolidation of Subsidiary after Instantaneous In-Substance Defeasance	Resolved by FAS 94			
84-42	Push-Down of Parent Company Debt to a Subsidiary	No EITF Consensus			
84-43	Income Taxes Effects of Asset Revaluations in Certain Foreign Countries	Nullified by FAS 109			
84-44	Partial Termination of a Defined Benefit Pension Plan	Resolved by FAS 88			
85-1	Classifying Notes Received for Capital Stock	Complete	Reject	72	310-10 505-10 850-10
85-2	Classification of Costs Incurred in a Takeover Defense	Nullified by TB 85-6 Complete	Reject	72	
85-3	Tax Benefits Relating to Asset Dispositions Following an Acquisition of a Financial Institution	Nullified by FAS 109			
85-4	Downstream Mergers and Other Stock Transactions between Companies under Common Control	Resolved by FTB 85-5			
85-5	Restoration of Deferred Taxes Previously Eliminated by Net Operating Loss Recognition	Resolved by FAS 109			
85-6	Futures Implementation Questions	Resolved by Q&A 80			
85-7	Federal Home Loan Mortgage Corporation Stock	Resolved by FTB 85-1			
85-8	Amortization of Thrift Intangibles	Nullified by FAS 141(R) Complete	N/A	App D - NA GAAP	
85-9	Revenue Recognition on Options to Purchase Stock of Another Entity	Complete	Adopt	15	470-20

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
85-10	Employee Stock Ownership Plan Contribution Funded by a Pension Plan Termination	Nullified by FAS 88			
85-11	Use of an Employee Stock Ownership Plan in a Leveraged Buyout	No longer technically helpful			
85-12	Retention of Specialized Accounting for Investments in Consolidation	Complete	N/A	App D - NA GAAP	810-10
85-13	Sale of Mortgage Service Rights on Mortgages Owned by Others	Complete	N/A	App D - NA GAAP	860-50
85-14	Securities That Can Be Acquired for Cash in a Pooling of Interests	Nullified by FAS 141 Complete	 Reject	 68	
85-15	Recognizing Benefits of Purchased Net Operating Loss Carryforwards	Nullified by FAS 109			
85-16	Leveraged Leases • Real Estate Leases and Sale-Leaseback Transactions • Delayed Equity Contributions by Lessors	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	840-30
85-17	Accrued Interest upon Conversion of Convertible Debt	Complete	Adopt	15	470-20 835-10
85-18	Earnings-per-Share Effect of Equity Commitment Notes	Partially Nullified by FAS 128 Complete	 N/A	 App D - NA GAAP	Not Directly Included in Codification. Included within FAS 128
85-19	(Not Used)				
85-20	Recognition of Fees for Guaranteeing a Loan	Complete Partially nullified by FAS 163	Adopt	27	310-10 460-10 605-20
85-21	Changes of Ownership Resulting in a New Basis of Accounting	No EITF Consensus			805-50
85-22	Retroactive Application of FASB Technical Bulletins	No longer technically helpful			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
85-23	Effect of a Redemption Agreement on Carrying Value of a Security	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to FAS 133
85-24	Distribution Fees by Distributors of Mutual Funds That Do Not Have a Front-End Sales Charge	Complete	N/A	App D - NA GAAP	946-605 946-720
85-25	Sale of Preferred Stocks with a Put Option	Nullified by FAS 125, 133 & 140			860-20
85-26	Measurement of Servicing Fee Under FASB Statement No. 65 When a Loan is Sold with Servicing Retained	Resolved by FTB 87-3 & FAS 125 & FAS 140			
85-27	Recognition of Receipts from Made-Up Rental Shortfalls	Complete	N/A	App D - NA GAAP	970-360
85-28	Consolidation Issues Relating to Collateralized Mortgage Obligations	Resolved by FAS 94			
85-29	Convertible Bonds with a “Premium Put”	Complete Partially Nullified by FAS 133	Adopt	15	Not Directly Included in Codification. Issue Subject to FAS 133, FAS 155 and FIN 45
85-30	Sale of Marketable Securities at a Gain with a Put Option	Resolved by FAS 125 & FAS 140			
85-31	Comptroller of the Currency’s Rule on Deferred Tax Debits	Complete	N/A	App D - NA GAAP	942-740
85-32	Purchased Lease Residuals	Nullified by FTB 86-2			
85-33	Disallowance of Income Tax Deduction for Core Deposit Intangibles	Nullified by FAS 109			
85-34	Banker’s Acceptances and Risk Participations	Resolved by FAS 125 and FAS 140			
85-35	Transition and Implementation Issues for FASB Statement No. 86	No longer technically helpful			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
85-36	Discontinued Operations with Expected Gain and Interim Operating Losses	Nullified by FAS 144 Complete	Reject	24	
85-37	Recognition of Note Received for Real Estate Syndication Activities	Resolved by SOP 92-1			
85-38	Negative Amortizing Loans	No longer technically helpful			
85-39	Implications of SEC Staff Accounting Bulletin No. 59 on Noncurrent Marketable Equity Securities	No EITF Consensus			
85-40	Comprehensive Review of Sales of Marketable Securities with Put Arrangements	Nullified by FAS 125 and partially nullified by FAS 140			
85-41	Accounting for Savings and Loan Associations under FSLIC Management Consignment Program	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to FAS 109, FAS 142 and FAS 141R
85-42	Amortization of Goodwill Resulting from Recording Time Savings Deposits at Fair Values	Nullified by FAS 141(R) Complete	N/A	App D - NA GAAP	
85-43	Sale of Subsidiary for Equity Interest in Buyer	Resolved by EITF 86-29			
85-44	Differences between Loan Loss Allowances for GAAP and RAP	Complete	N/A	App D - NA GAAP	Not Included in Codification As No Longer Applicable Or Relevant

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
85-45	Business Combinations: Settlement of Stock Options and Awards	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	Adopt Nullified	13 104R	
85-46	Partnership's Purchase of Withdrawing Partner's Equity	No EITF Consensus			
86-1	Recognizing Net Operating Loss Carryforwards	Nullified by FAS 109			
86-2	Retroactive Wage Adjustments Affecting Medicare Payments	No longer technically helpful Complete	N/A	App D - NA GAAP	
86-3	Retroactive Regulations regarding IRC Section 338 Purchase Price Allocations	No longer technically helpful Complete	N/A	App D - NA GAAP	
86-4	Income Statement Treatment of Income Tax Benefit for Employee Stock Ownership Plan Dividends	Nullified by FAS 109			
86-5	Classifying Demand Notes with Repayment Terms	Complete	N/A	App D - NA GAAP	470-10
86-6	Antispeculation Clauses in Real Estate Sales Contracts	Complete	Adopt	40R	360-20
86-7	Recognition by Homebuilders of Profit from Sales of Land and Related Construction Contracts	Complete	N/A	App D - NA GAAP	970-360
86-8	Sale of Bad-Debt Recovery Rights	Complete	Adopt	15	860-10
86-9	IRC Section 338 and Push-Down Accounting	Complete	Reject	68	805-50 805-740
86-10	Pooling with 10 Percent Cash Payout Determined by Lottery	Nullified by FAS 141 Complete	Reject	68	

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
86-11	Recognition of Possible 1986 Tax Law Changes	Resolved by FAS 109			
86-12	Accounting by Insureds for Claims-Made Insurance Policies	Codified in Issue 03-8 Complete	N/A	App D - NA GAAP	
86-13	Recognition of Inventory Market Declines at Interim Reporting Dates	Complete	N/A	App D - NA GAAP	330-10
86-14	Purchased Research and Development Projects in a Business Combination	No EITF Consensus			
86-15	Increasing-Rate Debt	Complete	Adopt	15	470-10 835-10
86-16	Carryover of Predecessor Cost in Leveraged Buyout Transactions	Superseded by EITF 88-16			
86-17	Deferred Profit on Sale-Leaseback Transaction with Lessee Guarantee of Residual Value	Superseded by ASU 2016-02 Complete	Reject N/A	22 22R	460-10 840-40
86-18	Debtor's Accounting for a Modification of Debt Terms	Resolved by FIN 39 and Superseded by Issue 96-19 Complete	Adopt	15	
86-19	Change in Accounting for Other Postemployment Benefits	Resolved by FAS 106			
86-20	Accounting for Other Postemployment Benefits of an Acquired Company	Nullified by FAS 106			
86-21	Application of the AICPA Notice to Practitioners regarding Acquisition, Development, and Construction Arrangements to Acquisition of an Operating Property	Complete	Adopt	38	310-10 815-15
86-22	Display of Business Restructuring Provisions in the Income Statement	No EITF Consensus			
86-23	(Not Used)				

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
86-24	Third-Party Establishment of Collateralized Mortgage Obligations	Nullified by FAS 125 and FAS 140 Complete	N/A	App D - NA GAAP	
86-25	Offsetting Foreign Currency Swaps	Complete	Adopt	64	815-10
86-26	Using Forward Commitments as a Surrogate for Deferred Rate Setting	Resolved by FAS 133			
86-27	Measurement of Excess Contributions to a Defined Contribution Plan or Employee Stock Ownership Plan	Complete	N/A	App D - NA GAAP	715-70
86-28	Accounting Implications of Indexed Debt Instruments	Nullified by FAS 133 Complete	Adopt	15	470-10
86-29	Nonmonetary Transactions: Magnitude of Boot and the Exceptions to the Use of Fair Value	Codified in EITF 01-2 Complete	Adopt	28, 95	
86-30	Classification of Obligations When a Violation is Waived by the Creditor	Complete	N/A	App D - NA GAAP	470-10
86-31	Reporting the Tax Implications of a Pooling of a Bank and a Savings and Loan Association	Nullified by FAS 141 Complete	N/A	App D - NA GAAP	
86-32	Early Extinguishment of a Subsidiary's Mandatorily Redeemable Preferred Stock	Complete	Reject	32	505-10 810-10
86-33	Tax Indemnifications in Lease Agreements	Superseded by ASU 2016-02 Complete	Adopt N/A	22 22R	460-10 840-10
86-34	Futures Contracts Used as Hedges of Anticipated Reverse Repurchase Transactions	Nullified by FAS 133 Complete	Reject	31	
86-35	Debentures with Detachable Stock Purchase Warrants	Superseded by EITF No. 96-13			

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
86-36	Invasion of a Defeasance Trust	Complete	Adopt	15	Not Included in Codification As No Longer Applicable Or Relevant
86-37	Recognition of Tax Benefit of Discounting Loss Reserves of Insurance Companies	Nullified by FAS 109			
86-38	Implications of Mortgage Prepayments on Amortization of Servicing Rights	Section A - Nullified by FAS 122 & FAS 125 Section B – Nullified by FAS 125 Section C – Superseded by EITF No. 89-4			
86-39	Gains from the Sale of Mortgage Loans with Servicing Rights Retained	Nullified by FAS 122, FAS 125 & FAS 140			
86-40	Investments in Open-End Mutual Funds That Invest in U.S. Government Securities	Complete	N/A	App D - NA GAAP	320-10
86-41	Carryforward of the Corporate Alternative Minimum Tax Credit	Nullified by FAS 109			
86-42	Effect of a Change in Tax Rates on Assets and Liabilities Recorded Net-of-Tax in a Purchase Business Combination	Nullified by FAS 109			
86-43	Effect of a Change in Tax Law or Rates on Leveraged Leases	Superseded by ASU 2016-02 Complete	Adopt N/A	22 22R	840-30
86-44	Effect of a Change in Tax Law on Investments in Safe Harbor Leases	Complete	N/A	App D - NA GAAP	Not Included in Codification As No Longer Applicable Or Relevant
86-45	Imputation of Dividends on Preferred Stock Redeemable at the Issuer's Option with Initial Below-Market Dividend Rate	No EITF Consensus			

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
86-46	Uniform Capitalization Rules for Inventory under the Tax Reform Act of 1986	Complete	N/A	App D - NA GAAP	330-10
87-1	Deferral Accounting for Cash Securities That Are Used to Hedge Rate or Price Risk	Resolved by FAS 133			
87-2	Net Present Value Method of Valuing Speculative Foreign Exchange Contracts	Nullified by FAS 133 Complete	 Reject	 31	
87-3	(Not Used)				
87-4	Restructuring of Operations: Implications of SEC Staff Accounting Bulletin No. 67	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to FAS 144 and EITF 94-3
87-5	Troubled Debt Restructurings: Interrelationship between FASB Statement No. 15 and the AICPA Savings and Loan Guide	Nullified by FAS 114			
87-6	Adjustments Relating to Stock Compensation Plans	Nullified by FIN 44 Complete	 Adopt Nullified	 13 104R	
87-7	Sale of an Asset Subject to a Lease and Nonrecourse Financing: "Wrap-Lease Transactions"	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	Not Directly included in Codification Issue Subject to EITF 88-1 and FAS 13
87-8	Tax Reform Act of 1986: Issues Related to the Alternative Minimum Tax	Superseded by ASU 2016-02 Issues 1 – 9 and 11 nullified by FAS 96 & 109 Issue 10	 Adopt N/A	 22 22R	740-10 840-30
87-9	Profit Recognition on Sales of Real Estate with Insured Mortgages or Surety Bonds	Complete	Adopt	40R	360-20

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
87-10	Revenue Recognition by Television (Barter) Syndicators	Guidance revised by FAS 139 Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to SOP 00-2
87-11	Allocation of Purchase Price to Assets to Be Sold	Nullified by FAS 144 Complete	Reject	68	
87-12	Foreign Debt-for-Equity Swaps	Complete	Reject	23	830-20
87-13	Amortization of Prior Service Cost for a Defined Benefit Plan When There Is a History of Plan Amendments	Resolved by Q&A 87, Question 20			
87-14	(Not Used)				
87-15	Effect of a Standstill Agreement on Pooling-of-Interests Accounting	Nullified by FAS 141 Complete	Reject	68	
87-16	Whether the 90 Percent Test for a Pooling of Interests is Applied Separately to Each Company or on a Combined Basis	Nullified by FAS 141 Complete	Reject	68	
87-17	Spinoffs or Other Distributions of Loans Receivable to Shareholders	Codified in EITF 01-2			
87-18	Use of Zero Coupon Bonds in a Troubled Debt Restructuring	Complete Partially resolved by FAS 125 & FAS 140	Adopt/M	36	310-40
87-19	Substituted Debtors in a Troubled Debt Restructuring	Complete	Adopt/M	36	310-40
87-20	Offsetting Certificates of Deposit against High-Coupon Debt	Partially resolved by FAS 125 and Superseded by EITF 96-19 Complete	N/A	App D - NA GAAP	

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
87-21	Change of Accounting Basis in Master Limited Partnership Transactions	Complete	Reject	46, 88, 97	805-50
87-22	Prepayments to the Secondary Reserve of the FSLIC	Issue Addressed in PB 3 and PB 3 was Withdrawn Complete	N/A	App D - NA GAAP	
87-23	Book Value Stock Purchase Plans	Issues 1 and 2 nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) and Issue 3 nullified by SOP 93-6 Complete	Adopt Nullified	13 104R	
87-24	Allocation of Interest to Discontinued Operations	Complete	N/A	App D - NA GAAP	205-20
87-25	Sale of Convertible, Adjustable-Rate Mortgages with Contingent Repayment Agreement	Resolved by FAS 125 & FAS 140			
87-26	Hedging of Foreign Currency Exposure with a Tandem Currency	Nullified by FAS 133 Complete	Reject	23	
87-27	Poolings of Companies That Do Not Have a Controlling Class of Common Stock	Nullified by FAS 141 Complete	Reject	68	
87-28	Provision for Deferred Taxes on Increases in Cash Surrender Value of Key-Person Life Insurance	Resolved by FAS 109			

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
87-29	Exchange of Real Estate Involving Boot	Codified in EITF 01-2 Complete	 Adopt	 40R	
87-30	Sale of a Short-Term Loan Made under a Long-Term Credit Commitment	Complete	N/A	App D - NA GAAP	860-10
87-31	Sale of Put Options on Issuer's Stock	Codified in EITF No. 96-13			
87-32	(Not Used)				
87-33	Stock Compensation Issues Related to Market Decline	Nullified by FIN 44 Complete	 Adopt Nullified	 13 104R	
87-34	Sale of Mortgage Servicing Rights with a Subservicing Agreement	Complete	Adopt	18, 91R, 103R	860-50
88-1	Determination of Vested Benefit Obligation for a Defined Benefit Pension Plan	Complete	Adopt	8, 89, 92, 102	715-20 715-30
88-2	(Not Used)				
88-3	Rental Concessions Provided by Landlord	Resolved by FTB 88-1 and EITF 88-10 and 94-3			
88-4	Classification of Payment Made to IRS to Retain Fiscal Year	Complete	N/A	App D - NA GAAP	740-10
88-5	Recognition of Insurance Death Benefits	Complete	Adopt	21	325-30
88-6	Book Value Stock Plans in an Initial Public Offering	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	 Adopt Nullified	 13 104R	
88-7	(Not Used)				

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
88-8	Mortgage Swaps	Partially nullified and partially resolved by FAS 133 Complete	Reject	31	
88-9	Put Warrants	Nullified by FAS 128, 133, and 150 or superseded by Issue No. 96-13 Complete	Adopt/M	72	
88-10	Costs Associated with Lease Modification or Termination	Superseded by ASU 2016-02 Nullified and resolved by FAS 146 Complete	Adopt (See FAS 146)	22 22R	
88-11	Allocation of Recorded Investment When a Loan or Part of a Loan Is Sold	Nullified by Statement 125 and Statement 140, as amended by Statement 156 Complete	Adopt	18, 91R, 103R	
88-12	Transfer of Ownership Interest as Part of Down Payment under FASB Statement No. 66	Complete	Adopt	40R	360-20
88-13	(Not Used)				
88-14	Settlement of Fees with Extra Units to a General Partner in a Master Limited Partnership	No EITF Consensus			810-10
88-15	Classification of Subsidiary's Loan Payable in Consolidated Balance Sheet When Subsidiary's and Parent's Fiscal Years Differ	No EITF Consensus			470-10 810-10

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
88-16	Basis in Leveraged Buyout Transactions	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
88-17	Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations	Partially nullified by FAS 125 & superseded by EITF 97-3 Complete	Reject	37	
88-18	Sales of Future Revenues	Complete	Adopt	18, 91R, 103R	470-10
88-19	FSLIC-Assisted Acquisitions of Thrifts	Complete	N/A	App D - NA GAAP	942-10
88-20	Difference between Initial Investment and Principal Amount of Loans in a Purchased Credit Card Portfolio	Complete	N/A	App D - NA GAAP	310-10
88-21	Accounting for the Sale of Property Subject to the Seller's Preexisting Lease	Superseded by ASU 2016-02 Complete	Reject N/A	22 22R	840-40
88-22	Securitization of Credit Card and Other Receivable Portfolios	Complete	Adopt	18, 91R, 103R	860-10 860-20
88-23	Lump-Sum Payments under Union Contracts	Complete	Reject	29	710-10
88-24	Effect of Various Forms of Financing under FASB Statement No. 66	Complete	Adopt	40R	360-20
88-25	Ongoing Accounting and Reporting for a Newly Created Liquidating Bank	Complete	N/A	App D - NA GAAP	852-10 942-810
88-26	Controlling Preferred Stock in a Pooling of Interests	Nullified by FAS 141 Complete	Reject	68	
88-27	Effect of Unallocated Shares in an Employee Stock Ownership Plan on Accounting for Business Combinations	Nullified by FAS 141 Complete	Reject	68	

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
89-1	Accounting by a Pension Plan for Bank Investment Contracts and Guaranteed Investment Contracts	Resolved by FAS 110 and SOP 94-4			
89-2	Maximum Maturity Guarantees on Transfers of Receivables with Recourse	Nullified by FAS 125 & partially nullified by FAS 140			
89-3	Balance Sheet Presentation of Savings Accounts in Financial Statements of Credit Unions	Complete	N/A	App D - NA GAAP	942-405
89-4	Accounting for a Purchased Investment in a Collateralized Mortgage Obligation Instrument or in a Mortgage-Backed Interest-Only Certificate	Superseded by EITF 99-20 Complete	 Reject	 43R	
89-5	Sale of Mortgage Loan Servicing Rights	Superseded by EITF 95-5			
89-6	(Not Used)				
89-7	Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity	Codified in EITF 01-2 Complete	 Reject	 68	
89-8	Expense Recognition for Employee Stock Ownership Plans	Nullified by SOP 93-6			
89-9	Accounting for In-Substance Foreclosures	Nullified by FAS 114			
89-10	Sponsor's Recognition of Employee Stock Ownership Plan Debt	Superseded by SOP 93-6			
89-11	Sponsor's Balance Sheet Classification of Capital Stock with a Put Option Held by an Employee Stock Ownership Plan	Complete	Reject	12	480-10
89-12	Earnings-per-Share Issues Related to Convertible Preferred Stock Held by an Employee Stock Ownership Plan	Superseded by SOP 93-6			
89-13	Accounting for the Cost of Asbestos Removal	Complete	Adopt	40R	410-20 410-30
89-14	Valuation of Repossessed Real Estate	Complete	Adopt	40R	310-40
89-15	Accounting for a Modification of Debt Terms When the Debtor is Experiencing Financial Difficulties	Superseded by EITF 02-4 Complete	 Adopt/M	 36	

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
89-16	Consideration of Executory Costs in Sale-Leaseback Transactions	Superseded by ASU 2016-02 Complete	 Adopt N/A	 22 22R	840-40
89-17	Accounting for the Retail Sale of an Extended Warranty Contract in Connection with the Sale of a Product	Nullified by FTB 90-1			
89-18	Divestitures of Certain Investment Securities to an Unregulated Commonly Controlled Entity under FIRREA	Nullified by FAS 115 Complete	 Reject	 26R	
89-19	Accounting for a Change in Goodwill Amortization for Business Combinations Initiated Prior to the Effective Date of FASB Statement No. 72	Nullified by FAS 141R Complete	 N/A	 App D - NA GAAP	
89-20	Accounting for Cross Border Tax Benefit Leases	Complete	N/A	App D - NA GAAP	840-40
90-1	(Not Used)				
90-2	Exchange of Interest-Only and Principal-Only Securities for a Mortgage-Backed Security	Nullified by FAS 125 and FAS 140 Complete	 Reject	 43R	
90-3	Accounting for Employers' Obligations for Future Contributions to a Multiemployer Pension Plan	Complete	Adopt	8, 89, 92, 102	715-80
90-4	Earnings-per-Share Treatment of Tax Benefits for Dividends on Stock Held by an Employee Stock Ownership Plan	Complete	N/A	App D - NA GAAP	718-40
90-5	Exchanges of Ownership Interests between Entities under Common Control	Nullified by FAS 141R and FAS 160 Complete	 Reject	 68	
90-6	Accounting for Certain Events Not Addressed in Issue No. 87-11 Relating to an Acquired Operating Unit to Be Sold	Nullified by FAS 144 Complete	 Reject	 68	

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
90-7	Accounting for a Reload Stock Option	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	Adopt Nullified	13 104R	
90-8	Capitalization of Costs to Treat Environmental Contamination	Complete	Adopt	40R	410-20 410-30
90-9	Changes to Fixed Employee Stock Option Plans as a Result of Equity Restructuring	Nullified by FIN 44 Complete	Adopt Nullified	13 104R	
90-10	Accounting for a Business Combination Involving a Majority-Owned Investee of a Venture Capital Company	Resolved by FAS 141			
90-11	Accounting for Exit and Entrance Fees Incurred in a Conversion from the Savings Association Insurance Fund to the Bank Insurance Fund	No longer technically helpful			
90-12	Allocating Basis to Individual Assets and Liabilities for Transactions within the Scope of Issue No. 88-16	Nullified by FAS 141R Complete	Reject	68	
90-13	Accounting for Simultaneous Common Control Mergers	Nullified by FAS 141R and FAS 160 Complete	Reject	68	
90-14	Unsecured Guarantee by Parent of Subsidiary's Lease Payments in a Sale-Leaseback Transaction	Superseded by ASU 2016-02 Complete	Adopt N/A	22 22R	460-10 840-40

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
90-15	Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions	Superseded by ASU 2016-02 Nullified by FIN 46 & FIN 46 (R) Complete	Reject N/A	22 22R	958-810 958-840
90-16	Accounting for Discontinued Operations Subsequently Retained	Nullified by FAS 144 Complete	N/A	App D - NA GAAP	
90-17	Hedging Foreign Currency Risks with Purchased Options	Affirmed by FAS 133; therefore no longer necessary Complete	Reject	31	
90-18	Effect of a "Removal of Accounts" Provision on the Accounting for a Credit Card Securitization	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to FAS 140 and FAS 156
90-19	Convertible Bonds with Issuer Option to Settle for Cash upon Conversion	Nullified by FSP APB 14-1 Complete	Adopt/M	15	Not Explicitly Included in Codification.
90-20	Impact of an Uncollateralized Irrevocable Letter of Credit on a Real Estate Sale-Leaseback Transaction	Superseded by ASU 2016-02 Complete	Adopt N/A	22 22R	460-10 840-40
90-21	Balance Sheet Treatment of a Sale of Mortgage Servicing Rights with a Subservicing Agreement	Complete	Adopt	18, 91R, 103R	460-10 860-10 860-50
90-22	Accounting for Gas-Balancing Arrangements	No EITF Consensus			932-10 932-815

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
91-1	Hedging Intercompany Foreign Currency Risks	Nullified by FAS 133 Complete	 Reject	 31	
91-2	Debtor's Accounting for Forfeiture of Real Estate Subject to a Nonrecourse Mortgage	No EITF Consensus			
91-3	Accounting for Income Tax Benefits from Bad Debts of a Savings and Loan Association	Resolved by FAS 109			
91-4	Hedging Foreign Currency Risks with Complex Options and Similar Transactions	Resolved by FAS 133 Complete	 Reject	 31	
91-5	Nonmonetary Exchange of Cost-Method Investments	Complete	Reject	68	325-20
91-6	Revenue Recognition of Long-Term Power Sales Contracts	Complete	N/A	App D - NA GAAP	440-10 980-605
91-7	Accounting for Pension Benefits Paid by Employers after Insurance Companies Fail to Provide Annuity Benefits	Complete	Adopt	8, 89	715-30
91-8	Application of FASB Statement No. 96 to a State Tax Based on the Greater of a Franchise Tax or an Income Tax	Complete	Reject	10, 10R, 101	740-10
91-9	Revenue and Expense Recognition for Freight Services in Process	Complete	N/A	App D - NA GAAP	605-20
91-10	Accounting for Special Assessments and Tax Increment Financing Entities (TIFEs)	Complete	N/A	App D - NA GAAP	460-10 970-470
92-1	Allocation of Residual Value or First-Loss Guarantee to Minimum Lease Payments in Leases Involving Land and Building(s)	Superseded by ASU 2016-02 Complete	 Reject N/A	 22 22R	460-10 840-10
92-2	Measuring Loss Accruals by Transferors for Transfers of Receivables with Recourse	Complete	Reject	18, 91R, 103R	Not Directly Included in Codification. Issue Subject to FAS 133, FAS 140, FAS 156 and FIN 45.

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
92-3	Earnings-per-Share Treatment of Tax Benefits for Dividends on Unallocated Stock Held by an Employee Stock Ownership Plan (Consideration of the Implications of FASB Statement No. 109 on Issue 2 of EITF Issue No. 90-4)	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to SOP 93-6
92-4	Accounting for a Change in Functional Currency When an Economy Ceases to Be Considered Highly Inflationary	Complete	Reject	23	830-10
92-5	Amortization Period for Net Deferred Credit Card Origination Costs	Complete	N/A	App D - NA GAAP	310-20
92-6	(Not Used)				
92-7	Accounting by Rate-Regulated Utilities for the Effects of Certain Alternative Revenue Programs	Complete	N/A	App D - NA GAAP	980-605
92-8	Accounting for the Income Tax Effects under FASB Statement No. 109 of a Change in Functional Currency When an Economy Ceases to Be Considered Highly Inflationary	Complete	Adopt	10, 10R, 101	830-740
92-9	Accounting for the Present Value of Future Profits Resulting from the Acquisition of a Life Insurance Company	Complete	Reject	68	944-20
92-10	Loan Acquisitions Involving Table Funding Arrangements	Nullified by FAS 125			
92-11	(Not Used)				
92-12	Accounting for OPEB Costs by Rate-Regulated Enterprises	Complete	N/A	App D - NA GAAP	715-60 980-715
92-13	Accounting for Estimated Payments in Connection with the Coal Industry Retiree Health Benefit Act of 1992	Complete	N/A	App D - NA GAAP	450-20 715-60 930-715
93-1	Accounting for Individual Credit Card Acquisitions	Complete	N/A	App D - NA GAAP	310-20
93-2	Effect of Acquisition of Employer Shares for/by an Employee Benefit Trust on Accounting for Business Combinations	Resolved by FAS 141			
93-3	Plan Assets under FASB Statement No. 106	Complete	Adopt	14	710-10 715-60
93-4	Accounting for Regulatory Assets	Nullified by FAS 121 & FAS 144			980-340 980-715
93-5	Accounting for Environmental Liabilities	Nullified by SOP 96-1			

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
93-6	Accounting for Multiple-Year Retrospectively Rated Contracts by Ceding and Assuming Enterprises D-035: FASB Staff Views on Issue No. 93-6, "Accounting for Multiple-Year Retrospectively Rated Contracts by Ceding and Assuming Enterprises"	Complete Complete	Adopt/M Adopt/M	12 15 62R 62R	944-20 944-20
93-7	Uncertainties Related to Income Taxes in a Purchase Business Combination	Nullified by FAS 141R Complete	Reject	68	
93-8	Accounting for the Sale and Leaseback of an Asset That is Leased to Another Party	Superseded by ASU 2016-02 Complete	Adopt N/A	22 22R	840-40
93-9	Application of FASB Statement No. 109 in Foreign Financial Statements Restated for General Price-Level Changes	Complete	N/A	App D - NA GAAP	830-740
93-10	Accounting for Dual Currency Bonds	Resolved by FAS 133			
93-11	Accounting for Barter Transactions Involving Barter Credits	Complete	Adopt	28, 95	845-10
93-12	Recognition and Measurement of the Tax Benefit of Excess Tax Deductible Goodwill Resulting from a Retroactive Change in Tax Law	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Included in FAS 109
93-13	Effect of a Retroactive Change in Enacted Tax Rates That is Included in Income from Continuing Operations	Complete	Reject	10, 10R, 101	740-10
93-14	Accounting for Multiple-Year Retrospectively Rated Insurance Contracts by Insurance Enterprises and Other Enterprises	Complete	Reject	66	450-10 720-20 944-20
93-15	(Not Used)				
93-16	Application of FASB Statement No. 109 to Basis Differences within Foreign Subsidiaries That Meet the Indefinite Reversal Criterion of APB Opinion No. 23	Complete	Reject	10, 10R, 101	740-30 830-740
93-17	Recognition of Deferred Tax Assets for a Parent Company's Excess Tax Basis in the Stock of a Subsidiary That Is Accounted for as a Discontinued Operation	Complete	Adopt	10, 10R, 101	740-30

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
93-18	Recognition of Impairment for an Investment in a Collateralized Mortgage Obligation Instrument or in a Mortgage-Backed Interest-Only Certificate	Superseded by EITF 99-20 Complete	 Reject	 43R	
94-1	Accounting for Tax Benefits Resulting from Investments in Affordable Housing Projects	Complete	Adopt/M	93	323-740 325-20
94-2	Treatment of Minority Interests in Certain Real Estate Investment	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification.
94-3	Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)	Nullified by FAS 146 Complete	 Reject	 24	
94-4	Classification of an Investment in a Mortgage-Backed Interest-Only Certificate as Held-to-Maturity	Resolved by FAS 125 & FAS 140			
94-5	Determination of What Constitutes All Risks and Rewards and No Significant Unresolved Contingencies in a Sale of Mortgage Loan Servicing Rights under Issue 89-5	Superseded by EITF 95-5			
94-6	Accounting for the Buyout of Compensatory Stock Options	Nullified by FIN 44 Complete	 Adopt Nullified	 13 104R	
94-7	Accounting for Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock	Codified in EITF 96-13			
94-8	Accounting for Conversion of a Loan into a Debt Security in a Debt Restructuring	Complete	Reject	36	310-40
94-9	Determining a Normal Servicing Fee Rate for the Sale of an SBA Loan	Nullified by FAS 125			
94-10	Accounting by a Company for the Income Tax Effects of Transactions among or with Its Shareholders under FASB Statement No. 109	Complete	Reject	10, 10R, 101	740-10 740-20
95-1	Revenue Recognition on Sales with a Guaranteed Minimum Resale Value	Complete	N/A	App D - NA GAAP	460-10 605-50 840-10 840-30
95-2	Determination of What Constitutes a Firm Commitment for Foreign Currency Transactions Not Involving a Third Party	Nullified by FAS 133 Complete	 Reject	 23	

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
95-3	Recognition of Liabilities in Connection with a Purchase Business Combination	Nullified by FAS 141R Complete	Reject	68	
95-4	Revenue Recognition on Equipment Sold and Subsequently Repurchased Subject to an Operating Lease	Complete	N/A	App D - NA GAAP	605-15 840-10
95-5	Determination of What Risks and Rewards, If Any, Can Be Retained and Whether Any Unresolved Contingencies May Exist in a Sale of Mortgage Loan Servicing Rights	Complete	Adopt	18, 91R, 103R	860-50
95-6	Accounting by a Real Estate Investment Trust for an Investment in a Service Corporation	Complete	N/A	App D - NA GAAP	974-323 974-840
95-7	Implementation Issues Related to the Treatment of Minority Interests in Certain Real Estate Investment Trusts	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification.
95-8	Accounting for Contingent Consideration Paid to the Shareholders of an Acquired Enterprise in a Purchase Business Combination	Nullified by FAS 141R Complete	Reject	68	
95-9	Accounting for Tax Effects of Dividends in France in Accordance with FAS Statement No. 109	Complete	Reject	10, 10R, 101	740-10
95-10	Accounting for Tax Credits Related to Dividend Payments in Accordance with FASB Statement No. 109	Complete	Reject	10, 10R, 101	740-10
95-11	Accounting for Derivative Instruments Containing Both a Written Option-Based Component and a Forward-Based Component	Resolved by FAS 133			
95-12	Pooling of Interests with a Common Interest in Joint Venture	Nullified by FAS 141 Complete	Reject	68	
95-13	Classification of Debt Issue Costs in the Statement of Cash Flows	Complete	Adopt	69	230-10
95-14	Recognition of Liabilities in Anticipation of a Business Combination	Nullified by FAS 146 Complete	Reject	68	
95-15	Recognition of Gain or Loss When a Binding Contract Requires a Debt Extinguishment to Occur at a Future Date for a Specified Amount	Superseded by EITF 96-19 Complete	Adopt/M	15	

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CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
95-16	Accounting for Stock Compensation Arrangements with Employer Loan Features under APB Opinion No. 25	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	Adopt Nullified	13 104R	
95-17	Accounting for Modifications to an Operating Lease That Do Not Change the Lease Classification	Superseded by ASU 2016-02 Complete	Adopt N/A	22 22R	840-20
95-18	Accounting and Reporting for a Discontinued Business Segment When the Measurement Date Occurs after the Balance Sheet Date but before the Issuance of Financial Statements.	Nullified by FAS 144 Complete	Reject	24	
95-19	Determination of the Measurement Date for the Market Price of Securities Issued in a Purchase Business Combination	Codified in EITF 99-12 Complete	Adopt	68	
95-20	Measurement in the Consolidated Financial Statements of a Parent of the Tax Effects Related to the Operations of a Foreign Subsidiary That Receives Tax Credits Related to Dividend Payments	Complete	Reject	10, 10R, 101	740-10
95-21	Accounting for Assets to Be Disposed Of Acquired in a Purchase Business Combination	Resolved by FAS 144			
95-22	Balance Sheet Classification of Borrowings Outstanding under Revolving Credit Agreements That Include both a Subjective Acceleration Clause and a Lock-Box Arrangement	Complete	N/A	App D - NA GAAP	470-10
95-23	The Treatment of Certain Site Restoration/ Environmental Exit Costs When Testing a Long-Lived Asset for Impairment	Complete	Adopt	40R	360-10 360-20
96-1	Sale of Put Options on Issuer's Stock That Require or Permit Cash Settlement	Codified in EITF 96-13			
96-2	Impairment Recognition When a Nonmonetary Asset Is Exchanged or Is Distributed to Owners and Is Accounted for at the Asset's Recorded Amount	Codified in EITF 01-2			

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
96-3	Accounting for Equity Instruments That Are Issued for Consideration Other Than Employee Services under FASB Statement No. 123	Superseded by EITF 96-18 Complete	Reject	13	
96-4	Accounting for Reorganizations Involving a Non-Pro Rata Split-off of Certain Nonmonetary Assets to Owners	Codified in EITF 01-2 Complete	Reject	28, 95	
96-5	Recognition of Liabilities for Contractual Termination Benefits or Changing Benefit Plan Assumptions in Anticipation of a Business Combination	Complete	Adopt	8, 89, 92, 102	420-10 450-10 710-10 712-10 715-60 718-10 805-20
96-6	Accounting for the Film and Software Costs Associated with Developing Entertainment and Educational Software Products	No EITF Consensus			985-705
96-7	Accounting for Deferred Taxes on In-Process Research and Development Activities Acquired in a Purchase Business Combination	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
96-8	Accounting for a Business Combination When the Issuing Company Has Targeted Stock	Nullified by FAS 141 Complete	Reject	68	
96-9	Classification of Inventory Markdowns and Other Costs Associated with a Restructuring	Removed from EITF Agenda			330-10 420-10
96-10	Impact of Certain Transactions on the Held-to-Maturity Classification under FASB Statement No. 115	Complete	Reject	26R	320-10
96-11	Accounting for Forward Contracts and Purchased Options to Acquire Securities Covered by FASB Statement No. 115	Complete	Reject	31	320-10 815-10
96-12	Recognition of Interest Income and Balance Sheet Classification of Structured Notes	Complete	Reject	43R	320-10 835-10
96-13	Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock	Codified in EITF 00-19			
96-14	Accounting for the Costs Associated with Modifying Computer Software for the Year 2000	No longer technically helpful Complete	Adopt	17	

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
96-15	Accounting for the Effects of Changes in Foreign Currency Exchange Rates on Foreign-Currency-Denominated Available-for-Sale Debt Securities	Complete	Reject	23	320-10 830-20
96-16	Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights	Complete	Reject	App D - NA GAAP	810-10
96-17	Revenue Recognition under Long-Term Power Sales Contracts That Contain both Fixed and Variable Pricing Terms	Complete	N/A	App D - NA GAAP	980-350 980-605
96-18	Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services	Complete	Adopted/M	104R	440-10
96-19	Debtor's Accounting for a Modification or Exchange of Debt Instruments	Complete Amended by EITF Issue No. 06-6	Adopt	18, 91R, 103R 103R	470-50
96-20	Impact of FASB Statement No. 125 on Consolidation of Special-Purpose Entities	Nullified by FAS 140 Complete	Reject	103R	
96-21	Implementation Issues in Accounting for Leasing Transactions involving Special-Purpose Entities	Superseded by ASU 2016-02 Complete	Reject N/A	22 22R	460-10 840-10 840-20 840-40 958-810 958-840
96-22	Applicability of the Disclosures Required by FASB Statement No. 114 When a Loan Is Restructured in a Troubled Debt Restructuring into Two (or More) Loans	Complete	Adopt	36	310-40
96-23	The Effects of Financial Instruments Indexed to, and Settled in, a Company's Own Stock on Pooling-of-Interests Accounting for a Subsequent Business Combination	Resolved by FAS 141			
97-1	Implementation Issues in Accounting for Lease Transactions, including Those involving Special-Purpose Entities	Complete	N/A	App D - NA GAAP	450-20 460-10 840-10 840-40 958-840
97-2	Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain Other Entities with Contractual Management Arrangements	Complete	N/A	App D - NA GAAP	718-10 810-10 954-810

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
97-3	Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations after the Issuance of FASB Statement No. 125	Complete	Reject	App D - NA GAAP	310-20 860-10
97-4	Deregulation of the Pricing of Electricity---Issues Related to the Application of FASB Statements No. 71 and 101	Complete	N/A	App D - NA GAAP	980-20
97-5	Accounting for the Delayed Receipt of Option Shares upon Exercise under APB Opinion No. 25	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	N/A	104R	
97-6	Application of Issue No. 96-20 to Qualifying Special-Purpose Entities Receiving Transferred Financial Assets Prior to the Effective Date of FASB Statement No. 125	Nullified by FAS 140 Complete	N/A	App D - NA GAAP	
97-7	Accounting for Hedges of the Foreign Currency Risk Inherent in an Available-for-Sale Marketable Equity Security	Complete	N/A	App D - NA GAAP	Not Directly Included in Codification. Issue Subject to FAS 130 and 133
97-8	Accounting for Contingent Consideration Issued in a Purchase Business Combination	Nullified by FAS 141R Complete	Adopt	68	
97-9	Effect on Pooling-of-Interests Accounting of Certain Contingently Exercisable Options or Other Equity Instruments	Nullified by FAS 141 Complete	N/A	App D - NA GAAP	
97-10	The Effect of Lessee Involvement in Asset Construction	Complete	Reject	App D - NA GAAP	460-10 840-40
97-11	Accounting for Internal Costs Relating to Real Estate Property Acquisitions	Complete	Adopt	40R	970-340 970-720

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
97-12	Accounting for Increased Share Authorizations in an IRS Section 423 Employee Stock Purchase Plan under APB Opinion No. 25	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	Adopt Nullified	INT 99-17 104R	
97-13	Accounting for Costs Incurred in Connection with a Consulting Contract or an Internal Project That Combines Business Process Reengineering and Information Technology Transformation	Complete	Adopt	17	720-45
97-14	Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested	Complete	Adopt/M	104R	260-10 710-10 810-10
97-15	Accounting for Contingency Arrangements Based on Security Prices in a Purchase Business Combination	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
98-1	Valuation of Debt Assumed in a Purchase Business Combination	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
98-2	Accounting by a Subsidiary or Joint Venture for an Investment in the Stock of Its Parent Company or Joint Venture Partner	Complete	Reject	97	Not Directly Included in Codification. Issue Subject to FIN 46R
98-3	Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business	Nullified by FAS 141R Complete	Adopt/M	INT 00-26	
98-4	Accounting by a Joint Venture for Businesses Received at Its Formation	No EITF Consensus			805-10 845-10
98-5	Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios	Complete	Reject	15	470-20 505-10

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
98-6	Investor's Accounting for an Investment in a Limited Partnership When the Investor Is the Sole General Partner and the Limited Partners Have Certain Approval or Veto Rights	Removed from EITF Agenda			
98-7	Accounting for Exchanges of Similar Equity Method Investments	Codified in EITF 01-2 Complete	Adopt	Nullifed by SSAP No. 95	
98-8	Accounting for Transfers of Investments That Are in Substance Real Estate	Complete	Adopt	40R, 77, 103R	360-20
98-9	Accounting for Contingent Rent	Superseded by ASU 2016-02 Complete	Adopt/M N/A	22 22R	450-20 450-30 840-10
98-10	Accounting for Contracts Involved in Energy Trading and Risk Management Activities	Superseded by EITF 02-03 Complete	N/A	App D - NA GAAP	
98-11	Accounting for Acquired Temporary Differences in Certain Purchase Transactions That Are Not Accounted for as Business Combinations	Pending			740-10
98-12	Application of Issue No. 00-19 to Forward Equity Sales Transactions	Nullified by FAS 150 Complete – Refer to review of FAS 150			
98-13	Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of the Investee	Complete	Adopt/M	INT 00-24	320-10 323-10
98-14	Debtor's Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements	Complete	Reject	15	470-50
98-15	Structured Notes Acquired for a Specified Investment Strategy	Complete	Reject	43R	320-10

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
99-1	Accounting for Debt Convertible into the Stock of a Consolidated Subsidiary	Superseded by EITF 08-08 Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification.
99-2	Accounting for Weather Derivatives	Complete Superseded by ASC Topic 105 and Incorporated into ASC 815-45	Adopt/M	86	815-45
99-3	Application of Issue No. 96-13 to Derivative Instruments with Multiple Settlement Alternatives	Codified in EITF 00-19 Complete	N/A	App D - NA GAAP	
99-4	Accounting for Stock Received from the Demutualization of a Mutual Insurance Company	Complete	Adopt	72	325-30
99-5	Accounting for Pre-Production Costs Related to Long-Term Supply Arrangements	Complete	N/A	App D - NA GAAP	340-10 460-10 730-10
99-6	Impact of Acceleration Provisions in Grants Made between Initiation and Consummation of a Pooling-of-Interests Business Combination	Nullified by FAS 141 Complete	N/A	App D - NA GAAP	
99-7	Accounting for an Accelerated Share Repurchase Program	Complete	N/A	App D - NA GAAP	260-10 505-30
99-8	Accounting for Transfers of Assets that are Derivative Instruments but that are not Financial Assets	Pending			815-10 860-10
99-9	Effect of Derivative Gains and Losses on the Capitalization of Interest	Pending			815-25 815-30
99-10	Percentage used to Determine the Amount of Equity Method Losses	Complete	Adopt	INT 00-24	323-10

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GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
99-11	Subsequent Events Caused by Year 2000	No longer technically helpful Complete	N/A	App D - NA GAAP	
99-12	Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination	Nullified by FAS 141R Complete	Adopt/M	INT 00-28	
99-13	Application of Issue No. 97-10 and FASB Interpretation No. 23 to Entities that Enter into Leases with Governmental Entities	Complete	N/A	App D - NA GAAP	840-40
99-14	Recognition by a Purchaser of Losses on Firmly Committed Executory Contracts	No EITF Consensus			
99-15	Accounting for Decreases in Deferred Tax Asset Valuation Allowances Established in a Purchase Business Combination As a Result of a Change in Tax Regulations	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
99-16	Accounting for Transactions with Elements of Research and Development Arrangements	Complete	N/A	App D - NA GAAP	810-30
99-17	Accounting for Advertising Barter Transactions	Complete	Adopt/M	95	605-20
99-18	Effect on Pooling-of-Interests Accounting of Contracts Indexed to a Company's Own Stock	Resolved by FAS 141 Complete	N/A	App D - NA GAAP	
99-19	Reporting Revenue Gross as a Principal versus Net as an Agent	Complete	N/A	App D - NA GAAP	605-45
99-20	Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to be Held by the Transferor in Securitized Financial Assets	Complete	Adopt	43R	310-20 310-30 320-10 325-40 835-10
00-1	Investor Balance Sheet and Income Statement Display under the Equity Method for Investments in Certain Partnerships and Other Ventures	Complete	Reject	48	323-30 810-10 910-810 930-810 932-810
00-2	Accounting for Web Site Development Costs	Complete	Adopt	16R 82	350-10 350-50

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GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
00-3	Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware	Complete	Adopt/M	16R 81	985-20 985-605
00-4	Majority Owner's Accounting for a Transaction in the Shares of a Consolidated Subsidiary and a Derivative Indexed to the Minority Interest in That Subsidiary	Nullified by FAS 150 Complete	 N/A	 App D - NA GAAP	460-10 480-10
00-5	Determining Whether a Nonmonetary Transaction is an Exchange of Similar Productive Assets	Codified in EITF 01-2			
00-6	Accounting for Freestanding Derivative Financial Instruments Indexed to, and Potentially Settled in, the Stock of a Consolidated Subsidiary	Superseded by EITF 08-8 Complete Partially Nullified by FAS 150	 N/A	 App D - NA GAAP	815-10
00-7	Application of Issue No. 96-13 to Equity Derivative Instruments That Contain Certain Provisions That Require Net Cash Settlement If Certain Events outside the Control of the Issuer Occur	Codified in EITF 00-19 Complete	 N/A	 App D - NA GAAP	
00-8	Accounting by a Grantee for an Equity Instrument to Be Received in Conjunction with Providing Goods or Services	Complete	Adopt/M	104R	845-10
00-9	Classification of a Gain or Loss from a Hedge of Debt That Is Extinguished	Pending			815-30
00-10	Accounting for Shipping and Handling Fees and Costs	Complete	N/A	App D - NA GAAP	605-45
00-11	Lessors' Evaluation of Whether Leases of Certain Integral Equipment Meet the Ownership Transfer Requirements of FASB Statement No. 13	Superseded by ASU 2016-02 Complete	 Adopt/M N/A	 22 22R	840-10
00-12	Accounting by an Investor for Stock-Based Compensation Granted to Employees of an Equity Method Investee	Pending			323-10 505-10 718-10
00-13	Determining Whether Equipment Is "Integral Equipment" Subject to FASB Statements No. 66 and No. 98	Complete	Adopt	40R, 77	360-20 978-10

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
00-14	Accounting for Certain Sales Incentives	Codified in EITF 01-9 Complete	N/A	App D - NA GAAP	
00-15	Classification in the Statement of Cash Flows of the Income Tax Benefit Received by a Company upon Exercise of a Nonqualified Employee Stock Option	Nullified by FAS 123R except for entities within the scope of paragraph 83 of FAS 123(R) Complete	N/A	App D - NA GAAP	
00-16	Recognition and Measurement of Employer Payroll Taxes on Employee Stock-Based Compensation	Complete	Adopt/M	104R	718-10
00-17	Measuring the Fair Value of Energy-Related Contracts in Applying Issue No. 98-10	Superseded by EITF 02-3 Complete	N/A	App D - NA GAAP	
00-18	Accounting Recognition for Certain Transactions involving Equity Instruments Granted to Other Than Employees	Complete	Adopt/M	104R	505-50
00-19	Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock	Complete Partially Nullified by FAS 150	N/A	App D - NA GAAP	480-10 505-10 815-10 815-15 815-40
00-20	Accounting for Costs Incurred to Acquire or Originate Information for Database Content and Other Collections of Information	No longer technically helpful			
00-21	Revenue Arrangements with Multiple Deliverables	Complete Nullified by ASU 2009-13	Adopt/M ASU 2009-13 deemed not applicable, nullifying INT 04-18.		605-25

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
00-22	Accounting for "Points" and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future	Codified in EITF 01-9 Complete	N/A	App D - NA GAAP	
00-23	Issues Related to the Accounting for Stock Compensation under APB Opinion No. 25 and FASB Interpretation No. 44	Nullified by FAS 123(R) except for entities within the scope of paragraph 83 of FAS 123(R) Complete	N/A	104R	
00-24	Revenue Recognition: Sales Arrangements That Include Specified-Price Trade-in Rights	No EITF Consensus			
00-25	Vendor Income Statement Characterization of Consideration Paid to a Reseller of the Vendor's Products	Codified in EITF 01-9			
00-26	Recognition by a Seller of Losses on Firmly Committed Executory Contracts	No EITF Consensus			
00-27	Application of Issue No. 98-5 to Certain Convertible Instruments	Pending Partially Nullified by FAS 150			260-10 470-20 505-10
01-1	Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash	Complete	Adopt/M	95	470-20
01-2	Interpretations of APB Opinion No. 29	Partially Nullified by FAS 153 Complete	Adopt/M	INT 06-13	810-10 845-10
01-3	Accounting in a Business Combination for Deferred Revenue of an Acquiree	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
01-4	Accounting for Sales of Fractional Interests in Equipment	No EITF Consensus			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
01-5	Application of FASB Statement No. 52 to an Investment Being Evaluated for Impairment That Will Be Disposed Of	Complete	Reject	App D - NA GAAP	830-30
01-6	The Meaning of "Indexed to a Company's Own Stock"	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification.
01-7	Creditor's Accounting for a Modification or Exchange of Debt Instruments	Complete	Adopt	103R	310-20
01-8	Determining Whether an Arrangement Contains a Lease	Superseded by ASU 2016-02 Complete	 Adopt/M N/A	 22 22R	440-10 815-10 840-10 840-20 840-30
01-9	Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)	Complete	N/A	App D - NA GAAP	330-10 605-50 908-360
01-10	Accounting for the Impact of the Terrorist Attacks of September 11, 2001	Complete	Nullifed as no longer relevant, including INT 01-32.		Not included in codification. No longer applicable or relevant.
01-11	Application of Issue No. 00-19 to a Contemporaneous Forward Purchase Contract and Written Put Option	Resolved by FAS 150			
01-12	The Impact of the Requirements of FASB Statement No. 133 on Residual Value Guarantees in Connection with a Lease	Complete	N/A	App D - NA GAAP	460-10 815-10 840-10
01-13	Income Statement Display of Business Interruption Insurance Recoveries	Complete	Adopt	24	225-30 450-30
01-14	Income Statement Characterization of Reimbursements Received for "Out-of-Pocket" Expenses Incurred	Complete	N/A	App D - NA GAAP	605-45
02-1	(Not Used)				
02-2	When Separate Contracts That Meet the Definition of Financial Instruments Should Be Combined for Accounting Purposes	No EITF Consensus Partially resolved by FAS 150			
02-3	Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities	Complete Modified by FAS 157	Reject	App D - NA GAAP	815-10 932-330 940-325
02-4	Determining Whether a Debtor's Modification or Exchange of Debt Instruments in within the Scope of FASB Statement No. 15	Complete	Adopt	36	470-60
02-5	Definition of "Common Control" in Relation to FASB Statement No. 141	No EITF Consensus			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
02-6	Classification in the Statement of Cash Flows of Payments Made to Settle an Asset Retirement Obligation within the Scope of FASB Statement No. 143	Complete	N/A	App D - NA GAAP	230-10 410-20
02-7	Unit of Accounting for Testing Impairment of Indefinite-Lived Intangible Assets	Complete	Reject	App D - NA GAAP	350-30
02-8	Accounting for Options Granted to Employees in Unrestricted, Publicly Traded Shares of an Unrelated Entity	Complete	N/A	App D - NA GAAP	815-10
02-9	Accounting for Changes That Result in a Transferor Regaining Control of Financial Assets Sold	Complete	Adopt/M	INT 04-21	860-20 860-50
02-10	Determining Whether a Debtor Is Legally Released as Primary Obligor When the Debtor Becomes Secondarily Liable under the Original Obligation	No longer technically helpful			
02-11	Accounting for Reverse Spinoffs	Complete	Adopt	INT 08-05	505-60
02-12	Permitted Activities of a Qualifying Special-Purpose Entity in Issuing Beneficial Interests under FASB Statement No. 140	Nullified by FAS 166			
02-13	Deferred Income Tax Considerations in Applying the Goodwill Impairment Test in FASB Statement No. 142	Complete	Reject	App D - NA GAAP	350-20
02-14	Whether the Equity Method of Accounting Applies When an Investor Does Not Have an Investment in Voting Stock of an Investee but Exercises Significant Influence through Other Means (The name of EITF 02-14 has been changed to – "Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock".)	Complete	Reject	App D - NA GAAP	323-10
02-15	Determining Whether Certain Conversions of Convertible Debt to Equity Securities Are within the Scope of FASB Statement No. 84	Complete	Adopt	15	470-20
02-16	Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor	Complete	N/A	App D - NA GAAP	605-50 705-20
02-17	Recognition of Customer Relationship Intangible Assets Acquired in a Business Combination	Nullified by FAS 141R Complete	Reject	App D - NA GAAP	
02-18	Accounting for Subsequent Investments in an Investee after Suspension of Equity Method Loss Recognition	Complete	Adopt/M	48, 97	323-10

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
03-1	The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments	Nullified by FSP FAS 115–1/ FAS124–1			
03-2	Accounting for the Transfer to the Japanese Government of the Substitutional Portion of Employee Pension Fund Liabilities	Complete	N/A	App D - NA GAAP	715-20 715-30
03-3	Applicability of Topic No. D–79 to Claims-Made Insurance Policies	Codified in EITF 03-8			
03-4	Determining the Classification and Benefit Attribution Method for a "Cash Balance" Pension Plan	Complete	Adopt/M	102	715-30
03-5	Applicability of AICPA Statement of Position 97-2 to Non-Software Deliverables in an Arrangement Containing More-Than-Incidental Software	Complete	Adopt	16R	985-605
03-6	Participating Securities and the Two-Class Method under FASB Statement No. 128	Complete	Reject	App D - NA GAAP	260-10
03-7	Accounting for the Settlement of the Equity-Settled Portion of a Convertible Debt Instrument That Permits or Requires the Conversion Spread to Be Settled in Stock (Instrument C of Issue No. 90-19)	Nullified by FSP APB 14-1 Complete	 Adopt	 15	Not Explicitly Included in Codification.
03-8	Accounting for Claims-Made Insurance and Retroactive Insurance Contracts by the Insured Entity	Pending			450-30 720-20 954-720
03-9	Determination of the Useful Life of Renewable Intangible Assets Under FASB Statement No. 142	Removed from EITF agenda			
03-10	Application of Issue No. 02-16 by Resellers to Sales Incentives Offered to Consumers by Manufacturers	Complete	N/A	App D - NA GAAP	605-50 705-20
03-11	Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133 and Not "Held for Trading Purposes" as Defined in Issue No. 02-3	Complete	Reject	App D - NA GAAP	815-10
03-12	Impact of FASB Interpretation No. 45 on Issue No. 95-1	Complete	N/A	App D - NA GAAP	460-10
03-13	Applying the Conditions in Paragraph 42 of FASB Statement No. 144 in Determining Whether to Report Discontinued Operations	Complete	N/A	App D - NA GAAP	205-20
03-14	Participants' Accounting for Emissions Allowances under a "Cap and Trade" Program	Removed from EITF agenda			
03-15	Interpretation of Constraining Conditions of a Transferee in a Collateralized Bond Obligation Structure	No EITF Consensus			

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
03-16	Accounting for Investments in Limited Liability Companies	Complete	Reject	App D - NA GAAP	272-10 323-30
03-17	Subsequent Accounting for Executory Contracts That Have Been Recognized on an Entity's Balance Sheet	No EITF Consensus			
04-1	Accounting for Preexisting Relationships between the Parties to a Business Combination	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
04-2	Whether Mineral Rights Are Tangible or Intangible Assets	Nullified by FAS 141R Complete	N/A	App D - NA GAAP	
04-3	Mining Assets: Impairment and Business Combinations	Complete	N/A	App D - NA GAAP	930-360 930-805
04-4	Allocation of Goodwill to Reporting Units for a Mining Enterprise	Removed from the EITF Agenda Complete	N/A	App D - NA GAAP	
04-5	Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights	Complete	N/A	App D - NA GAAP	810-20
04-6	Accounting for Stripping Costs Incurred during Production in the Mining Industry	Complete	N/A	App D - NA GAAP	930-10 930-330
04-7	Determining Whether an Interest Is a Variable Interest in a Potential Variable Interest Entity	Removed From Agenda – Issue Addressed in FSP FIN 46R-6 Complete	N/A	App D - NA GAAP	

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
04-8	The Effect of Contingently Convertible Instruments on Diluted Earnings per Share	Complete	N/A	App D - NA GAAP	260-10
04-9	Accounting for Suspended Well Costs	Resolved by FSP FAS 19-1			
04-10	Determining Whether to Aggregate Operating Segments That Do Not Meet the Quantitative Thresholds	Complete	N/A	App D - NA GAAP	280-10
04-11	Accounting in a Business Combination for Deferred Postcontract Customer Support Revenue of a Software Vendor	No longer technically helpful			
04-12	Determining Whether Equity-Based Compensation Awards Are Participating Securities	Removed from EITF agenda			
04-13	Accounting for Purchases and Sales of Inventory with the Same Counterparty	Complete	N/A	App D - NA GAAP	845-10
05-1	Accounting for the Conversion of an Instrument That Became Convertible upon the Issuer's Exercise of a Call Option	Pending			470-20
05-2	The Meaning of "Conventional Convertible Debt Instrument" in Issue No. 00-19	Pending			815-40
05-3	Accounting for Rental Costs Incurred during the Construction Period	Removed from EITF agenda			
05-4	The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument Subject to Issue No. 00-19	Removed from EITF agenda			
05-5	Accounting for Early Retirement or Postemployment Programs with Specific Features (Such As Terms Specified in Altersteilzeit Early Retirement Arrangements)	Complete	N/A	App D - NA GAAP	715-30
05-6	Determining the Amortization Period for Leasehold Improvements Purchased after Lease Inception or Acquired in a Business Combination	Complete	N/A INT 06-10 nullified.	App D - NA GAAP	805-20 840-10
05-7	Accounting for Modifications to Conversion Options Embedded in Debt Instruments and Related Issues	Superseded by EITF Issue No. 06-6			
05-8	Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature	Complete	N/A	App D - NA GAAP	740-10
06-1	Accounting for Consideration Given by a Service Provider to a Manufacturer or Reseller of Equipment Necessary for an End-Customer to Receive Service from the Service Provider	Complete	N/A	App D - NA GAAP	605-50
06-2	Accounting for Sabbatical Leave and Other Similar Benefits Pursuant to FASB Statement No. 43	Complete	Adopt	11	710-10

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
06-3	How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)	Complete	Adopt/M	35R	605-45
06-4	Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements	Complete	Adopt	92	715-60
06-5	Accounting for Purchases of Life Insurance—Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4	Complete	Adopt/M	21R	325-30
06-6	Debtor's Accounting for a Modification (or Exchange) of Convertible Debt Instruments	Pending			470-50
06-7	Issuer's Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133	Complete	N/A	App D - NA GAAP	470-20 815-15
06-8	Applicability of the Assessment of a Buyer's Continuing Investment under FASB Statement No. 66 for Sales of Condominiums	Complete	Adopt/M	40R	360-20
06-9	Reporting a Change in (or the Elimination of) a Previously Existing Difference between the Fiscal Year-End of a Parent Company and That of a Consolidated Entity or between the Reporting Period of an Investor and That of an Equity Method Investee	Complete	Adopt/M	48, 97	810-10
06-10	Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements	Complete	N/A	App D - NA GAAP	715-60
06-11	Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards	Pending			718-740
06-12	Accounting for Physical Commodity Inventories for Entities within the Scope of the AICPA Audit and Accounting Guide, Brokers and Dealers in Securities	No EITF Consensus			
07-1	Accounting for Collaborative Arrangements	Complete	N/A	App D - NA GAAP	808-10
07-2	Accounting for Convertible Debt Instruments That Are Not Subject to the Guidance in Paragraph 12 of APB Opinion No. 14	Removed from Agenda			
07-3	Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities	Complete	N/A	17, 29	730-10 730-20
07-4	Application of the Two-Class Method under FASB Statement No. 128 to Master Limited Partnerships	Complete	N/A	App D - NA GAAP	260-10

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
07-5	Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity's Own Stock	Complete	N/A	App D - NA GAAP	718-10 815-40
07-6	Accounting for the Sale of Real Estate Subject to the Requirements of FASB Statement No. 66, When the Agreement Includes a Buy-Sell Clause	Complete	Adopt	40R	360-20
08-1	Revenue Recognition for a Single Unit of Accounting (The name of EITF 08-1 has be changed to "Revenue Arrangements with Multiple Deliverables."	Reflected in ASU 2009-13			Not Explicitly Included in Codification.
08-2	Lessor Revenue Recognition for Maintenance Services	Removed from Agenda			
08-3	Accounting by Lessees for Maintenance Deposits	Superseded by ASU 2016-02 Complete	 Adopt/M N/A	 19, 22 22R	840-10
08-4	Transition Guidance for Conforming Changes to Issue No. 98-5	Pending			Not Explicitly Included in Codification.
08-5	Issuer's Accounting for Liabilities Measured at Fair Value with a Third-Party Credit Enhancement	Pending			820-10 825-10
08-6	Equity Method Investment Accounting Considerations	Pending			323-10
08-7	Accounting for Defensive Intangible Assets	Complete	Adopt/M	20	350-30
08-8	Accounting for an Instrument (or an Embedded Feature) with a Settlement Amount That Is Based on the Stock of an Entity's Consolidated Subsidiary	Complete	N/A	App D - NA GAAP	810-10 815-10 815-40
08-9	Milestone Method of Revenue Recognition	Reflected in ASU 2010-17			Not Explicitly Included in Codification.
08-10	Selected Statement 160 Implementation Questions	No EITF Consensus			
09-1	Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance	Reflected in ASU 2009-15			Not Explicitly Included in Codification.
09-2	Research and Development Assets Acquired in an Asset Acquisition	Removed from Agenda			
09-3	Applicability of AICPA Statement of Position 97-2 to Certain Arrangements That Include Software Elements	Reflected in ASU 2009-14			Not Explicitly Included in Codification.

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP CONSENSUS OPINIONS OF THE EMERGING ISSUES TASK FORCE

GAAP Pronounce-ment	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
09-4	Seller Accounting for Contingent Consideration	No EITF Consensus			

Note: "EITF Abstracts, Appendix D - Other Technical Matters" have been included in the FASB Codification, but have not previously been reviewed for statutory accounting. As such, these items have not been included in this Appendix D. Before the FASB Codification, these items were not considered to be in the top three levels of the FASB hierarchy and, thus, not reviewed as part of the statutory maintenance process.

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PRE-CODIFICATION STANDARDS - CATEGORY C GAAP
AICPA PRACTICE BULLETINS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
PB 1	Purpose and Scope of AcSEC Practice Bulletins and Procedures for Their Issuance	Complete			
	Exhibit A	Complete	Adopt	19	310-10
	Exhibit B through Exhibit H	Complete	N/A		360-10
	Exhibit I	Complete	Adopt	38	
PB 2	Elimination of Profits Resulting From Intercompany Transfers of LIFO Inventories	Complete	N/A	App D - NA GAAP	810-10
PB 3	Prepayments Into the Secondary Reserve of the FSLIC and Contingencies Related to Other Obligations of the FSLIC	Withdrawn 1990			
PB 4	Accounting for Foreign Debt/Equity Swaps	Complete	Adopt	26R	942-310
PB 5	Income Recognition on Loans to Financially Troubled Countries	Complete	N/A	App D - NA GAAP	942-310
PB 6	Amortization of Discounts on Certain Acquired Loans	Superseded by SOP 03-3			
		Complete	Reject	37	
PB 7	Criteria for Determining Whether Collateral for a Loan Has Been In-Substance Foreclosed	Withdrawn 1994			
PB 8	Application of FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses From the Sale of Investments, to Insurance Enterprises	Complete	Reject	51R, 52	944-20 944-30 944-60 944-605 944-825
PB 9	Disclosures of Fronting Arrangements by Fronting Companies	Superseded by FAS 113			
PB 10	Amendment to Practice Bulletin 7, Criteria for Determining Whether Collateral for a Loan Has Been In-Substance Foreclosed	Withdrawn 1994			
PB 11	Accounting for Preconfirmation Contingencies in Fresh-Start Reporting	Complete	N/A	App D - NA GAAP	Not Explicitly Included in Codification.
PB12	Reporting Separate Investment Fund Option Information of Defined Contribution Pension Plans	Superseded by SOP 99-3			
		Complete	N/A	App D - NA GAAP	
PB 13	Direct-Response Advertising and Probable Future Benefits	Complete	Reject	29	340-20 944-30
PB 14	Accounting and Reporting by Limiting Liability Companies and Limited Liability Partnerships	Complete	N/A	App D - NA GAAP	272-10 850-10
PB 15	Accounting by the Issuer of Surplus Notes	Complete	Reject	41R	944-470

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PRE-CODIFICATION STANDARDS - CATEGORY D GAAP
AICPA ACCOUNTING INTERPRETATIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
AIN-ARB43 Chapter 13B	Compensation Involved in Stock Option and Stock Purchase Plans: Unofficial Accounting Interpretations of Accounting Research Bulletin No. 43, Chapter 13B	Superseded by APB 25			
AIN-Key Man Life	Deferred Compensation Contracts: Unofficial Accounting Interpretations	Superseded by FTB 85-4			
AIN-ARB51	Consolidated Financial Statements: Accounting Interpretations of ARB No. 51	Superseded by FAS 111			
AIN-APB4	Accounting for the Investment Credit: Accounting Interpretations of APB Opinion No. 4	Complete Items 1, 2, & 3 Items 4, 5, & 6 Superseded by FAS 96, 109 & 111	Reject	10, 10R, 101	Not Included in Codification As No Longer Applicable Or Relevant
AIN-APB7	Accounting for Leases in Financial Statements of Lessors: Accounting Interpretations of APB Opinion No. 7	Superseded by FAS 111			
AIN-APB8	Accounting for the Cost of Pension Plans: Accounting Interpretation of APB Opinion No. 8	Superseded by FAS 111			
AIN-APB9	Reporting the Results of Operations: Unofficial Accounting Interpretations of APB Opinion No. 9	Complete Item 1 Item 2 Superseded by FAS 111	Reject	3	225-20
AIN-APB11	Accounting for Income Taxes: Accounting Interpretations of APB Opinion No. 11	Deleted by FAS 96 & FAS 109			
AIN-APB15	Computing Earnings per Share: Accounting Interpretations of APB Opinion No. 15	Superseded by FAS 128 Complete	N/A	App D – NA GAAP	
AIN-APB16	Business Combinations: Accounting Interpretations of APB Opinion No. 16	Superseded by FAS 141 Complete	Reject Reject No. 39	68 25	

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PRE-CODIFICATION STANDARDS - CATEGORY D GAAP
AICPA ACCOUNTING INTERPRETATIONS

GAAP Pronouncement	Name	Status	Disposition	Statutory Reference	Acctg. Stds. Codification Topic-Subt.
AIN-APB17	Intangible Assets: Unofficial Accounting Interpretations of APB Opinion No. 17	Superseded by FAS 142 Complete	 Reject	 68	
AIN-APB18	The Equity Method of Accounting for Investments in Common Stock: Accounting Interpretations of APB Opinion No. 18	Complete	Reject	46, 88, 97	323-10 323-30 810-10
AIN-APB19	Reporting Changes in Financial Position: Accounting Interpretations of APB Opinion No. 19	Superseded by FAS 95			
AIN-APB20	Accounting Changes: Accounting Interpretations of APB Opinion No. 20	Superseded by FAS 128 Complete	 Reject	 3	
AIN-APB21	Interest on Receivables and Payables: Accounting Interpretations of APB Opinion No. 21	Complete	Adopt	15	932-835
AIN-APB22	Disclosure of Accounting Policies: Accounting Interpretations of APB Opinion No. 22	Superseded by FAS 111			
AIN-APB23	Accounting for Income Taxes: Special Areas: Accounting Interpretations of APB Opinion No. 23	Superseded by FAS 96 & FAS 109			
AIN-APB25	Accounting for Stock Issued to Employees: Accounting Interpretations of APB Opinion No. 25	Superseded by FAS 123(R) Complete	 Adopt N/A	 13 104R	
AIN-APB26	Early Extinguishment of Debt: Accounting Interpretations of APB Opinion No. 26	Complete	Adopt	15	470-20 470-50
AIN-APB30	Reporting the Result of Operations: Accounting Interpretations of APB Opinion No. 30	Complete	Reject	24	225-20

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Appendix D
Nonapplicable GAAP Pronouncements for Statutory Accounting as of December 2023

In 2015, Issue Paper No. 99—Nonapplicable GAAP Pronouncements was removed from Appendix E and incorporated into this section of Appendix D.

For items presented to the Statutory Accounting Principles (E) Working Group, this table addresses Generally Accepted Accounting Principles (GAAP) pronouncements that are nonapplicable due to one of the following reasons:

a. The pronouncement does not relate to the insurance industry;

b. The pronouncement is not within the objectives of statutory accounting;

c. The pronouncement would not add a substantive amount of guidance to statutory accounting due to the narrow scope of the topic;

d. The pronouncement relates to transition of a previously issued GAAP pronouncement.

For items previously presented to the Emerging Accounting Issues (E) Working Group, this table includes references to EITFs that have been rejected for the following reasons:

a. Rejected as not applicable to statutory accounting;

b. Rejected without providing additional statutory guidance;

c. Rejected on the basis of issues rejected in a SSAP.

*NOTE: EITFs marked with an asterisk were rejected as not applicable to statutory accounting on the basis of issues rejected in a SSAP (paragraph c. above).

GAAP pronouncements[1] not considered applicable to NAIC statutory accounting principles are summarized as follows:

NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
FASB Accounting Standards Updates (ASU)	
ASU 2009-02	Omnibus Update—Amendments to Various Topics for Technical Corrections
ASU 2009-13	Revenue Recognition: Multiple Deliverable Revenue Arrangements
ASU 2009-15	Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing
ASU 2010-01	Equity: Accounting for Distributions to Shareholders with Components of Stock and Cash
ASU 2010-03	Extractive Activities—Oil and Gas (Topic 932): Oil and Gas Reserve Estimation and Disclosures
ASU 2010-16	Entertainment—Casinos (Topic 924): Accruals for Casino Jackpot Liabilities

[1] Non-EITF GAAP guidance that is rejected explicitly in an SSAP is not included within this listing.

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
ASU 2010-17	Revenue Recognition—Milestone Method (Topic 605): Milestone Method of Revenue Recognition
ASU 2010-24	Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries
ASU 2010-25	Plan Accounting—Defined Contribution Pension Plans (Topic 962): Reporting Loans to Participants by Defined Contribution Pension Plans
ASU 2010-27	Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers
ASU 2011-05	Comprehensive Income (Topic 220): Presentation of Comprehensive Income
ASU 2011-07	Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities
ASU 2011-12	Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU 2011-05
ASU 2012-01	Health Care Entities (Topic 954): Continuing Care Retirement Communities—Refundable Advance Fees
ASU 2012-04	Technical Corrections and Improvements
ASU 2012-07	Entertainment—Films (Topic 926): Accounting for Fair Value Information That Arises after the Measurement Date and Its Inclusion in the Impairment Analysis of Unamortized Film Costs
ASU 2013-02	Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income
ASU 2013-07	Presentation of Financial Statements (Topic 205): Liquidation Basis of Accounting
ASU 2013-08	Financial Services – Investment Companies – Amendments to the Scope, Measurement and Disclosure Requirements
ASU 2013-12	Definition of a Public Business Entity—An Addition to the Master Glossary
ASU 2014-06	Technical Corrections and Improvements Related to Glossary Terms
ASU 2014-10	Development Stage Entities (Topic 915): Elimination of Certain Financial Reporting Requirements, Including an Amendment to Variable Interest Entities Guidance in Topic 810, Consolidation
ASU 2014-13	Measuring the Financial Assets and Financial Liabilities of a Consolidated Collateralized Financing Entity
ASU 2015-06	Effects on Historical Earnings per Unit of Master Limited Partnership Dropdown Transactions
ASU 2015-08	Business Combinations—Pushdown Accounting, Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115
ASU 2015-10	Technical Corrections & Improvements
ASU 2015-11	Inventory (Topic 330)—Simplifying the Measurement of Inventory
ASU 2015-12	Plan Accounting: Defined Benefit Pension Plans (Topic 960); Defined Contribution Pension Plans (Topic 962); Health and Welfare Benefit Plans (Topic 965)
ASU 2015-13	Derivatives and Hedging (Topic 815)—Application of the Normal Purchases and Normal Sales Scope Exception to Certain Electricity Contracts within Nodal Energy Markets
ASU 2016-04	Liabilities—Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products
ASU 2016-11	Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting
ASU 2016-14	Presentation of Financial Statements of Not-for-Profit Entities
ASU 2017-02	Clarifying When a Not-for-Profit Entity That Is a General Partner or a Limited Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity
ASU 2017-03	Amendments to SEC Guidance

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
ASU 2017-06	Defined Benefit Pension Plans, Defined Contribution Pension Plans, and Health and Welfare Benefit Plan – Master Trust Reporting
ASU 2017-13	Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842), Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017, EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments
ASU 2017-14	Amendments to SEC Paragraphs in Topic 220, Topic 605 and Topic 606
ASU 2017-15	Codification Improvements to Topic 995, U.S. Steamship Entities, Elimination of Topic 995
ASU 2018-02	Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income
ASU 2018-04	Investments—Debt Securities (Topic 320) and Regulated Operations (Topic 980), Amendments to SEC Paragraphs
ASU 2018-05	Income Taxes (Topic 740), Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118
ASU 2018-06	Codification Improvements to Topic 942, Financial Services—Depository and Lending
ASU 2018-08	Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made
ASU 2018-09	Codification Improvements
ASU 2019-02	Improvements to Accounting for Costs of Films and License Agreements for Program Materials, a consensus of the FASB Emerging Issues Task Force
ASU 2019-03	Updating the Definition of Collections
ASU 2019-07	Codification Updates to SEC Sections: Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10532, Disclosure Update and Simplification, and Nos. 33-10231 and 33-10442, Investment Company Reporting Modernization, and Miscellaneous Updates
ASU 2019-09	Financial Services – Insurance: Effective Date
ASU 2020-02	Amendments to SEC Paragraphs in Credit Losses (Topic 326) and Leases (Topics 842)
ASU 2020-05	Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842), Effective Dates for Certain Entities
ASU 2020-07	Presentation and Disclosures by Not-for-Profit Entities
ASU 2020-09	Amendments to SEC Paragraphs Pursuant to SEC Release No. 33-10762—Debt (Topic 470)
ASU 2020-10	Codification Improvements
ASU 2020-11	Financial Services – Insurance: Effective Date and Early Application
ASU 2021-06	Presentation of Financial Statements (Topic 205), Financial Services—Depository and Lending (Topic 942), and Financial Services— Investment Companies (Topic 946), Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10786, Amendments to Financial Disclosures about Acquired and Disposed Businesses, and No. 33-10835, Update of Statistical Disclosures for Bank and Savings and Loan Registrants
Pre-Codification FASB Statements (FAS)	
FAS 03	Reporting Accounting Changes in Interim Financial Statements—An Amendment of APB Opinion No. 28
FAS 06	Classification of Short-Term Obligations Expected to Be Refinanced—An Amendment of ARB No. 43, Chapter 3A
FAS 11	Accounting for Contingencies: Transition Method—An Amendment of FASB Statement No. 5
FAS 14	Financial Reporting for Segments of a Business Enterprise
FAS 18	Financial Reporting for Segments of a Business Enterprise: Interim Financial Statements—An Amendment of FASB Statement No. 14
FAS 19	Financial Accounting and Reporting by Oil and Gas Producing Companies
FAS 21	Suspension of the Reporting of Earnings per Share and Segment Information by Nonpublic Enterprises—An Amendment of APB Opinion No. 15 and FASB Statement No. 14

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
FAS 24	Reporting Segment Information in Financial Statements That Are Presented in Another Enterprise's Financial Report—An Amendment of FASB Statement No. 14
FAS 25	Suspension of Certain Accounting Requirements for Oil and Gas Producing Companies—An Amendment of FASB Statement No. 19
FAS 30	Disclosure of Information about Major Customers—An Amendment of FASB Statement No. 14
FAS 35	Accounting and Reporting by Defined Benefit Pension Plans
FAS 37	Balance Sheet Classification of Deferred Income Taxes—An Amendment of APB Opinion No. 11
FAS 44	Accounting for Intangible Assets of Motor Carriers—An Amendment of Chapter 5 of ARB No. 43 and an Interpretation of APB Opinions 17 and 30
FAS 45	Accounting for Franchise Fee Revenue
FAS 47	Disclosure of Long-Term Obligations
FAS 48	Revenue Recognition When Right of Return Exists
FAS 49	Accounting for Product Financing Arrangements
FAS 50	Financial Reporting in the Record and Music Industry
FAS 51	Financial Reporting by Cable Television Companies
FAS 53	Financial Reporting by Producers and Distributors of Motion Picture Films
FAS 63	Financial Reporting by Broadcasters
FAS 65	Accounting for Certain Mortgage Banking Activities
FAS 68	Research and Development Arrangements
FAS 69	Disclosures about Oil and Gas Producing Activities—An Amendment of FASB Statements 19, 25, 33, and 39
FAS 71	Accounting for the Effects of Certain Types of Regulation
FAS 72	Accounting for Certain Acquisitions of Banking or Thrift Institutions—An Amendment of APB Opinion No. 17, an Interpretation of APB Opinions 16 and 17, and An Amendment of FASB Interpretation No. 9
FAS 73	Reporting a Change in Accounting for Railroad Track Structures—An Amendment of APB Opinion No. 20
FAS 75	Deferral of the Effective Date of Certain Accounting Requirements for Pension Plans of State and Local Governmental Units—An Amendment of FASB Statement No. 35
FAS 78	Classification of Obligations That Are Callable by the Creditor—An Amendment of ARB No. 43, Chapter 3A
FAS 85	Yield Test for Determining whether a Convertible Security Is a Common Stock Equivalent—An Amendment of APB Opinion No. 15
FAS 89	Financial Reporting and Changing Prices
FAS 90	Regulated Enterprises—Accounting for Abandonments and Disallowances of Plant Costs—An Amendment of FASB Statement No. 71
FAS 92	Regulated Enterprises—Accounting for Phase-In Plans— An Amendment of FASB Statement No. 71
FAS 93	Recognition of Depreciation by Not-for-Profit Organizations
FAS 99	Deferral of the Effective Date of Recognition of Depreciation by Not-for-Profit Organizations—An Amendment of FASB Statement No. 93
FAS 101	Regulated Enterprises—Accounting for the Dis-continuation of Application of FASB Statement No. 71
FAS 110	Reporting by Defined Benefit Pension Plans of Investment Contracts—An Amendment of FASB Statement No. 35
FAS 111	Rescission of FASB Statement No. 32 and Technical Corrections
FAS 117	Financial Statements of Not-for-Profit Organizations
FAS 124	Accounting for Certain Investments Held by Not-For-Profit Organizations
FAS 128	Earnings per Share
FAS 130	Reporting Comprehensive Income

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
FAS 131	Segment Disclosures
FAS 134	Accounting for Mortgage-Backed Securities Retained after the Securitization of Mortgage Loans Held for Sale by a Mortgage Banking Enterprise, An Amendment of FASB Statement No. 65
FAS 135	Rescission of FASB Statement No. 75 and Technical Corrections
FAS 136	Transfers of Assets to a Not-For-Profit Organization or Charitable Trust that Raises or Holds Contributions for Others
FAS 139	Rescission of FASB Statement No. 53
FAS 143	Accounting for Asset Retirement Obligations
FAS 147	Acquisitions of Certain Financial Institutions, An Amendment of FASB Statements No. 72 and 144 and FASB Interpretation No. 9
FAS 151	Inventory Costs, and amendment of ARB No. 43 (FAS 151), Chapter 4
FAS 159	The Fair Value Option for Financial Assets and Financial Liabilities
FAS 160	Noncontrolling Interests in Consolidated Financial Statements—An Amendment of ARB No. 51
Pre-Codification FASB Interpretations	
FIN 01 (APB 20)	Accounting Changes Related to the Cost of Inventory
FIN 08 (FASB 6)	Classification of a Short-Term Obligation Repaid Prior to Being Replaced by a Long-Term Security
FIN 09 (APB 16 & 17)	Applying APB Opinions No. 16 and 17 When a Savings and Loan Association or a Similar Institution is Acquired in a Business Combination Accounted for by the Purchase Method
FIN 31 (APB 15 & FASB 28)	Treatment of Stock Compensation Plans in EPS Computations
FIN 33 (FASB 34)	Applying FASB Statement No. 34 to Oil and Gas Producing Operations Accounted for by the Full Cost Method
FIN 36 (FASB 19)	Accounting for Exploratory Wells in Progress at the End of a Period
FIN 42 (FASB 116)	Accounting for Transfers of Assets in Which a Not-for-Profit Organization is Granted Variance Power
FIN 47 (FASB 143)	Accounting for Conditional Asset Retirement Obligations
Pre-Codification Accounting Principles Board Opinions (APB)	
APB 13	Amending Paragraph 6 of APB Opinion No. 9, Application to Commercial Banks
APB 15	Earnings Per Share
Pre-Codification Accounting Research Bulletins (ARB)	
ARB 43	Restatement and Revision of Accounting Research Bulletins, Chapter 4
ARB 45	Long-Term Construction-Type Contracts
Pre-Codification FASB Technical Bulletins (TB)	
TB 79-1	Purpose and Scope of FASB Technical Bulletins and Procedures for Issuance
TB 79-3	Subjective Acceleration Clauses in Long-Term Debt Agreements
TB 79-4	Segment Reporting of Puerto Rican Operations
TB 79-5	Meaning of the Term "Customer" as it Applies to Health Care Facilities under FASB Statement No. 14
TB 79-8	Applicability of FASB Statements 21 and 33 to Certain Brokers and Dealers in Securities

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
TB 82-2	Accounting for the Conversion of Stock Options into Incentive Stock Options as a Result of the Economic Recovery Tax Act of 1981
TB 84-1	Accounting for Stock Issued to Acquire the Results of a Research and Development Arrangement
TB 85-1	Accounting for the Receipt of Federal Home Loan Mortgage Corporation Participating Preferred Stock
TB 87-2	Computation of a Loss on an Abandonment
TB 87-3	Accounting for Mortgage Servicing Fees and Rights
TB 90-1	Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts
Pre-Codification FASB Staff Positions (FSP)	
FSP FAS 19-1	Accounting for Suspended Well Costs
FSP FAS 117-1	Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds
FSP FAS 126-1	Disclosure and Interim Reporting for Obligors for Conduit Debt Securities
FSP FAS 143-1	Accounting for Electronic Equipment Waste Obligations
FSP FAS 150-3	Effective Date, Disclosures and Transition for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests Under FASB Statement No. 150
FSP FAS 150-5	Issuer's Accounting Under FASB Statement 150 for Freestanding Warrants and Other Similar Instruments on Shares That are Redeemable
FSP FIN 46(R)-7	Application of FASB Interpretation No. 46(R) to Investment Companies
FSP AAGINV-1 and SOP 94-4-1	Reporting of Fully Benefit-Responsive Investment Contracts Held by Certain Investment Companies Subject to the AICPA Investment Company Guide and Defined-Contribution Health and Welfare and Pension Plans
FSP AUG AIR-1	Accounting for Planned Major Maintenance Activities
FSP SOP 78-9-1	Interaction of AICPA Statement of Position 78-9 and EITF Issue 04-5
FSP SOP 90-7-1	An Amendment of AICPA Statement of Position 90-7
FSP SOP 94-3-1 and AAG HCO-1	*Omnibus Changes to Consolidate and Equity Method Guidance for Not-For-Profit Organizations*
FSP SOP 07-1-1	Effective Date of AICPA Statement of Position 07-1
FSP EITF 85-24-1	Application of EITF Issue No. 85-24 When Cash for the Right to Future Distribution Fees for Shares Previously Sold is Received from Third Parties
Pre-Codification AICPA Statement of Positions	
SOP 14040	Confirmation of Insurance Policies in Force
SOP 14060	Auditing Property and Liability Reinsurance
SOP 14070	Auditing Life Reinsurance
SOP 74-8	Financial Accounting and Reporting by Colleges and Universities
SOP 75-2	Accounting Practices of Real Estate Investment Trusts
SOP 76-3	Accounting Practices for Certain Employee Stock Ownership Plans
SOP 78-9-1	Interaction of AICPA Statement of Position 78-9 and EITF Issue No. 04-5
SOP 78-10	Accounting Principles and Reporting Practices for Certain Nonprofit Organizations
SOP 81-1	Accounting for Performance of Construction-Type and Certain Production-Type Contracts
SOP 82-1	Accounting and Financial Reporting for Personal Financial Statements
SOP 83-1	Reporting by Banks of Investment Securities Gains or Losses
SOP 85-3	Accounting by Agricultural Producers and Agricultural Cooperatives
SOP 87-2	Accounting for Joint Costs of Informational Materials and Activities of Not-For-Profit Organizations That Include a Fund-Raising Appeal
SOP 88-1	Accounting for Developmental and Preoperating Costs, Purchases and Exchanges of Take-off and Landing Slots, and Airframe Modifications

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
SOP 89-2	Reports on Audited Financial Statements of Investment Companies
SOP 89-3	Questions Concerning Accountants' Services on Prospective Financial Statements
SOP 89-5	Financial Accounting and Reporting by Providers of Prepaid Health Care Services
SOP 89-7	Report on the Internal Control Structure in Audits of Investment Companies
SOP 90-1	Accountants' Services on Prospective Financial Statements for Internal Use Only and Partial Presentations
SOP 90-2	Report on Internal Control Structure in Audits of Futures Commission Merchants
SOP 90-7	Financial reporting by entities in reorganization under the Bankruptcy Code
SOP 90-8	Financial Accounting and Reporting by Continuing Care Retirement Communities
SOP 91-1	Software Revenue Recognition
SOP 92-2	Questions and Answers on the Term *Reasonably Objective Basis* and Other Issues Affecting Prospective Financial Statements
SOP 92-6	Accounting and Reporting by Health and Welfare Benefit Plans
SOP 92-8	Auditing Property/Casualty Insurance Entities Statutory Financial Statements—Applying Certain Requirements of the NAIC Annual Statement Instructions
SOP 92-9	Audits of Not-for-Profit Organizations Receiving Federal Awards
SOP 93-1	Financial Accounting and Reporting for High-Yield Debt Securities by Investment Companies
SOP 93-2	Determination, Disclosure, and Financial Statement Presentation of Income, Capital Gain, and Return of Capital Distributions by Investment Companies
SOP 93-3	Rescission of Accounting Principles Board Statements
SOP 93-4	Foreign Currency Accounting and Financial Statement Presentation for Investment Companies
SOP 93-5	Reporting on Required Supplementary Information Accompanying Compiled or Reviewed Financial Statements of Common Interest Realty Associations
SOP 93-8	The Auditor's Consideration of Regulatory Risk-Based Capital for Life Insurance Enterprises
SOP 94-1	Inquiries of State Insurance Regulators
SOP 94-2	The Application of the Requirements of Accounting Research Bulletins, Opinions of the Accounting Principles Board, and Statements and Interpretations of the Financial Accounting Standards Board to Not-for-Profit Organizations
SOP 94-3	Reporting of Related Entities by Not-for-Profit Organizations
SOP 94-4	Reporting of Investment Contracts Held by Health and Welfare Benefit Plans and Defined-Contribution Pension Plans
SOP 95-2	Financial Reporting by Nonpublic Investment Partnerships
SOP 95-3	Accounting for Certain Distribution Costs of Investment Companies
SOP 95-4	Letters for State Insurance Regulators to Comply with the NAIC Model Audit Rule
SOP 95-5	Auditor's Reporting on Statutory Financial Statements of Insurance Enterprises
SOP 98-2	Accounting for Costs of Activities of Not-for-Profit Organizations and State and Local Governmental Entities That Include Fund Raising
SOP 98-3	Audits of States, Local Governments, and Not-for-Profit Organizations Receiving Federal Awards
SOP 98-6	Reporting on Management's Assessment Pursuant to the Life Insurance Ethical Market Conduct Program of the Insurance Marketplace Standards Association
SOP 98-8	Engagements to Perform Year 2000 Agreed-Upon Procedures Attestation Engagements Pursuant to Rule 17a-5 of the Securities Exchange Act of 1934, Rule 17Ad-18 of the Securities Exchange Act of 1934, and Advisories No. 17-98 and No. 42-98 of the Commodity Futures Trading Commission
SOP 99-1	Guidance To Practitioners In Conducting And Reporting On An Agreed-Upon Procedures Engagement To Assist Management In Evaluating The Effectiveness Of Its Corporate Compliance Program
SOP 99-2	Accounting for and Reporting of 401(h) Features of Defined Benefit Pension Plans

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
SOP 99-3	Accounting and Reporting of Certain Defined Contribution Plan Investments and Other Disclosure Matters
SOP 00-1	Auditing Health Care Third-Party Revenues and Related Receivables
SOP 00-2	Accounting by Producers of Films
SOP 01-1	Amendment to Scope of Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships, to include Commodity Pools
SOP 01-2	Accounting and Reporting by Health and Welfare Benefit Plans
SOP 01-3	Performing Agreed-Upon Procedures Engagements That Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law
SOP 01-4	Reporting Pursuant to the Association for Investment Management and Research Performance Presentation Standards
SOP 01-6	Accounting by Certain Entities (Including Entities with Trade Receivables) That Lend to or Finance the Activities of Others
SOP 02-1	Performing Agreed Upon Procedures Engagements That Address Annual Claims Prompt Payment Reports as Required by the New Jersey Administrative Code
SOP 02-2	Accounting for Derivative Instruments and Hedging Activities by Not-for-Profit Health Care Organizations, and Clarification of the Performance Indicator
SOP 03-2	Attest Engagements on Greenhouse Gas Emissions Information
SOP 03-4	Reporting Financial Highlights and Schedule of Investments by Nonregistered Investment Partnerships: An Amendment to the Audit and Accounting Guide Audits of Investment Companies and AICPA Statement of Position 95-2, Financial Reporting by Nonpublic Investment Partnerships
SOP 03-5	Financial Highlights of Separate Accounts: An Amendment to the Audit and Accounting Guide "Audits of Investment Companies"
SOP 04-1	Auditing the Statement of Social Insurance
SOP 04-2	Accounting for Real Estate Time-Sharing Transactions
SOP 06-1	Reporting Pursuant to the Global Investment Performance Standards
SOP 07-1	Clarification of the Scope of the Audit and Accounting Guide Investment Companies and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies
SOP 07-2	Attestation Engagements That Address Specified Compliance Control Objectives and Related Controls at Entities That Provide Services to Investment Companies, Investment Advisers, or Other Service Providers
SOP 09-1	Performing Agreed-Upon Procedures Engagements That Address the Completeness, Accuracy or Consistency of XBRL-Tagged Data
Pre-Codification FASB EITF	
EITF 84-9	Deposit Float of Banks
EITF 85-8	Amortization of Thrift Intangibles
EITF 85-12	Retention of Specialized Accounting for Investments in Consolidation
EITF 85-13	Sale of Mortgage Service Rights on Mortgages Owned by Others
EITF 85-18	Earnings-per-Share Effect of Equity Commitment Notes
EITF 85-23	Effect of a Redemption Agreement on Carrying Value of a Security
EITF 85-24	Distribution Fees by Distributors of Mutual Funds That Do Not Have a Front-End Sales Charge
EITF 85-27	Recognition of Receipts from Made-Up Rental Shortfalls
EITF 85-31	Comptroller of the Currency's Rule on Deferred Tax Debits
EITF 85-41	Accounting for Savings and Loan Associations under FSLIC Management Consignment Program
EITF 85-42	Amortization of Goodwill Resulting from Recording Time Savings Deposits at Fair Values
EITF 85-44	Differences between Loan Loss Allowances for GAAP and RAP

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
EITF 86-2	Retroactive Wage Adjustments Affecting Medicare Payments
EITF 86-3	Retroactive Regulations regarding IRC Section 338 Purchase Price Allocations
EITF 86-5	Classifying Demand Notes with Repayment Terms
EITF 86-7	Recognition by Homebuilders of Profit from Sales of Land and Related Construction Contracts
EITF 86-12	Accounting by Insureds for Claims-Made Insurance Policies
EITF 86-13	Recognition of Inventory Market Declines at Interim Reporting Dates
EITF 86-24	Third-Party Establishment of Collateralized Mortgage Obligations
EITF 86-27	Measurement of Excess Contributions to a Defined Contribution Plan or Employee Stock Ownership Plan
EITF 86-30	Classification of Obligations When a Violation is Waived by the Creditor
EITF 86-31	Reporting the Tax Implications of a Pooling of a Bank and a Savings and Loan Association
EITF 86-40	Investments in Open-End Mutual Funds That Invest in U.S. Government Securities
EITF 86-44	Effect of a Change in Tax Law on Investments in Safe Harbor Leases
EITF 86-46	Uniform Capitalization Rules for Inventory under the Tax Reform Act of 1986
EITF 87-4	Restructuring of Operations: Implications of SEC Staff Accounting Bulletin No. 67
EITF 87-10	Revenue Recognition by Television (Barter) Syndicators
EITF 87-20	Offsetting Certificates of Deposit against High-Coupon Debt
EITF 87-22	Prepayments to the Secondary Reserve of the FSLIC
EITF 87-24	Allocation of Interest to Discontinued Operations
EITF 87-30	Sale of a Short-Term Loan Made under a Long-Term Credit Commitment
EITF 88-4	Classification of Payment Made to IRS to Retain Fiscal Year
EITF 88-16	Basis in Leveraged Buyout Transactions
EITF 88-19	FSLIC-Assisted Acquisitions of Thrifts
EITF 88-20	Difference between Initial Investment and Principal Amount of Loans in a Purchased Credit Card Portfolio
EITF 88-25	Ongoing Accounting and Reporting for a Newly Created Liquidating Bank
EITF 89-3	Balance Sheet Presentation of Savings Accounts in Financial Statements of Credit Unions
EITF 89-19	Accounting for a Change in Goodwill Amortization for Business Combinations Initiated Prior to the Effective Date of FASB Statement No. 72
EITF 89-20	Accounting for Cross Border Tax Benefit Leases
EITF 90-4	Earnings-per-Share Treatment of Tax Benefits for Dividends on Stock Held by an Employee Stock Ownership Plan
EITF 90-16	Accounting for Discontinued Operations Subsequently Retained
EITF 90-18	Effect of a “Removal of Accounts” Provision on the Accounting for a Credit Card Securitization
EITF 91-6	Revenue Recognition of Long-Term Power Sales Contracts
EITF 91-9	Revenue and Expense Recognition for Freight Services in Process
EITF 91-10	Accounting for Special Assessments and Tax Increment Financing Entities (TIFEs)
EITF 92-3	Earnings-per-Share Treatment of Tax Benefits for Dividends on Unallocated Stock Held by an Employee Stock Ownership Plan
EITF 92-5	Amortization Period for Net Deferred Credit Card Origination Costs
EITF 92-7	Accounting by Rate-Regulated Utilities for the Effects of Certain Alternative Revenue Programs
EITF 92-12	Accounting for OPEB Costs by Rate-Regulated Enterprises
EITF 92-13	Accounting for Estimated Payments in Connection with the Coal Industry Retiree Health Benefit Act of 1992
EITF 93-1	Accounting for Individual Credit Card Acquisitions
EITF 93-9	Application of FASB Statement No. 109 in Foreign Financial Statements Restated for General Price-Level Changes

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
EITF 93-12	Recognition and Measurement of the Tax Benefit of Excess Tax-Deductible Goodwill Resulting from a Retroactive Change in Tax Law
EITF 94-2	Treatment of Minority Interests in Certain Real Estate Investment Trusts
EITF 95-1	Revenue Recognition on Sales with a Guaranteed Minimum Resale Value
EITF 95-4	Revenue Recognition on Equipment Sold and Subsequently Repurchased Subject to an Operating Lease
EITF 95-6	Accounting by a Real Estate Investment Trust for an Investment in a Service Corporation
EITF 95-7	Implementation Issues Related to the Treatment of Minority Interests in Certain Real Estate Investment Trusts
EITF 95-22	Balance Sheet Classification of Borrowings Outstanding under Revolving Credit Agreements That Include both a Subjective Acceleration Clause and a Lock-Box Arrangement
EITF 96-7	Accounting for Deferred Taxes on In-Process Research and Development Activities Acquired in a Purchase Business Combination
EITF 96-16 *	Investor's Accounting for an Investee When the Investor Has a Majority of the Voting Interest but the Minority Shareholder or Shareholders Have Certain Approval or Veto Rights
EITF 96-17	Revenue Recognition under Long-Term Power Sales Contracts That Contain both Fixed and Variable Pricing Terms
EITF 97-1	Implementation Issues in Accounting for Lease Transactions, Including Those Involving Special-Purpose Entities
EITF 97-2	Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain Other Entities with Contractual Management Arrangements
EITF 97-3 *	Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations after the Issuance of FASB Statement No. 25
EITF 97-4	Deregulation of the Pricing of Electricity
EITF 97-6	Application of Issue No. 96-20 to Qualifying Special-Purpose Entities Receiving Transferred Financial Assets Prior to the Effective Date of FASB Statement No. 125
EITF 97-7	Accounting for Hedges of the Foreign Currency Risk Inherent in an Available-for-Sale Marketable Equity Security
EITF 97-9	Effect on Pooling-of-Interests Accounting of Certain Contingently Exercisable Options or Other Equity Instruments
EITF 97-10 *	The Effect of Lessee Involvement in Asset Construction
EITF 97-15	Accounting for Contingency Arrangements Based on Security Prices in a Purchase Business Combinations
EITF 98-1	Valuation of Debt Assumed in a Purchase Business Combination
EITF 98-10	Accounting for Contracts Involved in Energy Trading and Risk Management Activities
EITF 99-1	Accounting for Debt Convertible into the Stock of a Consolidated Subsidiary
EITF 99-3	Application of Issue No. 96-13 to Derivative Instruments with Multiple Settlement Alternatives
EITF 99-5	Accounting for Pre-Production Costs Related to Long-Term Supply Arrangements
EITF 99-6	Impact of Acceleration Provisions in Grants Made between Initiation and Consummation of a Pooling-of-Interests Business Combination
EITF 99-7	Accounting for an Accelerated Share Repurchase Program
EITF 99-11	Subsequent Events Caused by Year 2000
EITF 99-13	Application of Issue No. 97-10 and FASB Interpretation No. 23 to Entities that Enter into Leases with Governmental Entities
EITF 99-15	Accounting for Decreases in Deferred Tax Asset Valuation Allowances Established in a Purchase Business Combination as a Result of a Change in Tax Regulations
EITF 99-16	Accounting for Transactions with Elements of Research and Development Arrangements
EITF 99-18	Effect on Pooling-of-Interests Accounting on Contracts Indexed to a Company's Own Stock
EITF 99-19	Reporting Revenue Gross as a Principal versus Net as an Agent
EITF 00-4	Majority Owner's Accounting for a Transaction in the Shares of a Consolidated Subsidiary and a Derivative Indexed to the Minority Interest in That Subsidiary

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
EITF 00-6	Accounting for Freestanding Derivative Financial Instruments Indexed to, and Potentially Settled in, the Stock of a Consolidated Subsidiary
EITF 00-7	Application of Issue No. 96-13 to Equity Derivative Instruments That Contain Certain Provisions that Require Net Cash Settlement if Certain Events Outside the Control of the Issuer Occur
EITF 00-10	Accounting for Shipping and Handling Fees and Costs
EITF 00-14	Accounting for Certain Sales Incentives
EITF 00-15	Classification in the Statement of Cash Flows of the Income Tax Benefit Received by a Company upon Exercise of a Nonqualified Employee Stock Option
EITF 00-17	Measuring the Fair Value of Energy-Related Contracts in Applying Issue No. 98-10
EITF 00-19	Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, A Company's Own Stock
EITF 00-22	Accounting for "Points" and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to be Delivered in the Future
EITF 01-3	Accounting in a Business Combination for Deferred Revenue of an Acquiree
EITF 01-5 *	Application of FASB Statement No. 52 to an Investment Being Evaluated for Impairment That Will Be Disposed Of
EITF 01-6	The Meaning of "Indexed to a Company's Own Stock"
EITF 01-9	Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)
EITF 01-12	The Impact of the Requirements of FASB Statement No. 133 on Residual Value Guarantees in Connection with a Lease
EITF 01-14	Income Statement Characterization of Reimbursements Received for "Out-of-Pocket" Expenses Incurred
EITF 02-3 *	Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities
EITF 02-6	Classification in the Statement of Cash Flows of Payments Made to Settle an Asset Retirement Obligation within the Scope of FASB Statement No. 143
EITF 02-7 *	Unit of Accounting for Testing Impairment of Indefinite-Lived Intangible Assets
EITF 02-8	Accounting for Options Granted to Employees in Unrestricted, Publicly Traded Shares of an Unrelated Entity
EITF 02-13 *	Deferred Income Tax Considerations in Applying the Goodwill Impairment Test in FASB Statement No. 142
EITF 02-14 *	Whether the Equity Method of Accounting Applies When an Investor Does Not Have an Investment in Voting Stock of an Investee but Exercises Significant Influence through Other Means
EITF 02-16	Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor
EITF 02-17 *	Recognition of Customer Relationship Intangible Assets Acquired in a Business Combination
EITF 03-2	Accounting for the Transfer to the Japanese Government of the Substantial Portion of Employee Pension Fund Liabilities
EITF 03-6 *	Participating Securities and the Two-class Method under FASB Statement No. 128
EITF 03-10	Application of Issue No. 02-16 by Resellers to Sales Incentives Offered to Consumers by Manufacturers
EITF 03-11 *	Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133 and Not "Held for Trading Purposes" as Defined in Issue No. 02-3
EITF 03-12	The Impact of FASB Interpretation No. 45 on Issue No. 95-1
EITF 03-13	Applying the Conditions in Paragraph 42 of FASB Statement No. 144 in Determining Whether to Report Discontinued Operations
EITF 03-16 *	Accounting for Investments in Limited Liability Companies
EITF 04-1	Accounting for Preexisting Relationships between the Parties to a Business Combination
EITF 04-2	Whether Mineral Rights are Tangible or Intangible Assets

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NONAPPLICABLE GAAP PRONOUNCEMENTS FOR STATUTORY ACCOUNTING

GAAP Pronouncement	Title
EITF 04-3	Mining Assets: Impairment and Business Combinations
EITF 04-4	Allocation of Goodwill to Reporting Units for a Mining Enterprise
EITF 04-5	Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights
EITF 04-6	Accounting for Stripping Costs Incurred During Production in the Mining Industry
EITF 04-7	Determining Whether an Interest is a Variable Interest in a Potential Variable Interest Entity
EITF 04-8	The Effect of Contingently Convertible Instruments on Diluted Earnings per Share
EITF 04-10	Determining Whether to Aggregate Operating Segments That Do Not Meet the Quantitative Thresholds
EITF 04-13	Accounting for Purchases and Sales of Inventory with the Same Counterparty
EITF 05-5	Accounting for Early Retirement or Postemployment Programs with Specified Features (Such as Term Specified in Altersteilzeit Early Retirement Arrangements)
EITF 05-6	Determining the Amortization Period for Leasehold Improvements Purchased after Lease Inception or Acquired in a Business Combination
EITF 05-8	Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature
EITF 06-1	Accounting for Consideration Given by a Specific Provider to Manufacturers or Resellers of Equipment Necessary for an End-Customer to Receive Service from the Service Provider
EITF 06-07	Issuer's Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133
EITF 06-10	Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements
EITF 07-1	Accounting for Collaborative Arrangements
EITF 07-4	Application of the Two-Class Method under FAS 128 to Master Limited Partnerships
EITF 07-5	Determining Whether an Instrument (or Embedded Feature) is Indexed to an Entity's Own Stock
EITF 08-8	Accounting for an Instrument (or an embedded feature) with a Settlement Amount That is Based on the Stock of an Entity's Consolidated Subsidiary
Pre-Codification AICPA Practice Bulletins (PB)	
PB 2	Elimination of Profits Resulting From Intercompany Transfers of LIFO Inventories
PB 5	Income Recognition on Loans to Financially Troubled Countries
PB 11	Accounting for Preconfirmation Contingencies in Fresh-Start Reporting
PB 12	Reporting Separate Investment Fund Option Information of Defined-Contribution Pension Plans
PB 14	Accounting and Reporting by Limiting Liability Companies and Limited Liability Partnerships
Pre-Codification AICPA Accounting Interpretations (AIN)	
AIN-APB15	Computing Earnings per Share: Accounting Interpretations of APB Opinion No. 15

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Appendix D
FASB Codification Cross-Reference to GAAP Pronouncements as of December 2023

Information provided within this Appendix D supplement has been obtained from the FASB Cross-Reference Tool. This supplement serves as a reference tool in tracing the FASB Codification to pre-codification GAAP standards and post-codification GAAP accounting standard updates (ASU) that have been reviewed, or are pending review, as part of the current NAIC statutory accounting maintenance process. This supplement does not indicate which GAAP standards have been adopted, adopted with modification or rejected for statutory accounting, as this information is contained in previous sections of this appendix. The following information is not included within this supplement:

- Pre-codification GAAP guidance that has not been captured as part of the statutory accounting maintenance process, but that has been incorporated into the FASB codification, which includes FASB Derivative Implementation Group Issues; EITF Appendix D Topics; FASB Statement No. 138 Examples; FASB Staff Implementation Guides; AICPA Technical Inquiry Service and Audit and Accounting Guides

- SEC standards incorporated within the FASB Codification SEC Financial Reporting Releases; SEC Interpretive Releases; SEC Staff Accounting Bulletins; and SEC Regulation S-X.

- GAAP codification topics (and/or subtopics) that have been deemed not applicable to statutory accounting (e.g. Topic 920 – Entertainment-Films)

- GAAP codification topics (and/or subtopics) that had no reference to previous GAAP guidance reflected in the FASB Cross-Reference Tool.

The Audit and Accounting Guides (AAG) related to insurance have been reviewed for statutory accounting and are referenced in this supplement – HCO: Health Care Organizations, LHI: Life and Health Insurance and PLI: Property and Liability Insurance Companies.

GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
105 – Generally Accepted Accounting Principles			
105-10	Overall	2015-10; 2018-09; 2020-10; 2023-06	FAS 168
205 – Presentation of Financial Statements			
205-10	Overall	2011-05; 2013-07; 2014-08; 2019-07; 2020-10; 2021-06; 2023-05	FAS 52; FAS 130; FAS 144; ARB 43
205-20	Discontinued Operations	2014-08; 2015-10; 2023-05	FAS 128; FAS 142; FAS 144; SOP 94-6; EITF 87-24; EITF 03-13
205-30	Liquidation Basis of Accounting	2013-07	
205-40	Going Concern	2014-15	
210 –Balance Sheet			
210-10	Overall	2010-21; 2019-07	FAS 6; APB 12; ARB 43; SOP 81-1; SOP 90-7; SOP 00-2
210-20	Offsetting	2011-11; 2012-04; 2013-01	FIN 39; FIN 41; APB 10
215 – Statement of Shareholder Equity			

GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
220 – Comprehensive Income			
220-10	Overall	2011-05; 2011-12; 2013-02; 2016-01; 2016-13; 2017-07; 2017-12; 2018-02; 2018-09; 2018-12; 2019-07; 2020-10; 2023-03	FAS 130; FAS 133
225 – Income Statement			
225-10	Overall	2010-21	APB 09
225-20	Extraordinary and Unusual Items	2015-01	FAS 109; FAS 144; FIN 18; APB 09; APB 18; APB 28; APB 30; FTB 85-06; AIN-APB9; AIN-APB30
225-30	Business Interruption Insurance		EITF 01-13
230 – Statement of Cash Flows			
230-10	Overall	2010-08; 2012-04; 2012-05; 2013-08; 2014-08; 2015-07; 2016-01; 2016-02; 2016-09; 2016-13; 2016-14; 2016-15; 2016-18; 2018-07; 2018-08; 2023-06; 2023-08; 2023-09	FAS 95; FAS 102; FAS 132; EITF 95-13; EITF 02-06
235 – Notes to Financial Statements			
235-10	Overall	2014-09; 2019-07	APB 22
250 – Accounting Changes and Error Corrections			
250-10	Overall	2017-03; 2020-10; 2023-06	FAS 16; FAS 128; FAS 154; FAS 157; FIN 01; APB 9; APB 18; APB 28
255 – Changing Prices			
255-10	Overall	2016-02; 2021-05	FAS 52; FAS 89; SOP 93-3; EITF 04-03
260 – Earnings per Share			
260-10	Overall	2009-08; 2009-15; 2015-06; 2016-09; 2017-11; 2018-07; 2018-09; 2019-08; 2020-06; 2020-10; 2021-04; 2023-06	FAS 123(R); FAS 128; FAS 129; FAS 150; APB 18; FSP EITF 03-06-1; EITF 97-14; EITF 99-07; EITF 00-27; EITF 03-06; EITF 04-08; EITF 07-04
270 – Interim Reporting			
270-10	Overall	2010-20; 2011-11; 2013-02; 2014-04; 2014-08; 2014-09; 2015-09; 2015-11; 2016-01; 2016-02; 2016-13; 2018-12; 2019-07; 2020-09; 2020-10; 2022-02; 2022-04; 2023-02; 2023-06; 2023-07; 2023-08	FAS 16; FAS 157; APB 28
272 – Limited Liability Entities			
272-10	Overall	2010-08	FAS 109; EITF 03-16; PB 14
274 – Personal Financial Statements			
274-10	Overall	2015-10	SOP 82-1
275 – Risks and Uncertainties			
275-10	Overall	2014-09; 2014-10; 2015-11	FSP FAS 142-3; SOP 94-6
280 – Segment Reporting			
280-10	Overall	2014-08; 2023-07	FAS 131; FAS 142; FAS 146; TB 79-04; EITF 04-10
305 – Cash and Cash Equivalents			

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
310 – Receivables			
310-10	Overall	2010-20; 2010-25; 2011-01; 2011-04; 2012-04; 2014-04; 2014-09; 2014-14; 2016-02; 2016-13; 2016-20; 2019-04; 2020-10; 2021-05; 2022-01; 2022-02	FAS 5; FAS 65; FAS 95; FAS 102; FAS 107; FAS 114; FAS 118; FAS 133; FAS 140; APB 12; APB 21; ARB 43; FSP SOP 94-6-1; SOP 97-3; SOP 01-6; SOP 03-3; EITF 85-01; EITF 85-20; EITF 86-21; EITF 88-20; PB 01
310-20	Nonrefundable Fees and Other Costs	2016-13; 2017-08; 2020-08; 2022-02	FAS 91; EITF 84-19; EITF 92-05; EITF 93-01; EITF 97-03; EITF 99-20; EITF 01-07; SOP 01-6
310-30	Loans and Debt Securities Acquired with Deteriorated Credit Quality	2010-18; 2016-13	FAS 114; EITF 99-20; SOP 97-1; SOP 03-3
310-40	Troubled Debt Restructurings by Creditors	2010-18; 2010-20; 2011-02; 2014-04; 2014-14; 2016-13; 2016-19; 2022-02	FAS 15; FAS 114; FAS 118; TB 80-02; FSP FAS 144-1; EITF 87-18; EITF 87-19; EITF 89-14; EITF 94-08; EITF 96-22
320 – Investments–Debt and Equity Securities			
320-10	Overall	2015-10; 2016-01; 2016-13; 2018-04; 2018-09; 2019-04; 2019-11; 2022-01; 2022-02	FAS 115; FAS 140; TB 94-01; FSP FAS 115-1/124-1; SOP 78-9; EITF 86-40; EITF 96-10; EITF 96-11; EITF 96-12; EITF 96-15; EITF 98-13; EITF 98-15; EITF 99-20
321 – Investments-Equity Securities			
321-10	Overall	2018-03; 2019-04; 2020-01	
323 – Investments–Equity Method and Joint Ventures			
323-10	Overall	2010-02; 2013-08; 2014-02; 2016-01; 2016-07; 2016-13; 2017-05; 2018-07; 2019-06; 2020-01; 2021-03	FAS 128; FAS 130; FAS 142; FIN 35; FIN 46(R); APB 18; FSP APB 18-1; EITF 98-13; EITF 99-10; EITF 00-12; EITF 02-14; EITF 02-18; EITF 08-06; AIN-APB 18
323-30	Partnerships, Joint Ventures, and Limited Liability Entities		FSP APB 18-1; EITF 00-01; EITF 03-16; AIN-APB 18; SOP 78-9
323-740	Income Taxes	2014-01; 2016-01; 2017-03; 2023-02	EITF 94-01
325 – Investments–Other			
325-10	Overall	2016-01	FAS 60
325-20	Cost Method Investments	2016-01	APB 18; FSPFAS 115-1/124-1; EITF 91-05; EITF 94-01
325-30	Investments in Insurance Contracts		TB 85-04; FSP FTB 85-04-1; EITF 88-05; EITF 99-04; EITF 06-05
325-40	Beneficial Interests in Securitized Financial Assets	2016-13	EITF 99-20

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
326 – Financial Instruments – Credit Losses			
326-10	Overall	2016-13; 2017-03; 2018-19; 2019-04; 2019-05; 2019-10; 2019-11; 2020-03; 2022-01; 2022-02	
326-20	Measured at Amortized Cost	2016-13; 2018-19; 2019-04; 2019-11; 2020-02; 2020-03; 2022-01; 2022-02	
326-30	Available-for-Sale Debt Securities	2016-13; 2019-04; 2022-01	
330 – Inventory			
330-10	Overall	2012-04; 2014-09; 2015-11; 2017-07	FIN 01; ARB 43; EITF 86-13; EITF 86-46; EITF 96-09; EITF 01-09; SOP 94-6
340 – Other Assets and Deferred Costs			
340-10	Overall	2010-22; 2014-09	ARB 43 Chapter 3a; FSP AUG AIR-1; EITF 99-05
340-20	Capitalized Advertising Costs		SOP 93-7; PB 13
340-30	Insurance Contracts that Do Not Transfer Insurance Risk		SOP 98-7
340-40	Contracts with Customers	2014-09; 2016-20	
350 – Intangibles–Goodwill and Other			
350-10	Overall	2014-09; 2017-04; 2017-05; 2018-15; 2023-05; 2023-08	FAS 142; SOP 98-1; EITF 00-02
350-20	Goodwill	2010-28; 2011-08; 2012-04; 2014-02; 2016-03; 2017-04; 2019-06; 2019-10; 2021-03; 2023-05	FAS 131; FAS 142; EITF 02-13
350-30	General Intangibles Other than Goodwill	2012-02; 2017-04; 2018-01; 2018-12; 2023-05; 2023-08	FAS 142; FSP FAS 142-3; EITF 02-07; EITF 08-07
350-40	Internal Use Software	2014-09; 2015-05; 2016-19; 2017-04; 2018-15	SOP 98-1
350-50	Website Development Costs		SOP 98-1; EITF 00-02
350-60	Crypto Assets	2023-08	
360 – Property, Plant and Equipment			
360-10	Overall	2014-04; 2014-08; 2014-09; 2016-02; 2017-05; 2019-03; 2022-02	FAS 5; FAS 13; FAS 34; FAS 92; FAS 143; FAS 144; APB 12; ARB 43; TB 86-02; FSP AUG AIR-1; SOP 94-6; EITF 95-23; PB 1
360-20	Real Estate Sales	2011-10; 2014-09; 2016-19	FAS 66; FIN 43; EITF 84-17; EITF 86-06; EITF 87-09; EITF 88-12; EITF 88-24; EITF 95-23; EITF 98-08; EITF 00-13; EITF 06-08; EITF 07-06
405 – Liabilities			
405-10	Overall	2014-09; 2014-20; 2022-04; 2023-04	
405-20	Extinguishments of Liabilities	2016-04	FAS 140
405-30	Insurance-Related Assessments	2011-06	SOP 97-3
405-40	Obligations Resulting from Joint and Several Liabilities	2013-04; 2016-19	

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
405-50	Liabilities—Supplier Finance Programs	2022-04	
410 – Asset Retirement and Environmental Obligations			
410-20	Asset Retirement Obligations	2012-04; 2014-09	FAS 13; FAS 143; FIN 47; FSP FAS 143-1; EITF 89-13; EITF 90-08; EITF 02-06
410-30	Environmental Obligations	2012-04	SOP 94-6; SOP 96-1; EITF 89-13; EITF 90-08
420 – Exit or Disposal Cost Obligations			
420-10	Overall	2016-02	FAS 43; FAS 87; FAS 106; FAS 112; FAS 146; FSP FAS 146-1; EITF 96-05; EITF 96-09
430 – Deferred Revenue			
430-10	Overall	2014-09	SOP 00-2
440 – Commitments			
440-10	Overall	2014-09; 2018-07; 2023-06	FAS 5; FAS 13; FAS 47; FAS 52; FAS 65; FAS 66; FAS 68; FAS 91; FAS 116; FAS 133; ARB 43; ARB 45; AAG-HCO; SOP 96-1; EITF 91-06; EITF 96-18; EITF 01-08
450 – Contingencies			
450-10	Overall	2014-09; 2023-05	FAS 5; FAS 13; FAS 48; FAS 109; FAS 113; APB 28; FIN 30; SOP 97-2; SOP 98-7; EITF 93-14; EITF 96-05
450-20	Loss Contingencies	2010-20; 2016-13	FAS 5; FAS 15; FAS 16; FAS 132(R); FAS 143; FAS 146; FIN 14; FIN 47; ARB 43; AAG-HCO; SOP 93-1; SOP 94-6; SOP 96-1; SOP 97-3; EITF 92-13; EITF 97-01; EITF 98-09
450-30	Gain Contingencies	2016-02; 2021-05	FAS 5; FIN 39; EITF 98-09; EITF 01-13; EITF 03-08
460 – Guarantees			
460-10	Overall	2012-04; 2014-09; 2016-13; 2016-19; 2018-10; 2020-09; 2020-10	FAS 5; FAS 13; FAS 35; FAS 48; FAS 66; FAS 140; FAS 150; FIN 19; FIN 45; FIN 46(R); APB 18; TB 90-01; FSP FIN 45-1; FSP FIN 45-2; FSP FIN 45-3; SOP 81-1; SOP 93-6; SOP 94-6; SOP 00-2; SOP 01-6; EITF 84-05; EITF 85-20; EITF 86-17; EITF 86-33; EITF 90-14; EITF 90-20; EITF 90-21; EITF 91-10; EITF 92-01; EITF 95-01; EITF 96-21; EITF 97-01: EITF 97-10; EITF 99-02: EITF 99-05;

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
			EITF 00-04; EITF 01-12; EITF 03-12
470 – Debt			
470-10	Overall	2019-07; 2020-06; 2020-09; 2023-06	FAS 6; FAS 13; FAS 47; FAS 78; FAS 129; FIN 08; APB 21; ARB 43; TB 79-03; FSP FAS 129-1; EITF 86-05; EITF 86-15; EITF 86-28; EITF 86-30; EITF 88-15; EITF 88-18; EITF 95-22
470-20	Debt with Conversion and Other Options	2009-15; 2018-07; 2019-08; 2020-06	FAS 5; FAS 15; FAS 84; FAS 133; FAS 159; APB 14; FSP APB 14-1; FSP EITF 00-19-2; EITF 85-09; EITF 85-17; EITF 98-05; EITF 00-27; EITF 01-01; EITF 02-15; EITF 05-01; EITF 06-07; AIN APB 26
470-30	Participating Mortgage Loans	2015-10	SOP 97-1
470-40	Product Financing Arrangements	2014-09	FAS 49
470-50	Modifications and Extinguishments	2018-09; 2020-03; 2020-06; 2021-04	FAS 140; FAS 145; APB 26; TB 80-01; EITF 96-19; EITF 98-14; EITF 06-06; AIN-APB 26
470-60	Troubled Debt Restructurings by Debtors	2016-13; 2016-19; 2022-02	FAS 15; TB 80-02; TB 81-06; EITF 02-04
480 – Distinguishing Liabilities from Equity			
480-10	Overall	2017-11; 2018-07; 2018-09; 2023-03	FAS 150; FSP FAS 150-1; FSP FAS 150-2; FSP FAS 150-3; FSP FAS 150-4; FSP FAS 150-5; EITF 89-11; EITF 00-04; EITF 00-19
505 – Equity			
505-10	Overall	2010-21; 2015-10; 2017-11; 2018-07; 2019-07; 2020-06; 2020-09; 2021-04; 2023-06	FAS 5; FAS 129; FAS 130; APB 9; APB 12; APB 14; ARB 43; ARB 51; FSP FAS 129-1; EITF 85-01; EITF 86-32; EITF 98-05; EITF 00-12; EITF 00-19; EITF 00-27
505-20	Stock Dividends and Stock Splits	2010-01	ARB 43
505-30	Treasury Stock		ARB 43; TB 85-6; EITF 99-07
505-50	ASC Topic 505-50 was superseded by Topic 718 as detailed in ASU 2018-07 ASC Topic 505-50-S was superseded by ASU 2023-03		
505-60	Spinoffs and Reverse Spinoffs		FAS 123(R); EITF 02-11
605 – Revenue Recognition			
605	ASC Topic 605 was superseded by Topic 606 as detailed in ASU 2014-09		
606 – Revenue from Contracts with Customers			
606-10	Overall	2014-09; 2015-14; 2016-01; 2016-08; 2016-10; 2016-12; 2016-13; 2016-20; 2017-03; 2017-13; 2018-07; 2018-08;	

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
		2018-18; 2019-08; 2020-05; 2021-02	
610 – Other Income			
610-10	Overall	2014-09	
610-20	Gains and Losses from the Derecognition of Nonfinancial Assets	2014-09; 2017-05	
610-30	Gains and Losses on Involuntary Conversions	2014-09	FIN 30; APB 29
705 – Cost of Sales and Services			
705-10	Overall	2014-09; 2015-11	
705-20	Accounting for Consideration Received from a Vendor	2018-07	EITF 02-16; EITF 03-10
710 – Compensation-General			
710-10	Overall		FAS 43; FAS 88; FAS 106; APB 12; EITF 88-23; EITF 93-03; EITF 96-05; EITF 97-14; EITF 06-02
712 – Compensation-Nonretirement Postemployment Benefits			
712-10	Overall		FAS 88; FAS 106; FAS 112; FAS 146; FIN 46(R); EITF 96-05
715 – Compensation-Retirement Benefits			
715-10	Overall	2015-04; 2017-07	FAS 87; FAS 106
715-20	Defined Benefit Plans—General	2010-06; 2011-04; 2015-04; 2015-07; 2017-07; 2018-14; 2020-10	FAS 87; FAS 88; FAS 106; FAS 132(R); FAS 158; APB 12; EITF 88-01; EITF 03-02
715-30	Defined Benefit Plans—Pension	2011-09; 2012-04; 2015-04; 2017-07; 2020-10	FAS 87; FAS 88; FAS 106; FAS 130; FAS 146; FAS 158; FIN 46(R); FSP FAS 146-1; EITF 88-01; EITF 91-07; EITF 03-02; EITF 03-04; EITF 05-05
715-60	Defined Benefit Plans—Other Postretirement	2012-04; 2015-04; 2017-07	FAS 88; FAS 106; FAS 158; FIN 46(R); FSP FAS 106-2; EITF 92-12; EITF 92-13; EITF 93-03; EITF 96-05; EITF 06-04; EITF 06-10
715-70	Defined Contribution Plans		FAS 106; FAS 132(R); EITF 86-27
715-80	Multiemployer Plans	2011-09	FAS 87; FAS 106; FAS 132(R); EITF 90-03
718 – Compensation-Stock Compensation			
718-10	Overall	2010-13; 2014-12; 2018-07; 2019-08; 2020-06; 2021-04; 2021-07; 2023-03; 2023-05	FAS 5; FAS 123(R); FAS 128; FSP FAS 123(R)-1; FSP FAS 123(R)-2; FSP FAS 123(R)-4; EITF 96-05; EITF 97-02; EITF 00-12; EITF 00-16; EITF 07-05
718-20	Awards Classified as Equity	2017-09; 2018-07	FAS 123(R)
718-30	Awards Classified as Liabilities	2018-07; 2019-08	FAS 123(R)
718-40	Employee Stock Ownership Plans		SOP 93-6; EITF 90-04

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718-50	Employee Share Purchase Plans	2018-07	FAS 123(R); TB 97-01
718-740	Income Taxes	2016-09; 2018-07; 2018-09; 2019-12	FAS 109; FAS 123(R); SOP 93-6; EITF 06-11
720 – Other Expenses			
720-15	Start-Up Costs	2014-09	SOP 98-5
720-20	Insurance Costs		FAS 5; AAG-HCO; EITF 93-14; EITF 03-08
720-25	Contributions Made	2018-08	FAS 116
720-30	Real and Personal Property Taxes		ARB 43
720-35	Advertising Costs	2016-20; 2018-09	SOP 93-7
720-40	Electronic Equipment Waste Obligations		FSP FAS 143-1
720-45	Business and Technology Reengineering		EITF 97-13
720-50	Fees Paid to the Federal Government by Pharmaceutical Manufacturers and Health Insurers	2010-27; 2011-06	
730 – Research and Development			
730-10	Overall	2023-05	FAS 2; FAS 86; FIN 06; SOP 97-2; SOP 98-1; EITF 99-05; EITF 07-03
730-20	Research and Development Arrangements	2014-09	FAS 2; FAS 5; FAS 68; SOP 97-2; EITF 07-03
740 – Income Taxes			
740-10	Overall	2009-06; 2010-12; 2013-11; 2014-09; 2015-17; 2016-01; 2016-16; 2017-15; 2018-02; 2018-05; 2018-09; 2019-12; 2020-06; 2020-10; 2023-02; 2023-05; 2023-09	FAS 37; FAS 109; FAS 116; FAS 164; FIN 30; FIN 48; APB 2; APB 4; APB 10; APB 18; APB 21; FSP FAS 106-2; FSP FAS 109-1; FSP FIN 48-1; SOP 94-6; EITF 87-08; EITF 88-04; EITF 91-08; EITF 93-13; EITF 94-10; EITF 95-09; EITF 95-10; EITF 95-20; EITF 98-11; EITF 05-08
740-20	Intraperiod Tax Allocation	2019-12	FAS 109; EITF 94-10
740-30	Other Considerations or Special Areas	2018-06; 2019-12; 2023-09	FAS 109; APB 23; EITF 93-16; EITF 93-17
740-270	Interim Reporting	2016-09; 2019-12	FAS 109; FAS 144; FIN 18; APB 28; TB 79-09
805 – Business Combinations			
805-10	Overall	2010-02; 2010-29; 2013-05; 2014-13; 2015-16; 2017-01; 2021-05; 2023-05	FAS 141(R); FAS 164; FSP FAS 141(R)-1; EITF 98-04
805-20	Identifiable Assets and Liabilities, and Any Noncontrolling Interest	2011-04; 2012-06; 2014-09; 2014-18; 2015-16; 2016-02; 2016-03; 2016-13; 2019-06; 2019-11; 2021-03; 2021-05; 2021-08; 2023-05	FAS 5; FAS 13; FAS 87; FAS 106; FAS 141(R); FSP FAS 141(R)-1; EITF 96-05; EITF 05-06

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805-30	Goodwill or Gain from Bargain Purchase, Including Consideration Transferred	2016-09; 2018-07; 2021-03; 2023-05	FAS 141(R); FAS 142; FSP FAS 141(R)-1
805-40	Reverse Acquisitions	2023-05	FAS 141(R)
805-50	Related Issues	2010-08; 2014-17; 2015-08; 2017-05; 2023-05	FAS 141(R); FAS 164; EITF 85-21; EITF 86-09; EITF 87-21
805-740	Income Taxes	2016-09; 2018-07; 2018-09; 2023-05	FAS 109; FAS 141(R); FIN 48; EITF 86-09
808 – Collaborative Arrangements			
808-10	Overall	2018-18; 2021-05; 2023-05	
810 – Consolidation			
810-10	Overall	2010-02; 2010-10; 2010-22; 2011-10; 2013-05; 2013-08; 2014-07; 2014-09; 2014-10; 2014-13; 2015-02; 2016-03; 2016-13; 2016-14; 2016-17; 2018-04; 2018-17; 2019-07; 2023-02; 2023-05	FAS 94; FAS 167; FIN 46(R); APB 18; ARB 51; FSP FAS 140-4/FIN 46(R)-8; FSP FIN 46(R)-1; FSP FIN 46(R)-2; FSP FIN 46(R)-3; FSP FIN 46(R)-5; FSP FIN 46(R)-6; EITF 84-04; EITF 85-12; EITF 86-32; EITF 88-14; EITF 88-15; EITF 96-16; EITF 97-02; EITF 97-14; EITF 00-01; EITF 01-02; EITF 04-05; EITF 06-09; EITF 08-08; PB 01; PB 02; AIN APB 18
810-20	Control of Partnerships and Similar Entities		EITF 04-05
810-30	Research and Development Arrangements	2015-02	EITF 99-16
815 – Derivatives and Hedging			
815-10	Overall	2010-11; 2013-01; 2014-03; 2014-09; 2015-12 (Part I); 2015-13; 2016-01; 2016-03; 2016-11; 2016-13; 2016-14; 2016-20; 2017-11; 2017-12; 2018-03; 2018-07; 2018-09; 2018-12; 2018-16; 2019-04; 2020-01; 2020-06; 2022-01; 2023-05; 2023-06	FAS 95; FAS 123(R); FAS 133; FAS 138; FAS 149; FAS 157; FAS 161; FIN 39; FSP FAS 129-1; FSP EITF 00-19-2; EITF 84-20; EITF 86-25; EITF 96-11; EITF 99-08; EITF 00-06; EITF 00-19; EITF 01-08; EITF 01-12; EITF 02-03; EITF 02-08; EITF 03-11; EITF 08-08
815-15	Embedded Derivatives	2010-11; 2014-16; 2016-01; 2016-06; 2016-13; 2018-03; 2018-09; 2018-12; 2020-06	FAS 107; FAS 133; FAS 155; FSP APB 14-1; EITF 84-04; EITF 86-21; EITF 00-19; EITF 06-07; PB 01
815-20	Hedging—General	2013-10; 2014-03; 2016-03; 2016-05; 2017-12; 2018-16; 2019-04; 2019-10; 2022-01	FAS 52; FAS 95; FAS 133; FAS 138; FAS 140
815-25	Fair Value Hedges	2016-05; 2016-13; 2017-12; 2018-16; 2019-04; 2022-01	FAS 133; FAS 138; EITF 99-09

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815-30	Cash Flow Hedges	2010-08; 2016-05; 2016-13; 2017-12; 2018-16	FAS 133; FAS 138; EITF 99-09; EITF 00-09
815-35	Net Investment Hedges	2017-12	FAS 133
815-40	Contracts in Entity's Own Equity	2017-11; 2018-07; 2020-06; 2021-04	FSP EITF 00-19-2; EITF 00-19; EITF 05-02; EITF 07-05; EITF 08-08
815-45	Weather Derivatives		EITF 99-02
820 – Fair Value Measurements and Disclosures			
820-10	Overall	2009-05; 2009-12; 2010-06; 2011-04; 2013-08; 2013-09; 2014-09; 2014-13; 2015-07; 2015-10; 2016-13; 2016-19; 2018-07; 2018-09; 2018-13; 2020-03; 2020-07; 2022-03	FAS 157; EITF 08-05
825 – Financial Instruments			
825-10	Overall	2009-05; 2011-04; 2013-03; 2014-03; 2015-12 (Part I); 2016-01; 2016-04; 2016-13; 2016-14; 2018-03; 2018-09; 2019-04; 2020-01; 2020-03; 2020-06	FAS 107; FAS 126; FAS 159; FSP APB 14-1; FSP SOP 94-6-1; SOP 01-6; EITF 08-05
825-20	Registration Payment Arrangements	2020-06	FSP EITF 00-19-2
830 – Foreign Currency Matters			
830-10	Overall	2015-11; 2019-04	FAS 52; APB 30; EITF 92-04
830-20	Foreign Currency Transactions	2018-03; 2020-10	FAS 52; FAS 109; EITF 87-12; EITF 96-15
830-30	Translation of Financial Statements	2010-19; 2013-05; 2016-13	FAS 52; FIN 37; EITF 01-05
830-230	Statement of Cash Flows	2016-18	FAS 95
830-740	Income Taxes	2020-10	FAS 109; EITF 92-08; EITF 93-09; EITF 93-16
832 – Government Assistance			
832-10	Overall	2021-10	
835 – Interest			
835-10	Overall	2016-01; 2016-13	FAS 116; FAS 150; FIN 48; SOP 03-3; SOP 98-7; EITF 85-17; EITF 86-15; EITF 96-12; EITF 99-20
835-20	Capitalization of Interest		FAS 34; FAS 42; FAS 58; FAS 62; FAS 87; FAS 143; FAS 154; SOP 97-1
835-30	Imputation of Interest	2014-09; 2015-03; 2015-15; 2020-06; 2020-10	APB 12; APB 21; SOP 01-6
840 – Leases			
840	ASC Topc 840 was superseded by Topic 842, as detailed in ASU 2016-02		
842 – Leases			
842-10	Overall	2016-02; 2017-03; 2017-13; 2018-01; 2018-10; 2018-11; 2018-20; 2019-01; 2019-10; 2020-02; 2020-03; 2020-05; 2021-05; 2021-09; 2023-01; 2023-05	
842-20	Lessee	2016-02; 2018-10; 2021-05; 2021-09; 2023-01; 2023-05	

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842-30	Lessor	2016-02; 2016-13; 2018-10; 2018-11; 2018-20; 2019-01; 2021-05	
842-40	Sale and Leaseback Transactions	2016-02; 2018-10; 2021-05; 2021-09	
842-50	Leveraged Lease Arrangements	2016-02; 2016-13; 2022-02; 2023-05	
842-974	Real Estate Investment Trust	2016-02	
845 – Nonmonetary Transactions			
845-10	Overall	2010-02; 2014-09; 2017-05; 2018-07; 2019-08; 2023-05	APB 29; EITF 93-11; EITF 98-04; EITF 00-08; EITF 01-02; EITF 04-13
848 – Reference Rate Reform			
848-10	Overall	2020-04; 2021-01; 2022-06	
848-20	Contract Modifications	2020-04; 2020-06; 2021-01	
848-30	Hedging—General	2020-04; 2021-01	
848-40	Fair Value Hedges	2020-04; 2021-01; 2022-06	
848-50	Cash Flow Hedges	2020-04; 2021-01	
850 – Related Party Disclosures			
850-10	Overall		FAS 45; FAS 57; FIN 45; APB 18; APB 26; ARB 43; ARB 51; EITF 85-01; PB 14
852 – Reorganizations			
852-10	Overall	2012-04; 2020-10	SOP 90-7; EITF 88-25
852-20	Quasi-Reorganizations		ARB 43; SOP 90-7
852-740	Income Taxes		FAS 109; SOP 90-7
853 – Service Concession Arrangements			
853-10	Overall	2014-05; 2017-10	
855 – Subsequent Events			
855-10	Overall	2010-09; 2016-13	FAS 144; FAS 165; SOP 00-2
860 – Transfers and Servicing			
860-10	Overall	2011-03; 2014-11; 2015-10; 2016-02; 2017-05; 2021-05	FAS 5; FAS 57; FAS 91; FAS 140; FAS 159; FAS 166; FIN 46(R); ARB 51; TB 01-01; FSP FAS 140-3; SOP 90-3; SOP 04-2; EITF 84-20; EITF 86-08; EITF 87-30; EITF 88-22; EITF 90-21; EITF 97-03; EITF 99-08
860-20	Sales of Financial Assets	2014-11; 2016-13; 2016-19; 2020-03; 2022-01	FAS 95; FAS 115; FAS 140; FSP FAS 140-1; SOP 01-6; EITF 84-05; EITF 85-25; EITF 88-22; EITF 02-09
860-30	Secured Borrowing and Collateral	2013-01; 2014-11; 2023-06	FAS 140; FIN 41
860-50	Servicing Assets and Liabilities		FAS 65; FAS 140; FAS 156; TB 87-03; SOP 01-6; EITF 85-13; EITF 87-34; EITF 90-21; EITF 95-05; EITF 02-09
912 – Contractors–Federal Government			
912-10	Overall		ARB 43
912-20	Contract Costs		ARB 43; SOP 81-1

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912-210	Balance Sheet		ARB 43
912-225	Income Statement		ARB 43
912-275	Risks and Uncertainties		FAS 146; ARB 43
912-310	Receivables	2014-09	ARB 43
912-330	Inventory		ARB 43
912-405	Liabilities		ARB 43
912-605	Revenue Recognition		ARB 43
912-835	Interest	2014-09	
915 – Development Stage Entities			
915-10	Overall	2014-10	FAS 07; FIN 07
915-205	Presentation of Financial Statements		FAS 07
915-210	Balance Sheet		FAS 07
915-215	Statement of Shareholder Equity		FAS 07
915-225	Income Statement		FAS 07
915-230	Statement of Cash Flows		FAS 07
915-235	Notes to Financial Statements		FAS 07
915-340	Other Assets and Deferred Costs		FAS 07
915-605	Revenue Recognition		FAS 07
915-810	Consolidation		FAS 07; FIN 07
920 – Entertainment–Broadcasters			
920-10	Overall		FAS 63
920-230	Statement of Cash Flows	2019-02	
920-350	Intangibles—Goodwill and Other	2019-02	FAS 63
920-405	Liabilities		FAS 63
920-440	Commitments		FAS 63
920-845	Nonmonetary Transactions		FAS 63
924 – Entertainment–Casinos			
924-10	Overall	2016-20	
924-815	Derivatives and Hedging	2016-20	
932 – Extractive Activities–Oil and Gas			
932-10	Overall	2009-11; 2010-03; 2010-14; 2010-22; 2016-11; 2019-07	FAS 19; EITF 90-22
932-235	Notes to Financial Statements	2010-03; 2014-09; 2023-06	FAS 19; FAS 69
932-270	Interim Reporting		FAS 19
932-330	Inventory		EITF 02-03
932-350	Intangibles—Goodwill and Other		FSP FAS 142-2
932-360	Property, Plant, and Equipment	2012-04	FAS 19; FIN 36; FSP FAS 19-1
932-470	Debt		FAS 19
932-720	Other Expenses		FAS 19
932-740	Income Taxes		FAS 19
932-810	Consolidation		EITF 00-01
932-815	Derivatives and Hedging		EITF 90-22
932-835	Interest	2014-09	FIN 33; AIN-APB21
940 – Financial Services–Broker and Dealers			
940-10	Overall	2014-09	
940-20	Broker-Dealer Activities	2012-04, 2014-09	
940-210	Balance Sheet	2018-09	
940-310	Receivables	2012-04, 2014-09; 2016-19	

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940-325	Investments—Other		EITF 02-03
940-400	Other Assets and Deferred Costs	2016-01; 2016-19	
940-405	Liabilities	2018-09	
940-605	Revenue Recognition	2014-09	
940-720	Other Expenses	2014-09	
940-820	Fair Value Measurement	2011-04; 2012-04; 2022-03	
942 – Financial Services–Depository and Lending			
942-10	Overall	2019-07; 2021-06	SOP 01-6; EITF 88-19
942-210	Balance Sheet	2010-21; 2018-09; 2019-07; 2021-06	SOP 01-6
942-220	Income Statement—Reporting Comprehensive Income	2019-07	
942-225	Income Statement	2010-21	
942-230	Statement of Cash Flows	2016-13; 2019-01	FAS 95
942-235	Notes to the Financial Statements	2019-07	
942-305	Cash and Cash Equivalents		SOP 01-6
942-310	Receivables	2016-13; 2022-02	SOP 01-6; PB 4; PB 5
942-320	Investments—Debt and Equity Securities	2016-01; 2019-04; 2020-03	FAS 115; SOP 01-6
942-325	Investments—Other	2016-01	SOP 01-6
942-360	Property, Plant, and Equipment	2020-10	SOP 01-6
942-405	Liabilities		SOP 01-6; EITF 89-03
942-470	Debt	2016-01	FAS 107; SOP 01-6
942-505	Equity	2018-09	SOP 01-6
942-740	Income Taxes	2018-06	FAS 109; APB 23; EITF 85-31
942-810	Consolidation		EITF 88-25
942-825	Financial Instruments	2016-01; 2016-20	SOP 01-6; EITF 85-20
944 – Financial Services–Insurance			
944-10	Overall	2010-21; 2016-01; 2019-07	FAS 60; SOP 94-5
944-20	Insurance Activities	2016-13; 2016-19; 2018-12	FAS 5; FAS 60; FAS 97; FAS 113; FAS 120; FAS 163; SOP 94-5; SOP 95-1; SOP 03-1; EITF 92-09; EITF 93-06; EITF 93-14; PB 8
944-30	Acquisition Costs	2010-26; 2014-09; 2015-10; 2018-09; 2018-12	FAS 60; FAS 97; FAS 113; SOP 93-7; SOP 95-1; SOP 03-1; SOP 05-1; PB 8
944-40	Claim Costs and Liabilities for Future Policy Benefits	2012-04; 2015-09; 2018-12; 2019-09; 2020-11; 2022-05	FAS 5; FAS 60; FAS 97; FAS 113; FAS 163; SOP 94-5; SOP 95-1; SOP 03-1
944-50	Policyholder Dividends	2018-12	FAS 60; SOP 95-1; AAG LHI
944-60	Premium Deficiency and Loss Recognition	2018-12	FAS 5; FAS 60; FAS 97; PB 8
944-80	Separate Accounts	2010-15; 2016-01; 2016-13; 2018-12	FAS 60; SOP 03-1
944-210	Balance Sheet	2010-21; 2019-07	FAS 113
944-220	Income Statement—Reporting Comprehensive Income	2019-07	
944-225	Income Statement	2010-21	
944-235	Notes to the Financial Statements	2019-07	
944-310	Receivables	2016-13; 2016-19; 2018-09	FAS 60; FAS 113; FAS 163; AAG PLI

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944-320	Investments—Debt and Equity Securities	2012-04; 2016-01	SOP 01-06; SOP 03-01
944-325	Investments—Other	2015-10; 2016-01	FAS 60
944-340	Other Assets and Deferred Costs		FAS 113
944-360	Property, Plant, and Equipment	2016-01; 2018-09	FAS 60
944-405	Liabilities		FAS 113
944-470	Debt	2015-10	PB 15
944-505	Equity		FAS 60; SOP 94-5
944-605	Revenue Recognition	2016-01; 2018-12	FAS 60; FAS 97; FAS 113; FAS 163; FSP FAS 97-1; SOP 92-5; SOP 95-1; SOP 03-1; PB 8
944-720	Other Expenses	2010-26	AAG LHI
944-740	Income Taxes		FAS 60; FAS 109; AAG LHI
944-805	Business Combinations	2018-12	FAS 60; SOP 00-3
944-815	Derivatives and Hedging	2018-12	
944-825	Financial Instruments	2016-01; 2018-12	FAS 97; FAS 113; PB 8
946 – Financial Services–Investment Companies			
946-10	Overall	2013-08; 2019-07; 2021-06	SOP 07-1
946-20	Investment Company Activities	2013-08; 2023-06	SOP 95-2; SOP 95-3
946-205	Presentation of Financial Statements	2019-07	FSP AAG INV-1 and SOP 94-1-1
946-210	Balance Sheet	2016-19; 2019-07	FSP AAG INV-1 and SOP 94-4-1; SOP 95-2
946-220	Income Statement—Reporting Comprehensive Income	2019-07; 2020-10	
946-225	Income Statement		SOP 95-2
946-235	Notes to the Financial Statements	2019-07	
946-310	Receivables	2019-07	
946-320	Investments—Debt and Equity Securities	2013-08; 2017-08; 2019-07	SOP 93-1
946-323	Investments—Equity Method and Joint Ventures	2013-08	SOP 07-1
946-325	Investments—Other	2013-08	
946-605	Revenue Recognition		FSP EITF85-24-1; EITF 85-24
946-720	Other Expenses	2014-09; 2016-20	EITF 85-24
946-740	Income Taxes		FAS 109
946-810	Consolidation	2013-08	SOP 07-1
946-830	Foreign Currency Matters		SOP 93-4
948 – Financial Services—Mortgage Banking			
948-310	Receivables	2019-04; 2019-07; 2022-01	
950 – Financial Services–Title Plant			
950-350	Intangibles—Goodwill and Other	2014-09	FAS 61
952 – Franchisors			
952-606	Revenue from Contracts with Customers	2021-02	
954 – Health Care Entities			
954-10	Overall	2013-06; 2016-01; 2018-08	AAG HCO
954-205	Presentation of Financial Statements	2016-14; 2018-08	AAG HCO
954-210	Balance Sheet	2016-14	AAG HCO

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954-220	Income Statement—Reporting Comprehensive Income	2016-19; 2017-12; 2018-08	
954-225	Income Statement	2013-06; 2016-01; 2016-13	FAS 117; AAG HCO
954-280	Segment Reporting		TB 79-05
954-305	Cash and Cash Equivalents	2016-14	AAG HCO
954-310	Receivables	2011-07; 2014-09; 2016-13	AAG HCO
954-320	Investments—Debt and Equity Securities	2012-04; 2016-01; 2016-14	FAS 124; AAG HCO
954-325	Investments—Other		AAG HCO
954-340	Other Assets and Deferred Costs		AAG HCO
954-360	Property, Plant, and Equipment		AAG HCO
954-405	Liabilities		AAG HCO
954-430	Deferred Revenue	2012-01	AAG HCO
954-440	Commitments	2018-08	AAG HCO
954-450	Contingencies	2010-24	AAG HCO
954-460	Guarantees		FSP FIN 45-3
954-470	Debt	2018-08	AAG HCO
954-605	Revenue Recognition	2010-23; 2011-07; 2012-04; 2014-09; 2018-08	AAG HCO
954-720	Other Expenses	2010-24	AAG HCO; EITF 03-08
954-740	Income Taxes		AAG HCO
954-805	Business Combinations	2012-04; 2016-01; 2016-14	FAS 164; AAG HCO
954-810	Consolidation	2015-02; 2016-19; 2017-02	FAS 164; FIN 46(R); SOP 94-3; EITF 97-02; AAG HCO
954-815	Derivatives and Hedging	2012-04; 2017-12	SOP 02-2
954-825	Financial Instruments		FAS 159
958 – Not-For-Profit Entities			
958-10	Overall	2015-10; 2016-01; 2016-14; 2018-08; 2019-03; 2020-07	FAS 88; FAS 116
958-20	Financially Interrelated Entities	2016-14; 2018-08	FAS 57; FAS 136; APB 18
958-30	Split-Interest Agreements	2016-01; 2016-14; 2018-08; 2018-13	FAS 116; FAS 117; FAS 136
958-205	Presentation of Financial Statements	2015-01; 2015-10; 2016-14; 2016-18; 2018-08; 2020-07	FAS 116; FAS 117; FAS 124; FAS 136; FSP FAS 117-1; SOP 94-6
958-210	Balance Sheet	2014-06; 2016-01; 2016-14	FAS 117; ARB 43
958-220	Income Statement—Reporting Comprehensive Income	2017-07; 2018-08; 2020-07; 2020-10	
958-225	Income Statement	2016-01; 2016-14	FAS 116; FAS 117; FAS 136; FAS 144; FAS 146
958-230	Statement of Cash Flows	2012-05; 2015-10; 2016-18; 2018-08; 2023-08	FAS 117
958-310	Receivables	2016-14; 2018-08; 2018-13	FAS 116
958-320	Investments—Debt and Equity Securities	2012-04; 2015-10; 2016-01; 2016-13; 2018-08; 2022-02	FAS 65; FAS 107; FAS 116; FAS 117; FAS 124
958-325	Investments—Other	2012-04; 2015-10; 2016-01; 2016-13; 2018-08	FAS 116; FAS 124; FSP FAS 115-1/124-1
958-360	Property, Plant, and Equipment	2016-14; 2018-08; 2019-03	FAS 93; FAS 116; FAS 144
958-405	Liabilities	2018-08	
958-450	Contingencies	2018-08	FAS 5; FAS 116
958-605	Revenue Recognition	2013-06; 2014-09; 2015-10; 2016-01; 2016-14; 2016-19; 2018-08; 2020-07	FAS 57; FAS 116; FAS 136; SOP 94-6

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
958-715	Compensation—Retirement Benefits	2016-14; 2017-07; 2018-08; 2018-14	FAS 87; FAS 88; FAS 106; FAS 132(R); FAS 158
958-720	Other Expenses	2012-04; 2013-06; 2016-14; 2018-08; 2018-09; 2020-10	FAS 93; FAS 109; FAS 117; SOP 93-7; SOP 98-2
958-805	Business Combinations	2010-29; 2015-10; 2016-14; 2016-15; 2018-08; 2019-06; 2021-03; 2023-05	FAS 116; FAS 141R; FAS 164; FIN 21
958-810	Consolidation	2012-04; 2015-10; 2016-01; 2016-14; 2016-19; 2017-02; 2018-08	FAS 13; FAS 57; FAS 164; FIN 46(R); APB 18; ARB 51; FSP SOP 94-3-1 and AAG HCO-1; SOP 94-3; EITF 90-15; EITF 96-21
958-840	Leases		SOP 94-3; EITF 90-15; EITF 96-21; EITF 97-01
960 – Plan Accounting–Defined Benefit Pension Plans			
960-10	Overall		FAS 35; FAS 87
960-20	Accumulated Plan Benefits		FAS 35; SOP 99-2
960-30	Net Assets Available for Plan Benefits	2015-12 (Part II)	FAS 35; SOP 99-2
960-40	Terminating Plans	2013-07	
960-205	Presentation of Financial Statements	2015-12 (Part II); 2017-06	FAS 35 FAS 102 SOP 99-2
960-310	Receivables		FAS 35
960-325	Investments—Other	2015-12 (Part II & III); 2017-06	FAS 35; FAS 110; FAS 133
960-360	Property, Plant, and Equipment		FAS 35
962 – Plan Accounting–Defined Contribution Pension Plans			
962-10	Overall	2015-12 (Part I-III); 2017-06	FAS 35; FAS 87; SOP 94-4; SOP 99-3
962-40	Terminating Plans	2013-07	
962-205	Presentation of Financial Statements	2015-12 (Part I-II); 2017-06; 2018-09; 2019-07	FAS 102; SOP 94-4
962-310	Receivables	2010-25	
962-325	Investments—Other	2010-25; 2012-04; 2015-12 (Part I-III); 2017-06, 2018-09	SOP 92-6; SOP 94-4; SOP 99-3
962-360	Property, Plant, and Equipment	2018-09	
965 – Plan Accounting–Health and Welfare Benefit Plans			
965-10	Overall		FAS 35; FAS 87; SOP 92-6; SOP 99-2
965-20	Net Assets Available for Plan Benefits	2015-12 (Part I-II)	SOP 92-6
965-30	Plan Benefit Obligations	2016-19	SOP 92-6
965-40	Terminating Plans	2013-07	SOP 92-6
965-205	Presentation of Financial Statements	2012-04; 2015-12 (Part II); 2017-06; 2020-10	FAS 130; SOP 92-6; SOP 99-2
965-310	Receivables		SOP 92-6
965-320	Investments—Debt and Equity Securities		SOP 92-6
965-325	Investments—Other	2012-04; 2015-12 (Part I-II); 2017-06	SOP 92-6; SOP 94-4; SOP 99-3
965-360	Property, Plant, and Equipment		SOP 92-6

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
970 – Real Estate–General			
970-10	Overall		FAS 67
970-230	Statement of Cash Flows		FAS 102
970-323	Investments—Equity Method and Joint Ventures	2014-09; 2015-02; 2016-01; 2017-05	SOP 78-9; SOP 92-1
970-340	Other Assets and Deferred Costs	2014-09; 2016-02; 2021-05	FAS 67; EITF 97-11
970-360	Property, Plant, and Equipment	2014-09; 2019-07; 2020-10	FAS 67; EITF 85-27; EITF 86-07
970-470	Debt		EITF 91-10
970-605	Revenue Recognition		FAS 67; SOP 78-9; SOP 92-1
970-720	Other Expenses		FAS 67; EITF 97-11
970-810	Consolidation	2015-02	APB 18; ARB 51; FSP SOP 78-9-1; SOP 78-9
970-835	Interest		SOP 78-9
974 – Real Estate—Real Estate Investment Trusts			
974-10	Overall	2019-07; 2023-06	
976 – Real Estate–Retail Land			
976-10	Overall		FAS 66
976-310	Receivables		FAS 66
976-330	Inventory		FAS 66
976-605	Revenue Recognition		FAS 66
976-705	Cost of Sales and Services	2014-09	FAS 66
978 – Real Estate — Time-Sharing Activities			
978-10	Overall	2014-06; 2014-09; 2016-02	
978-230	Statements of Cash Flows	2014-06	
978-250	Accounting Changes and Error Corrections		
978-310	Receivables	2014-06; 2014-09; 2016-02; 2016-13; 2022-02	
978-330	Inventory	2014-06; 2014-09; 2016-02	
978-340	Other Assets and Deferred Costs	2014-06; 2014-09	
978-605	Revenue Recognition	2014-06; 2014-09	
978-720	Other Expenses	2014-06; 2014-09	
978-810	Consolidation	2014-06; 2016-01	
978-840	Leases	2014-06; 2014-09; 2016-02	
980 – Regulated Operations			
980-10	Overall	2018-04	FAS 7; FAS 71
980-20	Discontinuation of Rate-Regulated Accounting	2015-01	FAS 101; EITF 97-04
980-250	Accounting Changes and Error Corrections		FAS 71
980-340	Other Assets and Deferred Costs	2016-02	FAS 71; FAS 92; EITF 93-04
980-350	Intangibles—Goodwill and Other		FAS 71; EITF 96-17
980-360	Property, Plant, and Equipment		FAS 90; TB 87-02
980-405	Liabilities		FAS 71
980-410	Asset Retirement and Environmental Obligations		FAS 71; FAS 143
980-450	Contingencies		FAS 71
980-470	Debt		FAS 71
980-605	Revenue Recognition	2014-09; 2015-01	FAS 71; EITF 91-06; EITF 92-07; EITF 96-17
980-710	Compensation—General		FAS 71

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GAAP Codification Topic and Subtopic	Codification Section	ASU GAAP Reference	Pre-Codification GAAP Reference
980-715	Compensation—Retirement Benefits		FAS 87; FAS 106; EITF 92-12; EITF 93-04
980-740	Income Taxes		FAS 109; TB 87-02
980-810	Consolidation	2018-04	FAS 71
980-815	Derivatives and Hedging	2014-09	EITF 91-06
980-835	Interest		FAS 71; FAS 90
980-840	Leases	2016-02	FAS 13; FAS 71; FAS 98
980-842	Leases	2016-02	
985 –Software			
985-10	Overall	2014-09	
985-20	Costs of Software to Be Sold, Leased, or Marketed	2014-09; 2018-15; 2023-05	FAS 2; FAS 86; FIN 6; SOP 94-6; SOP 97-2; SOP 98-1; EITF 00-03
985-330	Inventory		FAS 86
985-605	Revenue Recognition	2009-14; 2014-09; 2018-15	FAS 86; SOP 97-2; EITF 00-03; EITF 03-05
985-705	Cost of Sales and Services		FAS 86; EITF 96-06
985-845	Nonmonetary Transactions	2014-09	

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Appendix E
Statutory Issue Papers

Introduction

Issue papers are used as the first step in developing new or revised SSAPs, and each contains a recommended conclusion, discussion and relevant literature section. While issue papers do not constitute an authoritative level of statutory accounting guidance as defined by the statutory hierarchy, they are an important part of the *Accounting Practices and Procedures Manual* (Manual) because they reference the history and discussion of the related SSAP.

Issue papers are published in the Manual within Appendix E the first year after adoption of the related SSAP, but are then removed from the subsequent year's Manual and posted for public reference on the Statutory Accounting Principles (E) Working Group (SAPWG) web page at https://content.naic.org/cmte_e_app_sapwg.htm.

Issue Papers Associated with SSAPs Adopted in 2023

IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
167	Derivatives and Hedging	86	86
168	Updates to the Definition of a Liability	5R	5R

Issue Papers Associated with SSAPs Adopted Prior to 2023

(Posted for public reference on the SAPWG web page)

IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
1	Consolidation of Majority-Owned Subsidiaries	3	3 and 97
2	Definition of Cash	2	2R
3	Accounting Changes	3	3
4	Definition of Assets and Nonadmitted Assets	4	4
5	Definition of Liabilities, Loss Contingencies and Impairments of Assets	5	5R
6	Amounts Due From Agents and Brokers	6	6
7	Asset Valuation Reserve and Interest Maintenance Reserve	7	7
8	Accounting for Pensions	8	102
9	Subsequent Events	9	9
10	Uncollected Premium Balances	6	6
11	Compensated Absences	11	11
12	Accounting for Drafts Issued and Outstanding	2	2R
13	Employers' Accounting for Postemployment Benefits	11	11
14	Employers' Accounting for Postretirement Benefits Other Than Pensions	14	92
16	Electronic Data Processing Equipment and Software	16	16R
17	Preoperating and Research and Development Costs	17	17
19	Furniture, Fixtures and Equipment	19	19
20	Gain Contingencies	5	5R

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IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
21	Bills Receivable For Premiums	6	6
22	Leases	22	22R
23	Property Occupied by the Company	40	40R
24	Discontinued Operations and Extraordinary Items	24	24
25	Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties	25	25
26	Bonds, Excluding Loan-Backed and Structured Securities	26	26R
27	Disclosure of Information about Financial Instruments with Concentration of Credit Risk	27	27
28	Short-Term Investments	2	2R
29	Prepaid Expenses (excluding deferred policy acquisition costs and other underwriting expenses, income taxes and guaranty fund assessments)	29	29
30	Investments in Common Stock (excluding investments in common stock of subsidiary, controlled, or affiliated entities)	30	30R
31	Leasehold Improvements Paid by the Reporting Entity as Lessee	19	19
32	Investments in Preferred Stock (excluding investments in preferred stock of subsidiary, controlled, or affiliated entities)	32	32R
33	Disclosures about Fair Value of Financial Instruments	27	27
34	Investment Income Due and Accrued	34	34
35	Accounting for Guaranty Fund and Other Assessments	35	35R
36	Troubled Debt Restructurings	36	36
37	Mortgage Loans	37	37
38	Acquisition, Development and Construction Arrangements	38	38
39	Reverse Mortgages	39	39
40	Real Estate Investments	40	40R
41	Surplus Notes	41	41R
42	Sale of Premium Receivables	42	42
43	Loan-Backed and Structured Securities	43	43R
44	Capitalization of Interest	44	44
45	Repurchase Agreements, Reverse Repurchase Agreements and Dollar Repurchase Agreements	45	103R
46	Accounting for Investments in Subsidiary, Controlled and Affiliated Entities	46	97
47	Uninsured Plans	47	47
48	Investments in Joint Ventures, Partnerships and Limited Liability Companies	48	48
49	Policy Loans	49	49
50	Classifications and Definitions of Insurance or Managed Care Contracts in Force	50	50
51	Life Contracts	51	51R
52	Deposit-Type Contracts	52	52
53	Property Casualty Contracts–Premiums	53	53
54	Individual and Group Accident and Health Contracts	54	54R

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IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
55	Unpaid Claims, Losses and Loss Adjustment Expenses	55	55
56	Universal Life-Type Contracts, Policyholder Dividends, and Coupons	51	51R
57	Title Insurance	57	57
59	Credit Life and Accident and Health Insurance Contracts	59	59
65	Property and Casualty Contracts	65	65
66	Accounting for Retrospectively Rated Contracts	66	66
67	Depreciation of Property and Amortization of Leasehold Improvements	19	19
68	Business Combinations and Goodwill	68	68
69	Financial Guaranty Insurance	60	60
71	Policy Acquisition Costs and Commissions	71	71
72	Statutory Surplus	72	72
73	Nonmonetary Transactions	28	95
74	Life, Deposit-Type and Accident and Health Reinsurance	61	61R
75	Property and Casualty Reinsurance	62	62R
76	Offsetting and Netting of Assets and Liabilities	64	64
77	Disclosure of Accounting Policies, Risks & Uncertainties, and Other Disclosures	1	1
78	Employee Stock Ownership Plans	12	12
80	Debt	15	15
81	Foreign Currency Transactions and Translations	23	23
82	Stock Options and Stock Purchase Plans	13	104R
83	Accounting for Income Taxes	10	101
84	Quasi-Reorganizations	72	72
85	Derivative Instruments	27 and 86	27 and 86
86	Securitization	33	103R
87	Other Admitted Assets	21	21R
88	Mortgage Guaranty Insurance	58	58
89	Separate Accounts	56	56
90	Nonadmitted Assets	20	20
92	Statement of Cash Flow	69	69
94	Allocation of Expenses	70	70
95	Holding Company Obligations	15	15
96	Other Liabilities	67	67
97	Underwriting Pools and Associations Including Intercompany Pools	63	63
99	Nonapplicable GAAP Pronouncements	Refer to Appendix D – Nonapplicable GAAP Pronouncements	
100	Health Care Delivery Assets—Supplies, Pharmaceuticals and Surgical Supplies, and Durable Medical Equipment	73	73
101	Health Care Delivery Assets—Furniture, Medical Equipment and Fixtures, and Leasehold Improvements in Health Care Facilities	73	73

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IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
103	Accounting for the Issuance of Insurance-Linked Securities Issued by a Property and Casualty Insurer through a Protected Cell	74	74
104	Reinsurance Deposit Accounting—An Amendment to SSAP No. 62—Property and Casualty Reinsurance	62R	62R
105	Reporting on the Costs of Start-Up Activities	76	76
106	Real Estate Sales—An Amendment to SSAP No. 40—Real Estate Investments	77	40R
107	Certain Health Care Receivables and Receivables Under Government Insured Plans	84	84
108	Multiple Peril Crop Insurance	78	78
109	Depreciation of Nonoperating System Software—An Amendment to SSAP No. 16—Electronic Data Processing Equipment and Software	79	16R
110	Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts, and SSAP No. 56—Separate Accounts	51, 52 and 56	51R, 52 and 56
111	Software Revenue Recognition	81	16R
112	Accounting for the Costs of Computer Software Developed or Obtained for Internal Use and Web Site Development Costs	82	16R
113	Mezzanine Real Estate Loans	83	83
114	Accounting for Derivative Instruments and Hedging Activities	86	86
116	Claim Adjustment Expenses, Amendments to SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses	85	55
118	Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46	68 and 97	68 and 97
119	Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29, 73, 79 and 82	87	4, 19, 29 and 73
121	Accounting for the Impairment or Disposal of Real Estate Investments	90	90
122	Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities	91	103R
123	Accounting for Pensions, A Replacement of SSAP No. 8	89	102
124	Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43	43R	43R
125	Accounting for Low-Income Housing Tax Credit Property Investments	48 and 93	48 and 93
126	Accounting for Transferable State Tax Credits	94	94R
127	Exchanges of Nonmonetary Assets, A Replacement of SSAP No. 28—Nonmonetary Transactions	90 and 95	90 and 95

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IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
128	Settlement Requirements for Intercompany Transactions, An Amendment to SSAP No.25—Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties	96	25
129	Share-Based Payment, A Replacement of SSAP No. 13—Stock Options and Stock Purchase Plans	104	104R
131	Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment	99	26R, 32R and 34
132	Accounting for Pensions, A Replacement of SSAP No. 89	102	102
133	Accounting for Postretirement Benefits Other Than Pensions, A Replacement of SSAP No. 14	92	92
134	Servicing Assets/Liabilities, An Amendment of SSAP No. 91	91R	103R
135	Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others	5R	5R
137	Transfer of Property and Casualty Reinsurance Agreements in Run-Off	62R	62R
138	Fair Value Measurements	100	100R
140	Substantive Revisions to SSAP No. 43—Loan-Backed and Structured Securities	43R	43R
141	Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities	103	103R
143R	Guaranty Fund Assessments	35R	35R
144	Substantive Revisions to SSAP No. 91R: Securities Lending	91R	103R
145	Accounting for Transferable and Non-Transferable State Tax Credits	94R	94R
146	Share-Based Payments With Non-Employees	104R	104R
147	Working Capital Finance Investments	105	105R
148	Affordable Care Act Section 9010 Assessment	35R	106
149	Wholly-Owned Single Real Estate Property in an LLC	40R	40R
150	Accounting for the Risk-Sharing Provisions of the Affordable Care Act	107	107
151	Valuation for Holders of Surplus Notes	41	41R
152	Short Sales	103	103R
153	Counterparty Reporting Exception for Asbestos and Pollution Contracts	62R	62R
154	Implementation of Principle-Based Reserving	51; 54	51R; 54R
155	Classification of Money Market Mutual Funds as Cash Equivalents	2	2R
156	Bonds	26	26R
157	Use of Net Asset Value	100	100R
158	Unaffiliated Common Stock	30	30R
159	Special Accounting Treatment for Limited Derivatives	108	108

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IP No.	Title	SSAP Reference	
		Original Authoritative Literature	Current Authoritative Literature
160	Structured Settlements Acquired as Investments	21R	21R
161	Leases	22	22R
162	Property and Casualty Reinsurance Credit	62R	62R
163	Working Capital Finance Investment Updates	105	105R
164	Preferred Stock	32	32R
165	Levelized Commission	71	71
166	Updates to the Definition of an Asset	4	4

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Statutory Issue Paper No. 167

Derivatives and Hedging

STATUS
Finalized March 22, 2023

Original SSAP and Current Authoritative Guidance: SSAP No. 86

Type of Issue:
Common Area

SUMMARY OF ISSUE

1. Statutory accounting guidance for derivatives is in *SSAP No. 86—Derivatives*. Although SSAP No. 86 indicates "adoption of the framework" of specific U.S. GAAP guidance, the accounting and reporting guidance for derivatives, particularly with regards to the four U.S. GAAP derivative cornerstones, is distinctly different between SSAP No. 86 and FAS 133/ASC 815. For example, under U.S. GAAP, assessment effectiveness under U.S. GAAP is largely an income statement management tool (to offset variations consistently through net income or other comprehensive income – OCI), but as SAP uses an amortized cost measurement method for a number of hedged items, the criteria for hedge effectiveness and the measurement approach for derivatives must be adjusted accordingly.

2. In August 2017, the FASB issued *ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* to improve the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements. In addition, the amendments incorporated certain targeted improvements to simplify the application of the hedge accounting guidance in current U.S. GAAP. ASU 2017-12 included a new concept for a 'last of layer' approach to make portfolio fair value hedge accounting more accessible for specific assets. With the issuance of the last-of-layer guidance, a number of questions were received. After considering those questions, *ASU 2022-01 Fair Value Hedging – Portfolio Layer Method* was issued. This ASU expanded the original guidance and provided additional specifications and guidance.

3. The Statutory Accounting Principles (E) Working Group has considered several revisions to SSAP No. 86 in response to the review of ASU 2017-12 and ASU 2022-01. This issue paper has been drafted to detail the revisions incorporated into statutory accounting. These revisions, except for those initially adopted in 2018, are considered new SAP concepts.

DISCUSSION

Topic 1: Hedge Documentation and Initial Assessment Efficiencies (Agenda Item 2018-30)

4. The overall intent of ASU 2017-12 was to reduce cost and complexity of applying hedge accounting by simplifying the way assessments of hedge effectiveness may be performed. It was noted that the efficiencies gained from the revisions in the ASU for U.S. GAAP filers would be lost if corresponding provisions were not considered for statutory accounting. Pursuant to a July 9, 2018, interested parties' comment letter, three elements were requested to be considered by the Statutory Accounting Principles (E) Working Group in a nonsubstantive (SAP clarification) proposal. Interested parties noted that these elements will reduce the costs associated with hedge accounting, while neither changing the underlying accounting, nor creating any additional regulatory risks or concerns:

a. Allow companies to perform subsequent assessments of hedge effectiveness qualitatively if certain conditions are met.

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b. Allow companies more time to perform the quantitative hedge effectiveness assessment.

c. Clarify that companies may apply the "critical terms match" method for a group of forecaster transactions if the transactions occur and the derivatives mature within the same 31-day period or fiscal month, and the other requirements for applying the critical match method are satisfied.

5. On August 4, 2018, the Working Group exposed revisions to incorporate hedge documentation and assessment efficiencies from ASU 2017-12. This item was exposed with a shortened comment period to allow for potential revisions and re-exposure if needed, to permit adoption and application prior to year-end 2018. On November 15, 2018, the Working Group adopted the exposed revisions as final. The revisions were adopted with an effective date of January 1, 2019, with early adoption permitted for year-end 2018. U.S. GAAP filers could only early adopt if they had also early adopted ASU 2017-12.

6. Additionally, in ASU 2017-12, in response to comments requesting a more flexible approach to hedging interest rate risk, the FASB decided to amend the guidance for hedging interest rate risk of financial instruments for both fair value and cash flow hedges. With the revisions, the FASB decided to redefine the term interest rate risk and eliminate the benchmark interest rate concept for variable-rate financial instruments. With the changes, the FASB incorporated the SIFMA rate in the list of eligible rates for fixed income instruments and noted that the FASB will add to the list of eligible benchmark rates as necessary. The revisions adopted to SSAP No. 86 are detailed in Exhibit A.

7. With the inclusion of revisions, certain elements from the U.S.GAAP guidance were not duplicated within statutory accounting. The elements were considered part of the prior adoption of the "FAS 133 / technical guidance" originally reflected in SSAP No. 86:

a. Exceptions from the initial prospective quantitative assessment were not captured in the statutory guidance as they were not necessarily new under ASU 2017-12. The following overview details when an initial prospective quantitative assessment would not be required:

i. In a cash flow or fair value hedge, the entity applies the short-cut method.

ii. In a cash flow or fair value hedge, the entity determines that the critical terms of the hedging instrument and the hedged item match.

iii. In a cash flow hedge, the hedging instrument is an option and it meets specific criteria detailed in the U.S. GAAP guidance

iv. In a cash flow hedge, a private company that is not a financial institution applies the simplified hedge accounting approach.

v. In a cash flow hedge, the entity assesses hedge effectiveness under the change in variable cash flows method permitted under U.S. GAAP, with all noted conditions being met.

vi. In a cash flow hedge, the entity assesses hedge effectiveness under the hypothetical derivative method permitted under U.S. GAAP and all the critical terms of the hypothetical derivative and the hedging instrument are the same.

vii. In a net investment hedge, the entity assesses hedge effectiveness using a method based on changes in spot exchange rates, and the conditions noted under U.S. GAAP are met.

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viii. In a net investment hedge, the entity assesses hedge effectiveness using a method based on changes in forward exchange rates and the noted condition under U.S. GAAP are met.

b. The short-cut method and critical terms match method are current method permitted under U.S. GAAP retained under ASU 2017-12. Under these methods, an entity may qualitatively assume, in very limited circumstances, that

8. Ultimately, the revisions incorporated in 2018, effective January 1, 2019, with early application permitted, from ASU 2017-12 were limited to specific provisions, and related transition guidance, pertaining to the documentation and assessment of hedge effectiveness: 1) provisions allowing more time to perform the initial qualitative hedge effectiveness assessment; 2) provisions allowing subsequent assessments of hedge effectiveness to be performed qualitatively if certain conditions are met; and 3) revisions regarding use of the critical terms and short-cut method for assessing hedge effectiveness. With the adoption of the limited provisions, it was identified that the remaining provisions of ASU 2017-12 would be subsequently assessed for statutory accounting and shall not be considered adopted for statutory accounting until that assessment is completed, with a conclusion to adopt the U.S. GAAP guidance.

9. The revisions adopted in November 2018 included revisions to both SSAP No. 86 as well as Exhibit B – Assessment of Hedging Effectiveness. The subsequent revisions adopted in 2022 eliminated Exhibit B as well as incorporated new guidance through the SSAP. Ultimately, the final adopted guidance, as reflected in the AP&P Manual, is the authoritative guidance.

Topic 2: Hedge Effectiveness and Measurement Methods for Excluded Components (Ref #2021-20)

10. In December 2011, consideration began on revisions to facilitate effective hedge assessments consistently between statutory accounting and U.S. GAAP. The Working Group exposed a concept agenda item to solicit comments and directed NAIC staff to work with regulators and industry in developing revisions for consistent hedge effectiveness assessments and with the treatment of excluded components.

11. After working with industry, on April 4, 2022, the Working Group exposed two documents for public comment. The first document proposed revisions in the form of a new exhibit A to SSAP No. 86, which would replace both Exhibit A and Exhibit B. This new exhibit A would adopt with modification U.S. Guidance in determining hedge effectiveness. The second document proposed revised guidance to SSAP No. 86 to update the permitted excluded components to mirror U.S. GAAP but establish statutory-specific measurement methods for the excluded components.

12. The new Exhibit A intends to reflect the position that the assessment of hedge effectiveness for derivatives should be consistent between U.S. GAAP and SAP. In order words, transactions identified to be highly effective hedges under U.S. would be identified as highly effective hedged under statutory accounting. If a hedging instrument results with offsetting changes (or other permitted aspects) to a hedged item pursuant to the guidelines under U.S. GAAP to qualify as a highly effective hedge, the same assessment as a highly effective hedge should occur under SAP.

13. The Exhibit A would adopt, with modification U.S. GAAP guidance pertaining to the criteria for initial and subsequent hedge effectiveness detailed in the FASB Accounting Standards Codification (ASC) paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12. Although the U.S. GAAP guidance for the assessment and determination of hedge effectiveness is proposed to be adopted, statutory modifications are captured to specify that the accounting and reporting of hedging instruments, including excluded components of the instruments, shall follow statutory specific guidance detailed in SSAP No. 86. The intent of this guidance is to clarify that the determination of whether a hedging instrument qualifies as an effective hedge shall converge with U.S. GAAP, but that the measurement method shall continue to follow statutory specific provisions. The adopt from U.S. GAAP only extends to

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revisions incorporated through ASU 2017-12, as such, any subsequent U.S. GAAP edits would require statutory accounting consideration before they were considered adopted.

14. In addition to new Exhibit A to SSAP No. 86, the Working Group also exposed proposed revisions to SSAP No. 86, paragraphs 23, 40-41 and Exhibit C, to expand the list of permitted excluded components in assessing derivative effectiveness to match U.S. GAAP and to establish statutory specific measurement requirements for each type of excluded component.

15. The prior SSAP No. 86 guidance reflected the list of permitted excluded components originally adopted from U.S. GAAP. Since the original inclusion in SSAP No. 86, and within ASU 2017-12, U.S. GAAP had expanded the list, and it was noted that the statutory accounting treatment of excluded components related to foreign currency transactions were hindering the ability to engage in those transactions. It was also identified that current measurement guidance within the SSAP was conflicting between the guidance and specific hedge procedures detailed in Exhibit C. Through the discussions with industry, it was identified that different measurement or recognition provisions should be considered to properly reflect the type of excluded component with the financial statements, with specific guidance included in SSAP No. 86 accordingly:

a. If the excluded component pertains to the difference between a foreign currency spot price and the forward or future price (e.g., a forward spot rate), then this premium/discount shall be amortized into income over the life of the contract or hedged program. (This guidance addresses the excluded component in Exhibit A, paragraph 8.d.)

b. If the excluded component pertains to a foreign currency swap cross-currency basis spread, the impact of fair value changes shall be reflected as a component of the foreign currency swap's periodic interest accrual. (This guidance addresses the excluded component in Exhibit A, paragraph 8.e.)

c. For all other excluded components, the excluded component shall be measured and reported at fair value, with changes in fair value recognized as unrealized gains or losses. (This guidance shall be applied to excluded components detailed in Exhibit A, paragraphs 8.a. through 8.c.)

16. On August 10, 2022, after the exposure timeframe, in which interested party comments were received supporting the proposed revisions, the Working Group adopted the exposed revisions. This adoption resulted with both the new Exhibit A that adopts with modification U.S. GAAP guidance in determining hedge effectiveness and the revisions to SSAP No. 86 to incorporate measurement method guidance for excluded components. These revisions were adopted with a January 1, 2023, effective date, with early adoption permitted. With the action to adopt, the Working Group directed a blanks proposal to incorporate Schedule DB reporting fields and templates to capture the new disclosures for excluded components. These disclosure and investment schedule changes will be in effect for year-end 2023. Companies that early adopt the revisions are directly to complete the required disclosures in a narrative format for year-end 2022.

Topic 3: Portfolio Layer Method and Partial Term Hedging (Ref #2022-09)

17. In August 2022, considerations began to expand statutory accounting guidance to incorporate the portfolio layer method detailed in *ASU 2022-01, Fair Value Hedging – Portfolio Layer Method*. The guidance in ASU 2022-01 reflects an expansion of the last-of-layer method detailed in ASU 2017-12.

18. Under the last-of-layer approach captured in ASU 2017-12, for a closed portfolio of prepayable financial assets or one or more beneficial interests secured by a portfolio of prepayable financial instruments, entities were allowed to hedge a stated amount of the asset or assets in the closed portfolio that is anticipated to be outstanding for the designated hedged period. If the requirements for the last-of-layer

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method were met, prepayment risk is not incorporated into the measurement of the hedged item. With the application of this guidance, a number of questions were received. After considering those questions, FASB issued *ASU 2022-01, Fair Value Hedging – Portfolio Layer Method,* which expanded the guidance and provided additional specifications for application. Ultimately, for a closed portfolio of financial assets or one of more beneficial interests secured by a portfolio of financial instruments, an entity may designate as the hedged item or items a hedged layer or layers if the following criteria is met:

a. As part of the initial hedge documentation, an analysis is completed and documented to support the entity's expectation that the hedged item or items (that is, the hedged layer or layers in aggregate) is anticipated to be outstanding for the designated hedge period. That analysis shall incorporate the entity's current expectations of prepayments, defaults, and other factors affecting the timing and amount of cash flows associated with the closed portfolio.

b. For purposes of its analysis, the entity assumes that as prepayments, defaults, and other factors affecting the timing and amount of cash flows occur, they first will be applied to the portion of the closed portfolio that is not hedged.

c. The entity applies the partial-term hedging guidance to the assets or beneficial interests used to support the entity's expectation. An asset that matures on a hedged layer's assumed maturity date meets this requirement.

19. Similar to concepts supporting the adoption of prior U.S. GAAP revisions, there is a general assessment that determination of effective hedges shall be consistent between statutory accounting and U.S. GAAP. As such, new SAP concepts revisions to reflect the portfolio layer method in establishing effective hedge dynamics was proposed to be consistent with U.S. GAAP. With the U.S. GAAP guidance limiting the application of this guidance to hedges of recognized financial assets, a consistent scope threshold was established for statutory accounting.

20. The review of the portfolio layer method identified that U.S. GAAP prevents basis adjustments directly to assets hedged in a portfolio and it was considered on whether statutory revisions would be necessary to address similar basis adjustment revisions under statutory accounting. However, after further assessments, it was identified that the fair value measurement method under U.S. GAAP, which results in ongoing basis adjustments from changes in fair value over the derivative term, would not be a prominent issue under statutory accounting, which predominantly uses an amortized cost approach for effective hedges. With the use of amortized cost, basis adjustments do not occur until hedge termination or at designation of the hedge, therefore this was identified as not a key statutory accounting impact.

21. In addition to considering guidance for the portfolio layer method, representatives from interested parties proposed to also capture concepts for partial term hedges from ASU 2017-12. (As detailed in the FASB criteria above in paragraph 18 for portfolio layer method hedges, application of a the partial-term hedging guidance is used to support the entity's expectation.) Prior review of partial term hedge concepts noted concern as how interim adjustments to hedged items, particularly for hedged liabilities, would be reflected in the financial statements. With the statutory accounting guidance to reflect derivative gains or losses as basis adjustments on the hedge item, if a hedge to a recognized liability resulted in a reduction to the presentation of the liability, this could misrepresent the financial statements as the liability itself had not been reduced. In considering these concerns and recognizing that a broader project would likely be needed to address these basis adjustments, representatives from industry recommended incorporated the U.S. GAAP guidance for partial term hedges, with a statutory modification to limit the application to hedges of recognized assets.

22. Although the proposal to limit partial term hedges to recognized assets is a modification from the overarching concept to mirror hedge effectiveness assessments between U.S. GAAP and SAP, it was

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identified as an approach that would be consistent with the U.S. GAAP scope application for the portfolio layer method and would reflect how industry currently uses partial term hedge transactions. As such, although the modification created a U.S. GAAP and SAP difference, the modification satisfies the current need for statutory guidance and prevents significant concerns on how the guidance could impact the presentation of liabilities. With this discussion, it was identified that subsequent consideration of the limitation to recognized assets could occur, with potential expansion to hedges of recognized liabilities as part of a broader discussion on how derivative gains and losses are recognized as basis adjustments.

23. The proposed revisions exposed to incorporate the portfolio layer method and the partial-term hedging method are summarized as follows:

a. Revisions to SSAP No. 86, predominantly in paragraph 26.d., 26.f., and 26.g., to detail the ability to hedge recognized assets under the portfolio layer method and partial-term hedge. Also, revisions to paragraph 62 for a new disclosure for portfolio layer derivatives that no longer qualify for hedge accounting and the circumstances that led to the breach, as well as guidance in paragraphs 65.c. and 74.f. to detail relevant U.S. GAAP literature and the effective date.

b. Revisions to SSAP No. 86 – Exhibit, Exhibit A – Assessment of Hedge Effectiveness, to add a new section on the assessment of portfolio layer method for hedge effectiveness. (Note – This exhibit was the new exhibit adopted in agenda item 2021-20 which replaced the prior Exhibit A and Exhibit B within SSAP No. 86.)

c. Revisions to SSAP No. 86 – Exhibit C, paragraph 2.d., for which a portfolio layer method is discontinued to detail how the basis adjustment shall be allocated to the remaining individual assets in the closed portfolio. (Note – With the adoption of agenda item 2021-20, this Exhibit was renamed as Exhibit B.)

24. The proposed revisions reflect adoption of U.S. GAAP for the criteria for the portfolio layer method detailed in ASU 2022-01, criteria to only consider how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity date in ASC 815-20-25-6B, adding option in calculating the change in the hedged item's fair value attributed to changes in the benchmark interest rate based on the benchmark rate components of the contractual cash flows detailed in FASB ASC 815-25-35-13, and the partial-term hedging method detailed in FASB ASC 815-25-35-13B. The adoption of the partial term hedging method reflects statutory modifications that limits its use only when the hedged item is a recognized asset. This is different than U.S. GAAP, which permits the partial term method for hedged liabilities. The statutory limitation is established to prevent interim basis adjustments to hedged liabilities that could present a reduction of reported liabilities on the financial statements when the actual liability has not been reduced. Reconsideration of this statutory limitation may occur after a broader project to consider how derivative basis adjustments to hedged liabilities shall be reflected in the financial statements.

25. On December 13, 2022, the Working Group adopted the exposed revisions. This adoption resulted with the revisions identified in paragraph 23 above. These revisions were adopted with a January 1, 2023, effective date, with early adoption permitted. The revisions shall be applied prospectively to qualifying new hedges.

26. An updated version of this issue paper was exposed on December 12, 2022, and adopted on March 22, 2023. The purpose of this issue paper is to document the historical actions resulting in new SAP concepts within *SSAP No. 86—Derivatives*. As issue papers are not represented in the statutory hierarchy, the adoption of this issue paper does not change the effective date of the previously adopted authoritative literature.

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Exhibit 1 – Revisions adopted to SSAP No. 86 on November 15, 2018 (Agenda Item 2018-30)

38. At inception of the hedge, documentation must include:

a. A formal documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge, including identification of the hedging instrument, the hedged item, the nature of the risk being hedged, and how the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or variability in cash flows attributable to the hedged risk will be assessed, including whether an entity will perform subsequent effectiveness assessments on a qualitative basis (per paragraph 42) and how it intends to carry out that qualitative assessment. There must be a reasonable basis for how the entity plans to assess the hedging instrument's effectiveness;

b. An entity's defined risk management strategy for a particular hedging relationship may exclude certain components of a specific hedging derivative's change in fair value, such as time value, from the assessment of hedge effectiveness, as discussed in paragraph 37 and Exhibit B;

c. Signature of approval, for each instrument, by person(s) authorized, either by the entity's board of directors or a committee authorized by the board, to approve such transactions; and

d. A description of the reporting entity's methodology used to verify that opening transactions do not exceed limitations promulgated by the state of domicile.

39. At inception, if an entity is required to perform an initial prospective assessment of hedge effectiveness on a quantitative basis (using information applicable as of the date of hedge inception[FN]), the assessment is considered to be performed concurrently at hedge inception if it completed by the earliest of the following: *(815-20-25-3)*

a. The first quarterly hedge effectiveness assessment date.

b. The date that financial statements that include the hedged transaction are available to be issued.

c. The date that the hedging instrument and hedged item no longer qualify for hedge accounting.

d. The date of expiration, sale, termination or exercise of the hedging instrument.

e. The date of dedesignation of the hedging relationship.

f. For a cash flow hedge of a forecasted transaction, the date that the forecasted transaction occurs.

New Footnote – Entities are required to perform an initial prospective assessment unless qualifying for an exception in accordance with ASU 2017-12, paragraph 815-20-25-3.

40. For all derivatives terminated, expired, or exercised during the year:

a. Signature of approval, for each instrument, by person(s) authorized, either by the entity's board of directors or a committee authorized by the board, to approve such transactions;

b. A description, for each instrument, of the nature of the transaction, including:

i. The date of the transaction;

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ii. A complete and accurate description of the specific derivative, including description of the underlying securities, currencies, rates, indices, commodities, derivatives, or other financial market instruments;

iii. Number of contracts or notional amount;

iv. Date of maturity, expiry or settlement;

v. Strike price, rate or index (termination price for futures contracts);

vi. Counterparty, or exchange on which the transaction was traded; and

vii. Consideration paid or received, if any, on termination.

c. Description of the reporting entity's methodology to verify that derivatives were effective hedges; and

d. Identification of any derivatives that ceased to be effective as hedges.

41. For derivatives open at quarter-end:

a. A description of the methodology used to verify the continued effectiveness of hedges, and whether the entity is using qualitative assessments pursuant to paragraph 42[FN];

b. An identification of any derivatives that have ceased to be effective as hedges;

c. A description of the reporting entity's methodology to determine fair values of derivatives;

d. Copy of Master Agreements, if any, where indicated on Schedule DB Part D.

New Footnote: For purposes of this requirement, this statement adopts the guidance for effectiveness assessment after initial designation reflected in ASU 2017-12, including the concepts and restrictions for use of the short-cut method and the critical terms match method.

42. An entity may subsequently qualitatively assess hedge effectiveness, on a hedge-by-hedge basis, if both the conditions in paragraphs 42.a. and 42.b. were initially met. When an entity performs subsequent qualitative assessments of hedge effectiveness, it shall verify and document whenever financial statements or earnings are reported and at least every three months that the facts and circumstances related to the hedging relationship have not changed such that it can assert qualitatively that the hedging relationship was and continues to be highly effective. An entity may perform a quantitative assessment in any reporting period to validate whether qualitative assessments remain appropriate. When facts and circumstances change such that an entity no longer can assert qualitatively that the hedging relationship continue to be highly effective, then the entity shall begin performing quantitative assessments. (815-20-35-2A, 2C and 2D abbreviated)

a. An entity performs an initial quantitative test of hedge effectiveness on a prospective basis (that is, it is not assuming that the hedging relationship is perfectly effective at hedge inception) and the results of that quantitative test demonstrate highly effective offset.

b. At hedge inception, an entity can reasonably support an expectation of high effectiveness on a qualitative basis in subsequent periods.

RELEVANT LITERATURE

6059. This statement adopts the framework established by FAS 133, FASB Statement No. 137, Accounting for Derivative Instruments and Hedging Activities—Deferral of the Effective Date of FASB Statement No. 133, An amendment of FASB Statement No. 133 (FAS 137) and FASB Statement No. 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities, An amendment of FASB

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Statement No. 133 (FAS 138), for fair value and cash flow hedges, including its technical guidance to the extent such guidance is consistent with the statutory accounting approach to derivatives utilized in this statement. This statement adopts the provisions of FAS 133 and 138 related to foreign currency hedges. With the exception of guidance specific to foreign currency hedges and amendments specific to refining the hedging of interest rate risk (under FAS 138, the risk of changes in the benchmark interest rate would be a hedged risk), this statement rejects FAS No. 137 and 138 as well as the various related Emerging Issues Task Force interpretations. This statement adopts paragraphs 4 and 25 of FASB Statement No. 149: Amendment of Statement 133 on Derivative Instruments and Hedging Activities (FAS 149) regarding the definition of an underlying and guidance for assessing hedge effectiveness. All other paragraphs in FAS 149 are rejected as not applicable for statutory accounting. This statement adopts FSP FAS 133-1 and FIN 45-5: Disclosures about Credit Derivatives and Certain Guarantees, An Amendment of FASB Statement No. 133 and FASB Interpretation No.45 and Clarification of the Effective Date of FASB Statement No. 161 (FSP FAS 133-1 and FIN 45-4) and requires disclosures by sellers of credit derivatives. This statement rejects FSP FIN 39-1, Amendments of FASB Interpretation No. 39, and ASU 2014-03, Derivatives and Hedging – Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps – Simplified Hedge Accounting Approach.

61. This statement adopts certain revisions to ASC 815-20 included in ASU 2017-12. This adoption is limited to specific provisions, and related transition guidance, pertaining to the documentation and assessment of hedge effectiveness and only includes: 1) provisions allowing more time to perform the initial quantitative hedge effectiveness assessment; 2) provisions allowing subsequent assessments of hedge effectiveness to be performed qualitatively if certain conditions are met; and 3) revisions regarding use of the critical terms and short-cut methods for assessing hedge effectiveness. The remaining provisions of ASU 2017-12 will be subsequently assessed for statutory accounting and shall not be considered adopted for statutory accounting until that assessment is complete.

62~~60~~. This statement adopts with modification revisions to ASC 815 as reflected within ASU 2016-05, Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships. This guidance is modified to require prospective application, as such it is only applicable to future counterparty changes in derivative instruments, and this guidance cannot be used to adjust derivative transactions previously terminated. This statement adopts revisions to ASC 815-20-25-15 as reflected within ASU 2010-08, Technical Corrections to Various Topics. This statement adopts revisions to ASC 815-10-50-4K as reflected within ASU 2010-11, Derivatives and Hedging (Topic 815), Scope Exception Related to Embedded Credit Derivatives, but rejects all other GAAP revisions from ASU 2010-11 and ASU 2014-16, Derivatives and Hedging, Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity and ASU 2016-06, Derivatives and Hedging, Contingent Put and Call Options in Debt Instruments. These GAAP revisions are rejected as embedded derivatives are not separated from the host contract and recognized as derivatives under SSAP No. 86. Revisions are also incorporated to SSAP No. 86 to require disclosures on embedded credit derivatives that expose the holder of a financial instrument to the possibility of being required to make future payments. This disclosure is a modification to the GAAP disclosures specific to statutory accounting as embedded credit derivatives are not separately recognized under statutory accounting. It should be noted that the conclusions reached in this statement are not intended to usurp the rules and regulations put forth by states in their respective investment laws. The contents of this statement are intended to provide accounting guidance on the use of derivatives as allowed by an insurer's state of domicile. It is not intended to imply that insurers may use derivatives or cash instruments that the insurer's state of domicile does not allow under the state's insurance regulatory requirements, e.g., in replication transactions.

63~~61~~. This statement adopts revisions to ASC 815-20 as reflected within ASU 2013-10, Derivatives and Hedging, Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a benchmark interest rate for Hedge Accounting Purposes. These revisions define a benchmark interest rate, clarify what can be used in the U.S. for a benchmark interest rate, and eliminate the prior restriction on using different benchmark rates for similar hedges.

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Effective Date and Transition

6765. This statement is effective for derivative transaction entered into or modified on or after January 1, 2003. A modification is any revision or change in contractual terms of the derivative. SSAP No. 31 applies to derivative transaction prior to January 1, 2003. Alternatively, an insurer may choose to apply this statement to all derivatives to which the insurer is a party as of January 1, 2003. In either case, the insurer is to disclose the transition approach that is being used. Revisions adopted to paragraph 59 to reject FSP FIN 39-1 is effective January 1, 2013, for companies that have previously reported a position in the balance sheet that was net of counterparty agreements. (Companies that have previously reported derivative instruments and/or related collateral gross shall not be impacted by these revisions.) Revisions adopted in paragraph 15 clarify the reporting for amounts received/paid to adjust variation margin until the derivative contract has ended and are effective January 1, 2018, on a prospective basis, for reporting entities that have previously considered these amounts to reflect settlement or realized gains/losses. (Companies that have previously reported variation margin changes in line with the revisions shall not be impacted by these revisions.) Revisions to incorporate limited provisions from ASU 2017-12 pertaining to the documentation of hedge effectiveness (detailed in paragraph 61) are effective January 1, 2019, with early adoption permitted for year-end 2018. However, if the reporting entity is a U.S. GAAP filer, the reporting entity may only elect early adoption if the entity has also elected early adoption of ASU 2017-12 for year-end 2018.

SSAP NO. 86 - EXHIBIT B – ASSESSMENT OF HEDGING EFFECTIVENESS

The following is based on paragraphs 62-70 of FAS 133 to offer additional guidance on assessing hedging effectiveness. The intent of such is to remain consistent with ~~FAS 133~~U.S. GAAP with respect to assessing hedge effectiveness, including guidance in ASU 2017-12 that outlines when an entity may perform subsequent assessments of hedge effectiveness qualitatively.

1. This statement requires that an entity define at the time it designates a hedging relationship the method it will use to assess the hedge's effectiveness in achieving offsetting changes in fair value or offsetting cash flows attributable to the risk being hedged. It also requires that an entity use that defined method consistently throughout the hedge period to assess at inception of the hedge and on an ongoing basis whether it expects the hedging relationship to be highly effective in achieving offset. If the entity identifies an improved method and wants to apply that method prospectively, it must discontinue the existing hedging relationship and designate the relationship anew using the improved method. Although this statement suggests a method for assessing whether a hedge is expected to be highly effective or measuring hedge ineffectiveness, the appropriateness of a given method of assessing hedge effectiveness can depend on the nature of the risk being hedged and the type of hedging instrument used. Ordinarily, however, an entity should assess effectiveness for similar hedges in a similar manner; use of different methods for similar hedges should be justified.

2. In defining how hedge effectiveness will be assessed, an entity must specify whether it will include in that assessment all of the gain or loss on a hedging instrument. As discussed in paragraph 33, this statement permits (but does not require) an entity to exclude all or a part of the hedging instrument's time value from the assessment of hedge effectiveness, as follows:

a. If the effectiveness of a hedge with an option contract is assessed based on changes in the option's intrinsic value, the change in the time value of the contract would be excluded from the assessment of hedge effectiveness.

b. If the effectiveness of a hedge with an option contract is assessed based on changes in the option's minimum value, that is, its intrinsic value plus the effect of discounting, the change in the volatility value of the contract would be excluded from the assessment of hedge effectiveness.

c. If the effectiveness of a hedge with a forward or futures contract is assessed based on changes in fair value attributable to changes in spot prices, the change in the fair value of the contract related to the changes in the difference between the spot price and the forward or futures price would be excluded from the assessment of hedge effectiveness.

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In each circumstance above, changes in the excluded component would be included in unrealized gains or losses. As noted in paragraph 1 of this Exhibit, the effectiveness of similar hedges generally should be assessed similarly; that includes whether a component of the gain or loss on a derivative is excluded in assessing effectiveness. No other components of a gain or loss on the designated hedging instrument may be excluded from the assessment of hedge effectiveness.

3. In assessing the effectiveness of a cash flow hedge, an entity generally will need to consider the time value of money if significant in the circumstances. Considering the effect of the time value of money is especially important if the hedging instrument involves periodic cash settlements. An example of a situation in which an entity likely would reflect the time value of money is a tailing strategy with futures contracts. When using a tailing strategy, an entity adjusts the size or contract amount of futures contracts used in a hedge so that earnings (or expense) from reinvestment (or funding) of daily settlement gains (or losses) on the futures do not distort the results of the hedge. To assess offset of expected cash flows when a tailing strategy has been used, an entity could reflect the time value of money, perhaps by comparing the present value of the hedged forecasted cash flow with the results of the hedging instrument.

4. ~~Whether a hedging relationship qualifies as highly effective sometimes will be easy to assess.~~ If the critical terms of the hedging instrument and of the ~~entire~~ hedged item~~asset or liability (as opposed to selected cash flows)~~ or hedged forecasted transaction are the same, the entity could conclude that changes in fair value or cash flows attributable to the risk being hedged are expected to completely offset at inception and on an ongoing basis. For example, an entity may assume that a hedge of a forecasted purchase of a commodity with a forward contract will be ~~highly~~ perfectly effective if:

a. The forward contract is for purchase of the same quantity of the same commodity at the same time and location as the hedged forecasted purchase.

b. The fair value of the forward contract at inception is zero.

c. Either the change in the discount or premium on the forward contract is excluded from the assessment of effectiveness and included directly in unrealized gains and losses pursuant to paragraph 22.B. or the change in expected cash flows on the forecasted transaction is based on the forward price for the commodity.

5. In a cash flow hedge of a group of forecasted transactions, an entity may assume that the timing in which the hedged transactions are expected to occur and the maturity date of the hedging instrument match in accordance with paragraph if those forecasted transactions occur and the derivative matures within the same 31-day period or fiscal month. *(815-20-25-84A)*

~~5~~6. However, assessing hedge effectiveness can be more complex. For example, hedge effectiveness would be reduced by the following circumstances, among others:

a. A difference between the basis of the hedging instrument and the hedged item or hedged transaction (such as a Deutsche mark-based hedging instrument and Dutch guilder-based hedged item), to the extent that those bases do not move in tandem

b. Differences in critical terms of the hedging instrument and hedged item or hedged transaction, such as differences in notional amounts, maturities, quantity, location, or delivery dates.

Hedge effectiveness also would be reduced if part of the change in the fair value of a derivative is attributable to a change in the counterparty's creditworthiness.

~~6~~7. A hedge that meets the effectiveness test specified in paragraphs 19.b. and 20.b. (that is, both at inception and on an ongoing basis, the entity expects the hedge to be highly effective at achieving offsetting changes in fair values or cash flows) also must meet the other hedge accounting criteria to qualify for hedge accounting. If the hedge initially qualifies for hedge accounting, the entity would continue to assess whether the hedge meets the effectiveness test. If the hedge fails the effectiveness test at any time (that is, if the entity does not expect the hedge to be highly effective at achieving offsetting changes in fair values or cash

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flows), the hedge ceases to qualify for hedge accounting. The discussions of measuring hedge effectiveness in the examples in the remainder of this Exhibit assume that the hedge satisfied all of the criteria for hedge accounting at inception.

Exhibit 2 – Revisions adopted to SSAP No. 86 on August 10, 2021 (Agenda Item 2021-20)

Derivatives Used in Hedging Transactions

22. Derivative instruments used in hedging transactions that meet the criteria of a highly effective hedge shall be considered an effective hedge and are permitted to be valued and reported in a manner that is consistent with the hedged asset or liability (referred to as hedge accounting). For instance, assume an entity has a financial instrument on which it is currently receiving income at a variable rate but wishes to receive income at a fixed rate and thus enters into a swap agreement to exchange the cash flows. If the transaction qualifies as an effective hedge and a financial instrument on a statutory basis is valued and reported at amortized cost, then the swap would also be valued and reported at amortized cost. Derivative instruments used in hedging transactions that do not meet or no longer meet the criteria of an effective hedge, or that meet the required criteria but the entity has chosen not to apply hedge accounting, shall be accounted for at fair value and the changes in the fair value shall be recorded as unrealized gains or unrealized losses (referred to as fair value accounting)[1].

23. Entities shall not bifurcate the effectiveness of derivatives. A derivative instrument is either classified as an effective hedge or an ineffective hedge. Entities must account for the derivative using fair value accounting if it is deemed to be ineffective or becomes ineffective. Derivative instruments classified as effective with excluded components in determining hedge effectiveness pursuant to Exhibit A, paragraph 8, shall account for the derivative and excluded components pursuant to the guidance in paragraph 40. Entities may redesignate a derivative in a hedging relationship even though the derivative was used in a previous hedging relationship that proved to be ineffective. A change in the counterparty to a derivative instrument that has been designated as the hedging instrument in an existing hedging relationship would not, in and of itself, be considered a termination of the derivative instrument. An entity shall prospectively discontinue hedge accounting for an existing hedge if any one of the following occurs:

a. Any criterion in paragraphs 26-38 is no longer met;

b. The derivative expires or is sold, terminated, or exercised (the effect is recorded as realized gains or losses or, for effective hedges of firm commitments or forecasted transactions, in a manner that is consistent with the hedged transaction – see paragraph 24);

c. The entity removes the designation of the hedge; or

d. The derivative is deemed to be impaired in accordance with paragraph 18. A permanent decline in a counterparty's credit quality/rating is one example of impairment required by paragraph 18, for derivatives used in hedging transactions.

Hedge Effectiveness

39. The measurement of hedge effectiveness for a particular hedging relationship shall be consistent with the entity's risk management strategy and the method of assessing hedge effectiveness that was documented at the inception of the hedging relationship, as discussed in paragraph 41.

40. The gain or loss on a derivative designated as a hedge and assessed to be effective is reported consistently with the hedged item. (Therefore, if the hedged item is reported at amortized cost, and the hedging instrument is consistent with that measurement method, fluctuations in fair value would not be recognized as unrealized gains or losses for either the hedging item or hedging instrument.) If an entity's defined risk management strategy for a particular hedging relationship excludes a specific component of the gain or loss, or related cash flows, on the hedging derivative from the assessment of hedge effectiveness (as discussed in Exhibit ~~B~~A, paragraph 8), specific accounting treatment shall be followed for

[1] Pursuant to paragraph 19, the gross reported value of a derivative and the determination of unrealized gains or losses shall exclude the impact of financing premiums. Premiums payable or receivable from the acquisition or writing of a derivative shall not be reflected in the gross reporting of derivatives or in determining the fair value change in a derivative.

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the ~~that~~ excluded component: ~~of the gain or loss shall be recognized as an unrealized gain or loss. For example, if the effectiveness of a hedge with an option contract is assessed based on changes in the option's intrinsic value, the changes in the option's time value would be recognized in unrealized gains or losses. Time value is equal to the fair value of the option less its intrinsic value.~~

a. If the excluded component pertains to the difference between a foreign currency spot price and the forward or future price (e.g., a forward spot rate), then this premium/discount shall be amortized into income over the life of the contract or hedged program. (This guidance addresses the excluded component in Exhibit A, paragraph 8.d.)

b. If the excluded component pertains to a foreign currency swap cross-currency basis spread, the impact of fair value changes shall be reflected as a component of the foreign currency swap's periodic interest accrual. (This guidance addresses the excluded component in Exhibit A, paragraph 8.e.)

c. For all other excluded components, the excluded component shall be measured and reported at fair value, with changes in fair value recognized as unrealized gains or losses. (This guidance shall be applied to excluded components detailed in Exhibit A, paragraphs 8.a.-8.c.

41. Hedging instruments with excluded components shall be identified in the financial statement investment schedule (Schedule DB) and shall be disclosed pursuant to paragraph 41.g.

Proposed New Disclosure Paragraph (This is proposed as a new paragraph 41.g. with reordering of subsequent paragraphs.)

g. For hedging instruments with excluded components for determining hedge effectiveness:

i. In the investment schedule, identify hedging instruments with excluded components, and report the current fair value of the excluded component, the fair value of the excluded component that is reflected in the reported BACV for the hedging instrument (this item would not be applicable for foreign-currency forwards and currency swaps where the forward points or cross-currency basis, respectively, are the excluded component), and the change in fair value reported as an unrealized gains/loss. (Note – These items will be proposed in electronic columns to Schedule DB.)

ii. In the notes to the financial statements, provide information on the aggregate excluded components by category: Time Value, Intrinsic Value, Forward Points and Cross Currency Basis Spread. The aggregate amounts reported should include the following (as applicable): current fair value, recognized unrealized gain/loss, the fair value reflected in BACV, and for the excluded forward points (e.g., forward spot rates), the aggregate amount owed at maturity, along with current year and remaining amortization. (Note – These items will be captured in a blanks proposal/template.)

Relevant Literature

64. This statement adopts the framework established by FAS 133, *FASB Statement No. 137, Accounting for Derivative Instruments and Hedging Activities—Deferral of the Effective Date of FASB Statement No. 133, An amendment of FASB Statement No. 133* (FAS 137) and *FASB Statement No. 138, Accounting* for *Certain Derivative Instruments and Certain Hedging Activities, An amendment of FASB Statement No. 133* (FAS 138), for fair value and cash flow hedges, including its technical guidance to the extent such guidance is consistent with the statutory accounting approach to derivatives utilized in this statement. This statement adopts the provisions of FAS 133 and 138 related to foreign currency hedges. With the exception of guidance specific to foreign currency hedges and amendments specific to refining the hedging of interest rate risk (under FAS 138, the risk of changes in the benchmark interest rate would be a hedged risk), this statement rejects FAS No. 137 and 138 as well as the various related Emerging Issues Task Force interpretations. This statement adopts paragraphs 4 and 25 of *FASB Statement No. 149:*

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Amendment of Statement 133 on Derivative Instruments and Hedging Activities (FAS 149) regarding the definition of an underlying and guidance for assessing hedge effectiveness. (The adoption from FAS 149 on the assessment of hedge effectiveness is impacted by the adoption with modification of guidance from ASU 2017-12 as detailed in paragraph 65.b., with the guidance from ASU 2017-12 superseding the prior adoption to the extent applicable.) All other paragraphs in FAS 149 are rejected as not applicable for statutory accounting. This statement adopts FSP FAS 133-1 and FIN 45-5*: Disclosures about Credit Derivatives and Certain Guarantees, An Amendment of FASB Statement No. 133 and FASB Interpretation No.45 and Clarification of the Effective Date of FASB Statement No. 161 (*FSP FAS 133-1 and FIN 45-4) and requires disclosures by sellers of credit derivatives. This statement rejects *FSP FIN 39-1, Amendments of FASB Interpretation No. 39*, and *ASU 2014-03, Derivatives and Hedging – Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps – Simplified Hedge Accounting Approach*.

65. This statement adopts, with modification, certain revisions to ASC 815-20 included in ASU 2017-12. Remaining provisions of ASU 2017-12 will be subsequently assessed for statutory accounting and shall not be considered adopted for statutory accounting until that assessment is complete.

a. Revisions effective January 1, 2019, with early adoption permitted, ~~This adoption is~~are limited to specific provisions, and related transition guidance, pertaining to the documentation and assessment of hedge effectiveness and only includes: 1) provisions allowing more time to perform the initial quantitative hedge effectiveness assessment; 2) provisions allowing subsequent assessments of hedge effectiveness to be performed qualitatively if certain conditions are met; and 3) revisions regarding use of the critical terms and short-cut methods for assessing hedge effectiveness.

b. Revisions effective January 1, 2023, with early adoption permitted, are limited to the criteria for initial and subsequent hedge effectiveness detailed in the FASB Accounting Standards Codification (ASC) paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12. This adoption reflects statutory modifications to specify that the accounting and reporting of hedging instruments, including excluded components of the instruments, shall follow statutory specific guidance detailed in the statement. The intent of this guidance is to clarify that the determination of whether a hedging instrument qualifies as an effective hedge shall converge with U.S. GAAP, but that the measurement method shall continue to follow statutory specific provisions. The adoption of the referenced ASC paragraphs only extends to revisions incorporated through ASU 2017-12; therefore, any subsequent U.S. GAAP edits would require statutory accounting consideration before considered adopted.

~~The remaining provisions of ASU 2017-12 will be subsequently assessed for statutory accounting and shall not be considered adopted for statutory accounting until that assessment is complete.~~

Effective Date and Transition

74.~~73~~ This statement is effective for derivative transaction entered into or modified on or after January 1, 2003. A modification is any revision or change in contractual terms of the derivative. SSAP No. 31 applies to derivative transaction prior to January 1, 2003. Alternatively, an insurer may choose to apply this statement to all derivatives to which the insurer is a party as of January 1, 2003. In either case, the insurer is to disclose the transition approach that is being used.

a. Revisions adopted to paragraph 64 to reject FSP FIN 39-1 is effective January 1, 2013, for companies that have previously reported a position in the balance sheet that was net of counterparty agreements. (Companies that have previously reported derivative instruments and/or related collateral gross shall not be impacted by these revisions.)

b. Revisions adopted in paragraph 16 clarify the reporting for amounts received/paid to adjust variation margin until the derivative contract has ended and are effective January 1, 2018, on a prospective basis, for reporting entities that have previously considered these amounts to reflect settlement or realized gains/losses. (Companies that have previously reported variation margin changes in line with the revisions shall not be impacted by these revisions.)

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c. Revisions to incorporate limited provisions from ASU 2017-12 pertaining to the documentation of hedge effectiveness (detailed in paragraph 65) are effective January 1, 2019, with early adoption permitted for year-end 2018. However, if the reporting entity is a U.S. GAAP filer, the reporting entity may only elect early adoption if the entity has also elected early adoption of ASU 2017-12 for year-end 2018.

d. Revisions adopted April 2019 to explicitly include structured notes in scope of this statement are effective December 31, 2019. Revisions adopted July 2020 to define "derivative premium," require gross reporting of derivatives without the impact of financing premiums and require separate recognition of premiums payable and premiums receivable, are effective January 1, 2021.

e. Revisions adopted August 2022 that adopt with modification the criteria for initial and subsequent hedge effectiveness detailed in the FASB ASC paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12 and that incorporate statutory accounting revisions for the accounting and reporting of excluded components are effective January 1, 2023, with early adoption permitted. These revisions shall be applied prospectively for all new and existing hedges. Entities shall detail the adoption of this guidance as a change in accounting principle pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors*.

With the adoption of the new Exhibit A as detailed in the subsequent section, Exhibit C will be renamed Exhibit B. Due to the details of Exhibit A (including the FASB ASC paragraphs not duplicated in the SSAP), the following Exhibit B section is included before the new Exhibit A in this issue paper for ease of readability.

EXHIBIT ~~C~~ B – SPECIFIC HEDGE ACCOUNTING PROCEDURES FOR DERIVATIVES

Specific hedge accounting procedures for derivative instruments are outlined below.

1. Call and Put Options, Warrants, Caps, and Floors:

   a. Accounting at Date of Acquisition (purchase) or Issuance (written): The premium paid or received for purchasing or writing a call option, put option, warrant, cap or floor shall either be (i) recorded as an asset (purchase) or liability (written) on the Derivative line on the Assets (or) Liabilities pages or (ii) combined with the hedged item(s) individually or in the aggregate;

   b. Statement Value:

      i. Open derivatives hedging items recorded at amortized cost:

         (a) Options, warrants, caps, and floors purchased or written shall be valued at amortized cost in a manner consistent with the hedged item. (Components of a hedging instrument excluded from the determination of hedge effectiveness shall be recognized at fair value, with changes in fair value recognized as unrealized gains/losses throughout the duration of the hedging instrument. These components are not captured within the guidance for effective hedges detailed within this section.);

         (b) The amortization period and methods used shall result in a constant effective yield over the life of the hedged item or program. (For floating rate hedged items, the estimated effective yield shall be based on the current rate so the changes in yields attributable to changes in interest rates will be recognized in the period of change). Specific treatment includes:

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(1) Holdings in derivatives purchased or written within a year of maturity or expiry need not be amortized;

(2) For hedges of forecasted transactions or firm commitments, the derivative may be recorded at cost until the hedged transaction occurs or it is determined that the hedge was not effective (see (d) in this section 1.b.i.);

(3) For other derivatives, the amortization period is usually from date of acquisition (issuance) of the derivative to maturity of the hedged item or program.

(c) For hedges where the cost of the derivative is combined with the hedged item, the statement value is zero. The fair value of the derivative and hedged item shall be determined and reported separately, either individually or in the aggregate;

(d) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost until (1) the hedged transaction occurs or (2) it is determined that the hedge was not effective (when the derivative is valued in accordance with (e) in this section);

(e) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, valuation at amortized cost ceases and the derivative or the designated portion of the derivative shall be valued at its current fair value with gains and losses recognized in unrealized gains or unrealized losses to the extent it ceased to be an effective hedge.

d. Gain/Loss on Termination of an option, warrant, cap or floor accounted for under hedge accounting (includes closing, exercise, maturity, and expiry):

i. Exercise of an Option: The remaining book value of the derivative shall become an adjustment to the cost or proceeds of the hedged item(s) received or disposed of individually or in aggregate;

ii. Sale, maturity, expiry, or other closing transaction of a derivative which is an effective hedge—Any gain or loss on the transaction, except for excluded components, will adjust the basis (or proceeds) of the hedged item(s) individually or in aggregate. Alternatively, if the item being hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination. For hedging instruments with excluded components in determining hedge effectiveness, the unrealized gain/loss from the change in fair value of the excluded component shall be realized upon the closing transaction. This gain/loss shall not be used to adjust the basis or proceeds of the hedged item.~~;~~

iii. Gain/loss on termination of derivatives will be recognized currently in net income (realized gain/loss) to the extent they ceased to be effective hedges.

iv. Upon the redesignation of a derivative from a currently effective hedging relationship:

(a) with an item(s) carried at amortized cost to another effective hedging relationship with an item(s) carried at amortized cost, the derivative shall continue to be recorded at amortized cost and no gain or loss on the derivative shall be recognized.

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(b) with an item(s) carried at amortized cost or fair value to an effective relationship with an item(s) carried at fair value, the accounting for the derivative shall be consistent with (ii) above.

(c) with an item(s) carried at fair value to an effective relationship with an item(s) carried at amortized cost, the accounting for the derivative shall be consistent with (ii) above.

2. Swaps, Collars, and Forwards (see also discussion in Introduction above):

a. Accounting at Date of Opening Position:

i. Any premium paid or received at date of opening shall either be (a) recorded on the Derivative line on the Assets (or) Liabilities pages or (b) combined with the hedged item(s), individually or in the aggregate;

b. Statement Value:

i. Open derivatives hedging items recorded at amortized cost:

(a) Swaps, collars, and forwards shall be valued at amortized cost in a manner consistent with hedged item. (Components of a hedging instrument excluded from the determination of hedge effectiveness not addressed in 2.b.iii. shall be recognized at fair value, with changes in fair value of the excluded component recognized as unrealized gains/losses throughout the duration of the hedging instrument. These components are not captured within the guidance for effective hedges detailed within this section.);

(b) The amortization period and methods used shall result in a constant effective yield over the life of the hedged item or program. (For floating rate hedged items the estimated effective yield shall be based on the current rate so the changes in yields attributable to changes in interest rates will be recognized in the period of change.) Specific treatment includes:

(1) Holdings in derivatives purchased or written within a year of maturity or expiry need not be amortized;

(2) For hedges of forecasted transactions or firm commitments, the derivative shall be recorded at cost until (a) the hedged transaction occurs or (b) it is determined that the hedge was not effective (see (5) in this section 2.b.i.);

(3) For other derivatives the amortization period is usually from date of acquisition (issuance) of the derivative to maturity of the hedged item or program;

(4) For hedges where the cost of the derivative is combined with the hedged item, the statement value is zero. The fair value of the derivative and hedged item shall be determined and reported separately, either individually or in the aggregate;

(5) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, valuation at amortized cost ceases and the derivative or a designated portion of the derivative shall be valued at its current fair value with gains and losses recorded in unrealized gains or unrealized losses to the

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extent that it ceased to be an effective hedge. Upon redesignation into an effective hedging relationship, the derivative's mark to fair value through unrealized gain or loss shall be reversed.

ii. Open derivatives hedging items recorded at fair value (where gains and losses on the hedged item are recognized as adjustments to unassigned funds (surplus):

(a) Swaps, collars, or forwards shall be valued at current fair value with changes in fair value recognized currently consistent with the hedged item; this will result in unrealized gain/loss treatment with adjustment to unassigned funds (surplus);

(b) For hedges where the derivative is combined with the hedged item, the fair value of the derivative and hedge item shall be determined and reported separately, either individually or in the aggregate. The cost (book value) basis used to figure gain/loss on the derivative is zero.

iii. Open foreign currency swap and forward contracts hedging foreign currency exposure on items denominated in a foreign currency and translated into U.S. dollars where fair value accounting is not being used:

(a) ~~The foreign exchange premium (discount) on the currency contract shall be amortized into income over the life of the contract or hedge program.~~ The foreign exchange premium (discount) is defined as the foreign currency (notional) amount to be received (paid) times the net of the forward rate minus the spot rate at the time the contract was opened. For forward contracts, an excluded component representing a foreign exchange premium (discount) (forward points) on the currency contract shall be amortized into income over the life of the contract or hedge program. Amortization is not required if the contract was entered into within a year of maturity. For foreign currency swaps, an excluded component representing a cross-currency basis spread, is recognized into income through the foreign currency swap's periodic interest accruals.

~~Amortization is not required if the contract was entered into within a year of maturity;~~

(b) A foreign currency translation adjustment shall be reflected as an unrealized gain/loss (unassigned funds (surplus) adjustment) using the same procedures as done to translate the hedged item;

(c) The unrealized gain/loss for the period equals the foreign currency (notional) amount to be received (paid) times the net of the current spot rate minus the prior period end spot rate;

(d) The statement value of the derivative equals the amortized cost plus:

1. For forward contracts, the amortized (premium) discount plus the cumulative unrealized gain/(loss) on the contract.

2. For foreign currency swaps, ~~T~~the cumulative unrealized gain/(loss) on the contract. The cross-currency basis spread is recorded through the Investment Income Due and Accrued or Other Liabilities, as a component of the foreign currency swap's periodic interest accrual.

The cumulative unrealized gain/loss equals the foreign currency (notional) amount to be received (paid) times the net of the current spot rate minus the spot rate at the time the contract was opened;

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(e) Recognition of unrealized gains/losses and amortization of foreign exchange premium/discount on derivatives hedging forecasted transactions or firm commitments shall be deferred until the hedged transaction occurs. These deferred gains/losses will adjust the basis or proceeds of the hedged transaction when it occurs;

(f) For hedges where the cost of the foreign currency contract is combined with the hedged item, the statement value on Schedule DB is zero. The fair value of the derivative and hedged item shall be determined and reported separately, either individually or in the aggregate;

(g) ~~If during the life of the currency contract it or a designated portion of the currency contract is not effective as a hedge,~~ The derivative shall be recorded at fair value and ~~valuation at amortized cost shall cease. To the extent it ceased to be an effective hedge,~~ a cumulative unrealized gain/loss (surplus adjustment) ~~will~~ shall be recognized equal to the difference between the carrying value of the derivative on the balance sheet and the fair value of the derivative if either of the following occur:

1. During the life of the currency contract it or a designated portion of the currency contract is not effective as a hedge.

2. The entity decides to terminate the derivative in advance of scheduled maturity.

~~notional amount or designated notional amount times the difference between the forward rate available for the remaining maturity of the contract (i.e., the forward rate as of the balance sheet date) and the forward rate at the time it ceased to be an effective hedge.~~

iv. Open derivatives hedging items recorded at fair value, where gains and losses on the hedged item are recognized currently in earnings: swaps, collars and forwards shall be valued at current fair value with changes in fair value recognized currently in earnings together with the gains and losses on the hedged item.

(a) If during the life of the derivative it or a designated portion of the derivative is no longer effective as a hedge, recognition of changes in fair value through earnings ceases. The derivative shall continue to be valued at its current fair value, but thereafter gains or losses shall be recognized in unrealized gains or unrealized losses to the extent it ceased to be an effective hedge.

c. Cash Flows and Income:

i. Where the cost of the derivative is not combined with the hedged item:

(a) Amortization of premium paid or received on derivatives is an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of the hedged item;

(b) Periodic cash flows and accruals of income/expense are to be reported in a manner consistent with the hedged item, usually as net investment income or another appropriate caption within operating income.

ii. Where the cost of the derivative is combined with the hedged item, the cash flows and income of the derivative on Schedule DB is zero. All related amortization and cash flow accounting shall be reported with the hedged item instead of with the derivative.

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d. Gain/Loss on Termination of a swap, collar or forward accounted for under hedge accounting (includes closing, exercise, maturity, and expiry):

i. Exercise—The remaining book value of the derivative shall become an adjustment to the cost or proceeds of the hedged item(s) received or disposed of individually or in aggregate;

ii. Sale, maturity, expiry, or other closing transaction of a derivative which is an effective hedge—Any gain or loss on the transaction, except for excluded components, will adjust the basis (or proceeds) of the hedged item(s) individually or in aggregate. Alternatively, if the item being hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination.;

iii. Gain/loss on termination of derivatives will be recognized currently in net income (realized gain/loss) to the extent they ceased to be effective hedges.

iv. Upon the redesignation of a derivative from a currently effective hedging relationship-

(a) with an item(s) carried at amortized cost to another effective hedging relationship with an item(s) carried at amortized cost, the derivative shall continue to be recorded at amortized cost and no gain or loss on the derivative shall be recognized.

(b) with an item(s) carried at amortized cost or fair value to an effective relationship with an item(s) carried at fair value, the accounting for the derivative shall be consistent with (ii) above.

(c) with an item(s) carried at fair value to an effective relationship with an item(s) carried at amortized cost, the accounting for the derivative shall be consistent with (ii) above.

The following new Exhibit A replaces both Exhibit A and Exhibit B within the existing SSAP No. 86. This is new guidance within SSAP No. 86, and the tracked changes shown in the section below reflect the modifications from U.S. GAAP. References to the FASB ASC are included in this issue paper for historical reference and will not be duplicated within the SSAP.

EXHIBIT A – DISCUSSION OF HEDGE EFFECTIVENESS

The guidance within this exhibit reflects the adoption, with modification, of *FASB Accounting Standards Codification (ASC) 815-20-25-72 through 815-20-35-20*, as revised through the issuance of *ASU 2017-12: Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities* (ASU 2017-12) (issued on August 28, 2017). This adoption captures the U.S. GAAP guidance for the assessment and determination of hedge effectiveness, with modification to require the accounting and reporting of hedging instruments, including excluded components of hedging instruments to follow specific statutory accounting guidance in SSAP No. 86. The intent of this guidance is to clarify that the determination of whether a hedging instrument and derivative transaction qualifies as an effective hedge shall converge with U.S. GAAP, but that the measurement and reporting of effective hedge transactions shall follow statutory specific provisions. The adoption only extends to revisions incorporated to the FASB ASC through ASU 2017-12, therefore any subsequent U.S. GAAP edits to the ASC would require statutory accounting adoption before application. The guidance within this Exhibit reflects excerpts from the U.S. GAAP ASC, but do not reflect the full U.S. GAAP guidance referenced in the adopted language. The exclusion of cited guidance is to manage the extent of detail included within SSAP No. 86. Excerpts not duplicated within from the cited U.S. GAAP guidance are considered adopted unless subject to the specific accounting and reporting statutory exclusion. This Exhibit intends to supplement the guidance in SSAP No. 86 on hedge

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effectiveness. In any event in which this Exhibit could be interpreted as conflicting with the SSAP No. 86 guidance, the guidance in the body of SSAP No. 86 shall be followed.

Hedge Effectiveness Criteria Applicable to Both Fair Value Hedges and Cash Flow Hedges

1. This guidance addresses hedge effectiveness criteria applicable to both fair value hedges and cash flow hedges. *(815-20-25-74)*

2. To qualify for hedge accounting, the hedging relationship, both at inception of the hedge and on an ongoing basis, shall be expected to be highly effective in achieving either of the following: *(815-20-25-75)*

   a. Offsetting changes in fair value attributable to the hedged risk during the period that the hedge is designated (if a fair value hedge)

   b. Offsetting cash flows attributable to the hedged risk during the term of the hedge (if a cash flow hedge), unless the hedging instrument is used to modify the contractually specified interest receipts or payments associated with a recognized financial asset liability from one variable rate to another variable rate. ~~except as indicated in paragraph 815-20-25-50~~

3. If the hedging instrument (such as an at-the-money option contract) provides only one-sided offset of the hedged risk, either of the following conditions shall be met: *(815-20-25-76)*

   a. The increases (or decreases) in the fair value of the hedging instrument are expected to be highly effective in offsetting the decreases (or increases) in the fair value of the hedged item (if a fair value hedge).

   b. The cash inflows (outflows) from the hedging instrument are expected to be highly effective in offsetting the corresponding change in the cash outflows or inflows of the hedged transaction (if a cash flow hedge).

4. There would be a mismatch between the change in fair value or cash flows of the hedging instrument and the change in fair value or cash flows of the hedged item or hedged transaction in any of the following circumstances, among others: *(815-20-25-77)*

   a. A difference between the basis of the hedging instrument and the hedged item or hedged transaction, to the extent that those bases do not move in tandem

   b. Differences in critical terms of the hedging instrument and hedged item or hedged transaction, such as differences in any of the following:

      i. Notional amounts

      ii. Maturities

      iii. Quantity

      iv. Location (not applicable for hedging relationships in which the variability in cash flows attributable to changes in a contractually specified component is designated as the hedged risk)

      v. Delivery Dates

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5. An entity shall consider hedge effectiveness in two different ways—in prospective considerations and in retrospective evaluations: *(815-20-25-79)*

a. Prospective considerations. The entity's expectation that the relationship will be highly effective over future periods in achieving offsetting changes in fair value or cash flows, which is forward looking, must be assessed on a quantitative basis at hedge inception unless one of the exceptions detailed in ASU 2017-12, paragraph 815-20-25-3(b)(2)(iv)(01)[2] is met. Prospective assessments shall be subsequently performed whenever financial statements or earnings are reported and at least every three months. The entity shall elect at hedge inception ~~in accordance with paragraph 815-20-25-3(b)(2)(iv)(03)~~ whether to perform subsequent retrospective and prospective hedge effectiveness assessments on a quantitative or qualitative basis. ~~See paragraphs 815-20-35-2A through 35-2F for additional guidance on qualitative assessments of hedge effectiveness.~~ A quantitative assessment can be based on regression or other statistical analysis of past changes in fair values or cash flows as well as on other relevant information. The quantitative prospective assessment of hedge effectiveness shall consider all reasonably possible changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument and the hedged items for the period used to assess whether the requirement for expectation of highly effective offset is satisfied. The quantitative prospective assessment may not be limited only to the likely or expected changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument or the hedged items. Generally, the process of formulating an expectation regarding the effectiveness of a proposed hedging relationship involves a probability-weighted analysis of the possible changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument and the hedged items for the hedge period. Therefore, a probable future change in fair value will be more heavily weighted than a reasonably possible future change. ~~That calculation technique is consistent with the definition of the term **expected cash flow** in FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements*.~~

b. Retrospective evaluations. An assessment of effectiveness may be performed on a quantitative or qualitative basis on the basis of the entity's election at hedge inception ~~in accordance with paragraph 815-20-25-3(b)(2)(iv)(03)~~. That assessment shall be performed whenever financial statements or earnings are reported, and at least every three months. ~~See paragraphs 815-20-35-2 through 35-4 for further guidance.~~ At inception of the hedge, an entity electing a dollar-offset approach to perform retrospective evaluations on a quantitative basis may choose either a period-by-period approach or a cumulative approach in designating how effectiveness of a fair value hedge or of a cash flow hedge will be assessed retrospectively under that approach, depending on the nature of the hedge initially documented ~~in accordance with paragraph 815-20-25-3~~. ~~For example, an entity may decide that the cumulative approach is generally preferred, yet may wish to use the period-by-period approach in certain circumstances. See paragraphs 815-20-35-5 through 35-6 for further guidance.~~

(ASC paragraph 815-20-25-79A not included in Exhibit A.)

6. All assessments of effectiveness shall be consistent with the originally documented risk management strategy for that particular hedging relationship. An entity shall use the quantitative effectiveness assessment method defined at hedge inception consistently for the periods that the entity either elects or is required to assess hedge effectiveness on a quantitative basis. *(815-20-25-80)*

[2] Reference to this ASU 2017-12 guidance is consistent with the guidance in SSAP No. 86, paragraph 42, footnote 5.

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7. This ~~Subtopic~~ guidance does not specify a single method for assessing whether a hedge is expected to be highly effective. The method of assessing effectiveness shall be reasonable. The appropriateness of a given method of assessing hedge effectiveness depends on the nature of the risk being hedged and the type of hedging instrument used. Ordinarily, an entity shall assess effectiveness for similar hedges in a similar manner, including whether a component of the gain or loss on a derivative instrument is excluded in assessing effectiveness for similar hedges. Use of different methods for similar hedges shall be justified. The mechanics of isolating the change in time value of an option discussed beginning in paragraph 13 ~~815-20-25-98~~ also shall be applied consistently. *(815-20-25-81)*

8. In defining how hedge effectiveness will be assessed, an entity shall specify whether it will include in that assessment all of the gain or loss on a hedging instrument. An entity may exclude all or a part of the hedging instrument's time value from the assessment of hedge effectiveness, as follows: *(815-20-25-82)*

a. If the effectiveness of a hedge with an option is assessed based on changes in the option's intrinsic value, the change in the time value of the option would be excluded from the assessment of hedge effectiveness.

b. If the effectiveness of a hedge with an option is assessed based on changes in the option's minimum value, that is, its intrinsic value plus the effect of discounting, the change in the volatility value of the contract shall be excluded from the assessment of hedge effectiveness.

c. An entity may exclude any of the following components of the change in an option's time value from the assessment of hedge effectiveness:

   i. The portion of the change in time value attributable to the passage of time (theta)

   ii. The portion of the change in time value attributable to changes due to volatility (vega)

   iii. The portion of the change in time value attributable to changes due to interest rates (rho).

d. If the effectiveness of a hedge with a forward contract or futures contract is assessed based on changes in fair value attributable to changes in spot prices, the change in the fair value of the contract related to the changes in the difference between the spot price and the forward or futures price shall be excluded from the assessment of hedge effectiveness.

e. An entity may exclude the portion of the change in fair value of a currency swap attributable to a cross-currency basis spread.

9. No other components of a gain or loss on the designated hedging instrument shall be excluded from the assessment of hedge effectiveness nor shall an entity exclude any aspect of a change in an option's value from the assessment of hedge effectiveness that is not one of the permissible components of the change in an option's time value. For example, an entity shall not exclude from the assessment of hedge effectiveness the portion of the change in time value attributable to changes in other market variables (that is, other than rho and vega). *(815-20-25-83)*

Note – The following ASC Paragraphs 815-20-25-83A and 83B are not adopted within SSAP No. 86 as they address measurement and recognition. Measurement and recognition guidance shall follow the provisions detailed in SSAP No. 86.

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For fair value and cash flow hedges, the initial value of the component excluded from the assessment of effectiveness shall be recognized in earnings using a systematic and rational method over the life of the hedging instrument. Any difference between the change in fair value of the excluded component and amounts recognized in earnings under that systematic and rational method shall be recognized in other comprehensive income. Example 31 beginning in paragraph 815-20-55-235 illustrates this approach for a cash flow hedge in which the hedging instrument is an option and the entire time value is excluded from the assessment of effectiveness. *(815-20-25-83A)*

For fair value and cash flow hedges, an entity alternatively may elect to record changes in the fair value of the excluded component currently in earnings. This election shall be applied consistently to similar hedges in accordance with paragraph 815-20-25-81 and shall be disclosed in accordance with paragraph 815-10-50-4EEEE. *(815-20-25-83B)*

10. If the critical terms of the hedging instrument and of the hedged item or hedged forecasted transaction are the same, the entity could conclude that changes in fair value or cash flows attributable to the risk being hedged are expected to completely offset at inception and on an ongoing basis. For example, an entity may assume that a hedge of a forecasted purchase of a commodity with a forward contract will be perfectly effective if all of the following criteria are met:

a. The forward contract is for purchase of the same quantity of the same commodity at the same time and location as the hedged forecasted purchase. Location differences do not need to be considered if an entity designates the variability in cash flows attributable to changes in a contractually specified component as the hedged risk and the requirements in paragraphs 815-20-25-22A through 25-22B of the FASB Codification are met. *(815-20-25-84)*

b. The fair value of the forward contract at inception is zero.

c. Either of the following criteria is met:

i. The change in the discount or premium on the forward contract is excluded from the assessment of effectiveness pursuant to paragraphs 7-9~~815-20-25-81 through 25-83~~.

ii. The change in expected cash flows on the forecasted transaction is based on the forward price for the commodity.

11. In a cash flow hedge of a group of forecasted transactions in accordance with paragraph 28.a. of the SSAP guidance~~815-20-25-15(a)(2)~~, an entity may assume that the timing in which the hedged transactions are expected to occur and the maturity date of the hedging instrument match in accordance with paragraph 10.a. ~~815-20-25-84(a)~~ if those forecasted transactions occur and the derivative matures within the same 31-day period or fiscal month. *(815-20-25-84A)*

12. If all of the criteria in paragraphs 10-11 ~~815-20-25-84 through 25-84A~~ are met, an entity shall still perform and document an assessment of hedge effectiveness at the inception of the hedging relationship and~~, as discussed beginning in paragraph 815-20-35-9~~, on an ongoing basis throughout the hedge period. No quantitative effectiveness assessment is required at hedge inception if the criteria in paragraphs 10-11 ~~815-20-25-84 through 25-84A~~ are met ~~(see paragraph 815-20-25-3(b)(2)(iv)(01))~~. *(815-20-25-85)*

(ASC paragraphs 815-20-25-86 to 815-20-25-97 not included in Exhibit A.)

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Computing Changes in an Option's Time Value

13. In computing the changes in an option's time value that would be excluded from the assessment of hedge effectiveness, an entity shall use a technique that appropriately isolates those aspects of the change in time value. Generally, to allocate the total change in an option's time value to its different aspects—the passage of time and the market variables—the change in time value attributable to the first aspect to be isolated is determined by holding all other aspects constant as of the beginning of the period. Each remaining aspect of the change in time value is then determined in turn in a specified order based on the ending values of the previously isolated aspects. *(815-20-25-98)*

14. Based on that general methodology, if only one aspect of the change in time value is excluded from the assessment of hedge effectiveness (for example, theta), that aspect shall be the first aspect for which the change in time value is computed and would be determined by holding all other parameters constant for the period used for assessing hedge effectiveness. However, if more than one aspect of the change in time value is excluded from the assessment of hedge effectiveness (for example, theta and vega), an entity shall determine the amount of that change in time value by isolating each of those two aspects in turn in a prespecified order (one first, the other second). The second aspect to be isolated would be based on the ending value of the first isolated aspect and the beginning values of the remaining aspects. The portion of the change in time value that is included in the assessment of effectiveness shall be determined by deducting from the total change in time value the portion of the change in time value attributable to excluded components. (815-20-25-99)

(ASC paragraphs 815-20-25-100 and 815-20-25-101not included in Exhibit A.)

Assuming Perfect Hedge Effectiveness in a Hedge with an Interest Rate Swap

15. The conditions for the shortcut method do not determine which hedging relationships qualify for hedge accounting; rather, those conditions determine which hedging relationships qualify for a shortcut version of hedge accounting that assumes perfect hedge effectiveness. If all of the applicable conditions in the list in paragraph 17 ~~815-20-25-104~~ are met, an entity may assume perfect effectiveness in a hedging relationship of interest rate risk involving a recognized interest-bearing asset or liability (or a firm commitment arising on the trade [pricing] date to purchase or issue an interest-bearing asset or liability) and an interest rate swap (or a compound hedging instrument composed of an interest rate swap and a mirror-image call or put option as discussed in paragraph 17.e. ~~815-20-25-104[e])~~ provided that, in the case of a firm commitment, the trade date of the asset or liability differs from its settlement date due to generally established conventions in the marketplace in which the transaction is executed. The shortcut method's application shall be limited to hedging relationships that meet each and every applicable condition. That is, all the conditions applicable to fair value hedges shall be met to apply the shortcut method to a fair value hedge, and all the conditions applicable to cash flow hedges shall be met to apply the shortcut method to a cash flow hedge. A hedging relationship cannot qualify for application of the shortcut method based on an assumption of perfect effectiveness justified by applying other criteria. The verb *match* is used in the specified conditions in the list to mean *exactly the same* or *correspond exactly*. *(815-20-25-102)*

16. Implicit in the conditions for the shortcut method is the requirement that a basis exist for concluding on an ongoing basis that the hedging relationship is expected to be highly effective in achieving offsetting changes in fair values or cash flows. In applying the shortcut method, an entity shall consider the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative that require the counterparty to make payments to the entity. *(815-20-25-103)*

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17. All of the following conditions apply to both fair value hedges and cash flow hedges: *(815-20-25-104)*

a. The notional amount of the interest rate swap matches the principal amount of the interest-bearing asset or liability being hedged.

b. If the hedging instrument is solely an interest rate swap, the fair value of that interest rate swap at the inception of the hedging relationship must be zero, with one exception. The fair value of the swap may be other than zero at the inception of the hedging relationship only if the swap was entered into at the relationship's inception, the transaction price of the swap was zero in the entity's principal market (or most advantageous market), and the difference between transaction price and fair value is attributable solely to differing prices within the bid-ask spread between the entry transaction and a hypothetical exit transaction. The guidance in the preceding sentence is applicable only to transactions considered *at market* (that is, transaction price is zero exclusive of commissions and other transaction costs, ~~as discussed in paragraph~~ 820-10-35-9B~~)~~. If the hedging instrument is solely an interest rate swap that at the inception of the hedging relationship has a positive or negative fair value, but does not meet the one exception specified in this paragraph, the shortcut method shall not be used even if all the other conditions are met.

c. If the hedging instrument is a compound derivative composed of an interest rate swap and mirror-image call or put option as discussed in (e), the premium for the mirror-image call or put option shall be paid or received in the same manner as the premium on the call or put option embedded in the hedged item based on the following:

i. If the implicit premium for the call or put option embedded in the hedged item is being paid principally over the life of the hedged item (through an adjustment of the interest rate), the fair value of the hedging instrument at the inception of the hedging relationship shall be zero (except as discussed previously in (b) regarding differing prices due to the existence of a bid-ask spread).

ii. If the implicit premium for the call or put option embedded in the hedged item was principally paid at inception-acquisition (through an original issue discount or premium), the fair value of the hedging instrument at the inception of the hedging relationship shall be equal to the fair value of the mirror-image call or put option.

d. The formula for computing net settlements under the interest rate swap is the same for each net settlement. That is, both of the following conditions are met:

i. The fixed rate is the same throughout the term.

ii. The variable rate is based on the same index and includes the same constant adjustment or no adjustment. The existence of a stub period and stub rate is not a violation of the criterion in (d) that would preclude application of the shortcut method if the stub rate is the variable rate that corresponds to the length of the stub period.

e. The interest-bearing asset or liability is not prepayable, that is, able to be settled by either party before its scheduled maturity, or the assumed maturity date if the hedged item is measured as a partial-term hedge of interest rate risk in which the assumed maturity of the hedged items occur on the date in which the last hedged cash flow is due and payable, ~~in accordance with paragraph~~ 815-25-35-13B, with the following qualifications:

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i. This criterion does not apply to an interest-bearing asset or liability that is prepayable solely due to an embedded call option (put option) if the hedging instrument is a compound derivative composed of an interest rate swap and a mirror-image call option (put option).

ii. The call option embedded in the interest rate swap is considered a mirror image of the call option embedded in the hedged item if all of the following conditions are met:

(a) The terms of the two call options match exactly, including all of the following:

(1) Maturities

(2) Strike price (that is, the actual amount for which the debt instrument could be called) and there is no termination payment equal to the deferred debt issuance costs that remain unamortized on the date the debt is called

(3) Related notional amounts

(4) Timing and frequency of payments

(5) Dates on which the instruments may be called.

(b) The entity is the writer of one call option and the holder (purchaser) of the other call option.

f. Any other terms in the interest-bearing financial instruments or interest rate swaps meet both of the following conditions:

i. The terms are typical of those instruments.

ii. The terms do not invalidate the assumption of perfect effectiveness.

18. All of the following incremental conditions apply to fair value hedges only: *(815-20-25-105)*

a. The expiration date of the interest rate swap matches the maturity date of the interest-bearing asset or liability or the assumed maturity date if the hedged item is measured as a partial-term hedge of interest rate risk in which the assumed maturity of the hedged items occur on the date in which the last hedged cash flow is due and payable~~in accordance with paragraph 815-25-35-13B~~.

b. There is no floor or cap on the variable interest rate of the interest rate swap.

c. The interval between repricings of the variable interest rate in the interest rate swap is frequent enough to justify an assumption that the variable payment or receipt is at a market rate (generally three to six months or less).

d. For fair value hedges of a proportion of the principal amount of the interest-bearing asset or liability, the notional amount of the interest rate swap designated as the hedging

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instrument ~~(see (a) in paragraph 815-20-25-104)~~ matches the portion of the asset or liability being hedged.

e. For fair value hedges of portfolios (or proportions thereof) of similar interest-bearing assets or liabilities, both of the following criteria are met:

i. The notional amount of the interest rate swap designated as the hedging instrument matches the aggregate notional amount of the hedged item (whether it is all or a proportion of the total portfolio).

ii. The remaining criteria for the shortcut method are met with respect to the interest rate swap and the individual assets or liabilities in the portfolio.

f. The index on which the variable leg of the interest rate swap is based matches the benchmark interest rate designated as the interest rate risk being hedged for that hedging relationship.

19. All of the following incremental conditions apply to cash flow hedges only: (815-20-25-106)

a. All interest receipts or payments on the variable-rate asset or liability during the term of the interest rate swap are designated as hedged.

b. No interest payments beyond the term of the interest rate swap are designated as hedged.

c. Either of the following conditions is met:

i. There is no floor or cap on the variable interest rate of the interest rate swap.

ii. The variable-rate asset or liability has a floor or cap and the interest rate swap has a floor or cap on the variable interest rate that is comparable to the floor or cap on the variable-rate asset or liability. For purposes of this paragraph, comparable does not necessarily mean equal. For example, if an interest rate swap's variable rate is based on LIBOR and an asset's variable rate is LIBOR plus 2 percent, a 10 percent cap on the interest rate swap would be comparable to a 12 percent cap on the asset.

d. The repricing dates of the variable-rate asset or liability and the hedging instrument must occur on the same dates and be calculated the same way (that is, both shall be either prospective or retrospective). If the repricing dates of the hedged item occur on the same dates as the repricing dates of the hedging instrument but the repricing calculation for the hedged item is prospective whereas the repricing calculation for the hedging instrument is retrospective, those repricing dates do not match.

e. For cash flow hedges of the interest payments on only a portion of the principal amount of the interest-bearing asset or liability, the notional amount of the interest rate swap designated as the hedging instrument ~~(see paragraph 815-20-25-104(a))~~ matches the principal amount of the portion of the asset or liability on which the hedged interest payments are based.

f. For a cash flow hedge in which the hedged forecasted transaction is a group of individual transactions (as permitted by paragraph 28.a. of the SSAP guidance ~~paragraph 815-20-25-15(a)~~), if both of the following criteria are met:

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i. The notional amount of the interest rate swap designated as the hedging instrument ~~(see paragraph (a))~~ matches the notional amount of the aggregate group of hedged transactions.

ii. The remaining criteria for the shortcut method are met with respect to the interest rate swap and the individual transactions that make up the group. For example, the interest rate repricing dates for the variable-rate assets or liabilities whose interest payments are included in the group of forecasted transactions shall match (that is, be exactly the same as) the reset dates for the interest rate swap.

g. The index on which the variable leg of the interest rate swap is based matches the contractually specified interest rate designated as the interest rate being hedged for that hedging relationship.

20. The shortcut method may be applied to a hedging relationship that involves the use of an interest rate swap-in-arrears provided all of the applicable conditions are met. (815-20-25-107)

21. Any discount or premium in the hedged debt's carrying amount (including any related deferred issuance costs) is irrelevant to and has no direct impact on the determination of whether an interest rate swap contains a mirror-image call option under paragraph 17.e.i.~~(e)~~. Typically, the call price is greater than the par or face amount of the debt instrument. The carrying amount of the debt is economically unrelated to the amount the issuer would be required to pay to exercise the call embedded in the debt. (815-20-25-108)

22. The fixed interest rate on a hedged item need not exactly match the fixed interest rate on an interest rate swap designated as a fair value hedge. Nor does the variable interest rate on an interest-bearing asset or liability need to be the same as the variable interest rate on an interest rate swap designated as a cash flow hedge. An interest rate swap's fair value comes from its net settlements. The fixed and variable interest rates on an interest rate swap can be changed without affecting the net settlement if both are changed by the same amount. That is, an interest rate swap with a payment based on LIBOR and a receipt based on a fixed rate of 5 percent has the same net settlements and fair value as an interest rate swap with a payment based on LIBOR plus 1 percent and a receipt based on a fixed rate of 6 percent. (815-20-25-109)

23. Comparable credit risk at inception is not a condition for assuming perfect effectiveness even though actually achieving perfect offset would require that the same discount rate be used to determine the fair value of the swap and of the hedged item or hedged transaction. To justify using the same discount rate, the credit risk related to both parties to the swap as well as to the debtor on the hedged interest-bearing asset (in a fair value hedge) or the variable-rate asset on which the interest payments are hedged (in a cash flow hedge) would have to be the same. However, because that complication is caused by the interaction of interest rate risk and credit risk, which are not easily separable, comparable creditworthiness is not considered a necessary condition for assuming perfect effectiveness in a hedge of interest rate risk. (815-20-25-111)

(ASC paragraphs 815-20-25-112 through 815-20-25-143 not included in Exhibit A.)

Hedge Effectiveness – After Designation

24. If a fair value hedge or cash flow hedge initially qualifies for hedge accounting, the entity would continue to assess whether the hedge meets the effectiveness test on either a quantitative basis (using either a dollar-offset test or a statistical method such as regression analysis) or a qualitative basis. ~~See paragraphs 815-20-35-2A through 35-2F for additional guidance on qualitative assessments of effectiveness~~. If the hedge fails the effectiveness test at any time (that is, if the entity does not expect the

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hedge to be highly effective at achieving offsetting changes in fair values or cash flows), the hedge ceases to qualify for hedge accounting. At least quarterly, the hedging entity shall determine whether the hedging relationship has been highly effective in having achieved offsetting changes in fair value or cash flows through the date of the periodic assessment.) (815-20-35-2)

Effectiveness Assessment on a Qualitative Basis

25. An entity may qualitatively assess hedge effectiveness if both of the following criteria are met: (815-20-35-2A)

a. An entity performs an initial quantitative test of hedge effectiveness on a prospective basis (that is, it is not assuming that the hedging relationship is perfectly effective at hedge inception ~~as described in paragraph 815-20-25-3(b)(2)(iv)(01)(A) through (H)~~), and the results of that quantitative test demonstrate highly effective offset.

b. At hedge inception, an entity can reasonably support an expectation of high effectiveness on a qualitative basis in subsequent periods.

26. An entity may elect to qualitatively assess hedge effectiveness in accordance with paragraph 25 ~~815-20-35-2A~~ on a hedge-by-hedge basis. If an entity makes this qualitative assessment election, only the quantitative method specified in an entity's initial hedge documentation must comply with paragraph 7~~815-20-25-81~~. (815-20-35-2B)

27. When an entity performs qualitative assessments of hedge effectiveness, it shall verify and document whenever financial statements or earnings are reported and at least every three months that the facts and circumstances related to the hedging relationship have not changed such that it can assert qualitatively that the hedging relationship was and continues to be highly effective. While not all-inclusive, the following is a list of indicators that may, individually or in the aggregate, allow an entity to continue to assert qualitatively that the hedging relationship is highly effective: (815-20-35-2C)

a. An assessment of the factors that enabled the entity to reasonably support an expectation of high effectiveness on a qualitative basis has not changed such that the entity can continue to assert qualitatively that the hedging relationship was and continues to be highly effective. ~~This shall include an assessment of the guidance in paragraph 815-20-25-100 when applicable.~~

b. There have been no adverse developments regarding the risk of counterparty default.

28. If an entity elects to assess hedge effectiveness on a qualitative basis and then facts and circumstances change such that the entity no longer can assert qualitatively that the hedging relationship was and continues to be highly effective in achieving offsetting changes in fair values or cash flows, the entity shall assess effectiveness of that hedging relationship on a quantitative basis in subsequent periods. In addition, an entity may perform a quantitative assessment of hedge effectiveness in any reporting period to validate whether qualitative assessments of hedge effectiveness remain appropriate. In both cases, the entity shall apply the quantitative method that it identified in its initial hedge documentation ~~in accordance with paragraph (b)(2)(iv)(03)~~. (815-20-35-2D)

29. When an entity determines that facts and circumstances have changed and it no longer can assert qualitatively that the hedging relationship was and continues to be highly effective, the entity shall begin performing subsequent quantitative assessments of hedge effectiveness as of the period that the facts and circumstances changed. If there is no identifiable event that led to the change in the facts and circumstances of the hedging relationship, the entity may begin performing quantitative assessments of effectiveness in the current period. (815-20-35-2E)

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30. After performing a quantitative assessment of hedge effectiveness for one or more reporting periods as discussed in paragraphs 28-29~~815-20-35-2D through 35-2E~~, an entity may revert to qualitative assessments of hedge effectiveness if it can reasonably support an expectation of high effectiveness on a qualitative basis for subsequent periods. ~~See paragraphs 815-20-55-79G through 55-79N for implementation guidance on factors to consider when determining whether qualitative assessments of effectiveness can be performed after hedge inception.~~ (815-20-35-2F)

Quantitative Hedge Effectiveness Assessments After Hedge Designation

31. Quantitative assessments can be based on regression or other statistical analysis of past changes in fair values or cash flows as well as on other relevant information. (815-20-35-2G)

32. If an entity elects at the inception of a hedging relationship to use the same regression analysis approach for both prospective considerations and retrospective evaluations of assessing effectiveness, then during the term of that hedging relationship both of the following conditions shall be met: (815-20-35-3)

a. Those regression analysis calculations shall generally incorporate the same number of data points.

b. That entity must periodically update its regression analysis (or other statistical analysis).

33. Electing to use a regression or other statistical analysis approach instead of a dollar-offset approach to perform retrospective evaluations of assessing hedge effectiveness may affect whether an entity can apply hedge accounting for the current assessment period. (815-20-35-4)

34. In periodically (that is, at least quarterly) assessing retrospectively the effectiveness of a fair value hedge (or a cash flow hedge) in having achieved offsetting changes in fair values (or cash flows) under a dollar-offset approach, an entity shall use either a period-by-period approach or a cumulative approach on individual fair value hedges (or cash flow hedges): (815-20-35-5)

a. Period-by-period approach. The period-by-period approach involves comparing the changes in the hedging instrument's fair values (or cash flows) that have occurred during the period being assessed to the changes in the hedged item's fair value (or hedged transaction's cash flows) attributable to the risk hedged that have occurred during the same period. If an entity elects to base its comparison of changes in fair value (or cash flows) on a period-by-period approach, the period cannot exceed three months. Fair value (or cash flow) patterns of the hedging instrument or the hedged item (or hedged transaction) in periods before the period being assessed are not relevant.

b. Cumulative approach. The cumulative approach involves comparing the cumulative changes (to date from inception of the hedge) in the hedging instrument's fair values (or cash flows) to the cumulative changes in the hedged item's fair value (or hedged transaction's cash flows) attributable to the risk hedged.

35. If an entity elects at inception of a hedging relationship to base its comparison of changes in fair value (or cash flows) on a cumulative approach, then that entity must abide by the results of that methodology as long as that hedging relationship remains designated. Electing to utilize a period-by-period approach instead of a cumulative approach (or vice versa) to perform retrospective evaluations of assessing hedge effectiveness under the dollar-offset method may affect whether an entity can apply hedge accounting for the current assessment period. (815-20-35-6)

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Assessing Effectiveness Based on Whether the Critical Terms of the Hedging Instrument and the Hedged Items Match

36. If, at inception, the critical terms of the hedging instrument and the hedged forecasted transaction are the same (see paragraphs 10-11~~815-20-25-84 through 25-84A~~), the entity can conclude that changes in cash flows attributable to the risk being hedged are expected to be completely offset by the hedging derivative. Therefore, subsequent assessments can be performed by verifying and documenting whether the critical terms of the hedging instrument and the forecasted transaction have changed during the period in review. (815-20-35-9)

37. Because the assessment of hedge effectiveness in a cash flow hedge involves assessing the likelihood of the counterparty's compliance with the contractual terms of the derivative instrument designated as the hedging instrument, the entity must also assess whether there have been adverse developments regarding the risk of counterparty default, particularly if the entity planned to obtain its cash flows by liquidating the derivative instrument at its fair value. (815-20-35-10)

38. If there are no such changes in the critical terms or adverse developments regarding counterparty default, the entity may conclude that the hedging relationship is perfectly effective. In that case, the change in fair value of the derivative instrument can be viewed as a proxy for the present value of the change in cash flows attributable to the risk being hedged. (815-20-35-11)

39. However, the entity must assess whether the hedging relationship is expected to continue to be highly effective using a quantitative assessment method (either a dollar-offset test or a statistical method such as regression analysis) if any of the following conditions exist: (815-20-35-12)

a. The critical terms of the hedging instrument or the hedged forecasted transaction have changed.

b. There have been adverse developments regarding the risk of counterparty default.

Possibility of Default by the Counterparty to Hedging Derivative

40. For an entity to conclude on an ongoing basis that the hedging relationship is expected to be highly effective in achieving offsetting changes in cash flows, the entity shall not ignore whether it will collect the payments it would be owed under the contractual provisions of the derivative instrument. In complying with the requirements of paragraph 2.b.~~815-20-25-75(b)~~, the entity shall assess the possibility of whether the counterparty to the derivative instrument will default by failing to make any contractually required payments to the entity as scheduled in the derivative instrument. In making that assessment, the entity shall also consider the effect of any related collateralization or financial guarantees. The entity shall be aware of the counterparty's creditworthiness (and changes therein) in determining the fair value of the derivative instrument. Although a change in the counterparty's creditworthiness would not necessarily indicate that the counterparty would default on its obligations, such a change shall warrant further evaluation. (815-20-35-14)

41. If the likelihood that the counterparty will not default ceases to be probable, an entity would be unable to conclude that the hedging relationship in a cash flow hedge is expected to be highly effective in achieving offsetting cash flows. (815-20-35-15)

42. In contrast, a change in the creditworthiness of the derivative instrument's counterparty in a fair value hedge would have an immediate effect because that change in creditworthiness would affect the change in the derivative instrument's fair value, which would immediately affect both of the following: (815-20-35-16)

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a. The assessment of whether the relationship qualifies for hedge accounting

b. The amount of mismatch between the change in the fair value of the hedging instrument and the hedged item attributable to the hedged risk recognized in earnings under fair value hedge accounting.

43. Paragraph 16~~815-20-25-103~~ states that, in applying the shortcut method, an entity shall consider the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative that require the counterparty to make payments to the entity. That paragraph explains that implicit in the criteria for the shortcut method is the requirement that a basis exist for concluding on an ongoing basis that the hedging relationship is expected to be highly effective in achieving offsetting changes in fair values or cash flows. (815-20-35-18)

Change in Hedge Effectiveness Method When Hedge Effectiveness if Assessed on a Quantitative Basis

44. If the entity identifies an improved method of assessing hedge effectiveness in accordance with the guidance in paragraph 6~~815-20-25-80~~ and wants to apply that method prospectively, it shall do both of the following: (815-20-35-19)

a. Discontinue the existing hedging relationship

b. Designate the relationship anew using the improved method.

45. The new method of assessing hedge effectiveness shall be applied prospectively and shall also be applied to similar hedges unless the use of a different method for similar hedges is justified. A change in the method of assessing hedge effectiveness by an entity shall not be considered a change in accounting principle as defined in ~~Topic 250~~SSAP No. 3—Accounting Changes and Corrections of Errors. (815-20-35-20)

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U.S. GAAP ASC Excerpts Excluded from Exhibit A

This information is included to illustrate the guidance within the adopted ASC references that are not captured in Exhibit A. The guidance within these paragraphs is considered part of the statutory adoption unless they include specific accounting and reporting guidance.

815-20-25-79A See paragraphs 815-20-25-139 through 25-142 about the timing of hedge effectiveness assessments required by paragraph 815-20-25-79 for a private company that is not a financial institution or a not-for-profit entity (except for a not-for-profit entity that has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market).

815-20-25-86 The remainder of this guidance on hedge effectiveness criteria applicable to both fair value hedges and cash flow hedges is organized as follows:

a. Hedge effectiveness when the hedging instrument is an option or combination of options

b. Hedge effectiveness when hedged exposure is more limited than hedging instrument

c. Hedge effectiveness during designated hedge period

d. Assuming perfect effectiveness in a hedge with an interest rate swap (the shortcut method).

Hedge Effectiveness When the Hedging Instrument Is an Option or Combination of Options

815-20-25-87 The hedge effectiveness criteria applicable to options and combinations of options are organized as follows:

a. Determining whether a combination of options is net written

b. Hedge effectiveness of written options

c. Hedge effectiveness of options in general.

Determining Whether a Combination of Options Is Net Written

815-20-25-88 This guidance addresses how an entity shall determine whether a combination of options is considered a net written option subject to the requirements of paragraph 815-20-25-94. A combination of options (for example, an interest rate collar) entered into contemporaneously shall be considered a written option if either at inception or over the life of the contracts a net premium is received in cash or as a favorable rate or other term. Furthermore, a derivative instrument that results from combining a written option and any other non-option derivative instrument shall be considered a written option. The determination of whether a combination of options is considered a net written option depends in part on whether strike prices and notional amounts of the options remain constant.

Strike Prices and Notional Amounts Remain Constant

815-20-25-89 For a combination of options in which the strike price and the notional amount in both the written option component and the purchased option component remain constant over the life of the respective component, that combination of options would be considered a net purchased option or a zero cost collar (that is, the combination shall not be considered a net written option subject to the requirements of paragraph 815-20-25-94) provided all of the following conditions are met:

a. No net premium is received.

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b. The components of the combination of options are based on the same underlying.

c. The components of the combination of options have the same maturity date.

d. The notional amount of the written option component is not greater than the notional amount of the purchased option component.

815-20-25-90 If the combination of options does not meet all of those conditions, it shall be subject to the test in paragraph 815-20-25-94. For example, a combination of options having different underlying indexes, such as a collar containing a written floor based on three-month U.S. Treasury rates and a purchased cap based on three-month London Interbank Offered Rate (LIBOR), shall not be considered a net purchased option or a zero cost collar even though those rates may be highly correlated.

Strike Prices and Notional Amounts Do Not Remain Constant

815-20-25-91 If either the written option component or the purchased option component for a combination of options has either strike prices or notional amounts that do not remain constant over the life of the respective component, the assessment to determine whether that combination of options can be considered not to be a written option under paragraph 815-20-25-88 shall be evaluated with respect to each date that either the strike prices or the notional amounts change within the contractual term from inception to maturity.

815-20-25-92 Even though that assessment is made on the date that a combination of options is designated as a hedging instrument (to determine the applicability of paragraph 815-20-25-94), it shall consider the receipt of a net premium (in cash or as a favorable rate or other term) from that combination of options at each point in time that either the strike prices or the notional amounts change, such as either of the following circumstances:

a. If strike prices fluctuate over the life of a combination of options and no net premium is received at inception, a net premium will typically be received as a favorable term in one or more reporting periods within the contractual term from inception to maturity.

b. If notional amounts fluctuate over the life of a combination of options and no net premium is received at inception, a net premium or a favorable term will typically be received in one or more periods within the contractual term from inception to maturity.

815-20-25-93 In addition, a combination of options in which either the written option component or the purchased option component has either strike prices or notional amounts that do not remain constant over the life of the respective component shall satisfy all of the conditions in paragraph 815-20-25-89 to be considered not to be a written option (that is, to be considered to be a net purchased option or zero cost collar) under paragraph 815-20-25-88. For example, if the notional amount of the written option component is greater than the notional amount of the purchased option component at any date that the notional amount changes within the contractual term from inception to maturity, the combination of options shall be considered to be a written option under paragraph 815-20-25-88 and, thus, subject to the criteria in the following paragraph.

Hedge Effectiveness of Written Options

815-20-25-94 If a written option is designated as hedging a recognized asset or liability or an unrecognized firm commitment (if a fair value hedge) or the variability in cash flows for a recognized asset or liability or an unrecognized firm commitment (if a cash flow hedge), the combination of the hedged item and the written option provides either of the following:

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a. At least as much potential for gains as a result of a favorable change in the fair value of the combined instruments (that is, the written option and the hedged item, such as an embedded purchased option) as exposure to losses from an unfavorable change in their combined fair value (if a fair value hedge)

b. At least as much potential for favorable cash flows as exposure to unfavorable cash flows (if a cash flow hedge).

815-20-25-95 The written-option test in the preceding paragraph shall be applied only at inception of the hedging relationship and is met if all possible percentage favorable changes in the underlying (from zero percent to 100 percent) would provide either of the following:

a. At least as much gain as the loss that would be incurred from an unfavorable change in the underlying of the same percentage (if a fair value hedge)

b. At least as much favorable cash flows as the unfavorable cash flows that would be incurred from an unfavorable change in the underlying of the same percentage (if a cash flow hedge).

815-20-25-96 The time value of a written option (or net written option) may be excluded from the written-option test if, in defining how hedge effectiveness will be assessed, the entity specifies that it will base that assessment on only changes in the option's intrinsic value. In that circumstance, the change in the time value of the options would be excluded from the assessment of hedge effectiveness in accordance with paragraph 815-20-25-82(a).

815-20-25-97 When applying the written-option test to determine whether there is symmetry of the gain and loss potential of the combined hedged position for all possible percentage changes in the underlying, an entity is permitted to measure the change in the intrinsic value of the written option (or net written option) combined with the change in fair value of the hedged item.

Hedge Effectiveness When Hedged Exposure Is More Limited Than Hedging Instrument

815-20-25-100 An entity may designate as the hedging instrument in a fair value hedge or cash flow hedge a derivative instrument that does not have a limited exposure comparable to the limited exposure of the hedged item to the risk being hedged. However, to make that designation, in accordance with paragraph 815-20-25-75, the entity shall establish that the hedging relationship is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period that the hedge is designated. See paragraph 815-20-25-79(a) for additional guidance on prospective considerations of hedge effectiveness in this circumstance.

Hedge Effectiveness during Designated Hedge Period

815-20-25-101 It is inappropriate under this Subtopic for an entity to designate a derivative instrument as the hedging instrument if the entity expects that the derivative instrument will not be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period that the hedge is designated, unless the entity has documented undertaking a dynamic hedging strategy in which it has committed itself to an ongoing repositioning strategy for its hedging relationship.

Application of Prepayable Criterion

815-20-25-112 An interest-bearing asset or liability shall be considered prepayable under the provisions of paragraph 815-20-25-104(e) if one party to the contract has the right to cause the payment of principal before the scheduled payment dates unless either of the following conditions is met:

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a. The debtor has the right to cause settlement of the entire contract before its stated maturity at an amount that is always greater than the then fair value of the contract absent that right.

b. The creditor has the right to cause settlement of the entire contract before its stated maturity at an amount that is always less than the then fair value of the contract absent that right.

815-20-25-113 However, none of the following shall be considered a prepayment provision:

a. Any term, clause, or other provision in a debt instrument that gives the debtor or creditor the right to cause prepayment of the debt contingent upon the occurrence of a specific event related to the debtor's credit deterioration or other change in the debtor's credit risk, such as any of the following:

1. The debtor's failure to make timely payment, thus making it delinquent

2. The debtor's failure to meet specific covenant ratios

3. The debtor's disposition of specific significant assets (such as a factory)

4. A declaration of cross-default

5. A restructuring by the debtor.

b. Any term, clause, or other provision in a debt instrument that gives the debtor or creditor the right to cause prepayment of the debt contingent upon the occurrence of a specific event that meets all of the following conditions:

1. It is not probable at the time of debt issuance.

2. t is unrelated to changes in benchmark interest rates, contractually specified interest rates, or any other market variable.

3. It is related either to the debtor's or creditor's death or to regulatory actions, legislative actions, or other similar events that are beyond the control of the debtor or creditor.

c. Contingent acceleration clauses that permit the debtor to accelerate the maturity of an outstanding note only upon the occurrence of a specified event that meets all of the following conditions:

1. It is not probable at the time of debt issuance.

2. It is unrelated to changes in benchmark interest rates, contractually specified interest rates, or any other market variable.

3. It is related to regulatory actions, legislative actions, or other similar events that are beyond the control of the debtor or creditor.

815-20-25-114 Furthermore, a right to cause a contract to be prepaid at its then fair value would not cause the interest-bearing asset or liability to be considered prepayable because that right would have a fair value of zero at all times and essentially would provide only liquidity to the holder.

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815-20-25-115 Application of this guidance to specific debt instruments is illustrated in paragraph 815-20-55-75.

Application of the Shortcut Method to a Portfolio of Hedged Items

815-20-25-116 Portfolio hedging cannot be used to circumvent the application of the shortcut method criteria beginning in paragraph 815-20-25-102 to a fair value hedge of an individual interest-bearing asset or liability. A portfolio of interest-bearing assets or interest-bearing liabilities cannot qualify for the shortcut method if it contains an interest-bearing asset or liability that individually cannot qualify for the shortcut method.

815-20-25-117 The fair value hedge requirements of paragraph 815-20-25-12(b)(1) ensure that the individual items in a portfolio share the same risk exposure and have fair value changes attributable to the hedged risk that are expected to respond in a generally proportionate manner to the overall fair value changes of the entire portfolio. That requirement restricts the types of portfolios that can qualify for portfolio hedging; however, it also permits the existence of a mismatch between the change in the fair value of the individual hedged items and the change in the fair value of the hedged portfolio attributable to the hedged risk in portfolios that do qualify. As a result, the assumption of perfect effectiveness required for the shortcut method generally is inappropriate for portfolio hedges of similar assets or liabilities that are not also nearly identical (except for their notional amounts). Application of the shortcut method to portfolios that meet the requirements of paragraph 815-20-25-12(b)(1) is appropriate only if the assets or liabilities in the portfolio meet the same stringent criteria in paragraphs 815-20-25-104(e), 815-20-25-104(g), and 815-20-25-105(a) as required for hedges of individual assets and liabilities.

Application of Whether the Shortcut Method Was Not or No Longer Is Appropriate

815-20-25-117A In the period in which an entity determines that use of the shortcut method was not or no longer is appropriate, the entity may use a quantitative method to assess hedge effectiveness and measure hedge results without dedesignating the hedging relationship if both of the following criteria are met:

a. The entity documented at hedge inception in accordance with paragraph 815-20-25-3(b)(2)(iv)(04) which quantitative method it would use to assess hedge effectiveness and measure hedge results if the shortcut method was not or no longer is appropriate during the life of the hedging relationship.

b. The hedging relationship was highly effective on a prospective and retrospective basis in achieving offsetting changes in fair value or cash flows attributable to the hedged risk for the periods in which the shortcut method criteria were not met.

815-20-25-117B If the criterion in paragraph 815-20-25-117A(a) is not met, the hedging relationship shall be considered invalid in the period in which the criteria for the shortcut method were not met and in all subsequent periods. If the criterion in paragraph 815-20-25-117A(a) is met, the hedging relationship shall be considered invalid in all periods in which the criterion in paragraph 815-20-25-117A(b) is not met.

815-20-25-117C If an entity cannot identify the date on which the shortcut criteria ceased to be met, the entity shall perform the quantitative assessment of effectiveness documented at hedge inception for all periods since hedge inception.

815-20-25-117D The terms of the hedged item and hedging instrument used to assess effectiveness, in accordance with paragraph 815-20-25-117A(b), shall be those existing as of the date that the shortcut criteria ceased to be met. For cash flow hedges, if the hypothetical derivative method is used as a proxy for the hedged item, the value of the hypothetical derivative shall be set to zero as of hedge inception.

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Hedge Effectiveness Criterion Applicable to Fair Value Hedges Only—Effectiveness Horizon

815-20-25-118 In documenting its risk management strategy for a fair value hedge, an entity may specify an intent to consider the possible changes (that is, not limited to the likely or expected changes) in value of the hedging derivative instrument and the hedged item only over a shorter period than the derivative instrument's remaining life in formulating its expectation that the hedging relationship will be highly effective in achieving offsetting changes in fair value for the risk being hedged. The entity does not need to contemplate the offsetting effect for the entire term of the hedging instrument.

Consideration of Prepayment Risk Using the Last-of-Layer Method

815-20-25-118A In a fair value hedge of interest rate risk designated under the last-of-layer method in accordance with paragraph 815-20-25-12A, an entity may exclude prepayment risk when measuring the change in fair value of the hedged item attributable to interest rate risk.

Hedge Effectiveness Criteria Applicable to Cash Flow Hedges Only

815-20-25-119 The hedge effectiveness criteria applicable to cash flow hedges only are organized as follows:

a. Consideration of the time value of money

b. Consideration of counterparty credit risk

c. Additional considerations for options in cash flow hedges

d. Assuming perfect hedge effectiveness in a cash flow hedge of a variable-rate borrowing with a receive-variable, pay-fixed interest rate swap recorded under the simplified hedge accounting approach.

Consideration of the Time Value of Money

815-20-25-120 In assessing the effectiveness of a cash flow hedge, an entity generally shall consider the time value of money, especially if the hedging instrument involves periodic cash settlements.

815-20-25-121 An example of a situation in which an entity likely would reflect the time value of money is a tailing strategy with futures contracts. When using a tailing strategy, an entity adjusts the size or contract amount of futures contracts used in a hedge so that earnings (or expense) from reinvestment (or funding) of daily settlement gains (or losses) on the futures do not distort the results of the hedge. To assess offset of expected cash flows when a tailing strategy has been used, an entity could reflect the time value of money, perhaps by comparing the present value of the hedged forecasted cash flow with the results of the hedging instrument.

Consideration of Counterparty Credit Risk

815-20-25-122 For a cash flow hedge, an entity shall consider the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative instrument that require the counterparty to make payments to the entity. Paragraph 815-20-35-14 states that, for an entity to conclude on an ongoing basis that a cash flow hedging relationship is expected to be highly effective in achieving offsetting changes in cash flows, the entity shall not ignore whether it will collect the payments it would be owed under the contractual provisions of the derivative instrument. See paragraphs 815-20-35-14 through 35-18 for further guidance.

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Additional Considerations for Options in Cash Flow Hedges

815-20-25-123 When an entity has documented that the effectiveness of a cash flow hedge will be assessed based on changes in the hedging option's intrinsic value pursuant to paragraph 815-20-25-82(a), that assessment (and the related cash flow hedge accounting) shall be performed for all changes in intrinsic value—that is, for all periods of time when the option has an intrinsic value, such as when the underlying is above the strike price of the call option.

815-20-25-124 When a purchased option is designated as a hedging instrument in a cash flow hedge, an entity shall not define only limited parameters for the risk exposure designated as being hedged that would include the time value component of that option. An entity cannot arbitrarily exclude some portion of an option's intrinsic value from the hedge effectiveness assessment simply through an articulation of the risk exposure definition. It is inappropriate to assert that only limited risk exposures are being hedged (for example, exposures related only to currency-exchange-rate changes above $1.65 per pound sterling as illustrated in Example 26 [see paragraph 815-20-55-205]).

815-20-25-125 If an option is designated as the hedging instrument in a cash flow hedge, an entity may assess hedge effectiveness based on a measure of the difference, as of the end of the period used for assessing hedge effectiveness, between the strike price and forward price of the underlying, undiscounted. Although assessment of cash flow hedge effectiveness with respect to an option designated as the hedging instrument in a cash flow hedge shall be performed by comparing the changes in present value of the expected future cash flows of the forecasted transaction to the change in fair value of the derivative instrument (aside from any excluded component under paragraph 815-20-25-82), that measure of changes in the expected future cash flows of the forecasted transaction based on forward rates, undiscounted, is not prohibited. With respect to an option designated as the hedging instrument in a cash flow hedge, assessing hedge effectiveness based on a similar measure with respect to the hedging instrument eliminates any difference that the effect of discounting may have on the hedging instrument and the hedged transaction. Pursuant to paragraph 815-20-25-3(b)(2)(iv), entities shall document the measure of intrinsic value that will be used in the assessment of hedge effectiveness. As discussed in paragraph 815-20-25-80, that measure must be used consistently for each period following designation of the hedging relationship.

Assessing Hedge Effectiveness Based on an Option's Terminal Value

815-20-25-126 The guidance in paragraph 815-20-25-129 addresses a cash flow hedge that meets all of the following conditions:

a. The hedging instrument is a purchased option or a combination of only options that comprise either a net purchased option or a zero-cost collar.

b. The exposure being hedged is the variability in expected future cash flows attributed to a particular rate or price beyond (or within) a specified level (or levels).

c. The assessment of effectiveness is documented as being based on total changes in the option's cash flows (that is, the assessment will include the hedging instrument's entire change in fair value, not just changes in intrinsic value).

815-20-25-127 This guidance has no effect on the accounting for fair value hedging relationships. In addition, in determining the accounting for seemingly similar cash flow hedging relationships, it would be inappropriate to analogize to this guidance.

815-20-25-128 For a hedging relationship that meets all of the conditions in paragraph 815-20-25-126, an entity may focus on the hedging instrument's terminal value (that is, its expected future pay-off amount at its maturity date) in determining whether the hedging relationship is expected to be highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the hedge. An entity's

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focus on the hedging instrument's terminal value is not an impediment to the entity's subsequently deciding to dedesignate that cash flow hedge before the occurrence of the hedged transaction. If the hedging instrument is a purchased cap consisting of a series of purchased caplets that are each hedging an individual hedged transaction in a series of hedged transactions (such as caplets hedging a series of hedged interest payments at different monthly or quarterly dates), the entity may focus on the terminal value of each caplet (that is, the expected future pay-off amount at the maturity date of each caplet) in determining whether each of those hedging relationships is expected to be highly effective in achieving offsetting cash flows. The guidance in this paragraph applies to a purchased option regardless of whether at the inception of the cash flow hedging relationship it is at the money, in the money, or out of the money.

815-20-25-129 A hedging relationship that meets all of the conditions in paragraph 815-20-25-126 may be considered to be perfectly effective if all of the following conditions are met:

a. The critical terms of the hedging instrument (such as its notional amount, underlying, maturity date, and so forth) completely match the related terms of the hedged forecasted transaction (such as the notional amount, the variable that determines the variability in cash flows, the expected date of the hedged transaction, and so forth).

b. The strike price (or prices) of the hedging option (or combination of options) matches the specified level (or levels) beyond (or within) which the entity's exposure is being hedged.

c. The hedging instrument's inflows (outflows) at its maturity date completely offset the change in the hedged transaction's cash flows for the risk being hedged.

d. The hedging instrument can be exercised only on a single date—its contractual maturity date.

The condition in (d) is consistent with the entity's focus on the hedging instrument's terminal value. If the holder of the option chooses to pay for the ability to exercise the option at dates before the maturity date (for example, by acquiring an American-style option), the hedging relationship would not be perfectly effective.

815-20-25-129A In a hedge of a group of forecasted transactions in accordance with paragraph 815-20-25-15(a)(2), an entity may assume that the timing in which the hedged transactions are expected to occur and the maturity date of the hedging instrument match in accordance with paragraph 815-20-25-129(a) if those forecasted transactions occur and the derivative matures within the same 31-day period or fiscal month.

Hedge Effectiveness of a Net-Purchased Combination of Options

815-20-25-130 The guidance in the following paragraph addresses a cash flow hedging relationship that meets both of the following conditions:

a. A combination of options (deemed to be a net purchased option) is designated as the hedging instrument.

b. The effectiveness of the hedge is assessed based only on changes in intrinsic value of the hedging instrument (the combination of options).

815-20-25-131 The assessment of effectiveness of a cash flow hedging relationship meeting the conditions in the preceding paragraph may be based only on changes in the underlying that cause a change in the intrinsic value of the hedging instrument (the combination of options). Thus, the assessment can exclude ranges of changes in the underlying for which there is no change in the hedging instrument's intrinsic value.

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Hedge Accounting Provisions Applicable to Certain Private Companies

Assuming Perfect Hedge Effectiveness in a Cash Flow Hedge of a Variable-Rate Borrowing with a Receive-Variable, Pay-Fixed Interest Rate Swap Recorded under the Simplified Hedge Accounting Approach

815-20-25-133 Paragraphs 815-10-35-1A through 35-1C, 815-10-50-3, 815-20-25-3A, 815-20-25-119, 815-20-25-134 through 25-138, 815-20-55-79A through 55-79B, 825-10-50-3, and 825-10-50-8 provide guidance for an entity electing the simplified hedge accounting approach. See paragraph 815-10-65-6 for transition guidance on applying the simplified hedge accounting approach.

815-20-25-134 The conditions for the simplified hedge accounting approach determine which cash flow hedging relationships qualify for a simplified version of hedge accounting. If all of the conditions in paragraphs 815-20-25-135 and 815-20-25-137 are met, an entity may assume perfect effectiveness in a cash flow hedging relationship involving a variable-rate borrowing and a receive-variable, pay-fixed interest rate swap.

815-20-25-135 Provided all of the conditions in paragraph 815-20-25-137 are met, the simplified hedge accounting approach may be applied by a **private company** except for a financial institution as described in paragraph 942-320-50-1. An entity may elect the simplified hedge accounting approach for any receive-variable, pay-fixed interest rate swap, provided that all of the conditions for applying the simplified hedge accounting approach specified in paragraph 815-20-25-137 are met. Implementation guidance on the conditions set forth in paragraph 815-20-25-137 is provided in paragraphs 815-20-55-79A through 55-79B.

815-20-25-136 In applying the simplified hedge accounting approach, the documentation required by paragraph 815-20-25-3 to qualify for hedge accounting must be completed by the date on which the first annual **financial statements are available to be issued** after hedge inception rather than concurrently at hedge inception.

815-20-25-137 An eligible entity under paragraph 815-20-25-135 must meet all of the following conditions to apply the simplified hedge accounting approach to a cash flow hedge of a variable-rate borrowing with a receive-variable, pay-fixed interest rate swap:

a. Both the variable rate on the swap and the borrowing are based on the same index and reset period (for example, both the swap and borrowing are based on one-month London Interbank Offered Rate [LIBOR] or both the swap and borrowing are based on three-month LIBOR).

b. The terms of the swap are typical (in other words, the swap is what is generally considered to be a “plain-vanilla” swap), and there is no floor or cap on the variable interest rate of the swap unless the borrowing has a comparable floor or cap.

c. The repricing and settlement dates for the swap and the borrowing match or differ by no more than a few days.

d. The swap’s fair value at inception (that is, at the time the derivative was executed to hedge the interest rate risk of the borrowing) is at or near zero.

e. The notional amount of the swap matches the principal amount of the borrowing being hedged. In complying with this condition, the amount of the borrowing being hedged may be less than the total principal amount of the borrowing.

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f. All interest payments occurring on the borrowing during the term of the swap (or the effective term of the swap underlying the forward starting swap) are designated as hedged whether in total or in proportion to the principal amount of the borrowing being hedged.

815-20-25-138 A cash flow hedge established through the use of a forward starting receive-variable, pay-fixed interest rate swap may be permitted in applying the simplified hedge accounting approach only if the occurrence of forecasted interest payments to be swapped is probable. When forecasted interest payments are no longer probable of occurring, a cash flow hedging relationship will no longer qualify for the simplified hedge accounting approach and the General Subsections of this Topic shall apply at the date of change and on a prospective basis.

Timing of Hedge Documentation for Certain Private Companies If Simplified Hedge Accounting Approach Is Not Applied

Concurrent Hedge Documentation

815-20-25-139 Concurrent with hedge inception, a **private company** that is not a financial institution as described in paragraph 942-320-50-1 shall document the following:

a. The hedging relationship in accordance with paragraph 815-20-25-3(b)(1)

b. The hedging instrument in accordance with paragraph 815-20-25-3(b)(2)(i)

c. The hedged item in accordance with paragraph 815-20-25-3(b)(2)(ii), including (if applicable) firm commitments or the analysis supporting a last-of-layer designation in paragraph 815-20-25-3(c), or forecasted transactions in paragraph 815-20-25-3(d)

d. The nature of the risk being hedged in accordance with paragraph 815-20-25-3(b)(2)(iii).

815-20-25-140 A private company that is not a financial institution is not required to perform or document the following items concurrent with hedge inception but rather is required to perform or document them within the time periods discussed in paragraph 815-20-25-142:

a. The method of assessing hedge effectiveness at inception and on an ongoing basis in accordance with paragraph 815-20-25-3(b)(2)(iv) and (vi)

b Initial hedge effectiveness assessments in accordance with paragraph 815-20-25-3(b)(2)(iv)(01) through (04).

815-20-25-141 Example 1A beginning in paragraph 815-20-55-80A illustrates hedge documentation when the critical terms of the hedging instrument and hedged forecasted transaction match. Although that Example illustrates the documentation of the method of assessing hedge effectiveness, private companies that are not financial institutions may complete hedge documentation requirements in accordance with paragraphs 815-20-25-139 through 25-140.

Hedge Effectiveness Assessments

815-20-25-142 For a private company that is not a financial institution, the performance and documentation of the items listed in paragraph 815-20-25-140, as well as required subsequent quarterly hedge effectiveness assessments, may be completed before the date on which the next interim (if applicable) or annual financial statements are available to be issued. Even though the completion of the initial and ongoing assessments of effectiveness may be deferred to the date on which financial statements are available to be issued the assessments shall be completed using information applicable as of hedge inception and each subsequent

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quarterly assessment date when completing this documentation on a deferred basis. Therefore, the assessment should be performed to determine whether the hedge was highly effective at achieving offsetting changes in fair values or cash flows at inception and in each subsequent quarterly assessment period up to the reporting date.

Hedge Accounting Provisions Applicable to Certain Not-for-Profit Entities

815-20-25-143 Not-for-profit entities (except for not-for-profit entities that have issued, or are a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market) may apply the guidance on the timing of hedge documentation and hedge effectiveness assessments in paragraphs 815-20-25-139 through 25-142. Specifically, those entities shall document the items listed in paragraph 815-20-25-139 concurrent with hedge inception, but they may perform and document the items listed in paragraph 815-20-25-140 and perform the required subsequent quarterly hedge effectiveness assessments in accordance with paragraph 815-20-25-142 within the time periods discussed in paragraph 815-20-25-142.

Exhibit 3 – Revisions adopted to SSAP No. 86 on December 12, 2022 (Agenda Item 2022-09)

Fair Value Hedges (Note – Paragraphs 26.a. through 26.c. are not affected and are omitted for brevity.)

26. Fair value hedges qualify for hedge accounting if all of the following criteria are met:

d. The hedged item is specifically identified as either all, ~~or~~ a specific portion, or the partial term of a recognized asset, or all or a specific portion of ~~or~~ a recognized liability or of an unrecognized firm commitment. The hedged item is a single asset or liability (or a specific portion or partial term thereof) or is a portfolio of similar assets or a portfolio of similar liabilities (or a specific portion thereof) or a closed portfolio of assets (pursuant to paragraph 26.f. and Exhibit A, paragraph 46) where assumed layer or layers is anticipated to be outstanding (or a specific portion thereof)[3]. For a partial term hedge of one or more consecutive selected contractual cash flows where the hedged item begins when the first hedge cash flow begins to accrue and ends at the end of the designation hedge period, the assumed maturity of the hedged item occurs at the end of the designated hedge period; *(ASC 815-25-35-13B Partial Term Hedging.)*

e. If similar assets or similar liabilities are aggregated and hedged as a portfolio, the individual assets or individual liabilities must share the risk exposure for which they are designated as being hedged. The change in fair value attributable to the hedged risk for each individual item in a hedged portfolio must be expected to respond in a generally proportionate manner to the overall change in fair value of the aggregate portfolio attributable to the hedged risk; and

f. For a closed portfolio of financial assets or one or more beneficial interests secured by a portfolio of financial instruments, an entity may designate as the hedged item or items a hedged layer or layers (this designation is referred to throughout as the "portfolio layer method" (detailed in Exhibit A). *(ASC 815-20-25-12A Portfolio Layer Method)*

~~f.~~g. If the hedged item is a financial asset or liability, a recognized loan servicing right, or a nonfinancial firm commitment with financial components, the designated risk being hedged is:

i. The risk of changes in the overall fair value of the entire hedged item;

[3] For clarity, partial-term hedges and portfolio hedges addressed in paragraph 26.f. are limited to the situations in which the hedged item(s) is a recognized asset or a closed portfolio of financial assets. These hedging accounting methods are not permitted to hedge liabilities.

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ii. The risk of changes in its fair value attributable to changes in benchmark interest rate;

iii. The risk of changes in its fair value attributable to changes in the related foreign currency exchange rates; or

iv. The risk of changes in its fair value attributable to both changes in the obligor's creditworthiness and changes in the spread over the benchmark interest rate with respect to the related financial asset's or liability's credit sector at inception of the hedge (referred to as credit risk).

If the risk designated as being hedged is not the risk in paragraph 26.f.i., two or more of the other risks (benchmark interest rate risk, foreign currency exchange risk, and credit risk) may simultaneously be designated as being hedged.

The benchmark interest rate being hedged in a hedge of interest rate risk must be specifically identified as part of the designation and documentation at the inception of the hedging relationship. In calculating the change in the hedged item's fair value attributable to changes in the benchmark interest rate, the estimated coupon cash flows used in calculating fair value shall ~~must~~ be based on either~~all of~~ the full contractual cash flows ~~of the entire hedged item~~ or the benchmark rate component of the contractual coupon cash flows of the hedged item determined at hedge inception. An entity may designate a fair value hedge of interest rate risk in which the hedged item is a prepayment instrument. The entity may consider only how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity (for example, an entity may consider only how change in the benchmark interest rate affect an obligor's decision to call a debt instrument when it has the right to do so.) The entity need not consider other factors that would affect this decision (for example, credit risk) when assessing hedge effectiveness. *(ASU 815-25-35-13 & 815-20-25-6B)*~~Excluding some of the hedged item's contractual cash flows (for example, the portion of the interest coupon in excess of the benchmark interest rate) from the calculation is not permitted.~~[4] An entity may not simply designate prepayment risk as the risk being hedged for a financial asset. However, it can designate the option component of a prepayable instrument as the hedged item in a fair value hedge of the entity's exposure to changes in the fair value of that "prepayment" option, perhaps thereby achieving the objective of its desire to hedge prepayment risk. The effect of an embedded derivative of the same risk class must be considered in designating a hedge of an individual risk. For example, the effect of an embedded prepayment option must be considered in designating a hedge of benchmark interest rate risk.

Disclosure Requirements

62. Reporting entities shall disclose the following for all derivative contracts used:

a. General disclosures:

vii. The net gain or loss recognized in unrealized gains or losses during the perioding period resulting from derivatives that no longer qualify for hedge accounting. For portfolio layer method hedges, disclose circumstances that led to the breach. *(ASC 815-10-50-5C.)*

Relevant Literature

64. This statement adopts the framework established by FAS 133, *FASB Statement No. 137, Accounting for Derivative Instruments and Hedging Activities—Deferral of the Effective Date of FASB*

[4] ~~The first sentence of paragraph 26.d. that specifically permits the hedged item to be identified as either all or a specific portion of a recognized asset or liability or of an unrecognized firm commitment is not affected by the provisions in this subparagraph.~~

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Statement No. 133, An amendment of FASB Statement No. 133 (FAS 137) and *FASB Statement No. 138, Accounting* for *Certain Derivative Instruments and Certain Hedging Activities, An amendment of FASB Statement No. 133* (FAS 138), for fair value and cash flow hedges, including its technical guidance to the extent such guidance is consistent with the statutory accounting approach to derivatives utilized in this statement. This statement adopts the provisions of FAS 133 and 138 related to foreign currency hedges. With the exception of guidance specific to foreign currency hedges and amendments specific to refining the hedging of interest rate risk (under FAS 138, the risk of changes in the benchmark interest rate would be a hedged risk), this statement rejects FAS No. 137 and 138 as well as the various related Emerging Issues Task Force interpretations. This statement adopts paragraphs 4 and 25 of *FASB Statement No. 149: Amendment of Statement 133 on Derivative Instruments and Hedging Activities* (FAS 149) regarding the definition of an underlying and guidance for assessing hedge effectiveness. (The adoption from FAS 149 on the assessment of hedge effectiveness is impacted by the adoption with modification of guidance from ASU 2017-12 as detailed in paragraph 65.b., with the guidance from ASU 2017-12 superseding the prior adoption to the extent applicable.) All other paragraphs in FAS 149 are rejected as not applicable for statutory accounting. This statement adopts FSP FAS 133-1 and FIN 45-5*: Disclosures about Credit Derivatives and Certain Guarantees, An Amendment of FASB Statement No. 133 and FASB Interpretation No.45 and Clarification of the Effective Date of FASB Statement No. 161 (*FSP FAS 133-1 and FIN 45-4) and requires disclosures by sellers of credit derivatives. This statement rejects *FSP FIN 39-1, Amendments of FASB Interpretation No. 39*, and *ASU 2014-03, Derivatives and Hedging – Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps – Simplified Hedge Accounting Approach*.

65. This statement adopts, with modification, certain revisions to ASC 815-20 included in ASU 2017-12. Remaining provisions of ASU 2017-12 will be subsequently assessed for statutory accounting and shall not be considered adopted for statutory accounting until that assessment is complete.

a. Revisions effective January 1, 2019 with early adoption permitted, are limited to specific provisions, and related transition guidance, pertaining to the documentation and assessment of hedge effectiveness and only includes: 1) provisions allowing more time to perform the initial quantitative hedge effectiveness assessment; 2) provisions allowing subsequent assessments of hedge effectiveness to be performed qualitatively if certain conditions are met; and 3) revisions regarding use of the critical terms and short-cut methods for assessing hedge effectiveness.

b. Revisions effective January 1, 2023, with early adoption permitted, are limited to the criteria for initial and subsequent hedge effectiveness detailed in the FASB Accounting Standards Codification (ASC) paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12. This adoption reflects statutory modifications to specify that the accounting and reporting of hedging instruments, including excluded components of the instruments, shall follow statutory specific guidance detailed in the statement. The intent of this guidance is to clarify that the determination of whether a hedging instrument qualifies as an effective hedge shall converge with U.S. GAAP, but that the measurement method shall continue to follow statutory specific provisions. The adoption of the referenced ASC paragraphs only extends to revisions incorporated through ASU 2017-12; therefore, any subsequent U.S. GAAP edits would require statutory accounting consideration before considered adopted**.**

c. Revisions effective January 1, 2022, with early adoption permitted, are limited to the criteria for the portfolio layer method detailed in ASU 2022-01, criteria to only consider how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity date in 815-20-25-6B, adding option in calculating the change in the hedged item's fair value attributed to changes in the benchmark interest rate based on the benchmark rate components of the contractual cash flows detailed in FASB ASC 815-25-35-13, and the partial-term hedging method detailed in FASB ASC 815-25-35-13B. The adoption of the partial term hedging method reflects statutory modifications that limits its use only when the hedged item is a recognized asset. This is different than U.S. GAAP, which permits the partial term method for hedged liabilities. The statutory limitation is established to prevent interim basis adjustments to hedged liabilities that could present a reduction of reported liabilities on the financial statements when the actual liability has not been reduced. Reconsideration of this statutory limitation may occur after a broader project

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to consider how derivative basis adjustments to hedged liabilities shall be reflected in the financial statements.

Effective Date and Transition

74.~~73~~ This statement is effective for derivative transaction entered into or modified on or after January 1, 2003. A modification is any revision or change in contractual terms of the derivative. SSAP No. 31 applies to derivative transaction prior to January 1, 2003. Alternatively, an insurer may choose to apply this statement to all derivatives to which the insurer is a party as of January 1, 2003. In either case, the insurer is to disclose the transition approach that is being used.

a. Revisions adopted to paragraph 64 to reject FSP FIN 39-1 is effective January 1, 2013, for companies that have previously reported a position in the balance sheet that was net of counterparty agreements. (Companies that have previously reported derivative instruments and/or related collateral gross shall not be impacted by these revisions.)

b. Revisions adopted in paragraph 16 clarify the reporting for amounts received/paid to adjust variation margin until the derivative contract has ended and are effective January 1, 2018, on a prospective basis, for reporting entities that have previously considered these amounts to reflect settlement or realized gains/losses. (Companies that have previously reported variation margin changes in line with the revisions shall not be impacted by these revisions.)

c. Revisions to incorporate limited provisions from ASU 2017-12 pertaining to the documentation of hedge effectiveness (detailed in paragraph 65) are effective January 1, 2019, with early adoption permitted for year-end 2018. However, if the reporting entity is a U.S. GAAP filer, the reporting entity may only elect early adoption if the entity has also elected early adoption of ASU 2017-12 for year-end 2018.

d. Revisions adopted April 2019 to explicitly include structured notes in scope of this statement are effective December 31, 2019. Revisions adopted July 2020 to define "derivative premium," require gross reporting of derivatives without the impact of financing premiums and require separate recognition of premiums payable and premiums receivable, are effective January 1, 2021.

e. Revisions adopted August 2022 that adopt with modification the criteria for initial and subsequent hedge effectiveness detailed in the FASB ASC paragraphs 815-20-25-72 through 815-20-35-20, as modified through the issuance of ASU 2017-12 and that incorporate statutory accounting revisions for the accounting and reporting of excluded components are effective January 1, 2023, with early adoption permitted. These revisions shall be applied prospectively for all new and existing hedges. Entities shall detail the adoption of this guidance as a change in accounting principle pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors.*

f. Revisions adopted December 12, 2022 that adopt U.S. GAAP guidance for the portfolio layer method, U.S. GAAP guidance to only consider how changes in the benchmark interest rate affect the decision to settle the hedged item before its scheduled maturity, U.S. GAAP guidance adding option in calculating the change in the hedged item's fair value attributed to changes in the benchmark interest rate based on the benchmark rate component of the contractual coupon cash flows, that and adopt with modification U.S. GAAP guidance for partial term hedging are effective January 1, 2023, with early adoption permitted. These revisions shall be applied prospectively to qualifying new hedges.

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Edits to New Exhibit A – Discussion of Hedge Effectiveness

17. All of the following conditions apply to both fair value hedges and cash flow hedges: *(815-20-25-104)*

e. The interest-bearing asset or liability is not prepayable, that is, able to be settled by either party before its scheduled maturity, or the assumed maturity date if the hedged item is measured as a partial-term hedge of interest rate risk in which the assumed maturity of the hedged items ~~occur on the date in which the last hedged cash flow is due and payable~~ ends at the end of the designated hedge period, in accordance with paragraph 815-25-35-13B, with the following qualifications:

i. This criterion does not apply to an interest-bearing asset or liability that is prepayable solely due to an embedded call option (put option) if the hedging instrument is a compound derivative composed of an interest rate swap and a mirror-image call option (put option).

ii. The call option embedded in the interest rate swap is considered a mirror image of the call option embedded in the hedged item if all of the following conditions are met:

18. All of the following incremental conditions apply to fair value hedges only: *(815-20-25-105 & 815-25-35-13B)*

a. The expiration date of the interest rate swap matches the maturity date of the interest-bearing asset or liability or the assumed maturity date if the hedged item is measured as a partial-term hedge of interest rate risk in which the assumed maturity of the hedged items ends at the end of the designated hedge period ~~occur on the date in which the last hedged cash flow is due and payable~~ in accordance with paragraph 815-25-35-13B.

Portfolio Layer Method (New paragraphs at the end of Exhibit A.)

46. For a closed portfolio of financial assets or one or more beneficial interests secured by a portfolio of financial instruments, an entity may designate as the hedged item or items a hedged layer or layers (this designation is referred to throughout as the "portfolio layer method.") *(ASU 815-20-25-12A)*

a. As part of the initial hedge documentation, an analysis is completed and documented to support the entity's expectation that the hedged item or items (that is, the hedged layer or layers in aggregate) is anticipated to be outstanding for the designated hedge period. That analysis shall incorporate the entity's current expectations of prepayments, defaults, and other factors affecting the timing and amount of cash flows associated with the closed portfolio.

b. For purposes of its analysis in paragraph 46.a., the entity assumes that as prepayments, defaults, and other factors affecting the timing and amount of cash flows occur, they first will be applied to the portion of the closed portfolio that is not hedged; and

c. The entity applies the partial-term hedging guidance to the assets or beneficial interest used to support the entity's expectation in paragraph 46.a. An asset that matures on a hedged layer's assumed maturity date meets this requirement.

47. After a closed portfolio is established in accordance with paragraph 46, and entity may designate new hedging relationships associated with the closed portfolio without dedesignating any existing hedging relationships associated with the closed portfolio if the criteria of paragraph 46 are met for those newly designated hedging relationships. *(ASU 815-20-25-12B)*

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48. For the portfolio layer method if both of the following conditions exist, the quantitative test described for similar assets (shared risk exposure) may be performed qualitatively on a hedge-by-hedge basis and only at hedge inception:

a. The hedged item is a hedged layer in a portfolio layer hedge and designated in accordance with paragraph 26.f. of SSAP No. 86.

b. An entity measures the change in fair value of the hedged item based on the benchmark rate component of the contractual coupon cash flows.

Using the benchmark rate component of the contractual coupon cash flows when all assets have the same assumed maturity date and prepayment risk does not affect the measurement of the hedged item results in all hedged items having the same benchmark rate component coupon cash flows. *(ASU 815-20-55-14A)*

49. For one or more hedging relationships designated under the portfolio layer method, an entity shall discontinue (or partially discontinue) hedge accounting in the following circumstances: *(ASU 815-25-40-8)*

a. If the entity cannot support on a subsequent testing date that the hedged layer or layers are anticipated to be outstanding for the designated hedge (that is, a breach is anticipated), it shall discontinue (or partially discontinue) hedge accounting for one or more hedging relationships for the portion of the hedged item that is no longer anticipated to be outstanding for the designated hedge period.

b. If on a subsequent testing date the outstanding amount of the closed portfolio of financial assets or one or more beneficial interests is less than the hedged layer or layers (that is, a breach has occurred), the entity shall discontinue (or partially discontinue) hedge accounting for one or more hedging relationships for the portion of the hedged item that is no longer outstanding.

50. In the event of either an anticipated breach (as described in paragraph 49.a.) or a breach that has occurred (as described in paragraph 49.b.) for portfolio layer method, if multiple hedged layers are associated with a closed portfolio, an entity shall determine which hedge or hedges to discontinue (or partially discontinue) in accordance with an accounting policy election. That accounting policy election shall specify a systematic and rational approach to determining which hedge or hedges to discontinue (or partially discontinue). An entity shall establish its accounting policy no later than when it first anticipates a breach or when a breach has occurred (whichever comes first). After an entity establishes its accounting policy, it shall consistently apply its accounting policy to all portfolio layer method breaches (anticipated and occurred). *(ASU 815-25-40-8A)*

U.S. GAAP references not pulled into Exhibit will also be updated as follows:

Consideration of Prepayment Risk Using the ~~Last-of-Layer~~ Portfolio Layer Method

815-20-25-118A In a fair value hedge of interest rate risk designated under the portfolio layer ~~last-of-layer~~ method in accordance with paragraph 815-20-25-12A, an entity may exclude prepayment risk when measuring the change in fair value of the hedged item attributable to interest rate risk.

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Edits to Exhibit ~~C~~ B – Specific Hedge Accounting Procedures for Derivatives

2. Swaps, Collars, and Forwards (see also discussion in Introduction above):

d. Gain/Loss on Termination of a swap, collar or forward accounted for under hedge accounting (includes closing, exercise, maturity, and expiry):

i. Exercise—The remaining book value of the derivative shall become an adjustment to the cost or proceeds of the hedged item(s) received or disposed of individually or in aggregate;

ii. Sale, maturity, expiry, or other closing transaction of a derivative which is an effective hedge—Any gain or loss on the transaction, except for excluded components, will adjust the basis (or proceeds) of the hedged item(s) individually or in aggregate. If a portfolio layer method hedging relationship is discontinued (or partially discontinued) in a voluntary dedesignation or in anticipation of a breach, the basis adjustment associated with the dedesignated amount as of the discontinuation date shall be allocated to the remaining individual assets in the closed portfolio that supported the dedesignated hedged layer using a systematic and rational method. Alternatively, if the item being hedged is subject to IMR, the gain or loss on the terminated hedging derivative may be realized and shall be subject to IMR upon termination. (ASU 815-25-40-9)

iii. Gain/loss on termination of derivatives will be recognized currently in net income (realized gain/loss) to the extent they ceased to be effective hedges.

iv. Upon the redesignation of a derivative from a currently effective hedging relationship,

(a) with an item(s) carried at amortized cost to another effective hedging relationship with an item(s) carried at amortized cost, the derivative shall continue to be recorded at amortized cost and no gain or loss on the derivative shall be recognized.

(b) with an item(s) carried at amortized cost or fair value to an effective relationship with an item(s) carried at fair value, the accounting for the derivative shall be consistent with (ii) above.

(c) with an item(s) carried at fair value to an effective relationship with an item(s) carried at amortized cost, the accounting for the derivative shall be consistent with (ii.) above.

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Statutory Issue Paper No. 168

Updates to the Definition of a Liability

STATUS
Finalized August 13, 2023

Original and Current Authoritative Guidance: SSAP No. 5R

Type of Issue:
Common Area

SUMMARY OF ISSUE

1. This issue paper documents the SAP clarification revisions to *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets.* The intent of the revisions is to align current statutory accounting guidance, specifically the definition of a "liability," with the term utilized by the Financial Accounting Standards Board (FASB).

SUMMARY CONCLUSION

2. The statutory accounting principle clarifications to SSAP No. 5R (illustrated in Exhibit A), reflect that for the purposes of statutory accounting, a liability shall be defined as: a present obligation of an entity to transfer an economic benefit. A liability has two essential characteristics: (1) it is a present obligation, and (2) the obligation requires an entity to transfer or otherwise provide economic benefit to others. For the purposes of these characteristics, *transfer* is typically used to describe obligations to pay cash or convey assets, while the term *provide* is used to describe obligations to provide services or stand by to do so. This includes, but is not limited to, liabilities arising from policyholder obligations (e.g., policyholder benefits, reported claims and reserves for incurred but not reported claims). Liabilities shall be recorded on a reporting entity's financial statements when incurred.

3. Estimates (e.g., loss reserves) are required in financial statements for many ongoing and recurring activities of a reporting entity. The mere fact that an estimate is involved does not of itself constitute a loss contingency. For example, estimates of losses utilizing appropriate actuarial methodologies meet the definition of liabilities as outlined above and are not loss contingencies. (The definition and recognition requirements of loss contingencies under SSAP No. 5R are not proposed to be revised and will continue as statutory accounting guidance.)

DISCUSSION

4. In December 2021, FASB issued *Concepts Statement No. 8, Conceptual Framework for Financial Reporting—Chapter 4, Elements of Financial Statements*, which introduced updated definitions of certain key elements used in financial reporting – most notably updating the fundamental definition of a liability. Through the FASB's adoption of Concept Statement No. 8, the original Concept Statement No. 6 has been superseded. As statutory accounting currently reflects FASB's historical definition, this issue paper is to review the prior concept definition (currently utilized by statutory accounting) and compare it to FASB's updated concept definition and assess whether the revised concept definition shall be reflected in statutory accounting.

5. FASB concept statements do not reflect authoritative U.S. GAAP guidance. Rather concept statements are intended to set forth objectives and fundamental concepts that will be the basis for development of financial accounting and reporting guidance. The term "liability" is not captured or defined in the FASB Accounting Standards Codification (which is the source of authoritative U.S. GAAP.) Furthermore, although the concept statement is intended to be used as a guide in establishing authoritative

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U.S. GAAP, the FASB is not restricted to the concepts when developing guidance, and the FASB may issue U.S. GAAP which may be inconsistent with the objectives and fundamental concepts set forth in Concept Statements. A change in a FASB Concept Statement does not 1) require a change in existing U.S. GAAP, 2) amend, modify or interpret the Accounting Standards Codification, or 3) justify either changing existing generally accepted accounting and reporting practices or interpreting the Accounting Standards Codification based on personal interpretations of the objectives and concepts in the concepts statement.

6. Under the prior FASB concept statement, which was reflected in SSAP No. 5R, a liability was defined as a probable future sacrifice of economic benefits arising from present obligations of a particular entity to transfer assets or to provide services to other entities in the future as a result of past transactions or events. In addition, the historical definition possessed three essential characteristics in that (1) it embodies a present duty or responsibility to one or more other entities that entails settlement by probable future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand, (2) the duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice, and (3) the transaction or other event obligating the entity has already happened.

7. Pursuant to the prior concept statement, and as incorporated in SSAP No. 5R, *probable,* as referenced both in the definition and essential characters, was used in a usual general meaning, rather than in a specific accounting or technical sense and referred to which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved.

8. With the new FASB conceptual framework chapter, a liability is now defined as a present obligation of an entity to transfer an economic benefit. In addition, the current definition has two essential characteristics in that the liability is (1) a present obligation, and (2) the obligation requires an entity to transfer or otherwise provide economic benefits to others.

9. The updated liability definition from Concept Statement No. 8 no longer includes the term *probable* or the phrase *in the future* and *as a result of past transactions or events.* The FASB concluded that the term *probable* has historically been misunderstood as implying that a future obligation must meet a probability to a certain threshold before the definition of a liability was met. Thus, if the probability of a future transfer of an asset (or the requirement to provide a service) was low, a liability would likely not be recognized. In removing the term *probable* (and replacing it with "present obligation"), FASB concluded that in almost all situations, the presence of an obligation will be apparent. It stated that most present obligations are legally enforceable, including obligations arising from binding contracts, agreements, statutes, or other legal or contractual means. Chapter 4 also discusses the prevalence of certain business risks and how to assess if they result in the recognition of a liability. The FASB concluded that while certain businesses have a risk that a future event will cause them to transfer an economic benefit (an asset), the risk itself does not represent a present obligation because exposure to a potential negative consequence does not constitute a present obligation.

10. However, the FASB also stated that situations lacking clear legal or contractual evidence of a present obligation may pose particular challenges that may make it difficult to discern whether a present obligation exists. In these settings, the FASB stated that constructive obligations or other noncontractual obligations are created by circumstance rather than by explicit agreement. In the absence of an explicit agreement, sufficient information to distinguish a present obligation is likely only available at the specific standards level. Thus, the FASB concluded that the specific facts and circumstances at the standards level (or in the case of statutory accounting, at the SSAP level) must be utilized to determine whether the entity has created a constructive obligation and must recognize a liability.

11. The FASB also struck the phrase *as the result of past transactions or events*. With this action, the FASB clarified that if the liability represents a *present obligation*, by default, the obligation must have occurred as the result of a past transaction or event and thus this phraseology was deemed redundant and unnecessary.

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12. When reviewing the substance of the revisions, the FASB concluded that the updated definition resulted in a clearer and more precise definition. Furthermore, while it did not fundamentally change the historical concept of a liability, the revised definition potentially expands the population of liabilities to include certain obligations to issue or potentially issue an entity's own shares rather than settle an obligation exclusively with assets. In essence, clarifying that instruments with characteristics of both liabilities and equity may in fact be classified as liabilities in certain situations.

13. In general, the FASB did not anticipate that the liability definition revisions would result in any material changes in instrument reclassification (e.g., items now being classified as a liability when previously they were not considered liabilities). Again, FASB Concept Statements are not authoritative and thus the guidance in any specific standard will still be utilized for instrument measurement and classification. For statutory accounting purposes, the updated definition should be viewed similarly, that is it does not change fundamental concepts, change current practices, or introduce a new, original or a modified accounting principle. The revisions to the definition of a liability clarify the definitional language and do not modify the original intent of SSAP No. 5R and thus the changes are deemed to be a statutory accounting principle clarification.

14. The remaining concepts and guidance articulated in SSAP No. 5R (e.g., contingencies, impairments, guarantees, etc.) were not proposed for revision and thus are not further discussed in this issue paper.

Actions of the Statutory Accounting Principles (E) Working Group

15. During the 2022 Spring National Meeting, the Working Group exposed this issue paper for public comment.

16. During the 2022 Summer National Meeting, the Working Group re-exposed this issue paper for public comment.

17. At the 2022 Fall National Meeting, the Working Group re-exposed this issue paper related to the definition change of a liability in *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets.* This exposure intends to provide additional time for industry to review the changes in accordance with statutory accounting statements. NAIC staff were directed to collaborate with interested parties on proposed clarifying language.

18. At the 2023 Spring National Meeting, the Working Group exposed this issue paper with revisions to: 1) add an additional footnote to the definition of a liability in SSAP No. 5R which defers to more topic specific contradictory guidance and 2) revise the relevant literature section of SSAP No. 5R to note the modification. These clarifications were because of the authoritative treatment that statutory accounting provides to the definition of an asset and a liability in SSAP No. 4 and SSAP No. 5R. For U.S. GAAP, the FASB Conceptual statements definitions are not authoritative, but rather are concepts to consider when developing and applying guidance. The FASB basis for conclusions noted that some existing authoritative FASB literature regarding liabilities is inconsistent with the updates to Concepts Statement No. 8. Therefore, a modification regarding topic specific liabilities guidance was incorporated to address variations from the definition of a liability. Examples of existing SAP variations from the definition of a liability include but are not limited to:

a. *SSAP No. 7—Asset Valuation Reserves and Interest Maintenance Reserves* – AVR and IMR establish liabilities for regulatory objectives.

b. *SSAP No. 62R—Property and Casualty Reinsurance* – contains the provision for reinsurance liability guidance which results in a liability that is a regulatory valuation allowance for overdue and slow paying reinsurance and also enforces credit for reinsurance (*Credit for Reinsurance Model Law* (#785)) collateral requirements.

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c. *SSAP No. 92—Post Retirement Benefits Other than Pensions*, provides liability recognition, which adopts several U.S. GAAP standards with modifications.

19. At the 2023 Summer National Meeting, the Working Group adopted the exposed revisions to SSAP No. 5R as documented in this issue paper and adopted this issue paper.

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

Statutory Accounting

20. Relevant excerpts of SSAP No. 5R, paragraphs 2-3 regarding the definition of a liability accounting are as follows:

> 2. A liability is defined as certain or probable[1] future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or to provide services to other entities in the future as a result of a past transaction(s) or event(s).
>
> 3. A liability has three essential characteristics: (a) it embodies a present duty or responsibility to one or more other entities that entails settlement by probable[1] future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand, (b) the duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice, and (c) the transaction or other event obligating the entity has already happened. This includes, but is not limited to, liabilities arising from policyholder obligations (e.g., policyholder benefits, reported claims and reserves for incurred but not reported claims). Liabilities shall be recorded on a reporting entity's financial statements when incurred.

Generally Accepted Accounting Principles

21. Relevant paragraphs from *Concepts Statement No. 8, Conceptual Framework for Financial Reporting—Chapter 4, Elements of Financial Statements* have been included below:

> **Liabilities**
>
> E37. A liability is a present obligation of an entity to transfer an economic benefit.
>
> **Characteristics of Liabilities**
>
> E38. A liability has the following two essential characteristics: a. It is a present obligation. B. The obligation requires an entity to transfer or otherwise provide economic benefits to others.[2]
>
> E39. Liabilities commonly have features that help identify them. For example, many liabilities require the obligated entity to pay cash to one or more identified other entities. Liabilities may not require an entity to pay cash but may require the entity to convey other assets, provide services, or transfer other economic benefits or to be ready to do so. Liabilities are based on a foundation of legal rights and duties.
>
> E40. Entities routinely incur liabilities in exchange transactions to acquire the funds, goods, and services they need to operate. For example, borrowing cash (acquiring funds) obligates an entity to repay the amount borrowed, acquiring assets on credit obligates an entity to pay for the assets,

[1] *FASB Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements*, states: Probable is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in *FASB Statement 5, Accounting for Contingencies*, paragraph 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved.

[2] This chapter continues the practice of describing liabilities as an obligation either to transfer or to provide economic benefits. For example, the term transfer has typically been used to describe obligations to pay cash or convey assets, and the term provide has typically been used to describe obligations to perform services or stand ready to do so.

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and selling products with a warranty or guarantee obligates an entity to either pay cash or repair or replace any products that prove defective. Often, obligations incurred in exchange transactions are contractual based on written or oral agreements to pay cash or to provide goods or services to specified or determinable entities on demand at specified or determinable dates or on the occurrence of specified events.

Present obligation

E41. A liability requires that an entity be obligated to perform or act in a certain manner. In most cases it is apparent that liabilities are legally enforceable. Legally enforceable obligations include those arising from binding contracts, agreements, rules, statutes, or other requirements that would be upheld by a judicial system or government. Judicial systems vary in type and form, and the term judicial systems includes any such system that would enforce laws, statutes, and regulations. In the context most relevant to financial reporting, an obligation is any condition that binds an entity to some performance or action. In a financial reporting context, something is binding on an entity if it requires performance. Performance is what the entity is required to do to satisfy the obligation.

E42. Many obligations that qualify as liabilities stem from contracts and other agreements that are enforceable by courts or from governmental actions that have the force of law. Agreements, contracts, or statutory requirements often will specify or imply how an obligation was incurred and when and how the obligation is to be settled. For example, borrowing and lease agreements specify the amount of charges and the dates when the payments are due. The absence of a specified maturity date or event to require settlement may cast doubt that an obligation exists.

E43. Liabilities necessarily involve other parties, society, or law. The identity of the other party or recipient need not be known to the obligated entity before the time of settlement. An obligation of an entity to itself cannot be a liability. For example, in the absence of external requirements an entity is not obligated to repair the roof of its building or maintain its plant and equipment. Although those actions may be wise business moves, the entity may forgo or defer such activities because there is no present obligation to perform the activity.

E44. Certain obligations require nonreciprocal transfers from an entity to one or more other entities. Such obligations include taxes imposed by governments, donations pledged to charitable entities, and cash dividends declared but not yet paid.

E45. To have a liability, an entity must have a present obligation, that is, the obligation exists at the financial statement date. The settlement date of the liability may occur in the future, but the obligation must be present at the financial statement date. Transactions or other events or circumstances expected to occur in the future do not in and of themselves give rise to obligations today.

E46. An intention to purchase an item, for example, an asset, does not in and of itself create a liability. However, a contractual obligation that requires an entity to pay more than the fair value of the asset at the transaction date may create a liability before the asset is received, reflecting what the entity might have to pay to undo the unfavorable contract.

E47. Business risks result from the conduct of an entity's business activities. A business risk is not a present obligation, though at some point in the future an event may occur that creates a present obligation. Some businesses have the potential of carrying out activities and creating present obligations as a result of those activities. However, no present obligation exists even if it is virtually certain that an obligating event will occur, though at present no such event has occurred. The essence of distinguishing business risks from liabilities is determining the point in time when an entity has a present obligation.

E48. Some business risks result from an entity's transactions, for example, selling goods in overseas markets might expose an entity to the risk of future cash flow fluctuations because of changes in foreign exchange rates. Other business risks result from an entity's operating environment, for example, operating in a highly specialized industry might expose an entity to the

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risk that it will be unable to attract sufficient skilled staff to sustain its operating activities. Those risks are not liabilities.

E49. To be presently obligated, an entity must be bound, either legally or in some other way, to perform or act in a certain way. Most liabilities are legally enforceable, including those arising from contracts, agreements, rules, and statutes. An entity also can become obligated by other means that would be expected to be upheld by a judicial process. However, the existence of a present obligation may be less clear in those circumstances.

E50. Some liabilities rest on constructive obligations, including some that arise in exchange transactions. A constructive obligation is created, inferred, or construed from the facts in a particular situation rather than contracted by agreement with another entity or imposed by government. An entity may become constructively obligated through customary business practice. In the normal course of business, an entity conducting certain activities may not create a clear contractual obligation but may nonetheless cause the entity to become presently obligated. For example, policies and practices for sales returns and those for warranties in the absence of a contract may create a present obligation because the pattern of behavior may create an enforceable claim for performance that would be upheld in the ultimate conclusion of a judiciary process.

E51. An entity's past behavior also may give rise to a present obligation. Repeated engagement in a certain behavior may obligate the entity to perform or act in a certain way on the basis of that pattern of behavior. For example, the entity may create a constructive obligation to employees for vacation pay or year-end bonuses by paying them every year even though it is not contractually bound to do so and has not announced a policy to do so.

22. The most notable changes regarding the definition of a liability included removal of the term *probable* and the phrase *as a result of past transactions or events.* Rationale for these changes were documented in *Chapter 4, Elements of Financial Statements* commentary as follows:

BC4.11. The definitions of both an asset and a liability in Concepts Statement 6 include the term probable and the phrases future economic benefit and past transactions or events. The term probable in the definitions in Concepts Statement 6 has been misunderstood as implying that a future economic benefit or a future sacrifice of economic benefit must be probable to a certain threshold before the definition of an asset or a liability is met. In other words, if the probability of future economic benefit is low, the asset definition is not met under that interpretation. A similar interpretation could be made for liabilities. The footnotes to the Concepts Statement 6 definition of assets and liabilities also were not helpful in clarifying the application of the term probable as used in the definitions of assets and liabilities. Accordingly, the Board decided to eliminate that term from the definitions of both assets and liabilities.

BC4.12. The term future in the definitions in Concepts Statement 6 focused on identifying a future flow of economic benefits to demonstrate that an asset exists or identifying a future transfer of economic benefits to demonstrate that a liability exists. The definitions in Concepts Statement 6 were often misunderstood as meaning that the asset (liability) is the ultimate future inflow (outflow). For example, in the instance of trade receivables, the definition in Concepts Statement 6 could be misunderstood to indicate that the asset is the successful collection of the receivable in the future. When applied appropriately, however, the definition would conclude that the asset is the present right to collection. Similar misunderstandings occurred in applying the liability definition. As a result, the Board concluded that a focus on the term present would appropriately shift the focus from identifying a future occurrence. Therefore, the Board decided to include the term present right to demonstrate that an asset exists and emphasize the term present obligation to demonstrate that a liability exists.

BC4.13. The definitions of assets and liabilities in Concepts Statement 6 both include the phrase past transactions or events. The Board concluded that if an entity has a present right or a present obligation, one can reasonably assume that it was obtained from some past transaction or event. Therefore, that phrase is considered redundant and has been eliminated from the definitions.

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23. The other significant change to the definition of a liability included changing *future sacrifices* to a *present obligation*. Rationale for these changes were documented in *Chapter 4, Elements of Financial Statements* commentary as follows:

> BC4.25. The term present obligation is included in the definition of a liability, both in this chapter and in Concepts Statement 6. Because the application of the liability definition under Concepts Statement 6 did not give sufficient emphasis to the term present obligation, the definition in this chapter more appropriately emphasizes that term. Assessing whether a present obligation exists is the primary criterion in the definition of a liability in this chapter. The primacy of the term present obligation is made more evident through the removal of many of the problematic terms in the definition of a liability in Concepts Statement 6, as discussed in paragraphs BC4.11–BC4.13.
>
> BC4.26. Almost always, the existence of a present obligation will be apparent. Most present obligations are legally enforceable, including obligations arising from binding contracts, agreements, statutes, or other legal or contractual means. However, situations lacking clear legal or contractual evidence of a present obligation pose particular challenges that may make it difficult to discern whether a present obligation exists.
>
> BC4.27. Determining when a present obligation exists has caused confusion with the existence of business risks. Business risks result from the nature of the business and where, when, and how an entity conducts its business. While certain businesses pose risks of future events occurring that will cause a transfer of economic benefits, the Board decided that the risks themselves are not present obligations because exposure to a potential negative consequence does not constitute a present obligation. Rather than viewing all business risks as liabilities, the Board decided that an entity has a present obligation only after an event occurs that demonstrates that the inherent business risk has created a present obligation. Thus, distinguishing when a business risk makes an entity presently obligated requires analysis of the facts and circumstances at the standards level.
>
> BC4.28. Determining the existence of a present obligation is particularly challenging in evaluating constructive obligations. Interpreting constructive obligations too narrowly will tend to exclude significant actual obligations of an entity, while interpreting them too broadly will effectively nullify the definition by including items that lack an essential characteristic of liabilities.
>
> BC4.29. Given that constructive obligations and other noncontractual obligations are created by circumstance rather than explicit agreement, it can be unclear whether a present obligation exists. In the absence of an explicit agreement, sufficient information to distinguish a present obligation is likely only available at the specific standards level. Thus, the Board decided that specific facts and circumstances at the standards level must be assessed to determine whether an entity has created a constructive obligation.

RELEVANT LITERATURE

Statutory Accounting

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy

Generally Accepted Accounting Principles

- FASB Statement of Financial Accounting Concepts No. 8, Conceptual Framework for Financial Reporting – Chapter 4, Elements of Financial Statements

Effective Date

24. As issue papers are not authoritative and are not represented in the Statutory Hierarchy (see Section V of the Preamble), the consideration and adoption of this issue paper will not have any impact on the SAP clarifications adopted to SSAP No. 5R by the Working Group on August 13, 2023.

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EXHIBIT A – SAP Clarification Revisions to *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* the other paragraphs of SSAP No. 5R are unchanged.

Statement of Statutory Accounting Principles No. 5 ~~–~~ Revised

Liabilities, Contingencies and Impairments of Assets

SCOPE OF STATEMENT

1. This statement defines and establishes statutory accounting principles for liabilities, contingencies and impairments of assets.

SUMMARY CONCLUSION

Liabilities

2. A liability is defined as a present obligation of an entity to transfer an economic benefit. ~~certain or probable FN1 future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or to provide services to other entities in the future as a result of a past transaction(s) or event(s).~~

3. A liability[1] has ~~three~~ two essential characteristics: (a) it is a present obligation ~~embodies a present duty or responsibility to one or more other entities that entails settlement by probable FN1 future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand~~, and (b) the obligation requires an entity to transfer or otherwise provide economic benefit to others ~~duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice, and (c) the transaction or other event obligating the entity has already happened~~. This includes, but is not limited to, liabilities arising from policyholder obligations (e.g., policyholder benefits, reported claims and reserves for incurred but not reported claims). Liabilities shall be recorded on a reporting entity's financial statements when incurred.

4. Estimates (e.g., loss reserves) are required in financial statements for many ongoing and recurring activities of a reporting entity. The mere fact that an estimate is involved does not of itself constitute a loss contingency. For example, estimates of losses utilizing appropriate actuarial methodologies meet the definition of liabilities as outlined above and are not loss contingencies.

~~FN1 – *FASB Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements*, states: Probable is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in *FASB Statement 5, Accounting for Contingencies*, paragraph 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved.~~

Relevant Literature

39. This statement adopts *FASB Statement No. 5, Accounting for Contingencies* (FAS 5), *FASB Statement 114, Accounting by Creditors for Impairment of a Loan* only as it amends in part FAS 5 ~~and paragraphs 35 and 36 of *FASB Statement of Financial Accounting Concepts No. 6—Elements of Financial Statements*~~. *FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss, An Interpretation*

[1] The guidance in this statement regarding the definition of a liability is applicable unless another authoritative statement of statutory accounting principles (SSAP) provides more topic-specific, contradictory guidance. In such cases the topic-specific guidance shall apply.

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of FASB Statement No. 5 (FIN No. 14) is adopted with the modification to accrue the loss amount as the midpoint of the range rather than the minimum as discussed in paragraph 3 of FIN No. 14. This statement adopts with modification *ASU 2013-04, Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date* with the same statutory modification adopted for FIN 14. This statement incorporates the definition of a liability from *FASB Statement of Financial Accounting Concepts No. 8, Chapter 4, Elements of Financial Statements,* paragraphs E37 and E38, with modification reflected in this statement regarding topic-specific guidance.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets*
- *Issue Paper No. 20—Gain Contingencies*
- *Issue Paper No. 135—Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*
- *Issue Paper No. 168—Updates to the Definition of a Liability*

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Appendix F
Policy Statements

Introduction

The policy statements contained within Appendix F are not included within the Statutory Hierarchy and thus should not be considered accounting guidance. As such, each policy statement is included for informational purposes only.

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NAIC Policy Statement on Maintenance of Statutory Accounting Principles

1. Statutory accounting principles (SAP) provide the basis for insurers to prepare financial statements to be filed with and utilized by state insurance departments for financial regulation purposes. Accuracy and completeness of such filings are critical to meaningful solvency monitoring. Accordingly, maintenance of SAP guidance for changes in the industry and changes in regulatory concerns is vital to preserving the usefulness of SAP financial statements.

2. The promulgation of new or revised SAP guidance by the NAIC ultimately requires action of the entire NAIC membership. Responsibility for proposing new or revised SAP guidance will be delegated through the NAIC committee structure to the Accounting Practices and Procedures (E) Task Force (Task Force). The Task Force will charge the Statutory Accounting Principles (E) Working Group (Working Group) with the exclusive responsibility to develop and propose new statements of statutory accounting principles (SSAPs), to revise existing SSAPs, and to issue interpretations.

Composition of the Statutory Accounting Principles (E) Working Group

3. The chair of the Task Force shall determine membership of the Working Group subject to approval by the Financial Condition (E) Committee. The Working Group shall be limited in size to no more than 15 members and will include representation from the four zones of the NAIC. Membership shall be vested in the state (until such time as the membership may be changed) but continuity of individuals, to the extent possible, is extremely desirable.

Development of New SSAPs or New SAP Concepts[1] in an Existing SSAP

4. New SSAPs will be developed to address, but will not be limited to: 1) concepts not previously addressed by a SSAP and that do not fit within the scope of an existing SSAP; 2) concepts that fit within the scope of an existing SSAP, but the Working Group elects to supersede existing SSAPs and 3) existing concepts that warrant significant revisions. New SAP concepts to existing SSAPs will be developed to address, but will not be limited to: 1) concepts that fit within the accounting topic of an existing SSAP, but have not been addressed by the Working Group; 2) changes to the valuation and/or measurement of an existing SSAP; and 3) modifications to the overall application of existing SSAPs. The decision to undertake development of a new SSAP or a new SAP concept in an existing SSAP will rest with the Working Group. New SSAPs or a new SAP concept in an existing SSAP will have a specified effective date.

5. Research and drafting of a new SSAP or a new SAP concept in an existing SSAP will be performed by NAIC staff under the direction and supervision of the Working Group which may enlist the assistance of interested parties and/or consultants with requisite technical expertise as needed or desired. The first step in developing new SSAPs and new SAP concepts in existing SSAPs will commonly be the drafting of an issue paper, which will contain a summary of the issue, a summary conclusion, discussion, and a relevant literature section. Public comments will be solicited on an issue paper (at least one exposure period), and at least one public hearing will be held before the issue paper is converted to a SSAP. Upon approval by the Working Group, all proposed SSAPs will be exposed for public comment for a period commensurate with the length of the draft and the complexities of the issue(s). After a hearing of comments, adoption of new SSAPs or new SAP concepts in existing SSAPs (including any amendments from exposure) may be made by simple majority. If no comments are received during the public comment period, the Working Group may adopt the proposal collectively (one motion/vote) with other non-contested positions after the opportunity is given during the hearing to separately discuss the

[1] Prior to December 11, 2021, the term used to describe a new SAP concept was "substantive" and the term used to describe a SAP clarification was "nonsubstantive." The new terms will be reflected in materials to describe revisions to statutory accounting principles on a prospective basis and historical documents will not be updated to reflect the revised terms.

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proposal. All new SSAPs and new SAP concepts in existing SSAPs must be on the agenda for at least one public hearing before presentation to the Task Force for consideration. Adoption by the Task Force, its parent and the NAIC membership shall be governed by the NAIC bylaws.

6. The Working Group may, by a super majority vote (7 out of 10 members, 8 out of 11 or 12, 9 out of 13, 10 out of 14, and 11 out of 15) elect to: 1) combine the IP and SSAP process, resulting in concurrent exposure of the two documents; 2) expose and adopt revisions to a SSAP prior to the drafting/adoption of the related IP; and/or 3) forego completion of an IP and only proceed with a new SSAP or new SAP concept in an existing SSAP.

7. If accounting guidance, reserving standards, asset valuation standards, or any other standards or rules affecting accounting practices and procedures are first developed by other NAIC working groups, task forces, subcommittees, or committees, such proposed guidance, standards or rules shall be presented to the Working Group for consideration. In cases where such guidance has already been subjected to substantial due process (e.g., public comment periods and/or public hearings), the Working Group may elect to shorten comment periods and/or eliminate public hearings, and in such cases, will notify the Task Force of these actions.

Development of SAP Clarifications[1]

8. SAP clarifications will be developed to address, but will not be limited to: 1) clarification of the intent or application of existing SSAPs; 2) new disclosures and modification of existing disclosures; 3) revisions that do not change the intent of existing guidance; and 4) revisions to *Appendix A—Excerpts of NAIC Model Laws* to reflect amendments to NAIC adopted model laws and regulations. Research and drafting of SAP clarification revisions will be performed by NAIC staff under the direction and supervision of the Working Group. Public comment will be solicited on these revisions, and the item will be included on the agenda for at least one public hearing before the Working Group adopts revisions. SAP clarification revisions are considered effective immediately after adoption by the Working Group, unless the Working Group incorporates a specific effective date. If comments are not received during the public comment period, the Working Group may adopt the proposal collectively (one motion/vote) with other "non-contested" positions after opportunity is given during the hearing to separately discuss the proposal. At its discretion, the Working Group may request that an issue paper be drafted for SAP clarification revisions in order to capture historical discussion and adopted revisions. Adoption of these revisions by the Task Force, its parent and the NAIC membership shall be governed by the NAIC bylaws.

Development of Interpretations to SSAPs and Referencing Interpretations Within SSAPs

Interpretations Which DO NOT Amend, Supersede or Conflict with Existing SSAPs

9. Interpretations may be developed to address issues requiring timely application or clarification of existing SAP, which shall not amend, supersede or conflict with effective SSAPs. Issues being considered as an interpretation must be discussed at no less than two open meetings. (Original introduction of the issue when the Working Group identifies the intent to address the issue as an "interpretation" during a public discussion is considered the first open meeting discussion.) The process must allow opportunity for interested parties to provide comments, but as interpretations are intended to provide timely responses to questions of application or interpretation and clarification of guidance, no minimum exposure timeframe is required.

10. As these interpretations do not amend, supersede or conflict with existing SSAP guidance, the interpretation is effective upon Working Group adoption unless specifically stated otherwise. The voting requirement to adopt an interpretation of this type is a simple majority. The Working Group shall report the adopted interpretation to the Accounting Practices and Procedures (E) Task Force as part of its public report during the next NAIC national meeting (or earlier if applicable). Interpretations can be overturned, amended or deferred by a two-thirds majority of the Task Force membership. For clarification, a two-

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thirds majority of the Task Force requires two-thirds of the entire Task Force membership, not just those electing to vote. Additionally, interpretations can be overturned, amended, deferred, or referred to either the Task Force and/or the Working Group by a simple majority of the Financial Condition (E) Committee.

Interpretations Which Amend, Supersede or Conflict with Existing SSAPs

11. In certain circumstances such as catastrophes and other time-sensitive issues requiring immediate, temporary statutory accounting guidance, the Working Group may adopt an interpretation which creates new SAP or conflicts with existing SSAPs. Historically, these interpretations temporarily modified statutory accounting principles and/or specific disclosures were developed in response to nationally significant events (e.g., Hurricane Sandy, September 11, 2001). (Examples of time-sensitive issues that have previously provided INT exceptions to SAP include the transition from LIBOR and special situations such as the federal TALF program.) Interpretations that conflict with existing SSAPs shall be temporary and restricted to circumstances arising from the need to issue guidance for circumstances requiring immediate guidance. In order to adopt an interpretation that creates new SAP or conflicts with existing SSAPs, the Working Group must have 67% of its members voting (10 out of 15 members) with a super majority (7 out of 10, 8 out of 11 or 12, 9 out of 13, 10 out of 14, or 11 out of 15) supporting adoption.

a. These interpretations are effective upon Working Group adoption, unless stated otherwise, and shall be reported to the Accounting Practices and Procedures (E) Task Force as part of its public report during the next NAIC national meeting (or earlier if applicable). In circumstances where the Working Group adopts an interpretation (which creates new SAP or conflicts with existing SSAPs) that is controversial in nature (i.e., due to regulator or industry feedback or could have a policy level impact), the Working Group may elect to postpone the effective date until the item has been discussed by the Task Force and the Financial Condition (E) Committee and both have had an opportunity to review the interpretation.

b. These interpretations can be overturned, amended or deferred by a two-thirds majority of the Task Force membership. For clarification, a two-thirds majority of the Task Force requires two-thirds of the entire Task Force membership, not just those electing to vote. Additionally, interpretations can be overturned, amended, deferred, or referred to either the Task Force and/or the Working Group by a simple majority of the Financial Condition (E) Committee.

12. As new SSAPs are developed, it is essential to review and, if necessary, update the status of interpretations related to SSAPs that are being replaced and/or new SSAPs being developed. The following options are available to the Working Group when a SSAP with existing interpretations is replaced:

a. **Interpretation of the new SSAP -** If the Working Group would like to maintain the interpretation, the new SSAP can be added to the list of statements interpreted by the interpretation. In addition, the status section of the new SSAP will list the interpretation number next to the heading “Interpreted by.”

b. **Nullification** - When an interpretation is nullified by a subsequent SSAP or superseded by another interpretation, the interpretation is deemed no longer technically helpful, is shaded and moved to Appendix H (Superseded SSAPs and Nullified Interpretations), and the reason for the change is noted beneath the interpretation title. The status section of the SSAP describes the impact of the new guidance and the effect on the interpretation (for example, nullifies, incorporated in the new SSAP with paragraph reference, etc.).

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c. **Incorporation** - When an interpretation is incorporated into a new SSAP, the Working Group can choose from the following two options:

i. If the interpretation only interprets one SSAP, then the interpretation is listed as being nullified under the "affects" section of the SSAP and is not referenced under the "interpreted by" section of the status page of the SSAP.

ii. If the interpretation references additional SSAPs, and the Working Group intends to maintain the guidance, the interpretation is unchanged (no nullification). The new SSAP (Summary of Issue section) reflects that the interpretation issue has been incorporated into the new statement.

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NAIC Policy Statement on Comments to GAAP & IFRS Exposure Drafts

1. As expressed in the Statement of Concepts, statutory accounting principles (SAP) utilize the framework established by U.S. Generally Accepted Accounting Principles (GAAP). The NAIC's guidance on SAP (defined in the *Accounting Practices and Procedures Manual*) is comprehensive for those principles that differ from GAAP based on the concepts of statutory accounting. Those GAAP pronouncements that are not applicable to insurance companies will not be adopted by the NAIC. GAAP pronouncements that do not differ from SAP may specifically be adopted by the NAIC to be included in statutory accounting. GAAP pronouncements do not become part of SAP until and unless adopted by the NAIC. Future SAP pronouncements will specifically identify any GAAP pronouncements that are to be included in SAP whether in whole, in part, or with modification as well as any GAAP pronouncements that are rejected. Future GAAP pronouncements, which SAP has not yet addressed, shall not be considered as providing authoritative statutory guidance.

2. As stated in the previous paragraph, the NAIC believes it is important to comment on GAAP exposure drafts that will affect SAP before such guidance is finalized. Exposing potentially contentious issues to the applicable GAAP bodies before completion will create a more efficient and effective maintenance process for the Statutory Accounting Principles (E) Working Group (Working Group). In addition, this allows the NAIC to be proactive to GAAP rather than reactive under the current system. The NAIC also believes that there may be instances in which it is important to comment on exposure drafts of the International Financial Reporting Standards (IFRS). This is particularly important on projects in which U.S. FASB and the International Accounting Standards Board (IASB) are attempting to converge, or to limit differences between U.S. GAAP and IFRS.

3. Comments on exposed GAAP pronouncements or IFRS exposure drafts will be developed at the discretion of the Working Group chair. After a comment letter has been agreed to by the Working Group, the chairs of the Accounting Practices and Procedures (E) Task Force and the Financial Condition (E) Committee must review and approve the comment letter before it is sent to the applicable standard board. Every reasonable attempt will be made to provide an adequate comment period to interested parties; however, FASB and IFRS deadlines may inhibit exposure in every instance. The chairs will consider factors such as comment deadline and level of controversy surrounding the issue. The chair of the parent task force or committee may override such a decision at any time.

4. Comment letters submitted to the FASB on GAAP exposure drafts may be considered when the Working Group is reviewing finalized GAAP pronouncements (as defined in the NAIC *Policy Statement on Maintenance of Statutory Accounting Principles*). Nevertheless, these letters will not bind the Working Group to its tentative position during its deliberation to adopt, modify or reject the final GAAP guidance.

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NAIC Policy Statement on Statutory Accounting Principles Maintenance Agenda Process

1. The purpose of this policy statement is to document the Statutory Accounting Principles (E) Working Group (Working Group) maintenance agenda process.

2. As acknowledged in the NAIC *Policy Statement on Maintenance of Statutory Accounting Principles*, the promulgation of statutory accounting principles (SAP) guidance will be delegated through the NAIC committee structure to the Accounting Practices and Procedures (E) Task Force (Task Force). The Task Force will charge the Working Group with the responsibility to develop and propose new statements of statutory accounting principles (SSAPs), to propose revisions to existing SSAPs, and to issue interpretations in response to questions of application and clarification on existing SSAPs.

3. Information and issues can be presented to the Working Group in a variety of ways. Issues can be recommended or forwarded from 1) other NAIC committees, task forces or working groups; 2) interested parties; 3) interested regulators; and 4) NAIC staff. Also, if any guidance within the Generally Accepted Accounting Principles (GAAP) Hierarchy (see § V of the Preamble to the *Accounting Practices and Procedures Manual* (AP&P Manual)) is added or revised, those changes must be considered by the Working Group for potential revisions to SAP. In order for an issue to be placed on the **Pending Listing**, the recommending party must complete a Statutory Accounting Principles Maintenance Agenda Submission Form (Form A) and submit it to the Working Group support staff no later than 20 business days prior to the next scheduled Working Group meeting. NAIC staff will prepare a submission form for all GAAP pronouncements that have not been previously addressed by the Working Group. NAIC staff will update the **Pending Listing** before each national meeting and will notify the recommending party of such action. If the Working Group does not wish to address the issue (e.g., issue deemed not applicable to statutory accounting) or rejects the position presented, then the Working Group may move the item to the **Rejected Listing**. Should the Working Group choose to address an issue, it is moved to the **Active Listing** where it is prioritized and categorized as a new SAP concept, clarification of an existing SAP, or an interpretation agenda item.

4. The **Active Listing** identifies agenda items that are in the process of development and includes the following:

   a. **New SAP Concept**: These agenda items address the development of new SSAPs and/or the introduction of a new SAP concept as defined in the NAIC *Policy Statement on Maintenance of Statutory Accounting Principles*.

   b. **Clarification of an Existing SAP**: These agenda items address the development of revisions which clarify an existing SAP as defined in the NAIC *Policy Statement on Maintenance of Statutory Accounting Principles.*

   c. **Interpretations**: These agenda items address the development of interpretations to SAP as defined in the NAIC *Policy Statement on Maintenance of Statutory Accounting Principles*. If SSAP revisions are subsequently deemed necessary, the Working Group shall re-categorize the agenda item as either a new SAP concept or clarification of an existing SAP, as applicable, and follow the appropriate process to consider and adopt revisions.

5. After review of the agenda item (including any interested party comments), at its discretion, the Working Group makes the ultimate determination of whether an agenda item is categorized (or re-categorized) as a new SAP concept, clarification of an existing SAP, or an interpretation.

6. The **Rejected Listing** identifies items that were proposed to the Working Group and rejected without consideration. The **Disposition Listing** includes all agenda items considered by the Working

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Group and provides the conclusions and guidance given for all adopted revisions to SAP and for all agenda items disposed without modification to SAP.

7. It should be noted that this policy statement addresses the process and the flow of information. The timing is left to the discretion of the Working Group. For instance, once public discussion requirements have been met, as detailed in the NAIC *Policy Statement on Maintenance of Statutory Accounting Principles*, the Working Group can take action on an item at its discretion. In determining whether it is appropriate to take specific actions (including adoption), the Working Group must consider when the last exposure period occurred, and the extent of any prior comments received and discussions held. Additionally, there is no timeframe in which items must be addressed. Items will remain on the Active Listing until formally disposed of by the Working Group.

8. NAIC staff will maintain the following on the Working Group Web page (*https://content.naic.org/cmte_e_app_sapwg.htm*): 1) A blank Form A (Attachment A to this policy statement); 2) The current Maintenance Agenda, and 3) Current statutory and/or interpretation revisions exposed for public comment. Attachment B to this policy statement will be attached to all exposures with proposed revisions that result in a new SAP concept and serves as the request for written comment and notice of a public hearing.

Correction of Editorial Errors

9. Over time, during review and publication of the AP&P Manual, NAIC staff may identify inadvertent editorial errors and necessary revisions to the content of the Manual. These are editorial in nature and include grammatical errors, reference changes (i.e., paragraphs, SSAPs, and Model Laws and Regulations) and formatting issues. To aid in correcting these items and improve the overall usefulness of the AP&P Manual, the Working Group has implemented the following process:

a. At each meeting of the Working Group, if NAIC staff have identified (or have been informed by interested parties or regulators) any grammatical errors, reference changes and/or formatting issues, NAIC staff will present a public memorandum to the Working Group outlining the proposed amendments to the AP&P Manual. These corrections are not intended to clarify or revise existing guidance and as such, do not ordinarily warrant the use of a Form A or addition to the Maintenance Agenda.

b. After presentation to the Working Group, the memorandum will be exposed for a public comment period. If no objections are raised by the Working Group, interested regulators or interested parties, the revisions will be considered "noncontested" and presented to the Working Group for adoption. Upon adoption, the revisions will be incorporated into the AP&P Manual, with the revisions being posted on the "Updates to the AP&P Manual" secure Web page. Under this process, these revisions will be shown as tracked changes to the Manual unless otherwise noted in the memorandum.

c. If objections are raised by the Working Group, interested regulators or interested parties, the proposed revisions will either be rejected without further discussion or incorporated into a Form A to be presented to the Working Group and subsequently exposed for a public comment period. Under this process, the revisions will follow the Maintenance Agenda process as outlined in this policy statement.

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Attachment A

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue:

_____

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☐	☐	☐
New issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

*Description of Issue:

_____

*Existing Authoritative Literature:

_____

*Activity to Date (issues previously addressed by Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

_____

*Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:

_____

Recommended Conclusion or Future Action on Issue:

_____

Recommending Party:

_____
(Organization, Person Submitting, Title)

_____
(Address, City, State, ZIP)

_____
(Phone and Email Address)

_____
(Date Submitted)

* Indicates required information before NAIC staff will accept form as a final document.

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Attachment B

EXPOSURE DRAFT NUMBER - TITLE

Notice of Public Hearing and Request for Written Comments

Hearing Date: _____ **Location: _____**
Deadline for Written Notice of Intent to speak: **Deadline for Receipt of Written Comments:**

Basis for hearings. The Statutory Accounting Principles (E) Working Group (Working Group) will hold a public hearing to obtain information from and views of interested individuals and organizations about the standards proposed in this Exposure Draft. The Working Group will conduct the hearing in accordance with the *National Association of Insurance Commissioners (NAIC) Policy Statement on Open Meetings*. An individual or organization desiring to speak must notify the NAIC in writing by _____. Speakers will be notified as to the date, location and other details of the hearings.

Oral presentation requirements. The intended speaker must submit a position paper, a detailed outline of a proposed presentation or comment letter addressing the standards proposed in this Exposure Draft by _____. Individuals or organizations whose submission is not received by this date will only be granted permission to present at the discretion of the Working Group chair. All submissions should be addressed to NAIC staff at the address listed below. Comments can also be submitted by electronic mail to _____@naic.org.

Format of hearings. Speakers will be allotted up to 10 minutes for their presentations to be followed by a period for answering questions from the Working Group. Speakers should use their allotted time to provide information in addition to their already submitted written comments as those comments will have been read and analyzed by the Working Group. Those submissions will be included in the public record and will be available at the hearings for inspection.

Copies. Exposure drafts can be obtained on the Working Group's Web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

Written comments. Participation at a public hearing is not a prerequisite to submitting written comments on this Exposure Draft. Written comments are given the same consideration as public hearing testimony.

The Statutory Accounting Principles Statement of Concepts was adopted by the Accounting Practices & Procedures (EX4) Task Force on September 20, 1994, in order to provide a foundation for the evaluation of alternative accounting treatments. All issues considered by the Working Group will be evaluated in conjunction with the objectives of statutory reporting and the concepts set forth in the Statutory Accounting Principles Statement of Concepts.

The exposure period is not meant to only measure support for, or opposition to, a particular accounting treatment but rather to accumulate an analysis of the issues from other perspectives and persuasive comments supporting them. Therefore, form letters and objections without valid support for their conclusions are not helpful in the deliberations of the Working Group. Comments should register agreement or disagreement with a detailed explanation, a description of the impact of the proposed guidelines, and possible alternative recommendations for accomplishing the regulatory objective.

Any individual or organization may send written comments to _____ by electronic mail in Microsoft Word format to _____@naic.org. After written comments have been reviewed by the Working Group, the letters will be posted publicly on the NAIC website.

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NAIC Policy Statement on the Impact of Statements of Statutory Accounting Principles on NAIC Publications

1. The purpose of this policy statement is to document the process and procedure for identifying the impact of statements of statutory accounting principles (SSAPs) on NAIC publications.

2. New and revised SSAPs can affect various NAIC publications in different ways. New accounting practices or procedures may result in new disclosures and reporting requirements (affecting annual statement blanks and instructions), modified analysis techniques (affecting RBC formula or IRIS ratios), or new examination procedures (affecting the *Financial Condition Examiners Handbook*).

3. The Statutory Accounting Principles (E) Working Group (Working Group) shall evaluate the impact that newly adopted SSAPs will have on other NAIC publications. To that end, the Working Group shall submit a referral to any group in response to new or revised SSAPs expected to impact other NAIC groups or publications. (Instead of a referral, a blanks proposal may be sponsored by the Working Group and submitted to the Blanks (E) Working Group). These referrals and blanks proposals are only required to be approved by the chair of the Working Group prior to submission to the other groups but may be shared with and approved by all Working Group members.

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NAIC Policy Statement on Coordination of the Accounting Practices and Procedures Manual and the Annual Statement Blank

1. The purpose of the codification of statutory accounting principles (SAP) project was to produce a comprehensive guide to SAP for use by insurance departments, insurers, and auditors. Statutory accounting principles, as they existed prior to codification did not always provide a consistent and comprehensive basis of accounting and reporting. Insurance companies were sometimes uncertain about what rules to follow, and regulators were sometimes unfamiliar with the accounting rules followed by insurers in other states. This was due in part to the fact that prior to codification, accounting guidance could be found in the NAIC *Accounting Practices and Procedures Manual*, annual statement instructions, the *Financial Condition Examiners Handbook*, and various states' laws and regulations. As a result, insurers' financial statements were not prepared on a comparable basis. Now that accounting requirements have been more rigidly stipulated by the NAIC, it is imperative that the accounting requirements and the reporting and disclosure requirements remain synchronized. This is an excellent opportunity to create a system of parallel requirements. This effort has already been recognized by the NAIC/AICPA (E) Working Group. In 1999, the NAIC/AICPA (E) Working Group modified the *Model Regulation Requiring Annual Audited Financial Reports* to require the following for audited financial statements:

> Notes to financial statements. These notes shall be those required by the appropriate NAIC annual statement instructions and the NAIC *Accounting Practices and Procedures Manual*. The notes shall include a reconciliation of differences, if any, between the audited statutory financial statements and the annual statement filed pursuant to Section [insert applicable section] of the [insert state] insurance law with a written description of the nature of these differences.

2. As stated in the model regulation, the NAIC/AICPA (E) Working Group has an expectation that the requirements of the annual statement instructions and the *Accounting Practices and Procedures Manual* will be identical in all pertinent parts that are subject to audit. There is no reason to create a different set of audit requirements in the annual statement instructions when a complete and comprehensive guide to statutory accounting exists. However, it must be noted that the statements of statutory accounting principles (SSAPs) are not intended to prescribe the specific format of the detailed financial statements.

3. The scope of this policy statement is defined as follows:

> Any change to the annual statement core financials (balance sheet, income statement, cash flow and notes to the financial statements) must be reviewed by the Statutory Accounting Principles (E) Working Group to determine whether it conflicts with the disclosure requirements of the SSAPs.

4. The scope is defined in broad terms because it is very difficult to specify what constitutes a conflict with the SSAPs. For example, the renumbering of the assets page does not conflict because there is not a SSAP that prescribes the order of asset presentation. Contrast this with a seemingly innocuous proposal to modify Schedule P - Part 1 that would create a disclosure conflict with the related SSAP.

5. In order to ascertain that the requirements of the annual statement instructions and blank are in harmony with the SSAPs (as they relate solely to the core financial statements), the following procedures shall be followed:

   a. The Blanks Agenda Item Submission Form will include an interrogatory that will indicate to the Blanks (E) Working Group whether the proposal:

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i. Affects the core financial statements

ii. Conflicts with an existing SSAP

iii. Is not currently required by a SSAP

iv. Has been reviewed by the Statutory Accounting Principles (E) Working Group

b. NAIC staff supporting the Statutory Accounting Principles (E) Working Group and the Blanks (E) Working Group are charged with verifying the accuracy of the interrogatory proposed in paragraph 5.a. After NAIC staff review the proposals, they will report their findings back to the applicable groups. If NAIC staff identify issues that need further exploration or consultation, the chairs of the two working groups or certain members from each group will hold a joint meeting.

c. The Blanks (E) Working Group will reject proposals that will delete/modify information contained within the core financial statements that are required by an existing SSAP.

d. The Blanks (E) Working Group will either reject proposals that would require additional audited disclosure or audited information within the core financial statements if that same item is not required by an existing SSAP; or move it outside the core financial statements. The sponsoring party will still have the option of placing this information outside the core financial statements (e.g., general interrogatories or interrogatories to schedules) until the disclosure is included in a SSAP. If the disclosure were added to a SSAP in the future, it could be moved to the Notes to the Financial Statements and subject to audit at that time.

e. The NAIC will maintain a SSAP to annual statement cross-reference. This cross-reference will contain two significant features. First, it will list all of the SSAP disclosures and reference them to where in the annual statement the disclosure requirement is met. Second, the cross-reference will identify the annual statement components that are required by a SSAP. The cross-reference can be used by the Blanks (E) Working Group and interested parties in completing the new Blanks Agenda Item Submission Form Interrogatory.

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NAIC Policy Statement on Coordination with the Valuation Manual

1. Proposed changes to the *Valuation Manual* must be consistent with the existing referenced model laws, including the *Standard Valuation Law* (Model #820), and, to the extent determinable, with models in development. To the extent that proposed changes to the *Valuation Manual* could have an impact on accounting and reporting guidance and other requirements as referenced by the *Accounting Practices and Procedures Manual*, proposed changes must be reviewed by the Statutory Accounting Principles (E) Working Group for consistency with the *Accounting Practices and Procedures Manual,* including consistency of implementation dates. The Life Actuarial (A) Task Force or its staff support will prepare a summary recommendation that will include as appropriate an analysis of the impact of proposed changes.

2. If the Statutory Accounting Principles (E) Working Group reaches the conclusion that the proposed changes to the *Valuation Manual* are inconsistent with the authoritative guidance in the *Accounting Practices and Procedures Manual*, The Life Actuarial (A) Task Force will work with the Statutory Accounting Principles (E) Working Group to resolve such inconsistencies prior to implementation.

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NAIC Policy Statement on Coordination of the Accounting Practices and Procedures Manual and the Purposes and Procedures Manual of the NAIC Investment Analysis Office

1. The purpose of this policy statement is to detail the coordination and collaboration between the Securities and Valuation Office (SVO) and the Statutory Accounting Principles (E) Working Group (Working Group) support staff, the relationship between the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) and *Accounting Practices and Procedures Manual* (AP&P Manual) and the expectations of the Valuation of Securities (E) Task Force (VOSTF) and the Working Group.

NAIC Designations Do Not Communicate Statutory Accounting or Reporting

2. The assessment of credit risk for an obligation or asset, as specified in the P&P Manual, is a separate and distinct process from the determination of statutory accounting or reporting under the AP&P Manual. The manner in which an NAIC designation is used within statutory accounting guidance is limited to that, if any, specified in a statement of statutory accounting principle (SSAP) and cannot be derived or implied by language in the P&P Manual. Obtaining an NAIC designation does not change an investment's applicable SSAP, annual or quarterly statement reporting schedule, or override other SSAP guidance required for the investment to be an admitted asset. There are limited instances in which a SSAP specifically identifies, within its scope, the inclusion of specific SVO-identified investments. The SVO review required for an investment to be included on a SVO listing is a separate evaluation process that focuses on the structure of the investment. This process is distinct from the SVO's assessment of an investment's credit risk, which results in a NAIC designation**.** As stated in the Statutory Hierarchy, Section V of the Preamble, the AP&P Manual is the highest level of authoritative guidance.

Sources and Application of Statutory Accounting Guidance

3. The authority to determine and interpret existing statutory accounting guidance in, or to develop new statutory accounting guidance for, the AP&P Manual, is a charge assigned by the Financial Condition (E) Committee through its Accounting Practices and Procedures (E) Task Force to the Statutory Accounting Principles (E) Working Group. The application of statutory accounting guidance to any specific obligation or asset to determine its status under the AP&P Manual is the obligation of the insurance company and its management. The state of domicile is the final authority with respect to statutory accounting and reporting guidance. Deviations from the authoritative guidance in the Statutory Accounting Hierarchy are reflected as a permitted or prescribed practice.

Impact on SVO Operations

4. Because SVO analytical determinations of credit quality do not convey opinions, conclusions or informational content relative to statutory accounting status, the SVO may assign an NAIC designation to any obligation or asset that is filed by an insurer, provided that its credit quality can be assessed consistently with the polices and methodologies specified in the P&P Manual.

Communication and Coordination Between SVO and SAPWG Staff

5. The following processes are intended to assist optimum communication and coordination between the SVO and SAPWG support staff functions.

a. Maintain ongoing dialogue regarding investments, investment related SSAPs and relevant developments in the areas assigned to support staff of both groups.

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b. Maintain an ongoing dialogue relative to obligations and assets filed with the SVO, including communications about new types of obligations or assets filed with the SVO and their likely treatment under existing investment related SSAPs.

c. Maintain an ongoing dialogue relative to new obligations or assets, in which no statutory accounting guidance exists, or uncertainty exists about how current statutory accounting guidance applies to features or characteristics of the obligation or asset.

d. The NAIC Investment Analysis Office (IAO) and Financial Regulatory Services (FRS) staff shall provide notice to, and consult with, each other when either staff determines that existing technical guidance or procedures administered by the staff are no longer adequate to secure the original regulatory objective for which it was designed. Upon receipt of such notice, both staff will formulate a statement of the issues and, if possible, recommendations, and thereafter coordinate discussion between the SAPWG and the VOSTF consistent with the NAIC procedures and policies that apply to the situation. Such proposed recommendations shall be discussed consistent with the NAIC open meetings policy and any revisions to the authoritative guidance will be exposed for comment for a period of time commensurate with the significance of the change, to provide a formal forum for interested parties and regulators to provide input and allow for adequate due process.

e. Situations in which NAIC staff (SVO or FRS) are contacted directly with questions on statutory accounting application, it shall be noted that opinions of NAIC staff are not authoritative and are based on the information provided and existing authoritative statutory accounting guidance. Information and issues can be submitted to the SAPWG for consideration, as detailed in the *NAIC Policy Statement on Statutory Accounting Principles Maintenance Agenda Process.*

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Appendix G
Implementation Guide for the
Annual Financial Reporting Model Regulation

Introduction

The new requirements within the Annual Financial Reporting Model Regulation (Model) related to auditor independence, corporate governance and internal control over financial reporting became effective in 2010. The Implementation Guide (Guide) is being published to assist companies in planning and preparing for compliance with the new requirements.

The Guide is intended to supplement the Model, not to create additional requirements, by providing interpretive guidance and clarifying the meaning of terms used in the Model. Such guidance is important to ensure common understanding between insurers and regulators and to memorialize the intent of the changes. Because issues and questions will occur from time-to-time, by placing the Guide outside of the Model, maintenance can be achieved in a cost-effective way without reopening the Model especially when the issue under consideration is an interpretation of the requirements. The Guide should not be viewed as a requirement of complying with the *Accounting Practices and Procedures Manual*.

Maintaining the Guide

The responsibility of developing and maintaining the Guide resides with the NAIC/AICPA (E) Working Group with changes to the Guide following the NAIC regulatory due process. The Guide resides as an informational appendix to the NAIC *Accounting Practices and Procedures Manual* (AP&P Manual). The AP&P Manual was selected as the logical repository since the Guide provides instruction about compliance with the Model, which directly relates to financial reporting and statutory accounting.

The regulatory due process for modifying this Guide requires the NAIC/AICPA (E) Working Group to send adopted proposals to the Accounting Practices and Procedures (E) Task Force for adoption and inclusion in the AP&P Manual. If the Accounting Practices and Procedures (E) Task Force recommends substantive changes to the proposal received from the NAIC/AICPA (E) Working Group, the proposal should be returned to the NAIC/AICPA (E) Working Group for further deliberation.

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Table of Contents

The Table of Contents for the Guide mirrors that of the Model. However, not all sections of the Model require interpretive guidance. Consequently, only those sections containing guidance are contained in the Guide. The presentation of the Guide is organized by the section title with the section number of the Model appearing after the title.

Title	Section	Page
Definitions	3	2
General Requirements Related to Filing and Extensions for Filing of Annual Audited Financial Reports and Audit Committee Appointment	4	4
Qualifications of Independent Certified Public Accountant	7	4
Communication of Internal Control Related Matters Noted in an Audit	11	10
Requirements for Audit Committees	14	11
Management's Report of Internal Control over Financial Reporting	17	13
Exemptions and Effective Dates	18	18
Appendix 1	17	22

Definitions (Section 3)

Certain terms and definitions contained in the Model need no further explanation. The Guide provides additional information for preparers and users for some definitions to facilitate their understanding.

"**Audited financial report**" (D), differs from the term "financial statements" in that the Audited financial report (see Section 5 of the Model) includes the financial statements plus the report of the independent certified public accountant. "Financial statements," therefore, excludes the report of the independent certified public accountant.

"**Group of insurers**" (H), as intended for use in the Model is to recognize the variety of structures that may exist. Companies within a holding company structure, or other set of insurers identified by management, may often share common management, systems or processes. Consequently, when management asserts to the effectiveness of their internal controls, it is appropriate to make such an assertion for those companies based upon the organization management determines to be most relevant to meet the reporting requirements. Because holding company structures, and other groups of insurers, can be complex and organized to meet corporate objectives, that structure may not align with the organizations that are responsible for managing and preparing the financial statements of the insurer. The Model provides flexibility to insurers to identify a "Group of insurers" for purposes of evaluating the effectiveness of their internal control over financial reporting. In determining the appropriate scope and level of testing for systems that are shared by a group of insurers, management is not required to expand the scope or perform additional testing that would be redundant for each legal entity included within the group of insurers. To the extent that a specific internal control or system is unique to and has a material impact on the preparation of the audited statutory financial statements of a legal entity included in a group of insurers and the legal entity exceeds the premium thresholds contained in Section 17, that control or system is to be included in management's evaluation of internal controls.

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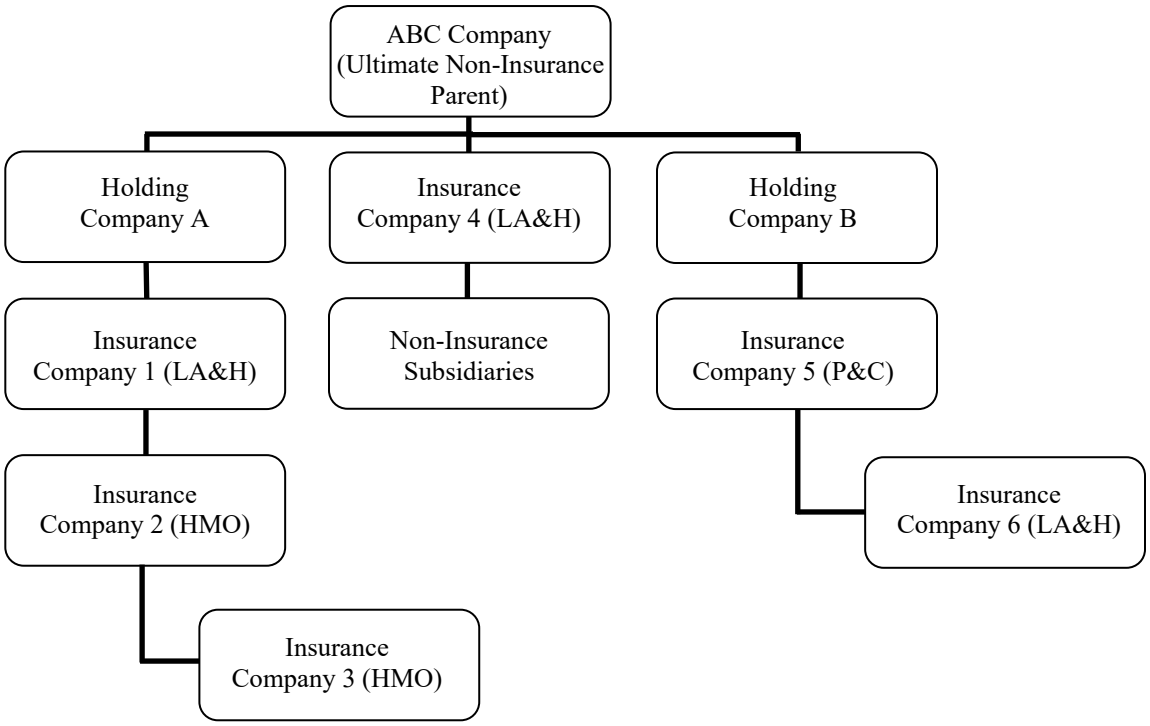
A "Group of insurers" that has been granted approval to file audited statutory consolidated or combined financial statements of a group of insurers (as described in Section 8) may set the scope and level of testing for purposes of determining effectiveness of internal controls over financial reporting consistent with the basis on which the audited statutory financial statements for the Group are prepared (i.e., at the combined or consolidated level).

The following example is intended to illustrate various ways that a "Group of insurers" could be determined. The example is not intended to be limiting in any way. Rather, it is intended to show the flexibility to be in compliance with the Model. Insurers are encouraged to notify the Commissioner of its initial "Group of insurers" and any subsequent changes to such group.



1. "Group of insurers" could be established at the ultimate parent level, i.e., one report of the effectiveness of internal controls for all insurers in the group-insurance companies 1-6.

2. Two "Group of insurers" could be established at the holding company level, i.e., holding company A and B. In this case, a separate report would be required for holding company A, holding company B, and if it met the reporting threshold, insurance company 4 since it is not in either group.

3. Two "Group of insurers" could be established based upon the type of insurance company, i.e., LA&H companies 1, 4 and 6 could be one group and HMO companies 2 and 3 in the second group. In this case, a separate report would be required for the LA&H companies, the HMO companies and if it met the reporting threshold, insurance company 5 since it is not in either group.

4. Two "Group of insurers" could be established based upon the way the entities are managed. For example, companies, 1, 2, 3 and 5 have the same management while companies 4 and 5 have common management.

5. If management elects not to identify a "Group of insurers" for purposes of evaluating the effectiveness of internal control over financial reporting then each reporting entity meeting the reporting requirements of Section 17 would prepare such a report.

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"**Internal control over financial reporting**" (I), as defined in the Model is intended to have the same meaning as understood in the public sector to comply with the requirements of the Sarbanes-Oxley Act of 2002. Because some terms might not be fully defined and to avoid misunderstanding, this Guide attempts to clarify such terms. For example, the word "reliability" used in the phrase "reliability of financial statements" has the same meaning as that contained in the generally accepted accounting principles (GAAP) framework, Statement of Financial Accounting Concepts Two. This Statement is referenced in the Preamble, Part III, paragraph 24 of the AP&P Manual.

General Requirements Related to Filing and Extensions for Filing of Annual Audited Financial Reports and Audit Committee Appointment (Section 4)

Section 4D stipulates that each insurer required to file an annual Audited financial report pursuant to the Model shall designate a group of individuals as constituting its Audit committee. Section 4D further states that the Audit committee of an entity that controls an insurer may be deemed to be the insurer's Audit committee for purposes of this regulation at the election of the controlling person. The definition of Audit committee in Section 3 of the Model references Section 14E for exercising this election. However, a disclaimer within Section 14 of the Model indicates that the section shall not apply to SOX Compliant Entities or wholly-owned subsidiaries of SOX Compliant Entities. Regardless of the disclaimer, in order to comply with the second sentence in Section 4D, the Audit committee of any entity that controls an insurer (a SOX Compliant entity or a non-SOX Compliant Entity) may be deemed to be the insurer's Audit committee at the election of the controlling person, and only if such election is completed in the manner outlined in Section 14E.

The responsibility of the Audit committee is defined in Section 14 of the Model. Section 14 states that each member of the Audit committee shall be a member of the Board of Directors and sets forth the requirements for the proportion of independent Audit committee members based on the insurer's direct written and assumed premiums. The definition of an independent Audit committee member is outlined in Section 14.

Qualifications of Independent Certified Public Accountant (Section 7)

Lead Audit Partner Rotation Requirement (Section 7D)

Purpose
The purpose of this section is to provide companies and their independent accountants with guidance to enable an orderly transition in meeting the revised lead audit partner rotation requirements as set forth in Section 7.

Background
Section 7 provides certain limitations on the number of years an audit partner may serve in the capacity of lead audit partner for an insurance company audit. Previously, the lead audit partner was permitted to serve for seven consecutive years in that capacity with a two-year break in service. Under the revised Model "…the lead …audit partner (having primary responsibility for the audit) may not act in that capacity for more than five (5) consecutive years. The person shall be disqualified from acting in that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five (5) consecutive years."

The new rotation requirements under Section 7 are effective beginning with audits of the 2010 financial statements. The rotation requirements of the Model and the interpretative guidance provided are applicable for statutory reporting and regulatory purposes. An insurer and its affiliates that are subject to the rotation requirements of the Securities and Exchange Commission (SEC) and Public Company Accounting Oversight Board (PCAOB) must also continue to comply with those rotation requirements.

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Relief from the Lead Audit Partner Rotation Requirement (Section 7D)

The Model states:

> An insurer may make application to the Commissioner for relief from the above rotation requirement on the basis of unusual circumstances. This application should be made at least thirty (30) days before the end of the calendar year. The Commissioner may consider the following factors in determining if the relief should be granted:
>
> (a) Number of partners, expertise of the partners or the number of insurance clients in the currently registered firm;
>
> (b) Premium volume of the insurer; or
>
> (c) Number of jurisdictions in which the insurer transacts business.

The following examples illustrate circumstances that the Commissioner may consider in determining if relief from the lead partner rotation requirement shall be granted:

1. No other partners in the firm's local office have the qualifications to serve as lead audit partner and the use of a qualified partner resident in another location could result in increased audit risk and higher audit fees.
2. Limited number of partners in the firm that have the qualifications to serve as the lead audit partner.
3. Switching firms could result in increased audit risk due to the new engagement team's lack of familiarity with the insurer.
4. Limited availability of other firms in a particular location with the requisite expertise.
5. The regulator believes that complex issues at an insurer make a particular partner best suited to continue as lead audit partner.
6. Short-term relief due to the occurrence of an unforeseeable event that renders a partner unable to continue as the lead audit partner on the engagement.
7. Short-term relief due to unexpected delays in the state's licensing or admission process that prevent the "new" lead audit partner from assuming that role.

Also, the granting of transitional relief may be warranted when the non-insurance parent or ultimate parent of an insurance company is an SEC registrant and the current lead audit partner on the SEC registrant has completed his or her rotation as the lead audit partner on insurance subsidiaries prior to completing his or her five-year rotation as the lead partner on the audit of the GAAP financial statements of the SEC registrant. In this situation the relief would allow the lead audit partner to complete his or her rotation on the SEC registrant as long as he or she no longer acts in the capacity of lead audit partner for any insurance subsidiaries and/or any downstream affiliates of the insurance subsidiaries.

Frequently Asked Questions (Section 7D)

Following are a series of frequently asked questions to assist companies and their independent accountants in interpreting this guidance. Dates provided refer to the year of financial statements under audit.

In determining when the lead audit partner must rotate, consecutive time served in the capacity of lead audit partner prior to the effective date of these rules would be counted (i.e., the lead audit partner is not

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afforded a "fresh start"). If the lead audit partner completed the two-year break in service required by the previous version of the Model prior to the effective date of these rules, the partner is eligible to resume service as a lead audit partner for a five-year period and need not wait additional years to accomplish a five-year break in service.

1. 2010 would be the fifth year that a partner would serve as lead audit partner of an insurance company. Would that partner be able to complete the 2010 year-end audit?

   Yes. The partner would be able to complete the 2010 year-end audit; however, the partner would be required to rotate off the engagement after the 2010 year-end audit.

2. 2010 would be the sixth or seventh year that a partner would serve as the lead audit partner. Would that partner be able to serve in that capacity for the 2010 audit?

   No. The partner would be required to rotate off for the 2010 year-end audit. In determining when the lead audit partner must rotate, consecutive time served in the capacity of lead audit partner since the most recent two-year break in service prior to the effective date of these rules would be counted.

3. If a partner serves as the concurring partner from 2007 – 2010, can that partner serve as the lead audit partner in 2011? If so, for how many years?

   Yes. The Model does not prohibit a partner that has served as the concurring partner from subsequently serving as the lead audit partner. The time served as concurring partner does not count towards the five-year limitation. In the situation above, the partner would be permitted to serve as lead audit partner from the 2011 year-end audit through the 2015 year-end audit.

4. Can a lead audit partner serve as the concurring review partner during the required five-year break in service?

   Yes. The Model specifies that a partner may not act in "that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five (5) consecutive years" where "that" refers to the role of lead audit partner. Therefore, the Model does not prohibit that partner from serving as concurring partner during that partner's five-year break in service.

5. During the five-year break in service, can a partner serve as lead audit partner on an insurance company affiliate of that company?

   No. The Model specifies a "person shall be disqualified from acting in that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five (5) consecutive years." The phrase "insurance subsidiaries or affiliates" is interpreted to mean any subsidiaries and affiliates (whether insurance or non-insurance).

6. If a lead audit partner serves for six years prior to the effective date of the revised Model (year-end audits from 2003 – 2008) then rotates off the engagement for two years (year-end audits 2009 – 2010), can that partner serve for five additional consecutive years (year-end audits from 2011 – 2015) as the lead audit partner?

   No. The requirement for a break in service of five consecutive years becomes effective for the 2010 year-end audits. If the partner has not completed the two-year break in service prior to the effective date of the new requirement, the partner becomes subject to the new requirement and must complete a five-year break in service. However, if the lead audit partner completes the two-year break in service by 2009 instead of 2010, that partner would be permitted to resume the lead audit partner role in 2010.

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7. A partner that served seven years as lead audit partner has not worked on the engagement for two years. Assuming 2010 otherwise would be year three of the break in service, can that partner assume the lead audit partner role for the 2010 year-end audit?

   Yes. The requirement for the five-year break in service starts with engagement years beginning 2010. Prior to 2010, the rotation requirement is for a two-year break in service.

8. If a lead audit partner served in that capacity for years 2007 – 2009 and was not on the engagement (or that of any subsidiary or affiliate) for 2010, would that partner have to complete a five-year break in service before again serving as the lead audit partner?

   No. However, the partner could only serve as the lead audit partner for two more years since the partner has already served three years on this engagement.

9. Can a former lead audit partner currently in a break in service continue to serve the client in a role other than the lead audit partner, for example concurring partner or auxiliary partner, such as tax review partner or other assisting role?

   Yes. The Model auditor rotation rules apply only to the role of lead audit partner on the audit of the insurance company and its insurance subsidiaries or affiliates.

10. 2010 is the first year that a partner serves as the lead audit partner on an insurer. The partner serves as the lead audit partner on that insurer for year-end audits of 2010 – 2012; however, during 2013 – 2015 that partner does not serve as the lead audit partner on that insurer or any of its affiliates. If that partner again serves the insurer (or any of its insurance subsidiaries or affiliates) as the lead audit partner for 2016 year-end audit, when must that partner rotate off the engagement?

    The partner is permitted to serve as the lead audit partner for the 2016 and 2017 year-end audits and must begin a five-year break in service with the year-end 2018 audit. The break in service during 2013 – 2015 would be for less than the five-year period required by the Model. In order for the partner to be permitted to begin a new five-year service period as lead audit partner on the insurer or any of its insurance subsidiaries or affiliates, a full five-year break in service is required to be completed by that partner.

11. How is service as the lead audit partner on the audit of the GAAP-basis financial statements of a separate account evaluated under the Model?

    A separate account is not a legal entity, but an accounting entity with accounting records for variable contract assets, liabilities, income, and expenses segregated as a discrete operation within the insurance company. Therefore, the separate account is considered to be an insurance affiliate for purposes of applying the Model.

    If the insurer is a part of a mutual fund complex, the mutual funds are considered to be non-insurance affiliates even if held as investments in the insurer's separate accounts.

12. An insurer changes to a new independent accounting firm. At the same time, the lead audit partner for that insurer joins the new independent accounting firm. Would the lead audit partner's time at the previous accounting firm count toward the five-year rule at the new accounting firm?

    Yes. The rule specifically applies to the lead audit partner and not the independent accounting firm.

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13. Some firms have individuals that are CPAs but not partners (i.e., nonequity participants such as directors or principals) that serve in the role of the lead audit partner. Can such a CPA serve in the role of the lead audit partner of an insurance company?

    Yes. The Model defines the lead audit partner as the individual having "primary responsibility for the audit." Whether this capacity is served by a partner or other CPA with the equivalent qualifications is at the discretion of the independent accounting firm. As such, the individual would be subject to the rotation requirements of the lead audit partner under Section 7.

Questions 14 through 23 are based on the following hypothetical fact pattern and assume there are no public registrants in the group.

Neither insurance subsidiary A nor insurance subsidiary B has any investment in non-insurance subsidiary C.

- Partner Smith served as the lead audit partner on non-insurance holding company H for six years through the 2010 year-end audit.
- Partner Jones served as the lead audit partner on insurance subsidiary A for four years through the 2010 year-end audit.
- Partner Little served as the lead audit partner on insurance subsidiary B for three years through the 2010 year-end audit.
- Partner Brown served as the lead audit partner on non-insurance subsidiary C for two years through the 2010 year-end audit.
- Partner Miller served as the lead audit partner on insurance subsidiary D for three years through the 2010 year-end audit.
- Partner King served as the lead audit partner on non-insurance subsidiary E for seven years through the 2010 year-end audit.

14. Can Partner Smith rotate from serving as the lead audit partner on non-insurance holding company H to serving as the lead audit partner on insurance subsidiary B for the 2011 year-end audit?

    Yes. The limitation under Section 7 initiates with service as the lead audit partner of an *insurer*. Assuming Partner Smith has not previously served as the lead audit partner on an insurer, he or she can then serve as the lead audit partner on insurance subsidiary B or any of its affiliates for up to five years.

15. Can Partner King rotate from serving as the lead audit partner on non-insurance subsidiary E to serving as the lead audit partner on insurance subsidiary B for the 2011 year-end audit?

    Yes. The limitation initiates with service as the lead audit partner of an *insurer*. Assuming Partner King has not previously served as the lead audit partner on an insurer, he or she can then serve as the lead audit partner on insurance subsidiary B or any of its affiliates for up to five years.

16. Can Partner Brown rotate from serving as the lead audit partner on non-insurance subsidiary C to serving as lead audit partner on insurance subsidiary B for the 2011 year-end audit?

    Yes. The limitation initiates with service as the lead audit partner of an *insurer*. Assuming Partner Brown has not previously served as the lead audit partner on an insurer, he or she can then serve as the lead audit partner on insurance subsidiary B or any of its affiliates for up to five years. Therefore, Brown could serve insurance subsidiary B for five years beginning with the 2011 year-end audit.

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17. Can Partner Brown rotate from serving as the lead audit partner on non-insurance subsidiary C to serving as lead audit partner on Holding Company H for the 2011 year-end audit?

    Yes. C is a non-insurance subsidiary and H is a non-insurance holding company; therefore, assuming Partner Brown has not previously served as the lead audit partner on an insurer, the partner rotation requirements of Section 7 are not applicable relative to non-insurance subsidiary C and non-insurance holding company H.

18. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner for insurance subsidiary B for the 2011 year-end audit?

    Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate).

19. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner on non-insurance subsidiary C for the 2011 year-end audit?

    Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

20. Can Partner King rotate from serving as the lead audit partner on non-insurance subsidiary E to serving as the lead audit partner on non-insurance subsidiary C for the 2011 year-end audit?

    Yes. E is a non-insurance subsidiary and C is a non-insurance subsidiary; therefore, assuming Partner King has not previously served as the lead audit partner on an insurer, the partner rotation requirements of Section 7 are not applicable relative to non-insurance subsidiary E and non-insurance subsidiary C.

21. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner on non-insurance subsidiary E for the 2011 year-end audit?

    Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

22. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner on insurance subsidiary D for the 2011 year-end audit?

    Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

23. Can Partner Little rotate from serving as the lead audit partner on insurance subsidiary B to serving as the lead audit partner on non-insurance subsidiary E for the 2011 year-end audit?

    Yes. However, Little can only serve for two years due to three years prior service as the lead audit partner on insurance subsidiary B (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

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Prohibited Services (Section 7 G)

The Model does not allow the Commissioner to accept an Audited financial report prepared by an accountant who provides the insurer, contemporaneously with the audit, non-audit services as outlined within the Model. One of the prohibited services outlined in the Model consists of bookkeeping or other services related to the accounting records or financial statements of the insurer. The prohibition in this area should include, but is not limited to, services related to the preparation of the Annual Statement to be submitted by the insurer. However, the drafting of the Audited financial report would not be prohibited, provided that the accountant does not assume decision-making authority (e.g., approval of journal entries) in compiling the draft report.

Communication of Internal Control Related Matters Noted in an Audit (Section 11)

In addition to the annual Audited financial report, each insurer must furnish the Commissioner with a written communication as to any unremediated material weakness in its internal control over financial reporting noted during the audit. The communication is prepared by the accountant within 60 days after the filing of the annual Audited financial report and is filed by the insurer. Recognizing it may not always be practical, insurers are encouraged to file the communication concurrently with the filing of the annual Audited financial report for those years in which the insurer is aware that a financial condition examination has been scheduled. The insurer is required to provide a description of remedial actions taken or proposed to correct unremediated material weaknesses, if the actions are not described in the accountant's communication.

The Model requires that the Commissioner be notified when unremediated material weaknesses in internal control over financial reporting were noted during the audit. Previous versions of the Model required such communication when any significant deficiencies in internal control over financial reporting were noted during the audit, whether remediated or not. This distinction is important because of the level of severity of the internal control deficiency that is applicable to each term. The terms "material weakness" and "significant deficiency" have the same meaning respectively as used in PCAOB or American Institute of Certified Public Accountants (AICPA) auditing literature - PCAOB Auditing Standard No. 5, An Audit of Internal Control over Financial Reporting That is Integrated With an Audit of Financial Statements or AICPA AU Section 325, Communicating Internal Control Matters Identified in an Audit (see Section 17E of this Guide for the definitions of material weakness and significant deficiency that are included in the auditing literature). However, the insurer is expected to maintain information about significant deficiencies that were communicated by its auditors and such information should be available for review during the financial condition examination.

Effective for audits as of December 31, 2021, and thereafter, the information required in Section 12 of the MAR required to be communicated by the accountant should be supplemented by providing both the name of the current lead audit partner and the year at which he or she began serving in that capacity. For the purpose of maintaining confidentiality, this information will not be included in the annual letter of qualifications, but instead shall be included in the internal control communication required in Section 11 of the MAR by the accountant as a footer or under the firm signature as follows:

> The engagement partner, [name], has served in that capacity with respect to the Company since [year that current term started],

Consistent with the Drafting Note[1] to Section 11 of the MAR, the information provided on the engagement partner shall remain confidential.

[1] The insurer is expected to maintain information about significant deficiencies communicated by the independent certified public accountant. Such information should be made available to the examiner conducting a financial condition examination for review and kept in such a manner as to remain confidential.

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The following is an example of the type of communication that an insurer should prepare to communicate the remedial actions taken or proposed to correct a material weakness in its internal control over financial reporting noted during an audit.

Communication of Internal Control Related Matter Noted in an Audit - Sample

Honorable Commissioner
State of Domicile Insurance Department
State of Domicile

Dear Honorable Commissioner:

During the audit completed for the year ended December 31, 20XX, for XYZ Holding Company Inc ("XYZ"), a material weakness was noted in XYZ's internal control over financial reporting related to the calculation of insurance reserves. Due to the manner in which the data for homeowners policies are captured by the systems used in its Southeastern US regional office, changes in XYZ's estimate of insurance reserves for certain policies are not reviewed by XYZ's Actuarial Department prior to being recorded in the company's accounting records.

A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. In connection with the weakness noted above, XYZ's management has taken remedial actions to change its procedures for coding policies issued in the states affected so that all homeowners' policy data are included in the Actuarial Department review of estimate of insurance reserves. This change was effective on July 1, 20XX.

Should you have any questions regarding this matter, please do not hesitate to contact me at the number noted above.

Regards,

XYZ Holding Company, Inc.

Requirements for Audit Committees (Section 14)

A disclaimer within Section 14 of the Model indicates that the section shall not apply to SOX Compliant Entities or wholly-owned subsidiaries of SOX Compliant Entities. This disclaimer was placed within the Model to avoid conflicts between the independence requirements of the Model and those required of public companies under Section 301 of the Sarbanes Oxley Act of 2002. The expectation of regulators in developing this disclaimer was that the same independent Audit committee required of public companies under Section 301 would be deemed to be the insurer's Audit committee for purposes of this regulation (pursuant to Section 4D of the Model) or would participate in the oversight of the insurers within the group. Therefore, if material weaknesses, significant deficiencies and/or significant solvency concerns are identified at the legal entity level, the independent Audit committee should be involved in addressing these issues, regardless of their materiality at the consolidated, parent company level.

Independence of an Audit Committee Member (Section 14C)

A policyholder would be considered "independent" unless they receive direct compensation from the insurer for other unrelated services.

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A person who is otherwise considered independent and also serves on the Board of Directors of a contracting entity (e.g., medical provider, vendors, banks, etc.) is considered independent.

An otherwise non-independent member of the Board of Directors is considered independent for Audit committee purposes if state law requires participation on the Board (e.g., Medical providers) as long as the member is not an officer or employee of the insurer or one of its affiliates.

Notification letter (Section 14E)

In accordance with Section 14E, upon the initial election by the insurer to designate the Audit committee of an entity that controls the insurer as its Audit committee, the insurer shall provide written notification to the Commissioner of the affected insurer. This notification shall identify the controlling entity and the basis for the election. This election remains in effect for perpetuity, until rescinded, at which time written notification would need to be provided to the Commissioner of the insurer. The notification letter should be timely filed with the Commissioner by the ultimate controlling person prior to the issuance of the statutory Audited financial report. However, each of the affected insurers (i.e. those that will have an Audit committee designated by its ultimate controlling person) that is subject to the provisions of Section 14 shall ensure that the notification letter is filed with the Commissioner. Absence such filing, each of the affected insurers would be individually responsible for complying with Section 14. For example, referring to the "Group of insurers" chart in Section 3, if the ABC Company is the ultimate controlling person and elects to have its Audit committee serve as the Audit committee for insurance company 5, then ABC Company would file the notification letter (insurance company 5 would have to ensure that the notification letter is filed or comply with Section 14 as a single entity). Once submitted, the election remains in effect until rescinded. The following example illustrates the reporting requirement.

> The XYZ insurance company (e.g., insurance company 5) is an indirect subsidiary of and controlled by ABC Company. ABC Company has an independent Audit committee comprised of directors of ABC Company. XYZ insurance Company has elected to designate the Audit committee of ABC Company as the Audit committee of XYZ insurance Company for purposes of complying with Audit committee requirements of the Annual Financial Reporting Model Regulation.

(Signed)_____ (Date)_____
(XYZ Insurance Company Chief Executive Officer)
(Signed)_____ (Date)_____
(ABC Company Chief Executive Officer)

Transitional Guidance (Section 14G)

Once a company exceeds the requisite thresholds for Audit committee requirements contained in Section 14 of the Model, it is required to comply with the Audit committee requirements by January 1 following one (1) complete calendar year. The following are examples of transitional period requirements.

A: Company surpasses $300 million threshold:

ABC Insurance Company has reached the $300 million requisite threshold in its December 31, 2011, audited statutory statement and therefore will be required to meet "majority (50% or more) member independence" Audit committee requirements by January 1, 2013, providing the company necessary time for recruitment and approvals.

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B: Company surpasses $500 million threshold:

ABC Insurance Company has subsequently reached the $500 million requisite threshold in its December 31, 2014, audited statutory statement and therefore will be required to meet the "Supermajority (75% or more) member independence" Audit committee requirements by January 1, 2016.

C: Company drops below threshold amount:

If ABC Insurance Company has penetrated the requisite $500 million threshold and has been in compliance with the requirements but subsequently drops below the $500 million threshold, e.g., $450 million in its December 31, 2018, audited statutory statements, the company would be subject to the "majority (50% or more) member independence" requirement and could reduce the Audit committee independence in 2019. Companies, however, are encouraged to structure their Audit committees with at least a supermajority of independent Audit committee members.

Hardship Waiver (Section 14H)

An insurer may make application to the Commissioner for a waiver from the Section 14 requirements based upon hardship. Examples may include, but are not limited to, requests based on the business type of the entity, the availability of qualified board members, or the ownership (e.g., entities owned by non-profit health systems) or organizational structure of the entity. If the application for a waiver is approved, the insurer would file, with its annual statement filing, the approval for relief from Section 14 with the states that it is licensed in or doing business in and the NAIC. If the nondomestic state accepts electronic filing with the NAIC, the insurer would file the approval in an electronic format acceptable to the NAIC.

Management's Report of Internal Control over Financial Reporting (Section 17)

Premium Threshold (Section 17A)

The term "direct written premium" is frequently associated with the property/casualty business. While the Model continues to use the term, it raises the question for other businesses, e.g., life and fraternal, what is the appropriate measure for assessing compliance? The following examples have been developed to illustrate the computation since the starting point is the audited financial statements of the reporting entity, and it is possible that the amount reported may not be consistent with written premium as reported in the regulatory reporting blank.

The annual direct written and assumed premium:

- will be derived from the annual Audited financial report of an individual insurer, as of December 31 immediately preceding;
- are generally reported in the Statement of Operations of the Audited Financial Report on an 'earned' and a 'net of reinsurance ceded' basis;
- will be computed by making the following adjustments:

P/C, Health and Title entities:

	$
Premiums earned (Statement of Income in Audited financial report)	A
Add/Deduct: Change in unearned premium	B
Add: Reinsurance ceded	C
Direct written and assumed premium *	D=A+B+C

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*Note: Direct written and assumed premium would be reduced by any premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program

- A - Premiums earned per the Statement of Income will generally equal the Annual Statement, Page 4.
- B - Change in unearned premium is the difference between the current period amount and the prior year-end amount reported in the liabilities section of the balance sheet. The amount may also be derived from other company prepared exhibits.
- C - Reinsurance ceded may be derived from the notes to the Audited financial report, if disclosed, or other company prepared exhibits or schedules. If the Statement of Income or Statement of Operations separately presents reinsurance ceded, an adjustment is not required.
- D - Must be equal to, or greater than, $500 million in order to be subject to Section 17 reporting.

Life and Fraternal entities:

	$
Premiums earned (Statement of Operations in Audited financial report)	A
Add: Reinsurance ceded	B
Direct written and assumed premium	C=A+B

- A - Premiums earned per the Statement of Operations will generally equal the Annual Statement, Page 4.
- B - Reinsurance ceded may be derived from the notes to the Audited financial report, if disclosed, or other company prepared exhibits or schedules. If the Statement of Operations separately presents reinsurance ceded, an adjustment is not required.
- C - Must be equal to, or greater than, $500 million in order to be subject to Section 17 reporting.

Companies in an RBC Level Event or in Hazardous Financial Condition (Section 17B)

For purposes of this subsection, the phrase “RBC level event” refers to any of the regulatory action levels described in the Risk-Based Capital requirements or the trend test. For example, if the reporting entity’s total adjusted capital is equal to or less than 200% of the required risk-based capital, the result would trigger regulatory action.

Management’s Report of Internal Control over Financial Reporting (Sections 17C & 17D)

Management must annually provide their domiciliary insurance department with a report on internal controls over the statutory financial statement process. Recognizing it may not always be practical, insurers are encouraged to file the report concurrently with the filing of the annual Audited financial report for those years in which the insurer is aware that a financial condition examination has been scheduled. The elements to be included in the report are outlined in 17D.

As outlined in Section 17C, an addendum is required for all reports that rely on a Section 404 Report (Sarbanes-Oxley). The Model states that the Section 404 Report means management’s report on internal control over financial reporting as defined by the SEC and the related attestation report of the independent certified public accountant. However, in 2010, the Dodd-Frank Act exempted non-accelerated SEC filers (those reporting companies that do not meet the definition of either an “accelerated filer” or a “large accelerated filer” under Exchange Act Rule 12b-2.) from the requirement to obtain the related attestation report of the independent certified public accountant. As such, non-accelerated SEC filers may file a

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Section 404 Report that does not include an attestation report of the independent certified public accountant, along with the appropriate addendum, to fulfill requirements in this area.

Alternately, insurers may utilize a report received as a result of work performed in accordance with Statement of Standards in Attestation Engagements (SSAE) No. 15 in a similar fashion to a Section 404 Report. As such, there are two main types of reports that can be provided:

- Reports from entities that have complied with all required elements of Section 404 of the Sarbanes-Oxley Act (or have received an SSAE No. 15 report) either as a requirement or on a voluntary basis.
- Reports from entities that have not complied with Section 404 of the Sarbanes-Oxley Act (or have not received an SSAE No. 15 report).

Appendix 1 of this guide provides examples of Management's Report of Internal Controls over Financial Reporting utilizing various facts and circumstances.

Section 17D(2): Management must make an assertion regarding the effectiveness of the insurer's Internal control over financial reporting to the best of its knowledge and belief after diligent inquiry. For purposes of filing the report, "diligent inquiry" means conducting a search and thorough review of relevant documents which are reasonably likely to contain significant information with regards to Internal control over financial reporting and making reasonable inquiries of current employees and agents whose duties include responsibility for Internal control over financial reporting.

Section 17D(5): The report must disclose any unremediated material weaknesses in Internal control over financial reporting that exist as of the balance sheet date. If the insurer or Group of insurers has identified an unremediated material weakness, management is not permitted to conclude that its Internal control over financial reporting is effective and it must include a description of the nature of any unremediated material weakness in the report. December 31 is used as the measurement date to whether a material control weakness is unremediated for purposes of reporting under this section of the Model.

Section 17D(6): Users of the report should be aware of the inherent limitations in Internal control over financial reporting. PCAOB Auditing Standard No. 5, An Audit of Internal Control over Financial Reporting That is Integrated With an Audit of Financial Statements provides the following description of such inherent limitations:

> Internal control over financial reporting has inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements will not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Additionally, readers of the report should be aware that projecting management's assertion regarding the effectiveness of Internal control over financial reporting to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate.

Section 17D(7): The report must include signatures of the chief executive officer and chief financial officer (or the equivalent position/title). If a report is being filed on behalf of a Group of insurers, management should identify the officeholders (i.e., the CEO and CFO of Company ABC) that have the

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authority to sign the report on behalf of all of the legal entities being reported upon within the Group of insurers.

Basis for Management's Review and Assertions (Section 17E)

One of the primary reasons for the new Section 17 of the Model is to bring additional focus and attention to internal control over financial reporting. Financial reporting is the underpinning of many of the solvency oversight activities of insurance regulators. Section 17 of the Model identifies management's responsibilities for internal control over financial reporting and provides regulators additional assurances of the effectiveness of internal control practices in a cost-effective manner.

The basis for Management's Report of Internal Control over Financial Reporting shall be subject to insurance departments' financial condition examinations. Because of this and other solvency tools available to regulators, there is no requirement that the independent certified public accountant be engaged to perform an examination of the effectiveness of internal control over financial reporting. However, Section 9 requires the independent public accountant to consider (as that term is defined in AICPA Statement on Auditing Standards (SAS) No. 102, Defining Professional Requirements in Statements on Auditing Standards, or its replacement) the most recently available Management's Report of Internal Control over Financial Reporting in planning and performing the audit of the statutory financial statements. SAS No. 102, paragraph 4 states, "If a SAS provides that a procedure or action is one that the auditor "should consider," the consideration of the procedure or action is presumptively required, whereas carrying out the procedure or action is not." AU Section 319 of the Professional Standards of the AICPA, Consideration of Internal Control in a Financial Statement Audit, requires that the auditor obtain an understanding of internal control sufficient to plan and execute the audit. It is in this context that the auditor is required to "consider" management's report. There is no requirement that the auditor test or otherwise use management's report.

The Model does not mandate a specific framework for management's review and evaluation of internal controls. SEC registrants typically (but are not required to) use the COSO Internal Control-Integrated Framework in assessing the effectiveness of internal control over financial reporting. The COSO-sponsored "Enterprise Risk Management-Integrated Framework" and the PCAOB Guidance for Smaller Public Companies Reporting on Internal Control over Financial Reporting are other examples of relevant literature companies may want to consider in applying such a framework. Under the Model, however, management, when making its assessment and preparing its report, has discretion as to the nature of the internal control framework used. Insurers shall have flexibility as to the frequency and scope of testing activities and the documentation provided upon examination to support the assertions. Management should assess and select an appropriate framework or approach based upon its business risks and objectives.

Management's assertions about the effectiveness of internal controls enhance oversight and understanding of insurer solvency by allowing regulators to have greater confidence in the accuracy of financial reporting, which also provides a benefit to policyholders and creditors. An expected benefit of this enhancement, where internal controls are effective, is that financial examinations will become more efficient and risk-focused.

Management's Report of Internal Control over Financial Reporting may span more than one legal entity. Because internal controls are primarily about processes and these processes are often applied across multiple legal entities within an organization, (e.g., investment systems, premium and loss/benefit systems, and financial reporting processes), management may consider common processes and the associated controls when determining the Group of insurers for reporting purposes.

The Model provides flexibility in meeting the requirements of Section 17D and E. The controls included in the scope of management's report should only include those controls deemed significant or critical by management. The following examples represent aspects and components of internal control that insurers

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may want to consider when making the assertions and determining relevant documentary evidence. These are not intended to serve as, and should not be considered, requirements:

- The internal control environment including oversight provided by the Audit committee of the Board of Directors. Insurers may want to consider how they can demonstrate "Tone at the Top." The insurer's compliance programs, code of conduct and the processes for reporting policy exceptions and overrides of controls may also be appropriate to consider.

- The risk assessment process utilized and identification of the areas of potential material internal control risk related to the financial statement. Risk areas that one might typically find for an insurance enterprise include:

    - Investments (including capital expenditures)
    - Policy and Claim Reserves
    - Benefit Payments
    - Premiums / Agent's Balances
    - Reinsurance
    - Related Party (Affiliate) Transactions
    - Operating Expenses/Taxes

- The control activities in place including procedures over financial reporting, which in management's judgment are appropriate under the circumstances. These might include the daily or monthly controls management relies upon in the normal course of its activities. They would also include any SAS 70 reports received from vendors upon which management relies. General information systems and technology controls might also be considered.

- The monitoring and testing processes used in the normal course of business to ascertain that the internal controls are in place and are working as intended. Insurers may want to consider describing the purpose, function or role of an internal audit department and/or describe other self-audit and analysis activities.

- The information and communication processes, including the frequency of reporting and monitoring activities and communication of internal control responsibilities.

Section 17D(5) of the Model indicates that if one or more unremediated material weaknesses in Internal control over financial reporting exists as of the balance sheet date, then management is not permitted to conclude that internal control over financial reporting is effective and it must include a description of the nature of any unremediated material weaknesses in the report. For purposes of this determination, material weakness has the same meaning as used in PCAOB or AICPA auditing literature – PCAOB Auditing Standard No. 5, An Audit of Internal Control over Financial Reporting That is Integrated With an Audit of Financial Statements or AICPA AU Section 325, Communicating Internal Control Related Matters Identified in an Audit. Such guidance provides the following definitions:

> Significant Deficiency – A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
>
> Material Weakness – A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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Insurers filing Management's Report of Internal Control over Financial Reporting as a Group of insurers may want to also consider identifying or documenting common systems and controls used by multiple companies within an insurance holding company system and how such information was used in the development of the Group of insurers for reporting purposes.

To allow insurers to comply with Section 17 in a cost-effective manner, management may base its assertions, in part, upon its review, monitoring and testing processes performed in the normal course of it activities. Management may also consider diligent inquiry of key process owners throughout the organization to provide additional assurance as to the operating effectiveness of its internal control over financial reporting. For purposes of filing the report, "diligent inquiry" means conducting a search and thorough review of relevant documents which are reasonably likely to contain significant information with regards to Internal control over financial reporting and making reasonable inquiries of current employees and agents whose duties include responsibility for Internal control over financial reporting.

Exemptions and Effective Dates (Section 18)

Hardship Waivers (Section 18A)

Notwithstanding any other provision of the Model, an insurer may make written application to the Commissioner for waiver from any or all provisions of the Model based upon financial or organizational hardship. For example, the Commissioner could under this section grant a waiver of the Section 14B audit committee independence requirements to a company exceeding the $500 million premium threshold, even though the Section 14H waiver would not apply. This exemption is granted at the discretion of the Commissioner, and may be granted at any time for a specified period or periods.

Specific Effective Dates (Section 18F)

An insurer will be required to file a Section 17 report if the insurer exceeds the premium threshold (as defined in Section 17A.)

1. Assume the insurer reports premiums as follows (note that the direct written and assumed premium in these examples would be reduced by any premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program) :

$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7	450.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	526.3	545.8	578.0

In the above example, the insurer has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3.

2. Assume the insurer reports premiums as follows:

$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	380.5	390.8	410.5	425.7
Add: Reinsurance ceded	100.5	110.7	115.7	115.8	120.1
Gross direct written and assumed premium	450.8	491.2	506.5	526.3	545.8

In the above example, the insurer has reached the requisite threshold in 201x+2 and therefore will file its first Section 17 report effective December 31, 201x+4.

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3. Assume the insurer reports premiums as follows:

$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	380.5	410.5	425.7
Add: Reinsurance ceded	100.5	115.7	110.7	115.8	120.1
Gross direct written and assumed premium	450.8	506.5	491.2	526.3	545.8

In the above example, the insurer has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3. Because the insurer dropped below the threshold in 201x+2, the insurer is not required to file a Section 17 report and thus, the reporting period starts over. The insurer reaches the threshold in 201x+3 and therefore, required to file the Section 17 report effective December 31, 201x+5. The insurer may choose to begin voluntarily filing the Section 17 report beginning with 201x+3 especially if the insurer has done the work to prepare the report.

Business Combination

A business combination is defined as acquisition of insurance/reinsurance business through:

A. a stock acquisition,
B. inforce reinsurance assumption, or
C. a merger of insurers in a Group of insurers.

A. Stock Acquisitions

Assume Company A, which has premiums of $500m or more, buys Company B and retains Company B as a separate legal entity.

If Company B has premiums of less than $500m (as derived from Section 17A), no Section 17 report is required.

If Company B has premiums of $500m or more (as derived from Section 17A), a Section 17 report is required.

1. Assume Company B is acquired effective January 1, 201x and subsequently reports premiums as follows. Assume further that Company A and B elect to file separate Section 17 reports:

$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7	450.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	526.3	545.8	578.0

In the above example, Company B has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3.

2. Assume Company B is acquired June 30, 201x+2 by Company A and Company B has premiums as follows. Assume further that Company A elects to file a single Section 17 report with the Group of insurers consisting of Company A and B:

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$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7	450.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	526.3	545.8	578.0

In the above example, Company B has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3. However due to the acquisition in 201x+2, the first combined Section 17 report, i.e., Group of insurers, would be effective December 31, 201x+4, two years subsequent to acquisition.

B. Inforce Reinsurance Assumption

For the purposes of determining premiums pursuant to Section 17A, assumed premiums from the assumption of an inforce reinsurance transaction will be excluded from the measurement of premiums, for two calendar years subsequent to acquisition.

Assume the insurer assumed an inforce transaction effective June 30, 201x+2 and reports premiums as follows:

$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	610.5	850.7	875.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	726.3	970.8	1,003.0
Less: Gross assumed premium resulting from a business combination	0	0	200.0	425.0	425.0
Gross direct written and assumed premium, subject to Section 17	450.8	506.5	526.3	545.8	578.0

In the above example, the insurer has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3, however only for business inforce in 201x+1 and still inforce in 201x+3. The business assumed at June 30, 201x+2 will be subject to a Section 17 report effective December 31, 201x+4, two calendar years after acquisition.

C. Mergers of Insurers in a Group of Insurers

If the merged insurer has premiums of less than $500m (as derived from Section 17A), a Section 17 report is not required.

If the merged insurer has premiums of $500m or more (as derived from Section 17A), a Section 17 report is required.

1. Assume that Insurer A and Insurer B have Gross direct written and assumed premiums as follows, and agree to merge effective January 1, 201x+1, with Insurer A as the surviving entity:

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$ millions	201x	201x+1	201x+2	201x+3	201x+4
Gross direct written and assumed premium – Insurer A	450.3	460.8	510.5	n/a	n/a
Gross direct written and assumed premium – Insurer B	100.5	115.7	115.8	n/a	n/a
Less: Intercompany transactions – gross	-	65.3	62.2	n/a	n/a
Combined gross direct written and assumed premiums Insurer A	-	511.2	564.1	n/a	n/a

In the above example, the merged entity (insurer A) has reached the requisite threshold in 201x+1, and will file its first Section 17 report effective December 31, 201x+3.

2. Assume that Insurer A and Insurer B have Gross direct written and assumed premiums as follows, and agree to merge effective January 1, 201x+2, with Insurer A as the surviving entity:

$ millions	201x	201x+1	201x+2	201x+3	201x+4
Gross direct written and assumed premium – Insurer A	450.3	460.8	510.5	n/a	n/a
Gross direct written and assumed premium – Insurer B	100.5	115.7	115.8	n/a	n/a
Less: Intercompany transactions – gross	-	-	62.2	n/a	n/a
Combined gross direct written and assumed premiums Insurer A	-	-	564.1	n/a	n/a

In the above example, the merged entity (insurer A) has reached the requisite threshold in 201x+2, and will file its first Section 17 report effective December 31, 201x+4, two years subsequent to merger.

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APPENDIX 1

Illustrative Examples of Management's Report of Internal Control over Financial Reporting

The following are examples of Management's Report of Internal Controls over Financial Reporting utilizing different facts and circumstances. These are only examples and individual company facts and circumstances will dictate the contents of their report. However, there are common elements that should be included in all reports as discussed in Sections 17C and 17D of the Model.

Example A: An SEC registrant or a member of a holding company system whose parent is an SEC registrant that had all material control processes over statutory financial reporting addressed in its Section 404 report ..... Page 23

Example B: An SEC registrant or a member of a holding company system who is a SEC registrant and is a non-accelerated filer that had all material control processes over statutory financial reporting addressed in its Section 404 report. For these non-accelerated filers, the Section 404 report does not require the report of independent registered public accounting firm on internal control over financial reporting..... Page 25

Example C: An SEC registrant or a member of a holding company system whose parent is an SEC registrant that did not have all material control processes over statutory financial reporting addressed in its Section 404 report..... Page 27

Example D: An SEC registrant or a member of a holding company system who is a SEC registrant and is a non-accelerated filer that did not have all material control processes over statutory financial reporting addressed in its Section 404 report. For these non-accelerated filers, the Section 404 report does not require the report of independent registered public accounting firm on internal control over financial reporting ..... Page 30

Example E: A non-SEC registrant or a member of a holding company system that voluntarily complied with Section 404 of the Sarbanes-Oxley Act and produced a report on internal controls which included an auditor's opinion..... Page 33

Example F: A company [or "group of insurers"] that is not subject to Section 404 and utilized their own framework to evaluate controls..... Page 35

Example G: An SEC registrant or a member of a holding company system whose parent is an SEC registrant that had all material control processes addressed in their Section 404 report and had an unremediated material weakness..... Page 37

Example H: An SEC registrant or member of a holding company system whose parent is an SEC registrant that did not include all material processes over statutory financial reporting addressed in its Section 404 report and had an unremediated material weakness noted ..... Page 39

Example I: An SEC registrant or member of a holding company system whose parent is an SEC registrant that had all material processes over statutory financial reporting addressed in its Section 404 report. However, they recently acquired another insurer that is not included in their assessment ..... Page 42

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EXAMPLE A: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT HAD ALL MATERIAL CONTROL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company Inc ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).* Based on our assessment under that framework, management concluded that the Group of insurers' internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ's Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers' internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this addendum, the "Section 404 Report" means Management's Report on Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE B: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHO IS A SEC REGISTRANT AND IS A NON-ACCELERATED FILER THAT HAD ALL MATERIAL CONTROL PROCESSES OVER STATUTORY REPORTING ADDRESSED IN ITS SECTION 404 REPORT. FOR THIS NON-ACCELERATED FILER, THE SECTION 404 REPORT DOES NOT REQUIRE THE REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING.

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model] as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our assessment under that framework, management concluded that the Group of insurers' internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17 of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting included in XYZ's Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). This does not include a report of independent registered public accounting firm on internal control over financial reporting for XYZ, as it is not required for non-accelerated filers In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers' internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting only contained in or incorporated by reference in the Company's Form 10-K/20-F. This does not include a report of independent registered public accounting firm on internal control over financial reporting, as it is not required for non-accelerated filers. Accordingly, as required by [relevant state statute or Section 17 of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE C: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT DID NOT HAVE ALL MATERIAL CONTROL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model] as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).* Based on our assessment under that framework, management concluded that the Group of insurers' internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ's Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers' internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Company's Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that the only material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report are the processes discussed below. Management of XYZ hereby affirms that all other material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers were included in the Section 404 Report. The following statutory financial reporting processes were reviewed separately from the internal controls reported by the Group of insurers in its Section 404 report:

Significant Control Processes not tested due to Group Materiality Considerations

The Section 404 report excludes certain control processes deemed material to individual insurance legal entities included within the Group of insurers. This exclusion was due to group materiality decisions made at the parent company level. These processes, and the legal entities within the Group of insurers impacted, are listed as follows:

Workers' Compensation Claims Processing – The HIJ claims processing system is utilized to process workers' compensation claims material to ABC Insurance Subsidiary and DEF Insurance Subsidiary.

Related Party Transactions Eliminated through Consolidation

The Section 404 report does not consider controls surrounding related party transactions as the effects of those transactions are eliminated through consolidation at the holding company financial statement level. Significant related party transactions, and the legal entities within the Group of insurers impacted, are listed as follows:

Affiliate reinsurance agreements – A significant amount of reinsurance coverage is obtained by ABC Insurance Subsidiary and DEF Insurance Subsidiary through contracts with XYZ Parent Company.

Management service agreements – ABC Insurance Subsidiary receives all of its management services through an agreement with XYZ Parent Company.

Tax allocation agreements – ABC Insurance Subsidiary and DEF Insurance Subsidiary are subject to an intercompany tax allocation agreement with XYZ Parent Company.

Deferred Income Taxes

Federal income taxes are provided for XYZ's estimated current and deferred liability. Deferred taxes are provided for differences between the financial statement and tax bases of assets and liabilities. Pursuant to *SSAP No. 101—Income Taxes*, changes in deferred tax assets and liabilities are recognized as a separate component of gains and losses in statutory surplus, while under GAAP/IFRS, these changes are included in income tax expense or benefit. Gross deferred tax assets not meeting the realization criteria outlined in SSAP No. 101 are not admitted.

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Nonadmitted Assets

Certain XYZ assets (principally furniture, equipment, prepaid expenses, agents' balances, and certain deferred tax assets) have been designated as nonadmitted assets under statutory accounting guidance (primarily in *SSAP No. 4—Assets and Nonadmitted Assets* and *SSAP No. 20—Nonadmitted Assets*). Such nonadmitted assets are excluded from assets by a charge to statutory surplus. Under GAAP/IFRS, such amounts are carried at amortized cost with an appropriate valuation allowance, as necessary.

Asset Valuation Reserve ("AVR")

The AVR represents a statutory contingency reserve for life and health insurers for credit related risk on most invested assets, and is charged to surplus pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve.* No such reserve is required under GAAP/IFRS accounting.

Interest Maintenance Reserve ("IMR")

The IMR represents the deferral of interest-related realized gains and losses, net of tax, on primarily fixed maturity investments, amortized into income over the remaining life of the investment sold pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Management of XYZ conducted an assessment of the internal controls over these processes and concluded that they were effective with respect to the audited statutory financial statements.

(Please note that this is not intended to be an all-inclusive list. It should only include material process that were not covered in the Section 404 Report. The facts and circumstances of each situation will determine the items to be included.)

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE D: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHO IS A SEC REGISTRANT AND IS A NON-ACCLERATED FILER THAT DID NOT HAVE ALL MATERIAL CONTROL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT. FOR THESE NON-ACCELERATED FILERS, THE SECTION 404 REPORT DOES NOT REQUIRE THE REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING.

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model] as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our assessment under that framework, management concluded that the Group of insurers' internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17 of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting included in XYZ's Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). This does not include a report of independent registered public accounting firm on internal control over financial reporting for XYZ, as it is not required for non-accelerated filers. In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers' internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting only contained in or incorporated by reference in the Company's Form 10-K/20-F. This does not include a report of independent registered public accounting firm on internal control over financial reporting, as it is not required for non-accelerated filers. Accordingly, as required by [relevant state statute or Section 17 of the Model], management of XYZ hereby affirms that the only material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report are the processes discussed below. Management of XYZ hereby affirms that all other material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers were included in the Section 404 Report.

Significant Control Processes not tested due to Group Materiality Considerations

The Section 404 report excludes certain control processes deemed material to individual insurance legal entities included within the Group of insurers. This exclusion was due to group materiality decisions made at the parent company level. These processes, and the legal entities within the Group of insurers impacted, are listed as follows:

Workers' Compensation Claims Processing – The HIJ claims processing system is utilized to process workers' compensation claims material to ABC Insurance Subsidiary and DEF Insurance Subsidiary.

Related Party Transactions Eliminated through Consolidation

The Section 404 report does not consider controls surrounding related party transactions as the effects of those transactions are eliminated through consolidation at the holding company financial statement level. Significant related party transactions, and the legal entities within the Group of insurers impacted, are listed as follows:

Affiliate reinsurance agreements – A significant amount of reinsurance coverage is obtained by ABC Insurance Subsidiary and DEF Insurance Subsidiary through contracts with XYZ Parent Company.

Management service agreements – ABC Insurance Subsidiary receives all of its management services through an agreement with XYZ Parent Company.

Tax allocation agreements – ABC Insurance Subsidiary and DEF Insurance Subsidiary are subject to an intercompany tax allocation agreement with XYZ Parent Company.

Deferred Income Taxes

Federal income taxes are provided for XYZ's estimated current and deferred liability. Deferred taxes are provided for differences between the financial statement and tax bases of assets and liabilities. Pursuant to *SSAP No. 101—Income Taxes*, changes in deferred tax assets and liabilities are recognized as a separate component of gains and losses in statutory surplus, while under GAAP/IFRS, these changes are included in income tax expense or benefit. Gross deferred tax assets not meeting the realization criteria outlined in SSAP No. 101 are not admitted.

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Nonadmitted Assets

Certain XYZ assets (principally furniture, equipment, prepaid expenses, agents' balances, and certain deferred tax assets) have been designated as nonadmitted assets under statutory accounting guidance (primarily in *SSAP No. 4—Assets and Nonadmitted Assets* and *SSAP No. 20—Nonadmitted Assets*). Such nonadmitted assets are excluded from assets by a charge to statutory surplus. Under GAAP/IFRS, such amounts are carried at amortized cost with an appropriate valuation allowance, as necessary.

Asset Valuation Reserve ("AVR")

The AVR represents a statutory contingency reserve for life and health insurers for credit related risk on most invested assets, and is charged to surplus pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Interest Maintenance Reserve ("IMR")

The IMR represents the deferral of interest-related realized gains and losses, net of tax, on primarily fixed maturity investments, amortized into income over the remaining life of the investment sold pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Management of XYZ conducted an assessment of the internal controls over these processes and concluded that they were effective with respect to the audited statutory financial statements.

(Please note that this is not intended to be an all-inclusive list. It should only include material process that were not covered in the Section 404 Report. The facts and circumstances of each situation will determine the items to be included.)

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE E: A NON-SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM THAT VOLUNTARILY COMPLIED WITH SECTION 404 OF THE SARBANES-OXLEY ACT AND PRODUCED A REPORT ON INTERNAL CONTROLS WHICH INCLUDED AN AUDITOR'S OPINION

Management's Report of Internal Control over Financial Reporting

As a non-SEC registrant, XYZ Holding Company, Inc. ("XYZ") is not required to prepare or file with the U.S. Securities and Exchange Commission a Sarbanes-Oxley Act Section 404 report on internal control over financial reporting. However, management has elected to prepare, and have audited by XYZ's independent certified public accountant, such a report for the fiscal year-ended December 31, 201X.

Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).* Based on our assessment under that framework, management concluded that the Group of insurers' internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] the attached copy of XYZ's Section 404 Report for the fiscal year ended December 31, 201X, which includes Management's Report of Internal Control over Financial Reporting and report of independent registered public accounting firm on internal control over financial reporting for XYZ. In addition, an Addendum (Attachment A) is included to this report that identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers' internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this addendum, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Annual Report to Stockholders. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE F: A COMPANY [OR "GROUP OF INSURERS"] THAT IS NOT SUBJECT TO SECTION 404 AND UTILIZED THEIR OWN FRAMEWORK TO EVALUATE CONTROLS

Management's Report of Internal Control over Financial Reporting

[As a non-SEC registrant, XYZ Holding Company, Inc. ("XYZ") is not required to prepare or file with the U.S. Securities and Exchange Commission a Sarbanes-Oxley Act Section 404 report on internal control over financial reporting. Each of the insurance companies listed on Attachment A is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment A.]

Management of ABC Insurance Company [or XYZ] is responsible for establishing and maintaining adequate internal control over statutory financial reporting. The Company has established an internal control system designed to provide reasonable assurance regarding the fair presentation of statutory financial reporting. The Company developed its own internal framework for evaluating the effectiveness of internal control over statutory financial reporting. The Company's framework includes the identification and evaluation of the company's internal control environment and areas of potential material internal control risk, documentation of existing internal controls, monitoring and testing of those key controls, documentation of remedial actions planned or taken, if any, and communication of the findings of the evaluation by the Company's senior management to the Audit committee of the Board of Directors.

Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Company's internal control over statutory financial reporting, which included identifying, reviewing, monitoring and testing significant internal controls over statutory financial reporting. Based on our assessment under the above described approach and through diligent inquiry, management has concluded that the Company's internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Company's internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of Insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE G: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT HAD ALL MATERIAL CONTROL PROCESSES ADDRESSED IN THEIR SECTION 404 REPORT AND HAD AN UNREMEDIATED MATERIAL WEAKNESS

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly-owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).*

A material weakness was noted in XYZ's internal control over financial reporting related to the calculation of insurance reserves. Due to the manner in which the data for homeowners policies are captured by the systems used in its Southeastern US regional office, changes in XYZ's estimate of insurance reserves for certain policies are not reviewed by XYZ's Actuarial Department prior to being recorded in the company's accounting records.

A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented, or detected and corrected on a timely basis. In connection with the weakness noted above, XYZ's management has taken remedial actions to change its procedures for coding policies issued in the states affected so that all homeowners policy data are included in the Actuarial Department review of estimate of insurance reserves. This change was effective on July 1, 20XX.

As a result of the unremediated material weakness described above, XYZ management has concluded that, as of December 31, 201X, XYZ's internal control over statutory financial reporting was not effective.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ's Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

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(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this addendum, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B

XYZ Holding Company Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE H: AN SEC REGISTRANT OR MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT DID NOT INCLUDE ALL MATERIAL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT AND HAD AN UNREMEDIATED MATERIAL WEAKNESS NOTED

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly-owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).*

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness was noted in XYZ's internal control over financial reporting related to the calculation of insurance reserves. Due to the manner in which the data for homeowners policies are captured by the systems used in its Southeastern US regional office, changes in XYZ's estimate of insurance reserves for certain policies are not reviewed by XYZ's Actuarial Department prior to being recorded in the company's accounting records.

A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the company's financial statements will not be prevented, or detected and corrected on a timely basis. In connection with the assessment above, XYZ's management identified a material weakness as of December 31, 201X in the controls over the calculation of insurance reserves.

As a result of the unremediated material weakness described above, XYZ management has concluded that, as of December 31, 201X, XYZ's internal control over statutory financial reporting was not effective.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ's Form 10-K for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

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(Signed)_____ (Date)_____
(Chief Executive Officer)

(Signed)_____ (Date)_____
(Chief Financial Officer)

ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Company's Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that the only material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report are the processes discussed below. Management of XYZ hereby affirms that all other material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers were included in the Section 404 Report. The following statutory financial reporting processes were reviewed separately from the internal controls reported by the Group of insurers in its Section 404 report:

Significant Control Processes not tested due to Group Materiality Considerations

The Section 404 report excludes certain control processes deemed material to individual insurance legal entities included within the Group of insurers. This exclusion was due to group materiality decisions made at the parent company level. These processes, and the legal entities within the Group of insurers impacted, are listed as follows:

Workers' Compensation Claims Processing – The HIJ claims processing system is utilized to process workers' compensation claims material to ABC Insurance Subsidiary and DEF Insurance Subsidiary.

Related Party Transactions Eliminated through Consolidation

The Section 404 report does not consider controls surrounding related party transactions as the effects of those transactions are eliminated through consolidation at the holding company financial statement level. Significant related party transactions, and the legal entities within the Group of insurers impacted, are listed as follows:

Affiliate reinsurance agreements – A significant amount of reinsurance coverage is obtained by ABC Insurance Subsidiary and DEF Insurance Subsidiary through contracts with XYZ Parent Company.

Management service agreements – ABC Insurance Subsidiary receives all of its management services through an agreement with XYZ Parent Company.

Tax allocation agreements – ABC Insurance Subsidiary and DEF Insurance Subsidiary are subject to an intercompany tax allocation agreement with XYZ Parent Company.

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Deferred Income Taxes

Federal income taxes are provided for XYZ's estimated current and deferred liability. Deferred taxes are provided for differences between the financial statement and tax bases of assets and liabilities. Pursuant to *SSAP No. 101—Income Taxes*, changes in deferred tax assets and liabilities are recognized as a separate component of gains and losses in statutory surplus, while under GAAP/IFRS, these changes are included in income tax expense or benefit. Gross deferred tax assets not meeting the realization criteria outlined in SSAP No. 101 are not admitted.

Nonadmitted Assets

Certain XYZ assets (principally furniture, equipment, prepaid expenses, agents' balances, and certain deferred tax assets) have been designated as nonadmitted assets under statutory accounting guidance (primarily in *SSAP No. 4—Assets and Nonadmitted Assets* and *SSAP No. 20—Nonadmitted Assets*). Such nonadmitted assets are excluded from assets by a charge to statutory surplus. Under GAAP/IFRS, such amounts are carried at amortized cost with an appropriate valuation allowance, as necessary.

Asset Valuation Reserve ("AVR")

The AVR represents a statutory contingency reserve for life and health insurers for credit related risk on most invested assets, and is charged to surplus pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve.* No such reserve is required under GAAP/IFRS accounting.

Interest Maintenance Reserve ("IMR")

The IMR represents the deferral of interest-related realized gains and losses, net of tax, on primarily fixed maturity investments, amortized into income over the remaining life of the investment sold pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve.* No such reserve is required under GAAP/IFRS accounting.

Management of XYZ conducted an assessment of the internal controls over these processes and concluded that they were effective with respect to the audited statutory financial statements.

(Please note that this is not intended to be an all-inclusive list. It should only include material processes that were not covered in the Section 404 Report. The facts and circumstances of each situation will determine the items to be included.)

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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EXAMPLE I: AN SEC REGISTRANT OR MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT HAD ALL MATERIAL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT. HOWEVER, THEY RECENTLY ACQUIRED ANOTHER INSURER THAT IS NOT INCLUDED IN THEIR ASSESSMENT

Management's Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. ("XYZ") is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ's Management's Report of Internal Control over Financial Reporting, management has identified its "Group of insurers," as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers' internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).* This assessment excluded an evaluation of internal controls over financial reporting for RST Insurance Company which was recently acquired. Based on our assessment under that framework, management concluded that the Group of insurers' internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers' obligation to deliver Management's Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ's Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers' internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed)_____ (Date)_____
(Chief Executive Officer)
(Signed)_____ (Date)_____
(Chief Financial Officer)

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ATTACHMENT A

XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X

For purposes of this addendum, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Form 10-K. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B

XYZ Holding Company, Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]

Name	NAIC No
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

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NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

UPDATES

to the

As of March 2024

Accounting Practices and Procedures Manual

Adopted items will be uploaded to the Updates section of this Manual following each interim and national meeting of the Statutory Accounting Principles (E) Working Group.

LAST UPDATED:

- January 10, 2024 – Interim Meeting
- February 20, 2024 – Interim Meeting
- February 20, 2024 – HATF Interim Meeting
- March 16, 2024 – Spring National Meeting
- May 15, 2024 – Interim Meeting
- August 13, 2024 – Summer National Meeting
- September 12, 2024 – E-Vote
- November 17, 2024 – Fall National Meeting
- December 17, 2024 – Interim Meeting

Revisions to the
As of March 2023 Accounting Practices and Procedures Manual

On **January 10, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2023 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
INT 23-04	SSAP No. 61R	Scottish Re Life Reinsurance Liquidation Questions *SAP Clarification* Effective (December 31, 2023)	*INT 23-04: Scottish Re Life Reinsurance Liquidation Questions* provides accounting and reporting guidance for ceding entities with reinsurance balances to or from Scottish Re, a U.S.-based life reinsurer in liquidation. The guidance focuses primarily on reinsurance recoverables.
2023-24	INT 06-07 SSAP No. 2R SSAP No. 5R SSAP No. 22R SSAP No. 26R SSAP No. 32R SSAP No. 34 SSAP No. 37 SSAP No. 39 SSAP No. 41R SSAP No. 43R SSAP No. 61R SSAP No. 62R SSAP No. 86 SSAP No. 103R SSAP No. 105R	ASU 2016-13 Measurement of Credit Losses on Financial Instruments (CECL) *SAP Clarification* Effective (December 31, 2023)	Revisions reject ASU 2016-13 and related subsequent ASUs in various SSAPs and *INT 06-07: Definition of Phrase "Other Than Temporary."* These revisions reject CECL for statutory accounting.

https://naiconline.sharepoint.com/teams/frsstatutoryaccounting/national meetings/a. national meeting materials/2024/01 1-10-24/adoptions/00 - adoptions toc.docx

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 23-04: Scottish Re Life Reinsurance Liquidation Questions

INT 23-04 Dates Discussed
October 23, 2023; October 24, 2023; December 1, 2023; January 10, 2024

INT 23-04 References

Current:
SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance

INT 23-04 Issue

Background:

1. Liquidations of U.S. licensed reinsurers are uncommon. Due to a 2023 liquidation order of a U.S.-based life reinsurer, life industry cedents have requested an interpretation to address the accounting and reporting for reinsurance receivables from the reinsurer's estate. This interpretation is intended to be applied generically; however, the following circumstances are relevant to the accounting issues identified.

   a. The recent liquidation order was for Scottish Re, a U.S. life reinsurance entity, which was in regulatory supervision for several years.

   b. The life reinsurer was not assuming new business but was receiving ongoing premium on yearly renewable contracts.

   c. The 2023 liquidation order cancelled reinsurance contracts on a cut-off basis, effective September 30, 2023.

   d. Settlement from the reinsurer's estate is expected to exceed one year.

   e. Settlement from the reinsurer's estate to the ceding entities is expected to be less than 100%. That is, cedents are expected to receive a portion of what they are owed.

   f. Some ceding insurers established trusts to hold assets backing the reserves under the reinsurance agreements.

Interpretation Discussion

2. This interpretation is applicable only to the accounting and reporting of reinsurance recoverables from Scottish Re, a U.S.-based life reinsurer in liquidation. The Statutory Accounting Principles (E) Working Group consensuses to the noted issues are included below.

Issue 1 – Commutation or Recapture of a Life Reinsurance Contract

3. If a liquidation order cancels a life reinsurance contract on a cut-off basis, should the life reinsurance commutation guidance in S*tatement of Statutory Accounting Principle*s (*SSAP) No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* be used as the primary accounting guidance for the commutation?

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4. Yes. SSAP No. 61R, paragraph 58, provides the primary guidance for a life reinsurance commutation. The guidance provides that:

> **Recaptures and Commutations**
>
> 58. A recapture or a commutation of a reinsurance agreement is a transaction which results in the complete and final settlement and discharge of all present and future obligations between the parties arising out of the agreement or a portion of the agreement. Commuted and recaptured balances shall be accounted for by writing them off through the accounts, exhibits and schedules in which they were originally recorded. The assumed reserves and reserve credits taken are eliminated by the reinsurer and ceding entity, respectively. The reinsurer and ceding entity must also make any required IMR liability adjustment changes. Any net gain or loss is reported in the summary of operations.

Issue 2 – Impairment of Reinsurance Recoverables

5. The reinsurer that was previously in regulatory supervision and is now in liquidation was known to have financial difficulties and many ceding entities have either established valuation allowances and/or written off reinsurance recoverables as impairment losses. Questions have been received in response to the diversity in practice on whether the ceding entities were reporting impairment losses or were reporting a valuation allowance on all categories of their expected reinsurance recoverables from the reinsurer which is now in liquidation.

6. Do reporting entities have the choice of setting up a valuation allowance or applying the impairment guidance in SSAP No. 61R to the reinsurance recoverables from the life reinsurer in liquidation?

7. No. Reporting entities do not have a choice of a valuation allowance or applying impairment analysis. SSAP No. 61R, paragraph 42, requires impairment analysis of uncollectible reinsurance amounts in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Asset.* The guidance requires that impaired amounts shall be written off through a charge to the Statement of Operations utilizing the same accounts which established the reinsurance recoverables. SSAP No. 5R and SSAP No. 61R do not permit a valuation allowance.

8. The liquidation order of a reinsurer should prompt an impairment analysis of all amounts recoverable from the reinsurer with a write-off of amounts not expected to be recovered.

9. The impairment analysis shall be updated at every reporting date.

Issue 3 – Reporting of Reinsurance Recoverables

10. The liquidation order results in a commutation and recapture of business for the ceding entity. A liquidation will determine the reinsurer's estate assets, then determine payments based on liquidation priority. This will result in a delay in settlement from the estate of the reinsurer. As previously detailed, the amounts paid by the estate shall be impaired to the amount expected to be received by the ceding entities.

11. Where shall the ceding entity report the remaining receivables for the reinsurer's estate?

12. In accordance with the recapture and commutation guidance in SSAP No. 61R, paragraph 58 (quoted above), the ceding entity shall remove balances through the schedules and exhibits originally reported. No reserve credit or contra-liabilities shall be reported. The reinsurance reserve credits shall be removed. Gains or losses are reported in the summary of operations.

13. Based on preliminary information received, it is expected that there will be an amount receivable for paid claims incurred before the reinsurance contract cancellation. This amount shall be reported on the asset page line 16.1 - Amounts Recoverable from Reinsurers.

14. Amounts recoverable from the reinsurer's estate for claims incurred before the reinsurance contract cancellation and unpaid as of the reporting date shall be reported on the asset page line 16.3 - Other Amounts Receivable Under Reinsurance Contracts.

15. If the ceding entity owes amounts to the reinsurer's estate, the amounts shall be reported as a liability on line 9.3 - Other Amounts Payable on Reinsurance.

16. After impairing the recoverables, any other amount expected to be recovered from the reinsurer's estate shall be reported on line 25 Aggregate Write-ins for Other Than Invested Assets.

Issue 4 – Admissibility of Reinsurance Recoverables

17. As noted above, quarterly impairment analysis of collectability is required. After evaluating for impairment, if there are remaining receivables from the reinsurer's estate, do those assets qualify as admitted reinsurance recoverable assets?

18. Reinsurance recoverables from Scottish Re in liquidation are admitted as follows:

a. The reinsurance recoverable amount from Scottish Re from paid claims incurred prior to the reinsurance contract cancellation which are reported on the asset page line 16.1 - Amounts Recoverable from Reinsurers which are not in dispute are admitted after impairment review.

b. To the extent reinsurance amounts recoverable are secured by assets in an Appendix A-785 - Credit for Reinsurance compliant trust, such recoverable amounts may be admitted to the extent the that the amounts are not in dispute and that the collateral in an Appendix A-785 compliant trust is sufficient.

19. Other reinsurance recoverables, which are not identified as admitted assets in paragraph 18 are nonadmitted until received. This includes amounts either in dispute or not secured by collateral in a trust that is compliant with Appendix A-785.

Issue 5 – Disclosures

20. Do the relevant disclosures in SSAP No. 61R and other relevant SSAPs apply to a commuted life reinsurance contract which has not been fully settled due to a liquidation?

21. Yes. The relevant disclosures in SSAP No. 61R and other relevant SSAPs continue to apply to a life reinsurance contract which is commuted and recaptured due to a liquidation. These disclosures include but are not limited to the disclosures regarding commutation, uncollectible reinsurance and anything else that is required.

22. Disclosure in the reinsurance notes to the financial statements shall include additional information necessary to obtain an understanding of the impact of Scottish Re reinsurance counterparties in liquidation, including but not limited to, reinsurance payable liabilities, reinsurance recoverables by paid claims and other amounts, information regarding the status of any collateral and its fair value. Where applicable, reporting entities should disclose any individual components (e.g., unreimbursed claims or provisions for future losses) of recoverable amounts that are presented in the aggregate on the financial statements. The

disclosure shall include measurement, impairment and collectability of any reinsurance recoverables including timing of expected payments and nonadmitted amounts.

INT 23-04 Summary

23. Although readers should refer to the detailed guidance above, a summary of the key provisions is as follows:

a. Issue 1 – Commutation or Recapture of a Life Reinsurance Contract: Follow SSAP No. 61R, paragraph 58, as it provides primary recapture and commutation guidance.

b. Issue 2 – Impairment of Reinsurance Recoverables: SSAP No. 61R paragraph 42, requires impairment of uncollectible reinsurance in accordance with SSAP No. 5R.

c. Issue 3 – Reporting of Reinsurance Recoverables: Follow the recapture and commutation guidance in SSAP No. 61R, then analyze for impairment. Report reinsurance payables separate from reinsurance recoverables. Amounts related to paid and unpaid claims incurred prior to reinsurance contract cancellation are reported on asset page line 16.1 - Amounts Recoverable from Reinsurers and asset page line 16.3 - Other Amounts Receivable Under Reinsurance Contracts, respectively. Any remaining reinsurance recoverables from the reinsurance counterparty after impairment assessment shall be reported on the asset page line 25 Aggregate Write-ins for Other than Invested Assets.

d. Issue 4 – Admissibility of Reinsurance Recoverables: Admit amounts related to claims incurred prior to contract cancellation which have been paid by the reporting entity as of the reporting date (reported on asset page line 16.1 - Amounts Recoverable from Reinsurers) which are not in dispute after impairment review. Admit reinsurance recoverables which are not in dispute, and which are secured by collateral in an A-785 compliant trust. Nonadmit all amounts recoverable from a life reinsurer in liquidation which are either in dispute or which are not secured by collateral in a trust compliant with Appendix A-785.

e. Issue 5 – Disclosures: Follow existing applicable disclosures and provide additional information sufficient to understand the nature and impact of a reinsurance counterparty in liquidation as described in paragraph 22.

INT 23-04 Status

24. The consensuses in this interpretation were adopted on January 10, 2024, with an effective date of reporting periods on or after December 31, 2023.

25. No further discussion is planned.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: ASU 2016-13 Measurement of Credit Losses on Financial Instruments

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In June 2016, the Financial Accounting Standards Board (FASB) issued *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments* (CECL*)* to change impairment and credit loss United States generally accepted accounting principles (GAAP) guidance from an "incurred loss" methodology to an "expected loss" methodology. These changes were made primarily in response to the 2008 Great Recession in which companies were anticipating significant credit losses but were unable to record these losses as the probable threshold had not yet been met. In response to this issue, FASB established the Financial Crisis Advisory Group (FCAG) to advise FASB on improvements to financial reporting in response to the Great Recession. The main recommendation from the FCAG to FASB was to investigate improvements to impairment and credit loss guidance through the development of an alternative to the "incurred loss" methodology. Based on this recommendation FASB developed CECL which replaces the "incurred loss" methodology and provides financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. CECL affects all entities holding financial assets that are not accounted for at fair value through net income, including loans, debt securities, trade receivables, net investments in leases, off-balance sheet credit exposures, reinsurance recoverables and any other financial assets not specifically excluded that have the contractual right to receive cash. The impact from applying CECL is anticipated to vary by reporting entity in accordance with the credit quality of assets held and how they apply current GAAP.

One significant difference between previous GAAP and CECL is that the impairment guidance for in-scope assets were superseded and replaced with credit loss guidance under *Topic 326–Financial Instruments—Credit Losses*. Beyond consolidating new credit loss guidance into a single topic, CECL fundamentally changed the methodology for calculating and recording credit losses by replacing the incurred credit loss model with the expected credit loss model, which requires expected losses to be assessed and recorded at the onset of the acquisition of in-scope assets. This requirement is applicable for all in-scope assets unless management assesses that the asset represents a zero-risk transaction, U.S. Treasuries for example. As a result, the calculation of a credit loss allowance is now required for many assets which previously would have only recorded a credit loss allowance once it has occurred, or the probable threshold had been met. The asset categories scoped into the new CECL credit loss guidance are as follows:

- Financing Receivables
- Receivables from Sales-Type or Direct Finance Leases
- Related Party Accounts and Loans Receivable, excluding related parties under common control.
- All financial instruments held at Amortized Cost (categorized as Held to Maturity under GAAP), excluding purchased financial assets with credit deterioration (PCDs).
    - Includes but is not limited to debt securities, trade and time-share receivables, contract assets, and reinsurance recoverables.
- Off-balance-sheet credit exposures not accounted for as insurance.
    - Includes but is not limited to loan commitments, forward commitments to purchase loans, letters of credit, and financial guarantees.
- Cash Equivalents

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While CECL does require the accrual of an allowance on expected credit losses, it does not require a specific evaluation method but rather adopts a principles-based approach which allows for any kind of credit loss evaluation if the end product of the evaluation meets certain defined criteria. Additionally, assets with similar risk profiles may be evaluated for expected credit losses collectively but these risk profiles must be assessed annually to determine if they remain similar. Note that Available for Sale securities are excluded from the expected credit loss methodology but are instead required to utilize a modified other-than-temporary impairment (OTTI) model detailed in Topic 326-30. The following information summarizes the key information on the accounting and reporting of credit losses under Topic 326:

Overview of CECL Concepts:

Accounting guidance is divided into securities reported at amortized cost (includes investment held at Held-to-Maturity, or HTM), and debt securities reported as available for sale (AFS), which reports fair value through OCI. The following reflects high-level concepts from CECL:

Amortized Cost Securities:

1. Allowance for credit losses is a valuation accounting that is deducted from the amortized cost basis of the financial assets to present the net amount expected to be collected on the financial assets. Net income is adjusted to reflect the allowance for credit losses based on the current expected estimate. The allowance shall be reported at each reporting date. Changes from current estimates shall be compared to estimates previously reported, with adjustments reflected in net income.

2. The entity shall measure credit losses on a collective basis when similar risk characteristics exist. If a financial asset does not share risk characteristics with other assets, the entity shall evaluate the asset on an individual basis. (Should not include individual and collective assessments on the same asset.)

3. The entity shall estimate expected credit losses over the contractual terms of the financial assets, considering prepayments. However, it shall not extend the contractual term for expected extensions, renewals, and modifications unless there is a reasonable expectation of executing a troubled debt restructuring.

4. When developing an estimate, the entity shall consider available information relevant to assessing collectability of cash flows. This may include internal information, external information, or a combination of past events, current conditions and reasonable and supportable forecasts. (Internal information may be determined sufficient.)

5. Historical credit loss information for assets with similar characteristics generally provides a basis for expected losses, but entities shall not rely solely on past events to estimate expected credit losses. When using historical information, the entity shall consider the need to adjust for management expectations about current conditions and reasonable and supported forecasts that differ from the historical period.

6. Estimate of expected credit losses shall include a measure of the expected risk of credit loss even if that risk is remote. However, entities are not required to measure expected credit losses when the expectation of nonpayment of the amortized cost basis is zero.

7. Estimate of expected credit losses shall reflect how credit enhancements (other than freestanding contracts) mitigate expected credit losses. However, freestanding contracts shall not be used to offset expected losses.

8. Assets purchased with existing credit deterioration are initially reported at the purchase price plus the allowance for credit losses to determine the initial amortized cost basis. Any noncredit discount or premium shall be allocated to each individual asset. At the acquisition date, the initial allowance for credits losses determined on a collective basis shall be allocated to individual assets to appropriately allocate any noncredit discount or premium.

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9. For collateral-dependent financial assets, entities shall measure expected credit losses based on the fair value of the collateral when the entity determines that foreclosure is probable. The entity may expect credit losses of zero when the fair value (less costs to sell) of the collateral at the reporting date is equal to or exceeds the amortized cost basis of the financial asset. If the collateral is less than the amortized cost basis, an entity shall recognize an allowance for credit losses as the difference between the collateral fair value and the amortized cost of the asset.

10. In the period when financial assets are deemed uncollectible, they shall be written off with a deduction from the allowance.

11. Detailed disclosures are included to enable users to understand: 1) credit risk inherent in a portfolio and how management monitors credit quality of a portfolio; 2) management's estimate of expected credit losses; and 3) changes in the estimate of expected credit losses that have occurred during the period. These disclosures include a rollforward of the allowance for credit losses and a reconciliation of the purchase price for assets purchased with credit deterioration.

12. Noted examples are included for collateral-dependent financial assets (real estate loans), assets with collateral maintenance provisions (reverse-repurchase agreements), and HTM debt securities when potential default is greater than zero, but expected nonpayment is zero (Treasury Securities).

Available-for-Sale Debt Securities

13. Investment is impaired if the fair value of the investment is less than amortized cost basis.

14. For individual AFS debt securities, the entity shall determine whether a decline in fair value below the amortized cost basis has resulted from a credit loss or other factors. Impairments related to credit losses shall be recorded through an allowance for credit losses. However, the allowance shall be limited by the amount that the fair value is less than the amortized cost basis.

15. At each reporting date, the entity shall record an allowance for credit losses that reflects the amount of impairment related to credit losses, limited by the fair value floor. Changes in the allowance shall be recorded in the period of the change as a credit loss expense (or reversal of credit loss expense).

16. Impairment shall be assessed at the individual security level. For example, debt securities bearing the same CUSIP – even if purchased in separate lots – may be aggregated by a reporting entity on an average cost basis if that corresponds to the basis used to measure realized or unrealized gains and losses for the debt securities. Providing a general allowance for an unidentified investment in a portfolio of debt securities is not appropriate.

17. In assessing whether a credit loss exists, an entity shall compare the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis of the security, a credit loss exists and an allowance for credit losses shall be recorded for the credit loss, limited by the amount that the fair value is less than amortized cost basis. Credit losses on an impaired security shall continue to be measured using the present value of expected future cash flows. (Entity would discount the expected cash flows at the effective interest risk implicit in the security at the date of acquisition.)

18. Estimates of expected future cash flows shall be on the entity's best estimate based on past events, current conditions and on reasonable and supportable forecasts.

19. If the entity intends to sell, or if more-likely-than-not will be required to sell before recovery of the amortized cost basis, any allowance for credit losses shall be written off and the amortized cost basis shall

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be written down to the debt security's fair value at the reporting date with any incremental impairment reflected in earnings.

20. Entities shall reassess the credit losses each reporting period when there is an allowance for credit losses. Subsequent changes shall be recorded in the allowance for credit losses, with a corresponding adjustment in the credit loss expense. Entities are not permitted to reverse a previously recorded allowance for credit losses to an amount below zero.

21. Once an AFS debt security has been written down, the previous amortized cost basis less write-offs, including noncredit related impairment reported in earnings, shall become the new amortized cost basis, and shall not be adjusted for subsequent recoveries in fair value.

22. For AFS debt securities for which impairments were reported in earnings as a write-off because of an intent to sell or a more-likely-than-not requirement to sell, the difference between the new amortized cost basis and the cash flows expected to be collected shall be accreted as interest income. Over the life of the security, continue to estimate the present value of cash flows expected to be collected. For all other AFS debt securities, if there is a significant increase in the cash flows expected to be collected or if actual cash flows are significantly greater than cash flows previously expected, those changes shall be accounted for as a prospective adjustment to the yield. Subsequent increases in fair value after the write-down shall be included in other comprehensive income.

23. These AFS debt securities shall be presented on the balance sheet at fair value, with parenthetical presentation of the amortized cost and the allowance for credit losses. The allowance for credit losses shall be separately presented as a component of accumulated other comprehensive income.

24. Detailed disclosures are included to allow users to understand: 1) credit risk inherent in AFS debt securities; 2) management's estimate of credit losses; and 3) changes in the estimate of credit losses that have taken place during the period. These disclosures include detailed information for situations in which AFS securities are in an unrealized loss position, but the entity has reached a conclusion that an allowance for credit losses is unnecessary. Other key disclosures include the methodology and significant inputs used to measure credit loss, a rollforward of the allowance for credit losses, and a reconciliation of purchased financial assets with credit deterioration.

25. Noted examples are included for AFS debt securities in an unrealized loss position for which no credit losses are reported (situations include Treasury Securities, Federal Agency MBS, and Corporate Bonds).

Additionally, CECL would make changes to how companies account for off-balance sheet credit exposures. Traditionally, most credit exposures have had no financial impact outside of disclosures until the probable threshold has been met. However, as credit exposures are within the scope of CECL entities will likely be required to assess and accrue a credit loss allowance at the inception of the credit exposure.

CECL also includes revisions to various other elements of the FASB Codification – Contingencies, Guarantees, Troubled Debt Restructuring, Revenue, Business Combinations, Consolidation, Derivatives, Fair Value Measurement, Foreign Currency Transactions, Leases, Transfer and Servicing, Insurance, Financial Guarantee Contracts, & Health Care Entities. Staff will evaluate these changes in detail, and if these revisions are applicable to SAP, as CECL is considered.

Subsequent Revisions:

Several ASUs have been issued after CECL to provide clarification and improvements to the guidance in ASC Topic 326. Note that references to CECL are inclusive of these subsequent revisions. For the discussion at the 2023 Fall National Meeting, NAIC staff will include the following ASUs:

- *ASU 2018-19, Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, amends CECL guidance by providing clarification on two specific issues.
    - Issue 1 amended the transition date effective for nonpublic entities from 2020 to 2021 year-end.
    - Issue 2 clarifies that receivables from operating leases are not within the scope of CECL and should be accounted for in accordance with Topic 820.
- *ASU 2019-04, Codification Improvements to Topics 326, 815, 825*, addresses several topics, which are further disaggregated by issue, intended to clarify or correct the original CECL guidance. The Topics are numbered from 1-5 with several individual issues addressed within each Topic.
    - Topic 1 provides clarifications on accrued interest, transfers between categories/classifications of loans and debt securities, and recoveries on previously written off financial assets.
    - Topic 2 corrects cross-references, clarifies that reinsurance recoverables are within the scope of CECL, and provides methodological clarifications in several areas involving the calculation of credit loss reserves (see Issues 2D through 2F).
    - Topic 3 provides clarifications and corrections on several issues involving Fair Value Hedges and Hedge Accounting and clarifies that non-profit organizations that do not separately report earnings may not adopt the amortization approach as detailed for fair value hedging.
    - Topic 4 clarifies that Health and Welfare Benefit plans are not within the scope of CECL, that the scope of certain disclosures is limited to only public entities and clarifies guidance on alternative to fair value valuations.
    - Topic 5 clarifies the presentation of line of credit converted to debt items and whether entities should consider extension or renewals when calculating contract terms.
- *ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*, amends the effective date for various ASUs. The transition date for CECL was moved to December 15, 2022, for all entities other than public SEC filers.
- *ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, addresses five issues identified with CECL.
    - Issues 1 and 2 involve clarifications and additional guidance on assets purchased with credit deterioration.
    - Issue 3 extends the disclosure relief detailed in ASU 2019-04 to additional disclosures on accrued interest receivables.
    - Issue 4 provides clarifications on CECL assessments which involve financial assets secured by collateral maintenance provisions.
    - Issue 5 corrects a cross-reference error.
- *ASU 2020-03 Codification Improvements to Financial Instruments* addresses several issues identified with CECL.
    - Issue 1 clarifies that all entities are required to provide the fair value option disclosures.
    - Issue 2 corrects certain paragraphs in Topic 820 to include the phrase nonfinancial items accounted for as derivatives under Topic 815 to be consistent with the previous amendments.
    - Issue 3 clarifies that the disclosure requirements in Topic 320 apply to the disclosure requirements in Topic 942 for depository and lending institutions.
    - Issues 4 and 5 correct and enhance various cross-references.
    - Issue 6 clarifies the correct contractual term used to measure the net investment in a lease.
    - Issue 7 clarifies that when an entity regains control of financial assets sold, an allowance for credit losses should be recorded in accordance with Topic 326.

Staff Analysis:

The main purpose of statutory accounting principles (SAP) is to address the concerns of regulators, primarily as it relates to assessing solvency, who are the primary users of statutory financial statements. To do so, SAP stresses measurement of a company's ability to pay claims in the future and adopts reasonably conservative principles of accounting to ensure that insurance companies' capital and surplus is reflective of funds in excess of policyholder

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liabilities which are available to pay claims should the assets backing reserves become insufficient. Risk-based capital then provides a basis for evaluating the sufficiency of this capital and surplus amount in the context of a particular company's risk-taking activities, including its exposure to credit risk. Capital requirements are calibrated to ensure sufficiency of capital even during periods of economic uncertainty and distress, within the intended level of statistical safety.

The statutory framework has long incorporated concepts that incorporate a prospective view of future credit risk that historical GAAP has not. The first is the Asset Valuation Reserve (AVR). AVR requires life insurance companies to establish a reserve to account for future impairment losses on all assets (with some minor exceptions). While this is much more formulaic than the allowance required under CECL, it is intended to accomplish the same objective. The second is that *SSAP No. 26R—Bonds* requires insurance companies that do not maintain AVR to report bonds at fair value if the bond is not considered high-quality (NAIC designations 3 to 6). While this requirement does not result in credit loss reserves, it does have a similar effect by requiring non-life companies to report lower quality bonds at fair value or convert previously highest or high-quality bonds to fair value in the event of credit quality degradation. Further, the RBC formula factors in the credit risk of each individual asset in calculating the amount of capital required to be held. These mechanisms incorporate an expectation of future credit losses. Therefore, while GAAP has just begun recognizing an expectation of future credit losses with the advent of CECL, the statutory framework has recognized and incorporated future credit loss potential for decades.

Although the statutory framework has long considered future credit losses, it is worth assessing CECL to determine whether it could introduce any improvements to the existing statutory framework if adopted. Based on the review performed, Staff does not recommend adoption of CECL for the following reasons:

- CECL is a framework that incorporates significant judgement and forecasting by the company to establish credit reserves. The assumptions and data that go into these estimates are required to be company-specific, reflecting the company's reasonable and supportable forecasts of future economic conditions. It also is required to consider current economic conditions, which results in sensitivity in the reserve to changing economic conditions. The statutory framework has historically limited insurer judgment in estimating reserves. Where judgment has been allowed, there are typically mechanisms in place to closely regulate and assess those assumptions for reasonableness. Further, loss reserves and RBC are generally set to already incorporate downside risk within a desire level of statistical safety. As the framework already incorporates an expectation of adverse experience, it is not particularly volatile with changes in economic conditions. It is intended to reflect risk through the economic cycle, not at a point in time. As a result of both the volatility and judgment involved, the CECL standard does not fit the overall design of the statutory accounting and solvency monitoring framework.
- CECL does not provide a specific method that companies must use to make expected loss estimates but is instead defined by several results-oriented principles. While this does allow companies the flexibility to adopt the forecasting process that best fits their investments and company, it also means that there will be a significant diversity in the methods used to calculate expected credit losses under CECL. Such optionality is generally not considered compatible with SAP and would also place a significant burden on regulators and examiners to assess the variety of forecasting methods utilized by insurance companies.
- The majority of insurance company investments are debt securities which are generally classified as Available for Sale (AFS) for GAAP reporting. Investments classified as AFS are held at fair value with changes in fair value recorded through other comprehensive income. The portion of the CECL standard that applies to AFS securities is markedly different than what applies to debt securities held at amortized cost. Unlike GAAP, statutory accounting requires the majority of debt securities to be held at amortized cost. As a result, using a CECL standard for statutory accounting would be significantly more expansive and impactful to a statutory balance sheet than under GAAP and would result in a significantly different application of CECL between statutory accounting and GAAP, even if the identical standard were adopted.
- CECL is a complex standard that requires companies to either develop internal models or to contract an external solution to support calculating a reserve. GAAP does allow companies to elect to hold their investments under the fair value option, in which case CECL is not required. This may be an appealing option for some insurers, particularly smaller ones that wish to avoid the operational cost of CECL. The

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fair value option does not exist for statutory accounting. As such, adopting CECL would likely force insurers to incur the cost of CECL that would not otherwise be necessary for their GAAP financial statements.

- Similarly, many insurance companies do not prepare GAAP financial statements. This means that they would need to learn about and adopt CECL for the first time for their statutory financial statements if CECL were to be adopted.
- As RBC has its own methodology for incorporating credit risk, any CECL allowance would need to be reversed in the RBC formula in order to avoid double counting expected losses. This would largely eliminate any benefit of CECL to regulators' solvency monitoring efforts.

As a result of these factors, NAIC Staff does not recommend adopting CECL for statutory accounting.

Existing Authoritative Literature:

Existing SAP guidance has predominantly adopted (or adopted with modification) GAAP guidance pertaining to other-than-temporary impairment. However, the adopted guidance, although coming from GAAP, does not reflect GAAP concepts for similar securities. For example, the guidance in SSAP No. 26R reflects concepts from GAAP applicable for receivables and loans (e.g., it is probable that the entity will be unable to collect all amounts due accordingly to the contractual terms.) The guidance in *SSAP No. 43R—Loan-Backed and Structured Securities* is more comparable to current GAAP concepts applicable for both HTM and AFS debt securities (e.g., assessment of whether an entity will recover the amortized cost basis based on a review of the present value of cash flows.)

The GAAP categories for debt securities have previously been rejected for statutory accounting. As such, SAP does not include the classifications of "Held-to-Maturity," "Available-for-Sale" or "Trading" for debt securities. All debt securities are captured within SSAP No. 26R or SSAP No. 43R and reported at either amortized cost, or the lower of amortized cost or fair value, based on NAIC designation.

Existing Authoritative Literature:

INT 06-07: Definition of the Phrase "Other Than Temporary" – This INT reflects the adoption with modification of *FSP FAS 115-1/124-1: The Meaning of Other Them Temporary Impairment and Its Application to Certain Investments*. **This FSP was subsequently included in the FASB Codification in ASC 320-10 and ASC 326-30 and this ASC guidance has been deleted (or significantly revised) with the issuance of ASU 2016-13**. (This INT has not been duplicated in this agenda item.)

Preamble – This guidance reflects some of the core principles of statutory accounting as it pertains to the Staff Analysis detailed above:

> 19. SAP is conservative in some respects but not unreasonably conservative over the span of economic cycles, or in recognition of the primary statutory responsibility to regulate for financial solvency. SAP attempts to determine at the financial statement date an insurer's ability to satisfy its obligations to its policyholders and creditors.
>
> 33. Conservative valuation procedures provide protection to policyholders against adverse fluctuations in financial condition or operating results. Statutory accounting should be reasonably conservative over the span of economic cycles and in recognition of the primary responsibility to regulate for financial solvency. Valuation procedures should, to the extent possible, prevent sharp fluctuations in surplus.

SSAP No. 26R, Paragraphs 12-13 – This guidance reflects adoption of *FSP FAS 115-1/124-1: The Meaning of Other Them Temporary Impairment and Its Application to Certain Investments.* **This FSP was subsequently included in the FASB Codification in ASC 320-10 and ASC 326-30 and this ASC guidance has been deleted (or significantly revised) with the issuance of ASU 2016-13**.

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13. An other-than-temporary(INT 06-07) impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of a debt security in effect at the date of acquisition.[1] A decline in fair value which is other-than-temporary includes situations where a reporting entity has made a decision to sell a security prior to its maturity at an amount below its carrying value. If it is determined that a decline in the fair value of a bond is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the entire difference between the bond's carrying value and its fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of the impairment loss shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR/IMR, the accounting for the entire amount of the realized capital loss shall be in accordance with SSAP No. 7. The other-than-temporary impairment loss shall be recorded entirely to either AVR or IMR (and not bifurcated between credit and non-credit components) in accordance with the annual statement instructions.

14. In periods subsequent to the recognition of an other-than-temporary impairment loss for a bond, the reporting entity shall account for the other-than-temporarily impaired security as if the security had been purchased on the measurement date of the other-than-temporary impairment. The fair value of the bond on the measurement date shall become the new cost basis of the bond and the new cost basis shall not be adjusted for subsequent recoveries in fair value. The discount or reduced premium recorded for the security, based on the new cost basis, shall be amortized over the remaining life of the security in the prospective manner based on the amount and timing of future estimated cash flows. The security shall continue to be subject to impairment analysis for each subsequent reporting period. Future declines in fair value which are determined to be other-than temporary shall be recorded as realized losses.

SSAP No. 43R, Paragraphs 12-13 – This guidance reflects concepts included within *FSP FAS 115-1/124-1: The Meaning of Other Them Temporary Impairment and Its Application to Certain Investments,* as well the adoption of *EITF 99-20, Exchange of Interest-Only and Principal-Only Securities for a Mortgage-Backed Security,* and *FSP ETIF 99-20-1, Amendments to the Impairment Guidance of ETIF Issue 99-20.* **The guidance reflected from this FSP was included in ASC 310-20, 325-40, and 326-30 and has been deleted or significantly revised with the issuance of ASU 2016-13:**

Collection of All Contractual Cashflows is Not Probable

19. The following guidance applies to loan-backed and structured securities with evidence of deterioration of credit quality since origination for which it is probable, either known at acquisition or identified during the holding period, that the investor will be unable to collect all contractually required payments receivable, except for those beneficial interests that are not of high credit quality or can contractually be prepaid or otherwise settled in such a way that the reporting entity would not recover substantially all of its recorded amount determined at acquisition (see paragraphs 22-25).

20. The reporting entity shall recognize the excess of all cash flows expected at acquisition over the investor's initial investment in the loan-backed or structured security as interest income on an effective-yield basis over the life of the loan-backed or structured security (accretable yield). Any excess of contractually required cash flows over the cash flows expected to be collected is the nonaccretable difference. Expected prepayments shall be treated consistently for determining cash flows expected to be collected and projections of contractual cash flows such that the nonaccretable difference is not affected. Similarly, the difference between actual prepayments and expected prepayments shall not affect the nonaccretable difference.

21. An investor shall continue to estimate cash flows expected to be collected over the life of the loan-backed or structured security. If, upon subsequent evaluation:

[1] If a bond has been modified from original acquisition, the guidance in *SSAP No. 36—Troubled Debt Restructuring* and paragraph 22 of *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* shall be followed, as applicable. After modification of original terms, future assessments to determine other-than-temporary impairment shall be based on the modified contractual terms of the debt instrument.

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a. The fair value of the loan-backed or structured security has declined below its amortized cost basis, an entity shall determine whether the decline is other than temporary (INT 06-07). For example, if, based on current information and events, there is a decrease in cash flows expected to be collected (that is, the investor is unable to collect all cash flows expected at acquisition plus any additional cash flows expected to be collected arising from changes in estimate after acquisition (in accordance with paragraph 19.b.), an other-than-temporary impairment shall be considered to have occurred. The investor shall consider both the timing and amount of cash flows expected to be collected in making a determination about whether there has been a decrease in cash flows expected to be collected.

b. Based on current information and events, if there is a significant increase in cash flows previously expected to be collected or if actual cash flows are significantly greater than cash flows previously expected, the investor shall recalculate the amount of accretable yield for the loan-backed or structured security as the excess of the revised cash flows expected to be collected over the sum of (1) the initial investment less (2) cash collected less (3) other-than-temporary impairments plus (4) amount of yield accreted to date. The investor shall adjust the amount of accretable yield by reclassification from nonaccretable difference. The adjustment shall be accounted for as a change in estimate in conformity with *SSAP No. 3—Accounting Changes and Corrections of Errors* (SSAP No. 3), with the amount of periodic accretion adjusted over the remaining life of the loan-backed or structured security (prospective method).

Unrealized Gains and Losses and Impairment Guidance

29. For reporting entities required to maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with paragraph 36 of this statement. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

30. The application of this reporting requirement resulting from NAIC designation (i.e., lower of cost or fair value) is not a substitute for other-than-temporary impairment recognition (paragraphs 33-37). For securities reported at fair value where an other-than-temporary impairment has been determined to have occurred, the realized loss recognized from the other-than-temporary impairment shall first be applied towards the realization of any unrealized losses previously recorded as a result of fluctuations in the security's fair value due to the reporting requirements. After the recognition of the other-than-temporary impairment, the security shall continue to report unrealized gains and losses as a result of fluctuations in fair value.

31. If the fair value of a loan-backed or structured security is less than its amortized cost basis at the balance sheet date, an entity shall assess whether the impairment is other than temporary. Amortized cost basis includes adjustments made to the cost of an investment for accretion, amortization, collection of cash, previous other-than-temporary impairments recognized as a realized loss.

32. If an entity intends to sell the loan-backed or structured security (that is, it has decided to sell the security), an other-than-temporary impairment shall be considered to have occurred.

33. If an entity does not intend to sell the loan-backed or structured security, the entity shall assess whether it has the intent and ability[2] to retain the investment in the security for a period of time sufficient to recover the amortized cost basis. If the entity does not have the intent and ability to retain the investment for the time sufficient to recover the amortized cost basis, an other-than-temporary impairment shall be considered to have occurred.

34. If the entity does not expect to recover the entire amortized cost basis of the security, the entity would be unable to assert that it will recover its amortized cost basis even if it does not intend to sell the

[2] This assessment shall be considered a high standard due to the accounting measurement method established for the securities within the scope of this statement (amortized cost).

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security and the entity has the intent and ability to hold. Therefore, in those situations, an other-than temporary impairment shall be considered to have occurred. (For mortgage-referenced securities, an OTTI is considered to have occurred when there has been a delinquency or other credit event in the referenced pool of mortgages such that the entity does not expect to recover the entire amortized cost basis of the security.) In assessing whether the entire amortized cost basis of the security will be recovered, an entity shall compare the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If present value of cash flows expected to be collected is less than the amortized cost basis of the security, the entire amortized cost basis of the security will not be recovered (that is, a non-interest related decline[3] exists), and an other-than-temporary impairment shall be considered to have occurred. A decrease in cashflows expected to be collected on a loaned-backed or structured security that results from an increase in prepayments on the underlying assets shall be considered in the estimate of the present value of cashflows expected to be collected.

35. In determining whether a non-interest related decline exists, an entity shall calculate the present value of cash flows expected to be collected based on an estimate of the expected future cash flows of the impaired loan-backed or structured security, discounted at the security's effective interest rate.

a. For securities accounted for under paragraphs 14-18 – the effective interest rate of the loan-backed or structured security is the rate of return implicit in the security (that is, the contractual interest rate adjusted for any net deferred fees or costs, premium, or discount existing at the origination or acquisition of the security).

b. For securities accounted for under paragraphs 19-21 – the effective interest rate is the rate implicit immediately prior to the recognition of the other-than-temporary impairment.

c. For securities accounted for under paragraphs 22-25 – the reporting entity shall apply the guidance in paragraph 24.b.

36. When an other-than-temporary impairment has occurred because the entity intends to sell the security or has assessed that that they do not have the intent and ability to retain the investments in the security for a period of time sufficient to recover the amortized cost basis, the amount of the other-than-temporary impairment recognized in earnings as a realized loss shall equal the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. (This guidance includes loan-backed and structured securities previously held at lower of cost or market. For these securities, upon recognition of an other-than-temporary impairment, unrealized losses would be considered realized.)

37. When an other-than-temporary impairment has occurred because the entity does not expect to recover the entire amortized cost basis of the security even if the entity has no intent to sell and the entity has the intent and ability to hold, the amount of the other-than-temporary impairment recognized as a realized loss shall equal the difference between the investment's amortized cost basis and the present value of cash flows expected to be collected, discounted at the loan-backed or structured security's effective interest rate in accordance with paragraph 35. (This guidance includes loan-backed and structured securities previously held at lower of cost or market. For these securities, upon recognition of an other-than-temporary impairment, unrealized losses would be considered realized for the non-interest related decline. Hence, unrealized losses could continue to be reflected for these securities due to the reporting requirements.)

Reinsurance recoverables are explicitly included in the scope of the new CECL guidance, but only for "*expected losses related to the credit risk of the reinsurer/assuming company"* (326-20-55-82). The current existing statutory accounting guidance does not include the concept of reserving for expected credit losses. It should be noted that while not related to creditworthiness, *SSAP No. 62R—Property and Casualty Reinsurance* does include the concept

[3] A non-interest related decline is a decline in value due to fundamental credit problems of the issuer. Fundamental credit problems exist with the issuer when there is evidence of financial difficulty that may result in the issuer being unable to pay principal or interest when due. An interest related decline in value may be due to both increases in the risk-free interest rate and general credit spread widening.

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of the provision for reinsurance, which is more focused on known overdue/uncollectible reinsurance and does not take the creditworthiness of the reinsurer into the calculation. However, impairment analysis is required for reinsurance balances in both *SSAP No. 61R—Life, Deposit -Type and Accident and Health Reinsurance* and SSAP No. 62R.

Multiple other SSAPs are impacted by the updated guidance, and NAIC Staff has prepared tables in Exhibit 1 which provide detailed summarizations of the updates made by CECL.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

The following ASUs were issued after CECL as clarifications and improvements to the guidance in ASC Topic 326 but have already been addressed for statutory accounting purposes by the Working Group:

- *ASU 2019-05 Financial Instruments—Credit Losses (Topic 326)—Targeted Transition Relief* was assessed and rejected for statutory accounting purposes by the Working Group. For further details see Agenda Item 2019-28.
- *ASU 2022-02 Financial Instruments—Credit Losses (Topic 326) Troubled Debt Restructurings and Vintage Disclosures* was assessed and rejected for statutory accounting purposes by the Working Group. For further details see Agenda Item 2022-10.
- *ASU 2022-01 Derivatives and Hedging (Topic 815) Fair Value Hedging—Portfolio Layer Method* was assessed and adopted with modification for statutory accounting purposes by the Working Group. For further details see Agenda Item 2022-09.

Agenda item 2016-20 was started on CECL and last exposed for comment on August 4, 2018.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None.

Convergence with International Financial Reporting Standards (IFRS):
The credit losses project began as a joint project with the IASB, but the Boards determined that convergence was not possible in 2012 due to the differing needs of their respective stakeholder groups. The IASB issued *IFRS 9, Financial Instruments* in July 2014. The FASB and IASB both sought to respond to concerns identified pertaining to the delayed recognition of credit losses; however, the IASB's stakeholders strongly preferred an impairment model that uses a dual measurement approach, while U.S. stakeholders strongly preferred the current expected credit loss model.

The main difference between ASU 2016-13 and IFRS 9 relates to the timing of recognition of expected losses. The ASU requires that the full amount of expected credit losses be recorded for all financial assets measured at amortized cost, whereas IFRS 9 requires an allowance for credit losses equal to 12 months of expected credit losses until there is a significant increase in credit risk, at which point lifetime expected losses are recognized. Consequently, the allowance for credit losses as measured and recorded under the ASU will be accounted for differently under GAAP than under IFRS and will have a different effect on the financial statements.

Staff Recommendation:
Based on the Staff Analysis detailed on Pages 6-7, Staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to reject *ASU 2016-13 Measurement of Credit Losses on Financial Instruments* and other related ASUs (see "Subsequent Revisions" on page 5) within the following SSAPs:

- *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments*
- *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*
- *SSAP No. 22R—Leases*

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- *SSAP No. 26R—Bonds*
- *SSAP No. 32R—Preferred Stock*
- *SSAP No. 34—Investment Income Due and Accrued*
- *SSAP No. 37—Mortgage Loans*
- *SSAP No. 39—Reverse Mortgages*
- *SSAP No. 41R—Surplus Notes*
- *SSAP No. 43R—Loan and Asset Backed Securities*
- *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*
- *SSAP No. 62R—Property and Casualty Reinsurance*
- *SSAP No. 86—Derivatives*
- *SSAP No. 103R—Transfer/Service of Financial Assets*
- *SSAP No. 105R—Working Capital Finance Investments*
- *INT 06-07: Definition of the Phrase "Other Than Temporary*

Staff also recommends modifying *INT 06-07: Definition of Phrase "Other Than Temporary"* to clarify that companies should adhere to the impairment guidance detailed within the SSAPs, which may reflect U.S. GAAP guidance prior to the FASB's issuance of ASU 2016-13.

Agenda item 2016-20 was started on CECL and last exposed for comment on August 4, 2018. Agenda item 2016-20 was reviewed by NAIC Staff, and we recommend it be formally disposed and replaced by this new agenda item.

Proposed Revisions to SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments

Relevant Literature

21. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets

43. This statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 22R—Leases

53. This statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842),

ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 26R—Bonds

33. This statement rejects the GAAP guidance for debt securities, which is contained in *ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs*, *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, ASU 2017-08, Premium Amortization on Purchased Callable Debt* Securities, ASU *2016-01, Financial Instruments – Overall*, *FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases, FASB Emerging Issues Task Force No. 89-18, Divestitures of Certain Investment Securities to an Unregulated Commonly Controlled Entity under FIRREA,* and *FASB Emerging Issues Task Force No. 96-10, Impact of Certain Transactions on Held-to-Maturity Classifications Under FASB Statement No. 115*. This statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments.

Proposed Revisions to SSAP No. 32R—Preferred Stock

21. This statement rejects *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial* Liabilities*, ASU 2016-01, Financial Instruments – Overall, FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities* and *FASB Emerging Issues Task Force No. 86-32, Early Extinguishment of a Subsidiary's Mandatorily Redeemable Preferred Stock*. This statement adopts *FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,* paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. This statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments.

Proposed Revisions to SSAP No. 34—Investment Income Due and Accrued

9. This statement adopts FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. This statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 37—Mortgage Loans

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31. This statement rejects *FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*, *FASB Emerging Issues Task Force No. 88-17, Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations,* and *AICPA Practice Bulletin 6, Amortization of Discounts on Certain Acquired Loans*. This statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments.

Proposed Revisions to SSAP No. 39—Reverse Mortgages

Relevant Literature

17. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments.*

Proposed Revisions to SSAP No. 41R—Surplus Notes

22. This statement rejects AICPA Practice Bulletin No. 15, Accounting by the Issuer of Surplus Notes, which requires surplus notes to be accounted for as debt and that interest be accrued over the life of the surplus note, irrespective of the approval of interest and principal payments by the insurance commissioner. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments*.

Proposed Revisions to SSAP No. 43R—Loan-Backed and Structured Securities

58. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments.*

Proposed Revisions to SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance

88. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842),*

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ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 62R—Property and Casualty Reinsurance

129. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 86—Derivatives

73. This statement rejects 2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40), Accounting for Convertible Instruments and Contracts in an Entity's Own Equity, ASU 2020-01, Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815), Clarifying the Interactions between Topic 321, Topic 323 and Topic 815, ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, and ASU 2016-03, Intangibles—Goodwill and Other, Business Combinations, Consolidation, Derivatives and Hedging. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 103R—Transfer/Service of Financial Assets

134. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 105R—Working Capital Finance Investments

Relevant Literature

32. This statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and ASU 2020-03 Codification Improvements to Financial Instruments*.

Proposed Revisions to INT 06-07: Definition of Phrase "Other Than Temporary"

INT 06-07 Discussion

13. On xx/xx/2024, the Working Group rejected *ASU 2016-13 Measurement of Credit Losses on Financial Instruments* and other related ASUs. As a result, companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect prior U.S. GAAP guidance.

Staff Review Completed by:
NAIC Staff – William Oden, September 2023

Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification and exposed this agenda item to reject ASU 2016-13, *ASU 2018-19, Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, *ASU 2019-04, Codification Improvements to Topics 326, 815, 825*, *ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)*, *ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*, within INT 06-07: Definition of Phrase "Other Than Temporary" and fifteen applicable SSAPs which are detailed above. The Working Group also moved agenda item 2026-20, which was started to address CECL, to the disposed listing. The Working Group directed NAIC staff to research how best to maintain pre-CECL GAAP impairment guidance for posterity.

On December 11, 2023, the Working Group chair approved an accelerated comment deadline that was requested by industry after the December 1, 2023 meeting. As a result, the comment deadline for the Fall National Meeting exposure of agenda item 2023-24 was shortened from February 4, 2024 to December 29, 2023, to allow the Working Group the ability to formally reject CECL and other related ASUs in January 2024.

On January 10, 2024, the Working adopted, as final, the exposed revisions, as detailed below, to INT 06-07 and SSAP Nos. 2R, 5R, 22R, 26R, 32R, 34, 37, 39, 41R, 61R, 62R, 86, 103R, and 105R to reject ASUs 2016-13, 2018-19, 2019-04, 2019-10, 2019-11, and 2020-03 as not applicable to statutory accounting. The Working Group also reiterated its direction to NAIC staff to research and prepare a document to maintain pre-CECL GAAP impairment guidance for posterity.

Note on January 10, 2024, Exposed Revisions: Subsequent to the Fall National Meeting Exposure, additional consistency revisions were made to the proposed revisions and are shown highlighted grey below for January 10, 2024, discussion. The sentence directing companies to continue applying the relevant statutory accounting impairment guidance was originally excluded from any revised SSAPs which was within scope of INT 06-07 as the INT already had this sentence. Staff later determined that it would be clearer and cleaner to have this sentence within all revised SSAPs. Additionally, Staff adjusted each of the revised SSAPs to specifically denote the effective date of the rejection.

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Proposed Revisions to SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments

Relevant Literature

21. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets

43. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 22R—Leases

53. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 26R—Bonds

33. This statement rejects the GAAP guidance for debt securities, which is contained in *ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs*, *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, ASU 2017-08, Premium Amortization on Purchased Callable Debt* Securities, ASU *2016-01, Financial Instruments – Overall*, *FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases, FASB Emerging Issues Task Force No. 89-18, Divestitures of Certain Investment Securities to an Unregulated Commonly Controlled Entity under FIRREA,* and *FASB Emerging Issues Task Force No. 96-10, Impact of Certain Transactions on Held-to-Maturity Classifications Under FASB Statement No. 115.* Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification*

Improvements to Financial Instruments. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 32R—Preferred Stock

21. This statement rejects *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial* Liabilities*, ASU 2016-01, Financial Instruments – Overall, FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities* and *FASB Emerging Issues Task Force No. 86-32, Early Extinguishment of a Subsidiary's Mandatorily Redeemable Preferred Stock*. This statement adopts *FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments,* paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. Effective December 31, 2023, ~~T~~this statement rejects ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, *ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 34—Investment Income Due and Accrued

9. This statement adopts FASB Staff Position 115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, paragraph 16, with modification to be consistent with statutory language in the respective statutory accounting statements. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 37—Mortgage Loans

31. This statement rejects *FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*, *FASB Emerging Issues Task Force No. 88-17, Accounting for Fees and Costs Associated with Loan Syndications and Loan Participations,* and *AICPA Practice Bulletin 6, Amortization of Discounts on Certain Acquired Loans*. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments*, *ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, *ASU 2019-04 Codification Improvements to Topics 326, 815, 825*, *ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842*), *ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 39—Reverse Mortgages

Relevant Literature

17. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 41R—Surplus Notes

22. This statement rejects AICPA Practice Bulletin No. 15, Accounting by the Issuer of Surplus Notes, which requires surplus notes to be accounted for as debt and that interest be accrued over the life of the surplus note, irrespective of the approval of interest and principal payments by the insurance commissioner. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 43R—Loan-Backed and Structured Securities

58. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance

88. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 62R—Property and Casualty Reinsurance

129. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to*

Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 86—Derivatives

73. This statement rejects 2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40), Accounting for Convertible Instruments and Contracts in an Entity's Own Equity, ASU 2020-01, Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815), Clarifying the Interactions between Topic 321, Topic 323 and Topic 815, ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, and ASU 2016-03, Intangibles—Goodwill and Other, Business Combinations, Consolidation, Derivatives and Hedging. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 103R—Transfer/Service of Financial Assets

134. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to SSAP No. 105R—Working Capital Finance Investments

Relevant Literature

32. Effective December 31, 2023, ~~T~~this statement rejects *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments*. Companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect U.S. GAAP guidance prior to FASB's issuance of ASU 2016-13 and other related ASUs.

Proposed Revisions to INT 06-07: Definition of Phrase "Other Than Temporary"

INT 06-07 Discussion

13. ~~On xx/xx/2024,~~ Effective December 31, 2023, ~~T~~the Working Group rejected *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses,* and *ASU 2020-03 Codification Improvements to Financial Instruments. ~~ASU 2016-13 Measurement of Credit Losses on Financial Instruments~~* ~~and other related ASUs.~~ As a result, companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect prior U.S. GAAP guidance.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/01 1-10-24/01 - 23-24 - ASU 2016-13 - CECL.docx

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Exhibit 1 – Summary of Changes from ASU 2016-13 and subsequent ASUs

ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Balance Sheet—Overall	210-10	Removal of disclosure guidance link.	45-15
Comprehensive Income—Overall	220-10	Supersede content and amend AFS guidance link.	45-10A 45-16A 55-15B
Statement of Cash Flows—Overall	230-10	Amends guidance to say amortized cost basis.	45-21
Interim Reporting—Overall	270-10	Amend guidance for new credit loss language and include references to transition guidance.	50-1
Receivables—Overall	310-10	Amends guidance for new CECL language, supersedes (or transfers to 326) several guidance paragraphs including OTTI, and adds new guidance on PCD interest income.	05-1 35-1 thru 49 35-53A thru C 45-1 45-4A 45-5 45-6 50-1 thru 35 55-1 thru 12 55-16 thru 22
Receivables—Nonrefundable Fees and Other Costs	310-20	Amends guidance for new CECL language and supersedes OTTI guidance.	15-3 15-4 35-9 60-1 60-2
Receivables—Loans and Debt Securities Acquired with	310-30	Supersedes entire subtopic and replaces with transition guidance.	All

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ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Deteriorated Credit Quality			
Receivables—Troubled Debt Restructurings by Creditors	310-40	Amends guidance for new CECL language, supersedes OTTI guidance, and eliminates exclusion of loan pools from the scope of 310-40.	15-11 15-12 35-7 thru 12 40-3 50-1 thru 6 55-7 55-13 thru 15
Investments—Debt Securities—Overall	320-10	Amends guidance for new CECL language and supersedes all OTTI and credit loss guidance.	15-4 15-9 15-10 35-1 35-17 thru 24 35-30 35-33A thru I 35-34 thru 37 35-43 40-1 40-2 45-7 thru 9A 50-1 thru 8B 55-16 thru 19 55-21A thru 23
Investments—Equity Method and Joint Ventures—Overall	323-10	Amendment conforms terminology to match CECL guidance.	35-25 55-30 55-34 55-38 55-42 55-44 55-46

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ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Investments—Other—Beneficial Interests in Securitized Financial Assets	325-40	Amends guidance for new CECL language and supersedes all OTTI and credit loss guidance. Also adds specific guidance for benefit interests acquired as with PCD and adds a requirement to use the PV of future cash flows to measure expected credit losses for benefit interests.	15-3 15-4 25-2 30-1 thru 2 35-2 thru 4C 35-6 35-6A thru 10B 35-13 35-14 55-1
Financial Instruments—Credit Losses	326-10 326-20 326-30	Creates Topic 326 codification; note that some guidance was moved from existing codification for inclusion within 326 and these transfers are underlined. Note that AFS and HTM classifications are not applicable for statutory accounting purposes.	All
Contingencies—Loss Contingencies	450-20	Amendment conforms terminology to match CECL guidance and includes codification links to topic 326.	15-2 50-2A 60-2 60-3
Guarantees—Overall	460-10	Amendment conforms terminology to match CECL guidance and requires that guarantees within the scope of 326 must bifurcate the instruments and apply Topic 326 guidance to the contingent portion and Topic 460 to the non-contingent portion.	25-2 25-3 30-5 35-3 35-4 45-1 50-4 50-5 55-21 55-22

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ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Debt —Troubled Debt Restructurings by Debtors	470-60	Amendment conforms terminology to match CECL guidance.	15-3 15-12
Revenue from Contracts with Customers—Overall	606-10	Amendment conforms terminology to match CECL guidance and includes codification links to topic 326.	45-3 45-4 50-4 55-108 55-109 55-231 55-237 55-239
Business Combinations—Identifiable Assets and Liabilities, and Any Noncontrolling Interest	805-20	Amendment conforms terminology to match CECL and guidance on recording PCD assets which are within the scope of CECL or are purchased with credit deterioration. Additionally, guidance was simplified for indemnification assets arising from government-assisted acquisitions of a financial institution.	30-2 30-4 thru 4B 30-10 30-12 30-26 35-4B
Consolidation—Overall	810-10	Amendment conforms terminology to match CECL guidance.	30-8C
Derivatives and Hedging—Overall	815-10	Amends guidance for new CECL language and supersedes OTTI guidance.	35-5
Derivatives and Hedging—Embedded Derivatives	815-15	Amends OTI guidance to instead direct reader to Topic 326.	25-5
Derivatives and Hedging—Fair Value Hedges	815-25	Amendments conforms terminology to match CECL guidance and includes codification links to topic 326.	35-10 thru 12 55-85 thru 90
Derivatives and Hedging—Cash Flow Hedges	815-30	Amendment conforms terminology to match CECL guidance.	35-42 35-43

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ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Fair Value Measurement—Overall	820-10	Amendment conforms terminology to match CECL guidance.	55-92
Financial Instruments—Overall	825-10	Amendment conforms terminology to match CECL guidance and supersedes old credit loss guidance.	05-2 25-4 35-1 thru 3 55-8 55-10
Foreign Currency Matters—Foreign Currency Transactions	830-20	Amendment conforms terminology to match CECL guidance and supersedes old AFS guidance for foreign currency debt securities.	35-6 35-7
Interest—Overall	835-10	Amendment supersedes interest income recognition on impaired or deteriorated credit quality loans.	60-2 60-3
Leases—Lessor	842-30	Amendment conforms terminology to match CECL guidance and supersedes impairment guidance/terminology with credit loss guidance.	25-2 25-6 25-9 35-3 40-2
Leases—Leveraged Lease Arrangements	842-50	Amendment removes original OTTI reference and adds codification references to Topic 326.	50-2
Subsequent Events—Overall	855-10	Amendment conforms terminology to match CECL guidance and remove examples now subject to Topic 326.	55-1 55-2
Transfers and Servicing—Sales of Financial Assets	860-20	Amendment conforms terminology to match CECL guidance and adds reference links to Topic 326 for the sale of financial assets which are receivables, purchased financial asset with credit deterioration, or is a beneficial interest that meets the criteria in paragraph 325-40-30-1A.	30-2 35-3 35-9 50-5 55-19
Financial Services—Depository and	942-230	Amendment terminology in implementation illustration to match CECL guidance.	55-2 55-4

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ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Lending—Statement of Cash Flows			
Financial Services—Depository and Lending—Receivables	942-310	Amendment conforms terminology to match CECL guidance and supersedes impairment guidance.	05-1 05-4 25-1 35-1 55-1
Financial Services—Insurance—Insurance Activities	944-20	Amendment removes impairment guidance/terminology.	55-37
Financial Services—Insurance—Separate Accounts	944-80	Amendment supersedes impairment and unrealized gain/loss guidance/terminology with credit loss guidance.	25-9 55-11 55-16
Financial Services—Insurance—Receivables	944-310	Amendment conforms terminology to match CECL guidance and adds requirement to assess credit losses on insurance receivables and references to Topic 326.	35-3 35-4 35-6 45-4 45-4A
Financial Services—Mortgage Banking—Receivables	948-310	Amendment conforms terminology to match CECL guidance and supersedes impairment guidance with Topic 326.	30-1 30-4 35-1 thru 3 35-5 35-5A 50-1
Health Care Entities—Income Statement	954-225	Amendment replaces impairment reference with credit loss language.	45-8
Health Care Entities—Receivables	954-310	Amendment replaces uncollectible accounts guidance with credit loss guidance.	30-1 35-1
Not-for-Profit Entities—Investments—Debt and Equity Securities	958-320	Amendment replaces impairment guidance with credit loss guidance.	55-5

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ASU 2016-13 Financial Instruments—Credit Losses (Topic 326)			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Not-for-Profit Entities—Investments—Other	958-325	Amendment replaces impairment guidance with credit loss guidance.	30-1 35-1
Real Estate—Time-Sharing Activities—Receivables	978-310	Amendment replaces uncollectible accounts guidance with credit loss guidance.	35-5 35-6

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ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Financial Instruments—Credit Losses—Overall	326-10	Extends effective date of CECL from 2020 to 2021.	65-1
Financial Instruments—Credit Losses—Measured at Amortized Cost	326-20	Add clarification that operating lease receivables are in scope of Topic 842.	15-3
Various	Various	Amend the transition dates of all pending content paragraphs that link to transition guidance paragraph 326-10-65-1 from 2020 to 2021.	Various

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Financial Instruments—Credit Losses—Measured at Amortized Cost & Financial Instruments—Credit Losses—Available-for-Sale Debt Securities	326-20 & 326-30	The amendments related to accrued interest receivables provide an entity with the ability to measure an allowance for credit losses on accrued interest receivables separately from the allowance for credit losses on the other components of the amortized cost basis and to make certain accounting policy elections and apply a practical expedient to operationalize the amendments in Update 2016-13.	30-5 30-5A 35-8A 45-5 50-3A thru 3D 30-1A 30-1B 35-13A 45-1 50-3A thru 4
Receivables—Overall & Investments—Debt Securities—Overall & Financial Instruments—Credit Losses—Measured at Amortized Cost & Financial Services—Mortgage Banking—Receivables	310-10 & 320-10 & 326-20 & 948-10	The amendments related to transfers between classifications or categories for nonmortgage loans and debt securities provide an entity with guidance on how to account for the allowance for credit losses or the valuation allowance when transferring loans and debt securities.	35-47 thru 48B 45-2 35-10 thru 10B 35-15 35-16 45-8B 55-24 55-25 35-7 30-4 35-2A 35-5A 45-2
Financial Instruments—Credit Losses—Measured at Amortized Cost &	326-20 & 326-30	The amendments clarify that an entity should consider expected recoveries when measuring the allowance for credit losses by superseding the guidance in paragraphs 326-20-35-8 through 35-9 that may have precluded an entity from	30-1 35-4 35-5 35-8 35-9

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Financial Instruments—Credit Losses—Available-for-Sale Debt Securities		considering recoveries when estimating expected credit losses on financial assets measured at amortized cost basis. Additionally, the amendments clarify that expected recoveries of amounts previously written off and expected to be written off should be included in the valuation account and should not exceed the aggregate of amounts previously written off and expected to be written off by the entity.	50-13 55-52 35-12 35-13
Receivables—Troubled Debt Restructurings by Creditors	310-40	The amendment clarifies paragraph 310-40-55-14 by removing the incorrect cross-reference to paragraph 326-20-35-2 and, instead, properly cross-referencing paragraphs 326-20-35-4 through 35-5, which require that an entity use 41 the fair value	55-14
Investments—Equity Method and Joint Ventures—Overall	323-10	The amendment to paragraph 323-10-35-26 clarifies the guidance by including references to both Subtopic 326-20, Financial Instruments—Credit Losses—Measured at Amortized Cost, and Subtopic 326-30, Financial Instruments—Credit Losses—Available-for-Sale Debt Securities, to require the subsequent measurement of credit losses on financial assets after the guidance on equity method losses is applied.	35-24 35-26
Financial Instruments—Credit Losses—Measured at Amortized Cost	326-20	The amendments clarify that reinsurance recoverables that result from insurance transactions that are within the scope of Topic 944, Financial Services—Insurance, are within the scope of Subtopic 326-20 even if those reinsurance recoverables are measured on a net present value basis in accordance with Topic 944.	05-1 15-2
Financial Instruments—Credit	326-20 &	The amendments clarify the Board's intent for how an entity should determine the effective	30-4

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Losses—Measured at Amortized Cost & Financial Instruments—Credit Losses—Available-for-Sale Debt Securities	326-30	interest rate and estimated expected future cash flows by removing the prohibition in the guidance and requiring that the projections used for determining the effective interest rate also be used in determining the estimated expected future cash flows. The amendments also clarify that if an entity projects future interest rate environments when using a discounted cash flow method to measure expected credit losses on variable-rate financial instruments, then the entity should adjust the effective interest rate to consider the timing (and changes in the timing) of expected cash flows resulting from expected prepayments.	35-11
Financial Instruments—Credit Losses—Measured at Amortized Cost & Financial Instruments—Credit Losses—Available-for-Sale Debt Securities	326-20 & 326-30	The amendments in paragraph 326-20-30-4A permit an entity to make an accounting policy election to adjust the effective interest rate used to discount expected cash flows of a financial asset. The amendments also clarify that an entity should not adjust the effective interest rate used to discount expected cash flows for subsequent changes in expected prepayments if the financial asset is restructured in a troubled debt restructuring. Paragraph 326-30-35-7A was also amended to allow an entity to make an accounting policy election to adjust the effective interest rate used to discount expected cash flows of a debt security classified as available-for-sale	30-4A 35-7A
Financial Instruments—Credit Losses—Measured at Amortized Cost	326-20	The amendments clarify the guidance and align the measurement of credit losses using fair value of collateral when foreclosure is probable and when an entity elects the collateral-dependent	35-4 35-5

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
		practical expedient by adding a requirement to adjust the fair value of the collateral for estimated costs to sell in paragraph 326- 20-35-4. Additionally, the amendments clarify the guidance that when an entity adjusts the fair value of the collateral for the estimated costs to sell, the estimated costs to sell should be undiscounted if the entity intends to sell rather than operate the collateral.	
Derivatives and Hedging—Hedging—General & Derivatives and Hedging—Fair Value Hedges	815-20 & 815-25	The amendments clarify that an entity may measure the change in fair value of a hedged item using an assumed term only for changes attributable to interest rate risk. They also clarify that an entity may measure the change in the fair value of the hedged item attributable to interest rate risk using an assumed term when the hedged item is designated in a hedge of both interest rate risk and foreign exchange risk. In addition, the amendments clarify that one or more separately designated partial term fair value hedging relationships of a single financial instrument can be outstanding at the same time.	25-12 35-13B 55-99
Derivatives and Hedging—Fair Value Hedges	815-25	The amendments clarify that an entity may, but is not required to, begin to amortize a fair value hedge basis adjustment before the fair value hedging relationship is discontinued. They also clarify that if an entity elects to amortize the basis adjustment during an outstanding partial-term hedge, the basis adjustment should be fully amortized by the hedged item's assumed maturity date in accordance with paragraph 815-25-35-13B.	35-9A

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Derivative and Hedging—Overall	815-10	The amendments clarify that an entity should disclose available-for-sale debt securities at their amortized cost and that fair value hedge basis adjustments related to foreign exchange risk should be excluded from the disclosures required by paragraph 815-10-50-4EE.	4EE
Derivatives and Hedging—Cash Flow Hedges	815-30	The amendment clarifies that an entity should consider the contractually specified interest rate being hedged when applying the hypothetical derivative method.	35-26
Derivative and Hedging—Overall & Derivatives and Hedging—Hedging—General	815-10 & 815-20	The amendments clarify that a not-for-profit entity that does not separately report earnings is not permitted to elect the amortization approach for amounts excluded from the assessment of effectiveness under fair value hedge accounting. The amendments also update the cross-references in paragraph 815-10-15-1 to further clarify the scope of Topic 815, Derivatives and Hedging, for entities that do not report earnings separately.	15-1 15-1 25-12
Derivatives and Hedging—Hedging—General	815-20	The amendments clarify that a private company that is not a financial institution as described in paragraph 942-320-50-1 should document the analysis supporting a last-of-layer designation concurrently with hedge inception. The amendments also clarify that not-for-profit entities (except for not-for-profit entities that have issued, or are a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market) qualify for the same 60 subsequent quarterly hedge effectiveness assessment timing relief for which certain private companies qualify in accordance with paragraph 815-20-25-142.	25-139 25-143

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Derivatives and Hedging—Hedging—General	815-20	The amendments clarify that the application of the first payments-received cash flow hedging technique to changes in overall cash flows on a group of variable interest payments continues to be permitted under Topic 815, Derivatives and Hedging.	55-33G
Derivatives and Hedging—Hedging—General	815-20	The amendments clarify various provisions to the amendments in Update 2017-12.	65-3 65-5
Investments—Debt Securities—Overall & Investments—Equity Securities—Overall	320-10 & 321-10	The amendments clarify the guidance in paragraphs 320-10-15-3 and 321-10-15-3, including adding health and welfare plans to the list of entities for which Topic 320, Investments—Debt Securities, does not apply.	15-3 15-3
Investments—Debt Securities—Overall & Financial Services—Depository and Lending—Investments—Debt and Equity Securities	320-10 & 942-320	The Board intended to eliminate all fair value disclosures for financial assets measured at amortized cost basis for entities other than public business entities through the amendments in Update 2016-01. The amendments clarify the guidance in paragraph 320-10-50-5 by eliminating the requirement for entities other than public business entities to disclose aggregate fair value of held-to maturity debt securities.	50-5 50-5A 50-3 50-3A
Investments—Equity Securities—Overall	321-10	The amendments clarify that all adjustments made under the measurement alternative upon the identified remeasurement events should be accounted for in accordance with Topic 820.	35-2 50-2B
Foreign Currency Matters—Overall & Financial Instruments—Overall	830-10 & 825-10	The amendments clarify that an entity is required to follow paragraph 830-10-45-18 for equity securities without readily determinable fair values accounted for under the measurement alternative in accordance with paragraph 321-10-35-2. Paragraph 830-10-45-18 requires remeasurement	45-18 65-5

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ASU 2019-04 Codification Improvements to Topics 326, 815, and 825			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
		at historical exchange rates. The amendments to paragraph 830-10-45-18(a)(1) and (a)(2) are not intended to change items that should be remeasured at historical exchange rates.	
Financial Instruments—Credit Losses—Measured at Amortized Cost	326-20	The amendments require an entity to present the amortized cost basis of line-of-credit arrangements that are converted to term loans in a separate column, as illustrated in Example 15.	50-6A 50-7 55-79
Financial Instruments—Credit Losses—Measured at Amortized Cost & Financial Instruments—Credit Losses—Overall	326-20 & 326-10	The amendments clarify that an entity should consider extension or renewal options (excluding those that are accounted for as a derivative in Topic 815) that are included in the original or modified contract at the reporting date and are not unconditionally cancellable by the entity.	30-6 65-1 65-2

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ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Financial Instruments—Credit Losses—Measured at Amortized Cost	326-20	The amendment intends to clarify that expected recoveries of amounts previously written off and expected to be written off should be included in the valuation account and should not exceed the aggregate of amounts previously written off and expected to be written off by an entity. In addition, the amendments clarify that when a method other than a discounted cash flow method is used to estimate credit losses, expected recoveries should not include any amounts that result in an acceleration of the noncredit discount; however, an entity may include increases in expected cash flows after acquisition	30-13 and 30-13A 55-86 thru 90
Financial Instruments—Credit Losses—Overall	326-10	The Board did not intend to introduce significant operational complexities when measuring expected credit losses on preexisting troubled debt restructurings. As a result. the amendment allows entities an accounting policy election to calculate the prepayment-adjusted effective interest rate on preexisting troubled debt restructurings using the prepayment assumptions that exist as of the date that an entity adopts the amendments in Update 2016-13, instead of the prepayment-adjusted effective interest rate immediately before the restructuring date.	65-1
Investments—Debt and Equity Securities—Overall	320-10	The amendment provides a practical expedient that allows an entity to exclude accrued interest receivable balances from the disclosure requirements in paragraphs 326-20-50-4 through 50-22 and 326-30-50-4	50-2A 50-5C

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ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
		through 50-10. The amendments in this Update extend the disclosure relief for accrued interest receivable balances as permitted in Update 2019-04 to certain other Topics in the Codification.	
Financial Instruments—Credit Losses—Measured at Amortized Cost	326-20	The amendment clarifies that an entity should reasonably expect the borrower to continually replenish collateral securing the financial asset(s) in accordance with the contractual terms of the financial asset to apply the practical 15 expedient. An entity is not required to consider remote scenarios in making this determination.	35-6
Business Combinations—Identifiable Assets and Liabilities, and Any Noncontrolling Interest & Financial Instruments—Credit Losses—Overall	805-20 & 326-10	The amendment clarifies paragraph 805-20-50-1 by removing the cross reference to Subtopic 310-30, Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality, which was superseded by Update 2016-13. The amendment instead correctly cross-references the guidance for purchased financial assets with credit deterioration in Subtopic 326-20.	50-1 65-4

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ASU 2020-03 Codification Improvements to Financial Instruments			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
Financial Instruments—Overall	825-10	Amendment clarifies that because financial assets and financial liabilities on which the fair value option have been elected are measured at fair value and not at amortized cost basis, all entities are subject to the fair value option disclosures in paragraphs 825-10-50-24 through 50-32.	50-23A 65-7
Fair Value Measurement—Overall	820-10	The amendments clarify the applicability of the portfolio exception in Subtopic 820-10, Fair Value Measurement—Overall, to nonfinancial items accounted for as derivatives under Topic 815, Derivatives and Hedging.	35-2A 35-18L
Financial Services—Depository and Lending—Investments—Debt and Equity Securities & Financial Instruments—Overall	942-320 & 825-10	The amendments on certain disclosures for depository and lending institutions clarify that the disclosure requirements in paragraphs 320-10-50-3 and 320-10-50-5 through 50-5C apply to the disclosure requirements in paragraphs 942-320-50-3 through 50-3A.	50-1 50-3 50-3A 65-5
Debt—Modifications and Extinguishments	470-50	The amendments clarify that paragraphs 470-50-40-17 through 40-18, which describe the accounting for fees between the debtor and creditor and third-party costs, respectively, directly related to exchanges or modifications of debt instruments, reference paragraph 470-50-40-21 for the accounting for modifications to or exchanges of line-of-credit or revolving-debt arrangements.	40-17 40-18 40-21
Fair Value Measurement—Overall	820-10	The amendment clarifies that the disclosure requirements in paragraph 820-10-50-2 do not	50-2

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ASU 2020-03 Codification Improvements to Financial Instruments			
Topic	**Codification**	**Abbreviated Summary of Change**	**Related Paragraphs**
		apply to entities using the net asset value per share (or its equivalent) practical expedient.	
Financial Instruments—Credit Losses—Measured at Amortized Cost & Financial Instruments—Credit Losses—Overall	326-20 & 326-10	The amendments align the contractual term to measure expected credit losses for a net investment in a lease under Topic 326 to be consistent with the lease term determined under Topic 842.	30-6A 55-8 65-4
Transfers and Servicing—Sales of Financial Assets	860-20	The amendments relate to the interaction of the guidance in Topic 326 and Subtopic 860-20, Transfers and Servicing—Sales of Financial Assets. The amendments to Subtopic 860-20 clarify that when an entity regains control of financial assets sold, an allowance for credit losses should be recorded in accordance with Topic 326.	25-13

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Revisions to the
As of March 2024 Accounting Practices and Procedures Manual

On **February 20, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2023-28	SSAP No. 21R	Collateral Loan Reporting *SAP Clarification* Effective Year End 2024	Adopted revisions to SSAP No. 21R incorporate a collateral loan disclosure for year-end 2024 to detail admitted and nonadmitted collateral loans in accordance with the underlying collateral supporting the loan

https://naiconline.sharepoint.com/teams/frsstatutoryaccounting/national meetings/a. national meeting materials/2024/02-20-24/adoptions/00 - adoptions toc.docx

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Collateral Loan Reporting

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to propose an expansion of reporting for collateral loans on Schedule BA to enable regulators the ability to quickly identify the type of collateral in support of admittance of collateral loans in scope of *SSAP No. 21R—Other Admitted Assets*. This agenda item has been drafted in response to comments that the current reporting detail on Schedule BA does not provide sufficient clarity on the type of collateral used in support of admittance of collateral loans. Furthermore, with the adoption of agenda item 2022-11, the statutory accounting guidance has been clarified that the collateral must reflect a qualifying investment, meaning that it would qualify for admittance if held directly by the insurer. This amendment further clarified that collateral that represents an investment in scope of *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* or *SSAP No. 97—Investments in Subsidiary, Controlled or Affiliated Entities* is required to be audited consistent with the admittance requirements of those SSAPs.

As detailed within, this agenda item proposes new disclosure requirements in SSAP No. 21R for collateral loans. The new disclosure requirement is proposed to be satisfied by an expansion of the reporting on Schedule BA, so that the collateral loans are separated by the type of collateral investment that secures the loan. Additionally, a new aggregated data-captured note is proposed to identify the admitted and nonadmitted collateral loans by the type of collateral that secures the loan.

Existing Authoritative Literature:

- **SSAP No. 21R—Other Admitted Assets - (Tracking shows the edits adopted on Oct. 23, 2023.)**

4. Collateral loans are unconditional obligations[1] for the payment of money secured by the pledge of a~~n~~ qualifying investment[2] and meet the definition of assets as defined in SSAP No. 4 and are admitted assets to the extent they conform to the requirements of this statement. The outstanding principal balance on the loan and any related accrued interest shall be recorded as an admitted asset subject to the following limitations:

a. Loan Impairment—Determination as to the impairment of a collateral loan shall be based on current information and events. When it is considered probable that any portion of amounts due under the contractual terms of the loan will not be collected the loan is considered impaired. The impairment shall be measured based on the fair value of the collateral less estimated costs to obtain and sell the collateral. The difference between the net value of the collateral and the recorded asset shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*;

b. Nonadmitted Asset—In accordance with *SSAP No. 20—Nonadmitted Assets*, collateral loans secured by assets that do not qualify as investments which would otherwise be admitted shall be nonadmitted. Further, any amount of the loan outstanding which is in excess of the permitted relationship of fair value of the pledged investment to the collateral loan shall be treated as a nonadmitted asset. To support the admissibility of collateral loans, reporting entities shall maintain documentation sufficient to support the reasonableness of the fair value measurement of the underlying collateral, which shall be made available to the applicable domiciliary regulator and independent audit firm upon request.

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Footnote 1: For purposes of determining a collateral loan in scope of this statement, a collateral loan does not include investments captured in scope of other statements. For example, *SSAP No. 26R—Bonds* includes securities (as defined in that statement) representing a creditor relationship whereby there is a fixed schedule for one or more future payments. Investments captured in SSAP No. 26R that are also secured with collateral shall continue to be captured within scope of SSAP No. 26R.

Footnote 2: A qualifying ~~I~~investment defined as those assets listed in Section 3 of *Appendix A-001—Investments of Reporting Entities* which would, if held by the insurer, qualify for admittance. For example, if the collateral would not qualify for admittance under SSAP No. 4 due to encumbrances or other third-party interests, then it does not meet the definition of "qualifying" and the collateral loan, or any portion thereof which is not adequately collateralized, is not permitted to be admitted. In the cases where the collateral is an equity/unit investment in a joint venture, partnership, limited liability company, and or SCA is pledged as collateral in a collateral loan, audited financial statements on a consistent annual basis are always required in accordance with SSAP No. 48 and/or SSAP No. 97.

Effective Date and Transition

22. ___This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3—Accounting Changes and Corrections of Errors. The guidance for structured settlements when the reporting entity acquires the legal right to receive payments is effective December 31, 2018. The clarification regarding audits of qualifying collateral pledged for collateral loans in the footnote 2 to paragraph 4, requires applicable audits to be obtained for the 2023 reporting period in the subsequent year. In periods after year-end 2023, the audits of equity collateral pledged for collateral loans are required to be obtained for the reporting year in which it was pledged and annually thereafter. The annual audit lag shall be consistent from period to period.

- **A/S Blank and Instructions** *(This reflects what is proposed to be adopted in 2023-12BWG.)*

Collateral Loans
Unaffiliated.....3199999
Affiliated.....3299999

Collateral Loans

Include: Refer to SSAP No. 21R—Other Admitted Assets for a definition of collateral loans. Loans that are backed by any form of collateral, regardless of if the collateral is sufficient to fully cover the loan, shall be captured in this category. Guidance in SSAP No. 21R shall be followed to determine nonadmittance.

In the description column, the name of the actual borrower and state if the borrower is a parent, subsidiary, affiliate, officer or director. Also include the type of collateral held.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

- Agenda Item 2022-11: Collateral for Loans clarified guidance on the criteria for collateral in order for a collateral loan to qualify as an admitted asset.

- Blanks Agenda Item 2023-12BWG incorporates revisions as part of the bond project to capture debt securities that do not qualify as bonds on Schedule BA. The revisions within this blanks item incorporate minor revisions to the instructions for collateral loans.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

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Convergence with International Financial Reporting Standards (IFRS): N/A

Recommendation:
NAIC staff recommend that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose this agenda item with proposed revisions to incorporate a new disclosure to SSAP No. 21R, for initial reporting as of year-end 2024, and to sponsor a blanks proposal for a new data-captured disclosure and to expand the reporting lines on Schedule BA to separate collateral loans by the type of collateral that secures the loan. NAIC staff recommends that the Working Group direct a corresponding blanks proposal to allow for concurrent exposure.

Proposed Revisions to SSAP No. 21R: *(Only new edits are tracked. Prior adopted revisions are shown clean.)*

4. Collateral loans are unconditional obligations[1] for the payment of money secured by the pledge of a qualifying investment[2] and meet the definition of assets as defined in SSAP No. 4 and are admitted assets to the extent they conform to the requirements of this statement. The outstanding principal balance on the loan and any related accrued interest shall be recorded as an admitted asset subject to the following limitations:

a. Loan Impairment—Determination as to the impairment of a collateral loan shall be based on current information and events. When it is considered probable that any portion of amounts due under the contractual terms of the loan will not be collected the loan is considered impaired. The impairment shall be measured based on the fair value of the collateral less estimated costs to obtain and sell the collateral. The difference between the net value of the collateral and the recorded asset shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*;

b. Nonadmitted Asset—In accordance with *SSAP No. 20—Nonadmitted Assets*, collateral loans secured by assets that do not qualify as investments which would otherwise be admitted shall be nonadmitted. Further, any amount of the loan outstanding which is in excess of the permitted relationship of fair value of the pledged investment to the collateral loan shall be treated as a nonadmitted asset. To support the admissibility of collateral loans, reporting entities shall maintain documentation sufficient to support the reasonableness of the fair value measurement of the underlying collateral, which shall be made available to the applicable domiciliary regulator and independent audit firm upon request.

5. Collateral loans shall be reported based on the type of qualifying investment that secures the loan. An aggregate note disclosure shall identify the total amount of collateral loans and the collateral loans admitted and nonadmitted by qualifying investment type.

Footnote 1: For purposes of determining a collateral loan in scope of this statement, a collateral loan does not include investments captured in scope of other statements. For example, *SSAP No. 26R—Bonds* includes securities (as defined in that statement) representing a creditor relationship whereby there is a fixed schedule for one or more future payments. Investments captured in SSAP No. 26R that are also secured with collateral shall continue to be captured within scope of SSAP No. 26R.

Footnote 2: A qualifying investment defined as those assets listed in Section 3 of *Appendix A-001—Investments of Reporting Entities* which would, if held by the insurer, qualify for admittance. For example, if the collateral would not qualify for admittance under SSAP No. 4 due to encumbrances or other third-party interests, then it does not meet the definition of "qualifying" and the collateral loan, or any portion thereof which is not adequately collateralized, is not permitted to be admitted. In the cases where the collateral is an equity/unit investment in a joint venture, partnership, limited liability company, and or SCA is pledged as collateral in a collateral loan, audited financial statements on a consistent annual basis are always required in accordance with SSAP No. 48 and or SSAP No. 97.

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Proposed Schedule BA Reporting Changes:

Collateral Loans – Reported by Qualifying Investment Collateral that Secures the Loan

Cash, Cash Equivalent & Short-Term Investments (SSAP No. 2R)
- Unaffiliated
- Affiliated

Bonds (SSAP No. 26R)
- Unaffiliated
- Affiliated

Asset-Backed Securities (SSAP No. 43R)
- Unaffiliated
- Affiliated

Preferred Stocks (SSAP No. 32R)
- Unaffiliated
- Affiliated

Common Stocks (SSAP No. 30R)
- Unaffiliated
- Affiliated

Mortgage Loans (SSAP No. 37R)
- Unaffiliated
- Affiliated

Real Estate (SSAP No. 40R)
- Unaffiliated
- Affiliated

Joint Venture, Partnerships or Limited Liability Companies (SSAP No. 48R)
- Unaffiliated
- Affiliated

Subsidiary, Controlled or Affiliated Investment (SSAP No. 97)
- Unaffiliated
- Affiliated

Other Qualifying Investment Category
- Unaffiliated
- Affiliated

Collateral Does Not Qualify as an Investment
- Unaffiliated
- Affiliated

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Collateral Loans

Include: Refer to SSAP No. 21R—Other Admitted Assets for a definition of collateral loans. Loans that are backed by any form of collateral, regardless of if the collateral is sufficient to fully cover the loan, shall be captured in this category. Guidance in SSAP No. 21R shall be followed to determine nonadmittance.

In the description column, the name of the actual borrower and state if the borrower is a parent, subsidiary, affiliate, officer or director. Also include the type of collateral held.

Classify the collateral loan in accordance with the type of collateral held, such that if the loan was to default and the collateral was to be claimed by the reporting entity, where it would be captured (investment type by SSAP) as a directly-held investment. If more than one form of collateral secures the loan, classification should occur based on the primary collateral source. The other qualifying investment category shall only be used to capture collateral loans secured by collateral in the form of contract loans, derivatives, other invested assets not separately reported, receivables for securities, securities lending and any investments that would qualify as a write-in for invested assets.

Proposed Data-Captured Disclosure:

Aggregate Collateral Loans by Qualifying Investment Collateral:

Collateral Type	Aggregate Collateral Loan	Admitted	Nonadmitted
Cash, Cash Equivalents & ST Investments			
Bonds			
Asset-Backed Securities			
Preferred Stocks			
Common Stocks			
Real Estate			
Mortgage Loans			
Joint Ventures, Partnerships, LLC			
Subsidiary, Affiliated and Controlled Entities			
Other Qualifying Investments			
Collateral Does not Qualify as an Investment			
Total			

Pursuant to SSAP No. 21R, nonadmittance of a collateral loan is required when the fair value of the collateral is not sufficient to cover the collateral loan or if the collateral securing the loan is not a qualifying investment. This includes situations in which collateral in form of joint ventures, partnerships, LLCs or SCAs is not supported by an audit as required by SSAP No. 48 or SSAP No. 97.

The other qualifying investment category shall only be used to capture collateral loans secured by collateral in the form of contract loans, derivatives, other invested assets not separately reported, receivables for securities, securities lending and any investments that would qualify as a write-in for invested assets. All collateral loans secured by collateral that does not qualify as an investment are~~is~~ required to be nonadmitted under SSAP No. 21R.

Staff Review Completed by: Julie Gann - NAIC Staff, September 2023

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Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification and exposed revisions to incorporate a new disclosure to SSAP No. 21R for initial reporting as of year-end 2024, and to sponsor a blanks proposal for a new data-captured disclosure and to expand the reporting lines on Schedule BA to separate collateral loans by the type of collateral that secures the loan. Comments are requested on whether any of the proposed reporting lines should be combined.

On February 20, 2023, the Statutory Accounting Principles (E) Working Group took the following two actions:

1) The Working Group **adopted** the exposed revisions to SSAP No. 21R incorporating a collateral loan disclosure for year-end 2024. With this adoption, the Working Group sponsored a blanks proposal to data-capture the disclosure. Adopted revisions to SSAP No. 21R are shown below:

> 5. Collateral loans shall be reported based on the type of qualifying investment that secures the loan. An aggregate note disclosure shall identify the total amount of collateral loans, and the collateral loans admitted and nonadmitted by qualifying investment type.

2) The Working Group exposed proposed reporting lines to Schedule BA for collateral loans with a comment deadline of April 19, 2024. Although the exposure does not contain AVR reporting revisions, the Working Group is specifically requesting feedback from regulators and industry on whether collateral loans backed by certain types of collateral should flow through AVR for RBC impact. Additionally, the Working Group directed a referral to the Life Risk-Based Capital (E) Working Group on the proposed reporting lines and the AVR mapping/RBC impact for collateral loans.

February 20, 2024, Exposed Schedule BA Reporting Changes:
(Tracking shows changes from the prior exposure.)

Collateral Loans – Reported by Qualifying Investment Collateral that Secures the Loan

~~Cash, Cash Equivalent & Short-Term Investments (SSAP No. 2R)~~
~~Unaffiliated~~
~~Affiliated~~

Bonds and Asset-Backed Securities (SSAP No. 26R & SSAP No. 43R)
Unaffiliated
Affiliated

~~Asset-Backed Securities (SSAP No. 43R)~~
~~Unaffiliated~~
~~Affiliated~~

Preferred Stocks (SSAP No. 32R)
Unaffiliated
Affiliated

Common Stocks (SSAP No. 30R)
Unaffiliated
Affiliated

Mortgage Loans (SSAP No. 37R)
Unaffiliated
Affiliated

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Real Estate (SSAP No. 40R)
Unaffiliated.....
Affiliated.....

Joint Venture, Partnerships or Limited Liability Companies (SSAP No. 48)
Fixed Income Investments (Unaffiliated) .....
Fixed Income Investments (Affiliated) .....

Common Stocks (Unaffiliated) .....
Common Stocks (Affiliated) .....

Real Estate (Unaffiliated) .....
Real Estate (Affiliated) .....

Mortgage Loans (Unaffiliated) .....
Mortgage Loans (Affiliated) .....

Other (Unaffiliated) .....
Other (Affiliated) .....
~~Unaffiliated.....~~
~~Affiliated.....~~

~~Subsidiary, Controlled or Affiliated Investment (SSAP No. 97)~~
~~Unaffiliated.....~~
~~Affiliated.....~~

Other ~~Qualifying~~ Investment Category
Cash, Cash Equivalent and Short-Term Investments (Unaffiliated) .....
Cash, Cash Equivalent and Short-Term Investments (Affiliated) .....

Other Long-Term Invested Assets (Unaffiliated) .....
Other Long-Term Invested Assets (Affiliated) .....
~~Unaffiliated.....~~
~~Affiliated.....~~

~~Collateral Does Not Qualify as an Investment~~
~~Unaffiliated.....~~
~~Affiliated.....~~

Non-Collateral Loans

Related Party/Affiliated Loans
All Other Non-Collateral Loans
~~Unaffiliated.....~~
~~Affiliated.....~~

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Revisions to the
As of March 2024, Accounting Practices and Procedures Manual

On **February 20, 2024**, the **Health Actuarial (B) Task Force** adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
N/A	**Health Actuarial (B) Task Force Memo** **AG 51**	*Actuarial Guideline LI–The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves*	Adopted revisions clarify that regardless of which annual statement blank an insurer files, it must make an AG 51 filing if the AG 51 filing requirements criteria are met.

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

MEMORANDUM

TO: Paul Lombardo (CT), Chair of the Long-Term Care Insurance (B) Task Force

FROM: Kevin Dyke (MI), Chair of the Health Actuarial (B) Task Force

DATE: February 20, 2024

RE: Modification to AG 51

The Health Risk-Based Capital (E) Working Group established the Health Test Ad Hoc Group in 2018 to review the health test language within the Annual Statement Instructions due to inconsistencies in reporting of health business across the different blanks, as well as a significant amount of health business reported on the life and fraternal blank. Through the evaluation and discussion of changes to the health test, there was a question brought up as to whether an entity would still be required to comply with *Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves* (AG 51) requirements for long-term care insurance (LTCI) business if the entity moved from the life blank to the health blank. In consideration of the Health Risk-Based Capital (E) Working Group's request for a sentence to be added to AG 51 to clarify the applicability to insurers filing health blanks, the Long-term Care Actuarial (B) Working Group adopted the following wording Nov. 20, 2023 that would indicate that regardless of the blank the entity files, AG 51 filing is required by the entity if the criteria stated in the Guideline are met. The Health Actuarial (B) Task Force adopted the addition, in red italicized font, to AG 51 on Feb. 20, 2024. The Health Actuarial (B) Task Force requests the Long-Term Care Insurance (B) Task Force review and consider adopting the modification.

3. Scope

This Guideline shall apply to a company with over 10,000 inforce lives covered by long-term care insurance contracts as of the valuation date, *regardless of which Annual Statement blank (Health, Life/Accident/Health & Fraternal, or Property/Casualty) the company files with its domiciliary state's insurance regulatory authority*. All long-term care insurance contracts, whether directly written or assumed through reinsurance are included. Accelerated death benefit products or other combination products where the substantial risk of the product is associated with life insurance or an annuity are not subject to this Guideline.

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Kansas City 1100 Walnut Street, Suite 1500, Kansas City, MO 64106-2197 p | 816 842 3600

New York One New York Plaza, Suite 4210, New York, NY 10004 p | 212 398 9000

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Adopted by the Long-Term Care Actuarial (B) Working Group on November 20, 2023
Adopted by the Health Actuarial (B) Task Force on February 20, 2024
Adopted by Executive/Plenary on August 15, 2024

Actuarial Guideline LI

THE APPLICATION OF ASSET ADEQUACY TESTING TO LONG-TERM CARE INSURANCE RESERVES

Background

The *Health Insurance Reserves Model Regulation (#010)* and the *NAIC Valuation Manual (VM-25)* contain requirements for the calculation of long-term care insurance (LTC) reserves. Regulators have observed a lack of uniform practice in the implementation of tests of reserve adequacy and reasonableness of LTC reserves. The reserve adequacy testing required by Model #10 and VM-25 does not provide regulators comfort as to the reserve adequacy of companies with material blocks of LTC business. As such, regulators must rely upon asset adequacy analysis required by the NAIC Valuation Manual (*VM-30*) to evaluate the solvency position of companies with sizable blocks of LTC business. This Guideline is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for the asset adequacy testing applied to a company's LTC block of contracts. In particular, this Guideline:

(1) Specifies that the appropriate form of asset adequacy analysis may be in the form of a gross premium valuation or in a more robust form, such as cash-flow testing, with Actuarial Standards of Practice providing guidance in this area;

(2) Clarifies the type of adequacy testing methods that must be used for aggregation with other blocks of business to be allowed for asset adequacy analysis purposes;

(3) Requires a uniform approach to supporting acceptable assumptions regarding future LTC premium rate increases;

(4) Provides requirements for documentation of assumptions associated with all key LTC risks; and

(5) Provides requirements for documentation of standalone LTC asset adequacy testing results.

Note: It is anticipated that the requirements contained in this Guideline will be incorporated into the *NAIC Valuation Manual* (VM-30) at a future date, effective for a future valuation year. This Guideline will cease to apply to annual statutory financial statements at the time the corresponding VM-30 requirements become effective.

Text

1. Effective Date

This Guideline shall be effective for reserves reported with the December 31, 2017 and subsequent annual statutory financial statements.

2. Authority

Pursuant to Section 1, paragraph 3, of *VM-30* of the *NAIC Valuation Manual*, the commissioner shall have the authority to specify specific methods of actuarial analysis and actuarial assumptions when, in the commissioner's judgment, these specifications are necessary for an acceptable opinion

to be rendered relative to the adequacy of reserves and related items.

3. Scope

This Guideline shall apply to a company with over 10,000 inforce lives covered by long-term care insurance contracts as of the valuation date, regardless of which Annual Statement blank (Health, Life/Accident/Health & Fraternal, or Property/Casualty) the company files with its domiciliary state's insurance regulatory authority. All long-term care insurance contracts, whether directly written or assumed through reinsurance are included. Accelerated death benefit products or other combination products where the substantial risk of the product is associated with life insurance or an annuity are not subject to this Guideline.

4. Asset Adequacy Analysis of LTC Business

A. As stated in Actuarial Standard of Practice (ASOP) No. 22, multiple asset adequacy analysis methods, including cash-flow testing and gross premium valuation, are available to actuaries for this analysis.

The method of analysis used for LTC shall conform with ASOP No. 22 in recognition of the typical significant asset- and liability-related risks associated with LTC.

B. Asset adequacy analysis specific to all inforce LTC business, and without consideration of results for other block of business within the company, must be performed for valuations associated with the December 31, 2017 and subsequent annual statutory financial statements. The analysis shall comply with applicable Actuarial Standards of Practice, including standards regarding identification of key risks. Material assumptions associated with the LTC business shall be determined testing moderately adverse deviations in actuarial assumptions.

C. When determining whether additional reserves are necessary:

1. A reserve deficiency in the LTC block may be aggregated with sufficiencies in the company's other blocks of business for the purposes of developing an actuarial opinion, if cash-flow testing is used for both the LTC business and for all significant blocks of non-LTC business within a company. If a reserve deficiency in the LTC block is not offset with sufficiencies in the company's other blocks of business, then additional reserves shall be established as required by section 2.C.2. of *VM-30*.

2. If cash-flow testing is not used for testing of the LTC business, then a reserve deficiency revealed from another method, e.g., a gross premium valuation, utilized for purposes of asset adequacy analysis of the LTC block under this Guideline shall not be offset with sufficiencies in the company's other blocks of business. The additional reserves under this Guideline shall be established based only upon the adequacy of the reserves in the LTC block.

D. When determining the effect of investment returns or the time value of money:

1. In the case where cash-flow testing is used, the company must allocate investment income to the LTC block of business consistently with the way investment income generated by the General Account is managed. If, however, a segment of the General Account is used to manage the investment risk for LTC business, the investment income generated by assets from that segment should be appropriately represented within the asset adequacy analysis.

2. In the case where a gross premium valuation method is used or asset cash flows are not explicitly modeled, the discount rate used by the actuary must reflect consideration of the yield on current assets held to support the liability as well as future yields on assets purchased with future premium income and reinvestments or anticipated divesture of existing assets.

E. The analysis shall only anticipate premium rate increases based upon a rate increase plan that is documented, is supported by and has been approved by management, is highly likely to be undertaken, and contains rate increase requests and timelines by jurisdiction. The assumptions used in the analysis should reflect a reasonable estimate of regulatory approved amounts and implementation timelines.

5. Documentation Required

The documentation requirements below are to be incorporated as a separate section of the appointed actuary's Actuarial Memorandum required by the *VM-30* or in a special Actuarial Memorandum containing LTC-specific information and shall be submitted to the commissioner of the company's state of domicile. The separate section of the companywide Actuarial Memorandum or the special Actuarial Memorandum shall be available to other state insurance commissioners in which the company is licensed upon request to the company. The confidentiality provisions regarding the Actuarial Memorandum contained in *VM-30* are applicable to the separate section of the Actuarial Memorandum and to the special Memorandum.

A. Results of the asset adequacy analysis of the LTC business shall be reported and documented in the separate section of the Actuarial Memorandum or the special Memorandum, as appropriate.

B. Assumptions on mortality shall be documented to state the reference standard valuation table, if applicable, and explicitly cite adjustments, select factors, and mortality improvement factors, where applicable. If a reference standard valuation table is not used in setting the mortality assumption, then a table of rates and comparison of the applied rates to rates from an unmodified standard mortality table for sample issue ages shall be provided. A summary of experience or other actuarial support of assumptions used shall be documented.

C. Assumptions on voluntary lapse shall be documented in table format by duration band and by other factors such as gender, marital status, with versus without inflation rider, and length of benefit period impacting the lapse assumption, where applicable. A summary of experience or other support of assumptions shall be documented.

D. Assumptions on morbidity shall be documented and actuarial support of the assumption shall be provided. If an outside source is used as the basis for morbidity assumptions, then the rationale for the applicability of that source and any adjustments to the factors from that source shall be documented.

E. Assumptions on investment returns and interest rates shall be documented. If a simplified approach is applied, such as implicit reflection of projected investment returns through the use of discount rates in a gross premium valuation as contemplated in Section 4.D.2., then justification shall be provided.

F. Any rate increases already approved shall be documented by jurisdiction with approved implementation timelines. Assumptions on future rate increases shall be documented by policy form or policy grouping. Such documentation should adequately describe the way in which future rate increase assumptions are developed. Unless the appointed actuary has

operational responsibility for carrying out the rate increase plan specified in Section 4.E., the Memorandum shall contain a signed and dated reliance statement from the person with operational responsibility for carrying out such actions that the rate increase plan(s) provided to the appointed actuary appropriately reflects management's plan.

G. Documentation of any other material assumptions shall be provided.

H. Documentation shall be provided for assumptions that have significantly changed from the prior year's analysis.

Revisions to the
As of March 2024, Accounting Practices and Procedures Manual

On **March 16, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2019-21	SSAP No. 21R	Principles-Based Bond Project & Residual Interests *New SAP Concept* Effective January 1, 2025	Adopted revisions provide guidance for debt securities that do not qualify as bonds under the principles-based bond definition, with a January 1, 2025, effective date. Adopted revisions prescribe accounting guidance (measurement method) for all residual interests regardless of legal form. This specific guidance is effective January 1, 2025, but can be early adopted for 2024.
2022-14 **2022-14a** **2022-14b** **2022-14c**	SSAP No. 93R SSAP No. 94R SSAP No. 34 SSAP No. 48	New Market Tax Credit Project *New SAP Concept* Effective January 1, 2025	Adopted revisions expand and amend guidance within SSAP No. 93 to include all tax credit investments regardless of structure and type of state or federal tax credit program. Revisions to SSAP No. 94R expand and amend guidance to include both purchased state and federal tax credits. Revisions in SSAP No. 34 and SSAP No. 48 include consistency revisions in response to the changes made to SSAP No. 93 and SSAP No. 94R.
2023-25	Appendix D	ASU 2023-03 – SEC Updates *SAP Clarification* Effective Immediately March 16, 2024	Adopted revisions reject ASU 2023-03 as not applicable for statutory accounting.
2023-27	Appendix D	ASU 2023-04 – SEC Updates, Crypto *SAP Clarification* Effective Immediately March 16, 2024	Adopted revisions reject ASU 2023-04 as not applicable for statutory accounting.
2023-29	Annual Statement Instructions	IMR Preferred Stock Revisions will be considered by the Blanks (E) Working Group for year-end 2024.	Adopted proposed revisions to the annual statement instructions which direct perpetual preferred stock (including SVO-Identified Preferred Stock ETFs), and mandatory convertible preferred stock through the AVR. This proposal did not result in SSAP revisions.

Ref #	SSAP/ Appendix	Title	Summary
2023-30	SSAP No. 97	SSAP No. 97 Admissibility Requirements *SAP Clarification* Effective Immediately March 16, 2024	Adopted revisions align the language in SSAP No. 97, paragraph 24, with the existing guidance provided in paragraphs 26 and 27.

https://naiconline.sharepoint.com/teams/frsstatutoryaccounting/national meetings/a. national meeting materials/2024/03-16-24 spring national meeting/adoptions/00 - adoptions 3.16.2024 toc.docx

The Revisions Shown in this Document are Effective January 1, 2025

Revisions to SSAP No. 21R—Other Admitted Assets

Bond Definition – Debt Securities that Do Not Qualify as Bonds

Residual Tranches or Interests/Loss Positions

Adopted March 16, 2024

On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted new statutory accounting guidance for "Debt Securities that Do Not Qualify as Bonds" and for "Residual Tranches or Interests/Loss Positions" within *SSAP No. 21—Other Admitted Assets.* The new sections are shown below. (Existing guidance from SSAP No. 21, paragraph 22 under 'Effective Date and Transition" is duplicated within and becomes paragraph 40 after the revisions.) The revisions are effective Jan. 1, 2025. Reporting entities may elect to adopt the residual guidance (detailed in paragraphs 28-37) for year-end 2024.

Debt Securities That Do Not Qualify as Bonds

20. The guidance within paragraphs 20-27 of this statement shall apply for any security, as defined in *SSAP No. 26R—Bonds*, whereby there is a fixed schedule for one or more future payments (referred to herein as debt securities), but for which the security does not qualify for bond reporting under SSAP No. 26R as an issuer credit obligation or an asset backed security. Investments in scope of this guidance are limited to:

a. Debt securities for which the investment does not reflect a creditor relationship in substance.

b. Debt securities that do not qualify for bond reporting due to a lack of substantive credit enhancement.

c. Debt securities that do not qualify for bond reporting due solely to a lack of meaningful cash flows.

21. Debt securities as described in this statement meet the definition of assets as defined in SSAP No. 4 and are admitted assets to the extent they conform to the requirements of this statement. The guidance in these paragraphs shall not be inferred to other securities or investment structures that are not otherwise addressed in statutory accounting, nor shall it be applied to any investments that are captured within other statutory accounting guidance.

22. Debt securities in scope of this standard that do not qualify as bonds under SSAP No. 26R and for which the primary source of repayment is derived through rights to underlying collateral, qualify as admitted assets if the underlying collateral primarily qualify as admitted invested assets. As detailed in paragraph 31, in the section pertaining to residual tranches, any residual tranches or first loss positions held from the same securitization that did not qualify as a bond under SSAP No. 26R also only qualify as admitted assets to the extent the underlying collateral primarily qualifies as admitted invested assets.

23. Debt securities in scope of this statement shall be initially reported at acquisition at cost, including brokerage and other related fees on *Schedule BA: Other Long-Term Invested Assets*.

24. Debt securities captured in scope of this statement shall be reported at the lower of amortized cost or fair value. Changes in measurement to reflect a lower value or to reflect changes in fair value shall be recorded as unrealized gains or losses.

25. Debt securities that do not qualify as bonds in the scope of this statement shall follow the guidance in *SSAP No. 43R—Asset-Backed Securities* for calculating amortized cost, for determining and recognizing other-than-temporary impairments and for allocating unrealized and realized gains and losses between the asset valuation reserve (AVR) and interest maintenance reserve (IMR).

26. Investment income shall be recorded, with assessments for collectability and nonadmittance completed and recognized, pursuant to *SSAP No. 34—Investment Income Due and Accrued*.

27. Securities captured within this section shall be included in all invested asset disclosures, along with the following disclosures:

a. Fair values in accordance with *SSAP No. 100R—Fair Value*.

b. Concentrations of credit risk in accordance with SSAP No. 27;

c. Basis at which the securities are stated;

d. The adjustment methodology used for each type of security (prospective or retrospective);

e. Descriptions of sources used to determine prepayment assumptions.

f. All securities within the scope of this statement with a recognized other-than-temporary impairment, disclosed in the aggregate, classified on the basis for the other-than-temporary impairment: (1) intent to sell, (2) inability or lack of intent to retain the investment in the security for a period of time sufficient to recover the amortized cost basis, or (3) present value of cash flows expected to be collected is less than the amortized cost basis of the security.

g. For each security with an other-than-temporary impairment, recognized in the current reporting period by the reporting entity, as the present value of cash flows expected to be collected is less than the amortized cost basis of the securities:

    i. The amortized cost basis, prior to any current-period other-than-temporary impairment.

    ii. The other-than-temporary impairment recognized in earnings as a realized loss.

    iii. The fair value of the security.

    iv. The amortized cost basis after the current-period other-than-temporary impairment.

h. All impaired securities (fair value is less than cost or amortized cost) for which an other-than-temporary impairment has not been recognized in earnings as a realized loss (including securities with a recognized other-than-temporary impairment for non-interest related declines when a non-recognized interest related impairment remains):

    v. The aggregate amount of unrealized losses (that is, the amount by which cost or amortized cost exceeds fair value) and

    vi. The aggregate related fair value of securities with unrealized losses.

i. The disclosures in (i) and (ii) above should be segregated by those securities that have been in a continuous unrealized loss position for less than 12 months and those that have been

in a continuous unrealized loss position for 12 months or longer using fair values determined in accordance with SSAP No. 100R.

j. Additional information should be included describing the general categories of information that the investor considered in reaching the conclusion that the impairments are not other-than-temporary.

k. When it is not practicable to estimate fair value, the investor should disclose the following additional information, if applicable:

i. The aggregate carrying value of the investments not evaluated for impairment, and

ii. The circumstances that may have a significant adverse effect on the fair value.

l. For securities sold, redeemed, or otherwise disposed as a result of a callable feature (including make whole call provisions), disclose the number of CUSIPs sold, disposed or otherwise redeemed and the aggregate amount of investment income generated as a result of a prepayment penalty and/or acceleration fee.

Residual Tranches or Interests/Loss Positions

28. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.

29. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a residual should be based on the substance of the investment and how cash flows to the holder are determined. Additionally, it would be expected that the equity position in an ABS Issuer, as defined in SSAP 26R, would be classified as a residual tranche.

a. Residuals often do not have contractual principal or interest.

b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance, and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.

c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.

d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.

e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.

30. Residual tranches or interests do not qualify for bond reporting. Residuals shall follow the accounting and admittance guidance within this statement and are required to be reported on Schedule BA: Other Long-Term Invested Assets.

31. As stated in paragraph 22, residuals are permitted to be admitted assets if debt securities from the same structure qualify (or would qualify) as admitted assets. If the debt security from a structure is (or would be) nonadmitted due to the requirements under paragraph 22, then any residual interests or first loss positions held from the same structure also do not qualify as admitted assets and shall be reported as nonadmitted assets.

32. Residuals shall be initially reported at cost, or allocated cost (using proportional fair values if acquired along with debt tranches from the securitization). Subsequent to initial acquisition, residuals shall be reported at either 1) the lower of amortized cost or fair value under the Allowable Earned Yield method detailed in paragraphs 33-34, with temporary reductions in fair value reported as an unrealized loss, or 2) at the calculated practical expedient method detailed in paragraph 35.

33. For purposes of this statement for residuals only, amortized cost shall be defined as the cost to acquire the residual reduced for distributions in excess of the Allowable Earned Yield and other-then-temporary impairments (OTTI). The Allowable Earned Yield shall be established at acquisition as the discount rate that equates the initial best estimate of the residual's cash flows to its acquisition cost. The Allowable Earned Yield is not to be updated after acquisition.

34. Interest income shall be recorded under the effective yield method using the Allowable Earned Yield, capped by the amount of cash distributions received. To the extent that the Allowable Earned Yield, applied to the current amortized cost, exceeds the cash distributions received, such unrecognized interest income may be carried forward to future periods to be recognized when sufficient cash distributions are received. To the extent cash distributions exceed the Allowable Earned Yield (including any unrecognized interest carried forward), the amortized cost shall be reduced by the excess. As a result of this method, the amortized cost shall not be increased unless there is a subsequent investment (i.e., an additional purchase with additional consideration remitted).

35. Reporting entities may elect a practical expedient in lieu of the Allowable Earned Yield detailed in paragraphs 33-34 and calculate Book/Adjusted Carrying Value (BACV) such that all distributions received are treated as a reduction in BACV. With this approach, the reporting entity will not recognize any interest or investment income until the residual tranche has a BACV of zero. Once the residual has a zero BACV, distributions received shall be recognized as interest income.

a. Reporting entities applying the practical expedient shall continue to report residuals on Schedule BA, including those with a zero BACV. Any subsequent distributions shall be reported as interest income until the structure matures/terminates, is unwound, or no longer meets the definition of a residual.

b. Reporting entities are required to apply the practical expedient to all residuals held.

c. Reporting entities that wish to discontinue use of the practical expedient approach and move towards the Allowable Earned Yield method are required to specify and disclose an explicit transition date, and only apply the Allowable Earned Yield method to residuals acquired after that date. Residuals held prior to the disclosed accounting method transition date shall continue to follow the practical expedient until those residuals mature/terminate or are unwound.

36. Residuals shall be assessed for other-than-temporary impairment (OTTI) on an ongoing basis, with required assessment anytime that fair value is less than the reported value.

a. For residuals measured using the Allowable Earned Yield method, as detailed in paragraphs 33-34, an OTTI shall be considered to have occurred if the present value of expected cash flows discounted by the Allowable Earned Yield, is less than amortized cost. Upon identification of an OTTI, the reporting entity shall recognize a realized loss equal to the difference between the amortized cost and the present value of expected cash flows, with the present value of expected cash flows becoming the new amortized cost to which the Allowable Earned Yield is applied. After the OTTI is recognized, distributions received from the residual shall continue to be recorded in accordance with paragraphs 33-34. Subsequent recoveries in cash flows shall not result in increases to the amortized cost.

b. For residuals measured under the practical expedient, as detailed in paragraph 35, an OTTI shall be considered to have occurred if the fair value of the residual is less than the BACV. The reporting entity shall recognize a realized loss equal to the difference between the fair value and the BACV, with the fair value becoming the new BACV. After the OTTI is recognized, distributions received from the residual shall continue to be recorded in accordance with paragraph 35. Subsequent recoveries in cash flows shall not result in increases to the BACV.

37. Residuals recognized on Schedule BA as of December 31, 2024, and accounted for under a different SSAP, shall follow the following measurement transition guidance as of January 1, 2025:

a. Reporting entity shall determine whether they will follow the Allowable Earned Yield method detailed in paragraphs 33-34, or the practical expedient detailed in paragraph 35, for all residuals.

b. Residuals previously accounted for under SSAP No. 26R or SSAP No. 43R shall prospectively apply the Allowable Earned Yield measurement method elected under this Statement using the amortized cost as of December 31, 2024 as the starting point in the calculation. Residuals that will follow the practical expedient shall be recognized on January 1, 2025 at the lower of amortized cost or fair value as of December 31, 2024, realizing any unrealized loss existing at that date.

c. Residuals reported under the equity method or fair value as of December 31, 2024 (as they were previously captured in scope of SSAP No. 30R, 32R or 48) with unrealized gains or losses recognized, shall recognize any unrealized position as realized, with the reported value as of December 31, 2024 becoming the January 1, 2025 cost basis for subsequent measurement under this statement.

Effective Date and Transition

~~22.~~40. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* The guidance for structured settlements

when the reporting entity acquires the legal right to receive payments is effective December 31, 2018. The clarification regarding audits of qualifying collateral pledged for collateral loans in the footnote 2 to paragraph 4 requires applicable audits to be obtained for the 2023 reporting period in the subsequent year. In periods after year-end 2023, the audits of equity collateral pledged for collateral loans are required to be obtained for the reporting year in which it was pledged and annually thereafter. The annual audit lag shall be consistent from period to period.

41. Revisions adopted March 16, 2024, to add guidance for "Debt Securities That Do Not Qualify as Bonds" and for "Residual Tranches or Interests/Loss Positions" are initially effective Jan. 1, 2025, to correspond with the effective date of the principles-based bond definition. The guidance for residual tranches is permitted for early application. Reporting entities that apply this guidance in 2024 shall continue to follow the transition guidance in paragraph 37 using the modified dates that correspond to the reporting entity's application date.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: New Market Tax Credits

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: The New Market Tax Credits (NMTC) Program was established by Congress in December 2000 and permits individual and corporate taxpayers to receive a non-refundable tax credit against federal income taxes for making equity investments in financial intermediaries known as Community Development Entities (CDEs). CDEs that receive the tax credit allocation authority under the program are domestic corporations or partnerships that provide loans, investments, or financial counseling in low-income urban and rural communities. The tax credit provided to the investors total 39% of the total cost of the investment and is claimed over a seven-year period. The CDEs in turn use the capital raised to make investments in low-income communities. CDEs must apply annually to the CDFI Fund to compete for NMTC allocation authority. The NMTC program is currently subject to expiration but has been extended to Dec. 31, 2025. The NMTC Extension Act of 2021 (introduced February 2021) would make the NMTC program permanent, modify the credit to provide for an inflation adjustment to the limitation amount for the credit after 2021, and allow an offset against the alternative minimum tax for the credit.

The success of the federal NMTC program has led to states adopting their own NMTC legislation. Per one noted article, the majority of state NMTC programs follow the federal rules with some modifications that vary from state to state. State modifications have been noted to specifically target smaller businesses, simplifying the application process, prohibiting the use of real estate business, and capping the amount of tax credits that can be allocated to one project. The economic impact of the state NMTC programs is typically less than the impact of federal NMTC programs because the economic return to investors for state tax credits is generally lower than what they receive for federal credits. Some states require that state tax credits can only be used in conjunction with federal credits. Pairing federal and state programs is beneficial to the qualifying business as they keep more of the investment without an obligation to return as the investors receives more tax credits.

Overview of Federal Program:

- Federal government authorizes an annual credit authority for NMTCs (amount of tax credits available).

- The Community Development Fund Institutions (CDFI fund) is a division of the U.S. Treasury responsible for implementing the NMTC program. Since there are limited tax credits each year, the CDFI fund has a competitive application process for the right to grant tax credits to investors and to make qualified NMTC investments.

- The right to grant tax credits is referred to as "NMTC Allocation" and is awarded to Community Development Entities (CDEs) that invest in low-income communities. The CDEs offer the tax credits to cash investors, and then use the cash to make investments (typically loans to a qualifying project – a "Qualifying Active Low-Income Community Business" - QALICB) that further the mission and objectives of the NMTC program.

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- The program specifies that the investor must provide cash as an equity investment (qualified equity investment – QEI) and it must stay invested in the CDE and the resulting NMTC qualifying project (QALICB) for a period of seven years.

    - The restrictions are specific that the investment is an equity investment as stock (other than nonqualified preferred) in an entity that is a corporation for federal tax purposes or any capital interest in an entity that is a partnership for federal tax purposes. (The investor is generally a 99.99% or 100% equity owner.)

- NMTC investments must remain in a qualified business for a seven-year period. Any principal amount repaid during that period must be reinvested by the CDE until the seven-year period expires. Most CDEs and investors avoid the reinvestment requirement and structure interest-only loans that prohibit principal repayment within the seven-year timeframe.

    - The 39% tax credit is provided as 5% of the investment in the first 3 years and then 6% of the investment for the next 4 years.

    - For tax purposes, the basis adjustment in the qualified equity investment is reduced by the amount of any new market tax credits on each credit allowance date.

    - Programs that cease to qualify are subject to tax credit recapture.

- Investors enter these transactions recognizing that the original investment amount will not be fully returned. Rather, a portion (or perhaps all) of the equity investment will be unpaid without an obligation to return from the borrowing business. NMTC investments with these terms have specific maturing terms / actions. One approach could be that an option (put/call) is held by the investor that gives them the right to sell its equity investment to the borrower for a nominal price.

- The designs are often complex and introduce leverage lenders to maximize tax credits to the equity investor:
    - Equity investor provides $3M to acquire 100% equity interest in an investment fund.
    - Investment fund borrows $7M from a leverage lender.
    - This results with a $10M qualifying NMTC transaction, resulting with the equity investor receiving $3.9M in tax credits over 7 years from an initial $3M investment.
    - The investment fund provides two loans to the qualified low-income business (QALICB). The first loan is for the $7M leverage loan, the second is for the $3M equity investment.
    - Both loans only pay interest for the seven-year period to meet the NMTC terms.
    - At the conclusion of the 7 years, the project sponsor purchases the second loan via a ‘put/call’ agreement, converting the $3M into a permanent subsidiary for the project.
    - The borrower / project sponsor refinances the $7M loan to repay the leverage lender.
    - The ultimate result is that the equity investor received $3.9M over 7 years in tax credits for $3M.

- Example without leverage lender:
    - Investor provides a $10M NMTC Investment
    - Investor receives $3.9M in tax credits over seven years.
    - Investor receives $7.4M of original investment at the end of the seven years.
    - Borrower keeps $2.6M of the original investment to further their low-income qualifying activities.
    - Investor receives a net return of $1.3M. ($10M less $3.9M tax credits less return of 7.4M principal.)

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FASB Discussion

The FASB has a current Emerging Issues Task Force project to assess whether the proportional amortization method of accounting, which is used for Low-Income Housing Tax Credits (LIHTC), should be expanded to investments in tax credit structures beyond LIHTC. The proportional amortization method results in the tax credit investment being amortized in proportion to the allocation of tax credits in each period and allows the investment amortization and tax credits to be presented on a net basis within the income tax line item. Currently, investments in other tax credit structures are typically accounted for using the equity method or the cost method. Under the equity and cost methods, investment gains/losses and tax credits are presented on a gross basis on an entity's income statement. The FASB has received two requests asking that the proportional amortization method be made applicable to New Market Tax Credit Structures as well as other investment structures that are made primarily for the purpose of receiving tax credits and other tax benefits. The FASB added a project to the Emerging Issues Task Force agenda on Sept. 22, 2021. The FASB Task Force reached a consensus-for-exposure on June 16, 2022, that the proportional amortization method can be elected on a tax credit program by tax credit program basis. This proposed ASU was exposed in August 2022, with comments due Oct. 6, 2022. A final ASU is expected later in 2022 or early in 2023 (ASU 2023-02 was issued in March of 2023).

IRS Provisions – The NMTC is captured as a nonrefundable 'general business credit' and is limited to tax liability. If tax liability is not sufficient to take the credit, then the tax credit is subject to carryforward / carryback provisions. Per instructions from the *2021 Instructions for Form 3800 – General Business Credit*, general business credits that cannot be used because of a tax liability limit are first carried-back 1 year through an amended return. If there are unused credits after carrying back 1 year, the tax credit can be carried forward to each of the 20 tax years after the year of the credit.

Inflation Reduction Act Provisions – The Inflation Reduction Act was signed by President Biden on Aug. 16, 2022. Although there are several elements within the Act, it includes a 15% corporate minimum tax rate for corporations with at least $1 billion in income and includes numerous investments in climate protection, clean energy production and tax credits aimed at reducing carbon emissions. Although the Act has been signed, several elements are pending further application guidance. From preliminary information, the act allows for general business credits, such as the low-income housing tax credit (LIHTC), new markets tax credit (NMTC), historic tax credit (HTC) and renewable energy tax credits (RETCs) to be taken against the minimum tax. **However, further monitoring of application / interpretation guidance that is still forthcoming is required to assess the actual application and impact of tax credits on companies subject to the minimum tax.**

Statutory Accounting Considerations:

- Although the design is an equity investment of stock or interest in a corporation or partnership, which would normally be subject to *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, the intent of NMTC investments is for tax credits and not equity returns. As such, this structure is closer to the existing low-income housing tax credits guidance in SSAP No. 93 than the partnership / LLC guidance in SSAP No. 48.

- Although *SSAP No. 93—Low Income Housing Tax Credit Property Investments* provides guidance for an equity investment, that provides tax credits with a limited (or zero) residual investment value, the guidance in SSAP No. 93 is specific to LIHTC programs.

- It has been identified that there are structures that have been designed to resemble fixed-income notes that do not pay regular cash interest, but rather provide NMTC tax credits as interest returns. These structures are in substance that same as other investments in NMTC, with an underlying equity interest in the CDE that generates tax credits. However, they have been structured with a guarantee for compensatory interest in the form of cash for the amount of the tax credit expected to have been received that year. These structures are also being considered within scope of this agenda item. Such structures have to meet specific criteria to qualify for tax credits under the IRS rules.

Existing Authoritative Literature:

SSAP Authoritative Guidance:

- **SSAP No. 93—Low Income Housing Tax Credit Property Investments**
  This statement establishes accounting principles for investments in federal certain state sponsored Low Income Housing Tax Credit (LIHTC) properties owned through limited liability entities that are flow-through entities for tax purposes. The guidance requires LIHTC investments to be initially recorded at cost and carried at proportional amortized cost unless the investment is identified as impaired. Under the proportional amortization method, amortization of the LLC investment is recognized in the income statement as a component of net investment income/expense and the current tax credit is accounted for as a component of income tax expense:

  - Federal tax credits are recognized in the income statement as an offset to federal taxes in the tax reporting year in which the tax credit is utilized in accordance with *SSAP No. 101—Income Taxes*.
  - State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized.
  - Tax benefits received, other than tax credits, shall be accounted for pursuant to SSAP No. 101.

  SSAP No. 93 indicates that immediate recognition of the entire benefit of the tax credit to be received during the term of the investment in a low-income housing project is not appropriate. It also indicates that low-income housing tax credits shall not be recognized in the financial statements before their inclusion in the investor's tax return.

- **SSAP No. 94R—Transferable and Non-Transferable State Tax Credits**
  This statement establishes accounting principles for investments transferable and non-transferable state tax credits, with an explicit exclusion for LIHTCs (or similar tax credits) captured in scope of SSAP No. 93.

  Guidance for admittance of state tax credits under this statement varies based on whether it is transferable or non-transferable:

  Transferable – Per the SSAP, all the following criteria must be met for admittance:

  1) The holder of the transferable state tax credit may sell or otherwise transfer the transferable state tax credit to another entity, which can likewise sell or transfer the credit;
  2) The transferable state tax credit will expire is not used by a predetermined date; and
  3) The transferable state tax credit can be applied against either state income tax or state premium tax.

  Non-Transferable – Per the SSAP, all the following criteria must be met for admittance:

  1) Successive holder of a state tax credit must redeem the credit by April 15 of the subsequent year to the entity's acquisition of the state tax credit and is not permitted to carry-over, carry-back, obtain a refund, sell or assign the credit;
  2) The non-transferable state tax credit will expire if not used by the predetermined date; and
  3) The non-transferable state tax credits can be applied against either state income tax or state premium tax.

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Review of Existing Statutory Accounting Guidance for NMTC and Overall Application:

- Existing statutory accounting guidance does not encompass federal NMTC (or other federal tax credits), as SSAP No. 93 is limited to LIHTC and SSAP No. 94 is specific to state tax credits.

- Provisions in SSAP No. 93 do not fully address earned (received) tax credits that carryforward for future use.

- The admittance criteria in SSAP No. 94 are applied to characteristics that perhaps may not be factors that would impact admittance:

    - A tax credit that does not expire would be precluded as an admitted asset under the guidance.

    - A non-transferable tax credit that can be carried-forward, carried-back, able to be refunded or that can be sold or assigned is precluded as an admitted asset under the guidance.

Statutory Accounting Reporting Guidance:

Guaranteed and non-guaranteed federal low-income housing tax credits have separate reporting lines on Schedule BA along with an "all other" low-income housing tax credit line. The guidance is specific that these lines are only for low-income tax credits (or tax credits for affordable housing) that are in the form of a partnership or limited liability company. Non-qualifying LIHTC are to be reported in the "All Other" category. With this current guidance, there is no explicit reporting provision for tax credits that are not captured in LIHTC.

Reporting Lines and Instructions:

Guaranteed Federal Low Income Housing Tax Credit
Unaffiliated 3599999
Affiliated 3699999
Non-Guaranteed Federal Low Income Housing Tax Credit
Unaffiliated 3799999
Affiliated 3899999
Guaranteed State Low Income Housing Tax Credit
Unaffiliated 3999999
Affiliated 4099999
Non-Guaranteed State Low Income Housing Tax Credit
Unaffiliated 4199999
Affiliated 4299999
All Other Low Income Housing Tax Credit
Unaffiliated 4399999
Affiliated 4499999

Low Income Housing Tax Credit

Include: All Low-Income Housing Tax Credit Investments (LIHTC or affordable housing) that are in the form of a Limited Partnership or a Limited Liability Company including those investments that have the following risk mitigation factors:

A. Guaranteed Low Income Housing Tax Credit Investments. There must be an all-inclusive guarantee from a CRP-rated entity that guarantees the yield on the investment.

B. Non-guaranteed Low Income Housing Tax Credit Investments.

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I. A level of leverage below 50%. For a LIHTC Fund, the level of leverage is measured at the fund level.

II. There is a Tax Credit Guarantee Agreement from General Partner or managing member. This agreement requires the General Partner or managing member to reimburse investors for any shortfalls in tax credits due to errors of compliance, for the life of the partnership. For a LIHTC Fund, a Tax Credit Guarantee is required from the developers of the lower tier LIHTC properties to the upper tier partnership and all other LIHTC investments.

III. There are sufficient operating reserves, capital replacement reserves and/or operating deficit guarantees present to mitigate foreseeable foreclosure risk at the time of the investment.

Non-qualifying LIHTCs should be reported in the "All Other" category.

Statutory Accounting RBC Impact:

Life: The RBC factors for LIHTC are captured as part of the real estate on LR007:

(17)	Federal Guaranteed Low Income Housing Tax Credits	AVR Equity Component Column 1 Line 75	0.0014
(18)	Federal Non-Guaranteed Low Income Housing Tax Credits	AVR Equity Component Column 1 Line 76	0.0260
(19)	State Guaranteed Low Income Housing Tax Credits	AVR Equity Component Column 1 Line 77	0.0014
(20)	State Non-Guaranteed Low Income Housing Tax Credits	AVR Equity Component Column 1 Line 78	0.0260
(21)	All Other Low Income Housing Tax Credits	AVR Equity Component Column 1 Line 79	0.1500
(22)	Total Schedule BA Real Estate	Lines (16) + (17) + (18) + (19) + (20) + (21)	

P/C and Health: The RBC factors for LIHTC are captured as components of other long-term assets. The reporting lines and factors are the same as they are for life (as shown above).

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): NA

Recommendation:
NAIC staff recommend that the Working Group expose additional revisions described below to SSAP No. 93 and SSAP No. 94R. Staff also recommends that the Working Group expose changes to *SSAP No. 34—Investment Income Due and Accrued* and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, which detail miscellaneous changes which update the scope of each statement for the proposed updates to SSAP No. 93 and SSAP No. 94R. The following are key revisions to SSAP No. 93R and 94R are proposed for exposure:

- *SSAP No. 93R—Investments in Tax Credit Structures* – NAIC staff recommends the following revisions in response to comments, from interested parties, public comments and NAIC staff internal review:
  - Various editorial changes to the admittance test described in paragraph 18 to clarify technical aspects of the assessment.
  - Addition of a Glossary of key terms at the end of the SSAP.
  - Revised guidance effective date to be 1/1/2025, applied prospectively without option to early adopt.

  - Added a new paragraph to the Impairment of Tax Credit Investments section to provide guidance on tax credit programs which allocate variable amounts of tax credits.
  - Clarified in footnote 4 that tax credit strips derived from tax equity investments are not an example of an investment structure exempt from the audit requirement.
  - Added disclosures for unused tax credits allocated from tax credit investments as these tax credits would not be within the scope of SSAP No. 94R disclosures.

- *SSAP No. 94R—State and Federal Tax Credits* – NAIC staff recommends the following revisions in response to comments, from interested parties, public comments and NAIC staff internal review:
  - Revised guidance effective date to be 1/1/2025 with early adoption permitted.
  - Added language to clarify that awarded tax credits (neither purchased nor allocated from an investment) are not within the scope of SSAP No. 94R.
  - Added commitment and contingency guidance to the Accounting and Disclosure sections.

- Other SSAPs – In response to the proposed revisions to SSAP Nos 93 and 94R, NAIC staff recommends the following:
  - *SSAP No. 34—Investment Income Due and Accrued* – Staff proposes revisions to clarify that tax credits earned or purchased are not within the scope of SSAP No. 34.
  - *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* – Staff proposes revisions which update paragraph 2 for the new tax credit investment language.

Interested parties' comment letter recommended revisions which would narrow the scope of the paragraph 18 admittance test to only tax credit investments which allocate non-transferable tax credit and prohibit the sale of ownership interests. NAIC staff did not revise the SSAP No. 93R draft for these recommendations but intends to continue working with industry to address their concerns that the new guidance may nonadmit previously admitted tax credit investments.

Additionally, NAIC staff requests comments on the annual statement reporting categories for tax credit investment RBC. The current RBC categories are LIHTC Investment specific and are mapped to the real estate grouping.

Staff Review Completed by: William Oden and Julie Gann - NAIC Staff, May 2023

Status:
December 13, 2022 - Fall National Meeting Recommendation:
NAIC staff recommends that the Working Group direct NAIC staff to draft statutory accounting guidance in the form of a new or revised SSAP that expands the current LIHTC guidance for equity investments that general federal business tax credit and state premium tax credits. Although this agenda item is focusing on NMTC, it is recommended that consideration be given to guidance that does not name specific designs, such as NMTC or other specific tax credits, so that it can be applicable for all qualifying tax equity investments. This guidance will consider the proposed FASB guidance as well as admittance and impairment provisions, recognizing that tax credits cannot be used to provide direct payment to policyholders, but rather are utilized to impact a reporting entity's tax liability. This agenda item also recommends a review of SSAP No. 94—Transferable and Non-Transferable State Tax Credits to ensure the guidance properly reflects items that should be captured in scope and appropriate admittance provisions. With the proposal of a new or revised SSAP, this agenda item is proposed to be captured as a 'New SAP Concept' with a corresponding issue paper. Along with statutory accounting revisions, a resulting blanks proposal and a potential RBC referral are anticipated to update blanks reporting and RBC references accordingly. As detailed within, all Schedule BA reporting lines and RBC instructions (for both federal and state) only reference Low-Income Housing Tax Credits. The BA instructions also need to be updated as the concept for 'guaranteed' provisions from a CRP-rated entity seems to only be applicable to limited NMTC designs, as a guarantee may disqualify an entity from being able to use tax credits under IRS provisions.

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On December 13, 2022, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a new SAP concept, and exposed a discussion document to expand current statutory accounting guidance for low-income housing tax credits to capture all tax equity investments that provide general federal business tax credit and state premium tax credits if they meet specified criteria.

On February 10, 2023, NAIC staff received Interested Parties' comment letter on the exposed discussion document which were presented to the Working Group:

> Interested parties agree with having uniformity in accounting and reporting for equity investments for which the return is earned primarily through tax credits. Interested parties agree that the proportional amortization method is an appropriate method to use for any type of investment (debt or equity) where the return is primarily earned through tax credits. We are providing responses to the questions exposed in the Discussion Paper in this document. There are two key take aways from our responses:
>
> 1. Interested parties ask the Working Group to consider allowing for the reporting of both the amortization of the investments and the use of the tax credits themselves in the same income statement line similar to what is required under U.S. GAAP.
>
> 2. Interested parties have concerns regarding tax credit investments that are issued in debt form and requiring those investments to be reported on Schedule BA instead of Schedule D. Interested parties believe that tax credit investments issued in debt form are better suited for Schedule D reporting.

March 22, 2023 – Spring National Meeting Recommendation:
NAIC staff recommends that the Working Group direct NAIC staff to proceed with drafting revised statutory accounting guidance and a related issue paper to expand the guidance in SSAP No. 93 for tax credits, as well as to draft revisions to SSAP No. 94—Transferable and Non-Transferable State Tax Credits for future Working Group discussion. NAIC staff proposes to consider the feedback from interested parties on the discussion document as well as the revised FASB guidance, which is expected to be issued in the near future, in updating the proposed revised statutory accounting guidance for subsequent exposure consideration.

On March 22, 2023, the Statutory Accounting Principles (E) Working Group directed NAIC staff to draft statutory accounting guidance in the form of a new or revised SSAP that expands the current LIHTC guidance for equity investments that general federal business tax credit and state premium tax credits.

May 16, 2023 – Interim Meeting Recommendation:
NAIC staff recommend that the Working Group include this item on their maintenance agenda as a new SAP concept and expose the draft revisions to SSAP No. 93 and SSAP No. 94R, which intend to capture all tax equity investments that provide federal business tax credit and state premium tax credits if they meet specified criteria.

On May 16, 2023, the Statutory Accounting Principles (E) Working Group exposed revisions to SSAP No. 93 and 94R. The revisions to SSAP No. 93 propose adoption with modification of *ASU 2023-02–Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method* and expansion of the SSAP scope to include all tax credit programs and tax investment structures. The revisions to SSAP No. 94R expand the scope of the SSAP to include all state and federal tax credits whether purchased or allocated, and that tax received should be recorded at face value with losses realized immediately and gains deferred.

On June 20, 2023, NAIC staff received Interested Parties' comment letter on the exposed revisions to SSAP Nos. 93 and 94R. Interested Parties provided several comments on both SSAPs which are summarized below along with NAIC Staff responses.

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The comments provided on SSAP No. 93 were:

1. Interested Parties noted that paragraph 3 does not provide specific direction for which SSAPs would be applicable for tax credit investment which do not fall within SSAP No. 93.
    a. NAIC Staff agreed with the recommendation and updated paragraph 3 to provide readers with specific SSAPs which could apply to non-qualifying equity or debt structure tax credit investments.
2. Interested Parties noted that the current draft directed readers to refer to SSAP 94R for how to account for tax credits allocated from tax credit investments. They felt that this cross-reference was confusing and could potentially lead to conflicting interpretations.
    a. To reduce confusion, NAIC Staff opted to remove the paragraph directing readers to SSAP 94R and instead pulled in the specific paragraphs from SSAP 94R which would be applicable to tax credits allocated from tax credit investments.
3. Interest Parties noted that they were unclear on whether the tax credits earned, or the tax credit investments were subject to the admittance criteria detailed in Paragraphs 18(a)-(c). Interested Parties feels that admissibility concerns are adequately addressed by the tax opinion and audit requirements. Additionally, if NAIC Staff's concern is the admittance of tax credits carried forward to a future period, then this should be adequately addressed by the admittance rules detailed in *SSAP No. 101–Income Taxes* for Deferred Tax Assets. Interested Parties suggested that paragraphs 18(a)-(c) be deleted in full.
    a. NAIC Staff noted that the admittance rules detailed in paragraphs 18(a)-(c) do NOT provide guidance on the admittance of allocated tax credits. For tax credit investment structures to fall within the scope of SSAP 93, substantially all benefits must be from tax credits or other tax benefits which essentially means that balance of a tax credit investment represents a future stream of tax credits and tax benefit. As such, the admittance rules in paragraph 18(a)-(c) would require a company to assess its ability to utilize that future stream of tax credits to what amount of the tax credit investment would be non-admitted. If the company's projections determine it will be unable to substantially utilize the future stream of tax credits (i.e., the tax credit investment balance) then potentially all or a portion of the tax credit investment would be considered non-admitted as the company is unable to utilize the future stream of tax credits to offset tax liabilities.
4. Interested Parties noted that GAAP requires retrospective adoption of ASU 2023-02 and that this would result in GAAP vs. Statutory accounting differences.
    a. NAIC Staff noted that prospective adoptions of accounting updates are often simpler to implement than retrospective adoptions. However, since this would lead to unintended variance between GAAP and Stat NAIC Staff has updated SSAP 93 to be adopted on the retrospective basis to conform with the GAAP adoption requirements.

The comments provided on SSAP No. 94R were:

1. Interest Parties requested that paragraph 1 of the scope of statement section be amended to clarify which types of tax credits are within scope of SSAP No. 94R. Interested Parties feel that the key difference between SSAP 94R and SSAP 93 is that the former is for purchased tax credits and the ladder is for tax credits earned from investments.
    a. NAIC Staff generally agree with the comments provided but opted to remove the term "certificate" from the requested changes. The intent of SSAP No. 94R is to provide guidance on all purchased state and federal tax credits, not just certificated tax credits. NAIC Staff also included language to clarify the scope of SSAP No. 94R for allocated tax credits, as detailed in the next bullet point.
2. Interested Parties noted that they do not believe allocated tax credits from SSAP No. 93 investments should be within the scope of SSAP No. 94R as the guidance was confusing and could potentially lead to conflicting interpretations. Additionally, Interested Parties believe that tax credits from investments vs. purchased tax credits are distinctly different assets. The only similarity in accounting for the tax credits relates to instances when the credits earned under a SSAP No. 93 investment cannot be utilized in the current year. Under that scenario, a DTA would be recorded, which would be subject to the admissibility rules under SSAP No. 101.
    a. NAIC Staff elected to remove tax credits allocated from SSAP No. 93 investments from the scope of SSAP No. 94R to avoid confusion. However, NAIC Staff note that tax credits earned from

investments bear many similarities to purchased tax credits. Irrespective of how the tax credit are acquired, they represent the same type of financial instruments which can be utilized as an offset to tax liabilities, sold, or redeemed for cash as a tax refund. Additionally, irrespective of how the tax credits are earned they are recorded at face value upon acquisition. The only significant difference is that tax credits purchased at a premium or discount may result in a recognized loss or deferred gain, respectively, whereas any premium or discount on an allocated tax credit is recognized as part of proportional amortization calculation.

b. NAIC Staff amended the draft to exclude tax credits allocated from SSAP No. 93 investments in response to the Interested Party comments on SSAP No. 93. However, NAIC Staff did include language noting that allocated tax credits earned from tax credit investments NOT within the scope of SSAP No. 93 should refer to SSAP 94R for guidance on how to record allocated tax credits. NAIC staff noted that without this language there would be no guidance within Accounting Practices and Procedures Manual for allocated tax credits from investments which fall outside the scope of SSAP No. 93.

3. Interested Parties noted that most tax certificates reduce a reporting entity's tax liability and do not directly impact the income statement at the time they are used. In addition, interested parties believe that upon purchase, the tax credits should be reported as an other-than-invested asset since the asset represents a right to receive future benefits. As the tax credits become available for use, a reduction to the insurer's income tax payable or premium/state taxes payable should take place.
    a. NAIC Staff disagrees with this proposed change as purchased federal tax credits would be reported as other-than-invested assets, versus allocated federal tax credits which would report as a deferred tax asset. This would result in the same type of asset being reported on two separate lines based on the manner in which it was acquired. As noted above, NAIC Staff's position is that allocated and purchased tax credits are substantially the same assets irrespective of the way in which they are acquired. Additionally, the Interested Parties also propose that if a tax credit cannot be utilized in the same period in which it was purchased it should be transferred to Deferred Tax Assets. NAIC Staff notes that this does not resolve the short-term reporting discrepancy noted previously and adds further complications to the accounting process by requiring a reporting line transfer if the asset is held for longer than a year.
4. Interested Parties noted that the accounting for purchased tax credits in the SSAP No. 94R exposure is different from the current guidance in that the credits will be recorded at face value instead of at cost. This is not an issue perse but Interested Parties did want to point out this discrepancy as compared to the accounting treatment for other assets like bonds and mortgage loans.
    a. NAIC Staff's position is that tax credits, whether received via purchase or allocation, do not represent investments, and has opted to propose accounting guidance that differs from bonds or mortgage loans. The position that tax credits do not represent investments was the main reason for the original SSAP No. 94R guidance which required state tax credits be recorded to Other Than Invested Assets and effectively required companies tax credits purchased at a discount at cost and effectively defer the gain off the balance sheet. NAIC Staff felt that it would be less confusing and provide a more accurate financial picture to record the tax credit at face value and defer any gains from discount purchases on the balance sheet.
5. Interested Parties proposed changes to Exhibit B to reflect a pro-rata utilization of purchased tax credits in relation to the quarterly accrual of income tax liabilities. The main purpose of these changes were to reflect Interested Parties' proposed changes in item #2.
    a. NAIC Staff made these changes to Exhibit B and believe that this method of recognizing tax credit utilization is applicable to exposed draft of SSAP No. 94R.

Outside of the changes made in response to Interested Parties' Comment Letter, both Exhibits in SSAP No. 93 were revised to provide example journal entries of the Proportional Amortization method. Additionally, the assumptions in Exhibit B were revised so it would provide a journal entry example for a residual sale at the end of the proportional amortization period. A new footnote was also added to SSAP No. 94R on page 2 based verbal comments received

from the public. The new footnote provides clarification on what processes constitute a purchase vs an allocation of tax credits.

August 13, 2023 - Summer National Meeting Recommendation:
NAIC staff recommend that the Working Group expose additional revisions described below to SSAP No. 93 and SSAP No. 94R. Additionally, NAIC staff recognizes that revisions to the annual statement Schedule BA reporting lines will need to be considered, as well as how those reporting lines flow through to the AVR. NAIC staff recommends that the Working Group direct staff to work with interested parties throughout the interim to discuss to allow subsequent (or interim) exposure.

On August 13, 2023, the Statutory Accounting Principles (E) Working Group exposed additional revisions made to SSAP No. 93 and SSAP No. 94R. Additionally, the Working Group directed NAIC staff to work with interested parties to draft revisions to the annual statement instructions and reporting updates.

On September 29, 2023, NAIC received Interested Parties' comment letter on the exposed revisions to SSAP No. 93 and 94R. Interested Parties provided several comments on both SSAPs which are summarized below along with NAIC Staff responses (effective October 11, 2023). The comments provided on SSAP No. 93 are below and have been summarized for brevity and clarity:

1) Interested Parties noted that SSAP 93 Paragraph 18 requires reporting entities to annually assess the future utilization of the unallocated tax credits associated with an entity's ownership interest in a tax credit investment project to determine if the investment can be admitted. However, Interested Parties suggest that this admittance criteria only be applicable to investments which do not allocate transferable or refundable tax credit and if the reporting entity is contractually restricted from selling its ownership interest. Additionally, Interested Parties suggest deleting paragraphs 18a and 18b as admissibility is adequately addressed through the impairment analysis required in paragraph 25; mainly that since both the tax credits and investment are saleable there is not a significant concern about the reporting entity's ability to utilize these investments and their tax credit returns for policyholder liabilities.

    i. NAIC staff noted that Interested Parties' argument is twofold, first is that the usage of the investment fair value as a carve out in paragraphs 18a and 18b are confusing due to the requirement to test for impairment based on fair value. NAIC staff amended paragraph 18a to clarify that the carve out allows for admittance of the fair value of unallocated transferable/certificated tax credits rather than the fair value of the tax credit investment. The tax credit investment balance includes other tax benefits which cannot be sold apart from the investment ownership. The intent of paragraph 18a is to allow a reporting entity to at least admit the fair value of the tax credits which can be sold, which is potentially higher than the admitted amount calculated in paragraph 18.

    ii. The second part of Interested Parties' argument is that since these investments may be sold, the admittance assessment of the reporting entity's ability to utilize the tax credits is not needed unless the reporting entity contractually restricted from the selling the investment. As part of this comment, it was noted that these investments may be actively managed and are readily saleable. NAIC staff noted that acquiring tax credit investments with the intent of re-sale puts an insurance company in a similar position as a syndicator in which tax credit investments are developed or acquired for the purpose of sale. SSAP 93 was revised under the assumption that tax credit investments are acquired for the purpose of obtaining returns through the receipt of tax credits and other tax benefits rather than through the sale of the tax credit investment. NAIC staff does not believe the paragraph 18 admittance criteria should be amended to provide a carve out for actively managed tax credit investments as it is not feasible to delineate between tax credit investments purchased for sale vs. purchased for generation of tax benefits without introducing some kind of

available-for-sale and held-to-maturity framework which is not compatible with statutory accounting concepts. NAIC staff noted that restrictions which prevent investors from selling their ownership represent a minority of tax credit programs. As such, limiting the scope of paragraph 18 to only tax credit investments which cannot be sold would effectively carve out the majority of tax credit investment structures from its scope. Additionally, the assertion that these investments are readily saleable does not change the fact that the balance sheet value of a tax credit investment is predicated on the assumption that the company can use the tax credits and benefits and if they company cannot use these tax credits then the investment returns have no value. Until the investment has been sold, its ability to satisfy future policyholder obligations is beholden to the company's ability to utilize the generated tax credits and benefits. Interested Parties noted that there are other investments which do not have as stringent admittance criteria as have been proposed in paragraph 18. NAIC staff note that other investments generate returns primarily through the receipt of fungible cash income or by providing a claim to the entity's earnings and assets (bonds, stocks, joint ventures, partnerships and LLCs). In comparison, the main purpose of a tax credit investment is to provide returns in the form of tax credits and other tax benefits, and this purpose is further borne out by the commonly used partnership flip structure for tax credit investments and that once the tax credits have been fully allocated the residual value of a tax credit investment is typically nominal.

iii. Additionally, the requirement to assess tax credit investments by looking at the company's ability to realize future tax credits is not a new concept. Under existing OTTI guidance companies are required to record OTTI if the company determines it is probable that future tax benefits will not be received as expected (SSAP No. 93 paragraph 17, sentence 1). Per SSAP No. 93 paragraph 17, to determine if OTTI has occurred companies are required to assess whether the investment will continue to issue the tax credits as anticipated (see sentence 5) AND whether the company will be able to realize/utilize the future tax benefits to be received (see sentences 2 and 3). As part of the re-write of SSAP No. 93 Staff moved the requirement to assess the company's ability to utilize future tax credits out of impairment to admissibility. As currently revised, the impairment test specifically addresses the functionality of the investment whereas the paragraph 18 admittance test specifically addresses the ability of the company to realize/utilize the future tax benefits. This change intended to simplify the impairment analysis by focusing on investment functionality, but also because Staff felt that the company's ability to utilize/realize future tax benefits was more accurately characterized as an admittance concern rather than an impairment of the investment itself.

2) Interested Parties suggested a number of editorial changes to affect clearer guidance in paragraphs 18 and 18a. These included clarifying that the paragraph 18 assessment of unallocated tax credit utilization should be performed over the life of the tax credits rather than the life of the investments, including its carryforward periods. Interested Parties also suggested clarifying in paragraph 18 that tax planning strategies are to be used when assessing the utilization of unallocated tax credits, similar to the valuation allowance requirements under SSAP No. 101. In paragraph 18a Interested Parties suggested removing the sentence detailing what to do if fair value is not non-determinable.

i. NAIC staff agreed with substantially all the editorial clarifications suggested by Interested Parties and updated accordingly.

3) Interested Parties suggested adding a definitions section to the guidance regarding the following terminology:

"unallocated tax credits" - the portion of tax credits expected to be earned and allocated to the reporting entity through the investment structure.

"current portion" - the credits to be allocated within one year of the reporting period.

i. NAIC staff agreed with the suggestion by Interested Parties to add definitions and updated accordingly with some minor modifications. NAIC staff also added some additional definitions to provide clarifications on other terms used in SSAP 93.

4) Interested Parties suggested that the new SSAP 93 be applied prospectively effective 1/1/2025, but no early adoption.

i. NAIC staff agreed with the changes suggested by Interested Parties and updated accordingly.

The comments provided on SSAP No. 94R are below and have been summarized for brevity:

5) Interested parties suggested that the revised SSAP 94R also be applied prospectively effective 1/1/2025 with early adoption permitted. Additionally, Interested Parties suggested a clarification of the scope of SSAP 94R by adding the following language to paragraph 1:

"This statement establishes statutory accounting principles for state and federal tax credits that are purchased by the reporting entity without being ~~a~~an bond or equity investor in the entity from which the tax credit were purchased."

i. NAIC staff agrees with prospective application of SSAP 94R with an effective date of 1/1/2025, however we have elected to not include the changes to the scope of SSAP 94R. The reasoning is that this guidance intends to exclude tax credits allocated from SSAP 93 investments, which does not specifically identify which tax credit investment structures are within scope of the guidance. However, NAIC staff did make other adjustments to the scope paragraph to better clarify that tax credits from SSAP No. 93 investments are not within scope of SSAP 94R.

On December 1, 2023, the Statutory Accounting Principles (E) Working Group exposed revisions made to SSAP Nos. 34, 48R, 93, and 94R as part of the new market tax credit project. Revisions to SSAP No. 93 include a glossary of key terms, impairment guidance on variable tax credit allocations, disclosures on unused tax credits, and editorial changes to paragraph 18. Revisions to SSAP No. 94R include guidance clarifying that awarded tax credits are not within scope and commitment/contingency language. The exposure includes new revisions to SSAP Nos. 34 and 48 which clarified that tax credits are not within the scope of investment income guidance and updated for new SSAP No. 93 language, respectively. Additionally, the Working Group requested comments from regulators and industry on new RBC reporting categories.

On January 29, 2024, the Statutory Accounting Principles (E) Working Group exposed, through an evote, further revisions made to SSAP Nos. 93R and 94R as part of the New Market Tax Credit project. Revisions to SSAP No. 93 and 94R included minor consistency and clarifying revisions. More substantial revisions were made to SSAP No. 93 in response to concerns raised by interested parties over the administrative burden of the paragraph 18 admittance tests (now referred to as the Prospective Utilization Assessment). The Prospective Utilization Assessment was revised to remove the initial assessment of the current portion of unallocated tax credits and replaced with language that required companies to perform the Prospective Utilization Assessment only if certain conditions exist.

On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, the exposed revisions to SSAP No. 93, updated for the corrections to example 2, and SSAP No. 34, SSAP No. 48, and SSAP No. 94R to expand and amend statutory guidance to include all tax credit investments regardless of structure and type of state or federal tax credit program, and all state and federal purchased tax credits. The effective date of the revisions is January 1, 2025.

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The Working Group also directed staff to:

1. Sponsor a blanks proposal on the annual statement reporting categories for tax credit investment RBC by using the suggestion from the interested parties comment letter to maintain the same categories but without reference to LIHTC (bullet 1) and to also update/clarify the instructions accordingly.
2. Send a referral to the Life Risk-Based Capital (E) Working Group to inform them of the planned reporting line changes, which may indicate review of the RBC charges as different categories of tax credits will be reported in the form.
3. To draft an Issue Paper to document the discussions and revisions.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/03-16-24 Spring National Meeting/Adoptions/22-14 - NMTC.docx

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Note: *The issue paper will include the final revisions made to SSAP No. 93—Low-Income Housing Tax Credit Property Investments shown as tracked changes. ASC references will be removed from the final document.*

Spring National Meeting Adoption: *Revisions to SSAP No. 93 made* ***after*** *the exposure on January 31, 2024, have been shown as tracked changes highlighted in grey. This document represents the final adopted version of SSAP No. 93R.*

Statements of Statutory Accounting Principles No. 93 - Revised

Investments in Tax Credit Structures

STATUS

Type of Issue	Common Area
Issued	June 13, 2005; Conceptually revised March 16, 2024
Effective Date	January 1, 2006; Conceptual revisions detailed in Issue Paper No. xxx effective January 1, 2025
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	INT 06-07
Relevant Appendix A Guidance	None

STATUS **1**

SCOPE OF STATEMENT **2**

SUMMARY CONCLUSION **2**

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EXHIBIT A – APPLICATION OF PROPORTIONAL AMORTIZATION METHOD **12**

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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for qualifying tax credit investments[1] in programs made primarily for the purpose of receiving allowable general business federal tax credits and/or state tax credits, including state premium tax credit programs. Although these investments are often in the form of equity, this statement shall be applied to all investments (regardless of the structure of the investment) that qualify pursuant to paragraph 2.

2. A reporting entity that invests in projects or programs that generate general business federal tax credits, corresponding state tax credits or state premium tax credits that meet the following conditions at the time of initial investment are required to capture the investment in scope of this statement:

   a. It is probable that the tax credits allocable to the investor will be available.

   b. Reporting entity investor does not have the ability to exercise significant influence over the operating and financial policies of the underlying projects.

   c. Substantially all the projected benefits are from tax credits and other tax benefits, determined on a discounted basis using a discount rate that is consistent with the cash flow assumptions utilized by the reporting entity for the purpose of deciding to invest in the project.

   d. The reporting entity's projected yield based solely on the cash flows from the tax credits and other tax benefits is positive.

3. Tax credit investments that do not meet the conditions in paragraph 2 shall be captured within the statutory accounting statement that addresses the underlying investment structure. Equity structured tax credit investments would generally fall within *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*. Debt structured tax credit investments should be assessed in accordance with *SSAP No. 26R—Bonds* to determine eligibility for reporting as a bond. ~~Investments intax credit structures that do not meet the conditions in paragraph 2 shall be captured within the statutory accounting statement applicable to the investment held.~~

4. Investments in a CAPCO (Certified Capital Company), organized as a partnership or an LLC, which is a company, authorized by state statute that borrows from investors, to make venture capital investments in "qualified" businesses, are not within the scope of this statement. Although associated with tax credits, the reporting entity is paid principal and interest on its investment with the CAPCO. Depending upon the terms of the CAPCO offering, principal and interest payments to the reporting entity will come from the CAPCO and/or the state. The CAPCO will make cash payments directly to the investors while the state will make payments in the form of premium or income tax credits. Investments in a CAPCO shall be accounted for in accordance with *Interpretation (INT) 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)* and specific statutory accounting guidance addressing CAPCOs.

SUMMARY CONCLUSION

5. Investments in tax credit structures are generally acquired to obtain a positive yield through tax credits and other tax benefits. The value of the investment is primarily based on the value of the remaining stream of tax credits and deductible expenses available to the reporting entity investor. The primary purpose of investing in these tax credit structures is to generate tax credits which benefit reporting entities, most

[1] The scope of *ASC 323-740–Investments—Equity Method and Joint Ventures—Income Taxes—Proportional Amortization Method* only extends to income tax equity investments, whereas this statement is intended to capture all tax credit investments which meet the criteria in paragraphs 2.a-2.d, regardless of structure. This includes, but is not limited to, tax equity investments and tax credit debt investments.

commonly through a reduction in tax liability or, when ~~transferability is~~ permitted by IRS or state tax provisions, through the sale of ~~the~~ certificated/transferable tax credits.

6. Investments in tax credit structures held by reporting entities meet the definition of an asset as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement.

Accounting

7. This guidance addresses the methodology for measuring an investment that is accounted for using the proportional amortization method. At initial recognition, investments in scope of this statement shall be recorded at cost.

8. Subsequent to initial recognition, the investment shall be carried at proportional amortized cost. Under the proportional amortization method, the reporting entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits allocated to the investor. The amortization amount shall be calculated as follows (ASC 323-740-35-2):

a. The initial investment balance less any expected residual value of the investment, multiplied by;

b. The percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be received by the reporting entity over the amortization timeframe (life of the investment)~~the life of the investment~~.

9. Reporting entities shall recognize tax credits in the period they are allocated to the investor for tax purposes. Unless all tax credits are allocated to the reporting entity at the date of initial investment, immediate recognition of the entire benefit of the tax credits to be received during the term of the investment project that generates tax credits and other tax benefits is not permitted. Tax credits shall not be recognized in the financial statements before the year in which the tax credits ~~arisesis~~ are allocated. (ASC 323-740-25-5)

10. Any expected residual value of the investment shall be excluded from the proportional amortization calculation. Non-tax related benefits received from the investment shall be included as a component of net investment income when realized or realizable. Gains or losses on the sale of the investment, if any, shall be included as a capital gain or loss at the time of the sale. (ASC 323-740-35-5) Determination of gain or loss will depend on the reported value (e.g., residual value at the end of the amortization timeframe) compared to the amount received in exchange for the investment. Liquidation of the investment commonly occurs at the end of the tax credit timeframe through a put or call agreement, often reflecting a nominal residual value that was established at the time of acquisition. The liquidation amount from such agreements shall reflect the expected residual value when available.

11. At the end of the amortization timeframe ~~(life of the investment)~~, if the reporting entity retains the investment, the investment shall be subsequently measured and assessed within the statutory accounting statement applicable to the investment held. Retained investments will remain on Schedule BA until disposal and cannot exceed the initial expected residual value.

12. Exhibit A illustrates the application of accounting guidance in two examples that generate tax credits and tax benefits using the proportional amortization method. The first example illustrates the application of a standard project. The second example illustrates the application of accounting guidance in a project that has expected residual value and generates non-tax related benefits in addition to tax credits and other tax benefits using the proportional amortization method. (ASC 323-740-35-3)

Application of Proportional Amortization Method

13. Under the proportional amortized cost method, the amortization of the investment is to be recognized in the income statement as an expense component of the net investment income calculation. Non-tax related benefits received from operations, or sale of the investment should be accounted for in accordance with paragraph 10.

14. Tax credits and other tax benefits, not to include amortization of the investment, shall be reflected as follows:

a. ~~Tax credits allocated are to be recorded, and assessed for admittance, in accordance with *SSAP No. 94R Transferable and Non-Transferable Tax Credits*.~~Tax credits shall be recognized in the period that they are allocated to the reporting entity for tax purposes:

i. Federal tax credits that can be utilized in the year allocated shall be reported in the income statement as an offset to federal taxes in accordance with *SSAP No. 101—Income Taxes*. Federal tax credits that cannot be utilized in the year allocated and are carried forward to a future tax year shall be reported as a deferred tax asset (DTA) in accordance with SSAP No. 101.

ii. State tax credits that can be utilized in the year allocated shall be reported in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized. State tax credits that cannot be utilized in the year allocated and are carried forward to a future tax year shall be reported gross of any related state tax liabilities and reported in the category of other-than-invested assets (not to be reported net).

iii. Use of tax credits carried forward in a~~Tax credits carried forward to a~~ future period shall be reflected as an offset to the corresponding income or premium tax in the tax reporting year in which the tax credit is utilized.

~~i.~~iv. Tax credits allocated from tax credit investments, as defined within this SSAP, and held by reporting entities meet the definition of assets as specified in SSAP No. 4 and are admitted assets to the extent that they comply with the requirements of this statement. The admissibility of tax credits ~~are~~ is subject to SSAP No. 101.

b. Federal tax benefits other than tax credits (e.g., tax benefits from investment depreciation) shall be recognized in the year allocated pursuant to SSAP No. 101~~—*Income Taxes*~~. When utilized, the federal tax benefits are recognized as a component of income tax expense.

c. State tax benefits other than tax credits shall be recognized in the year allocated ~~shall be recognized in the year allocated~~ gross of any related state tax liabilities pursuant to SSAP No. 101. When utilized, the state tax benefits are recognized as a component of taxes, licenses, and fees.

Admittance ~~Requirements~~of Tax Credit Investments

15. Although investments in tax credit programs do not represent investments that can be ~~directly~~ readily liquidated for policyholder claims, the reduction of tax liability or sale~~transfer~~ of allocated tax credits represents a benefit that supports admittance of these investments, but only if the tax credits will be received and can be utilized by the reporting entity. Investments in tax credit programs that will not result in any of the anticipated tax credits or that will result in tax credits which cannot be utilized or sold~~transferred~~ by the reporting entity shall be considered impaired and should refer to paragraphs 27 and 28.

16. Reporting entities shall, at initial investment, obtain a clean[2] fund level tax opinion[3] on the validity of the credits and structure of the underlying program and investment fund. Investments not supported by an initial tax opinion shall be nonadmitted. If the program is a permitted syndicated program with a yield guarantee, the opinion must verify that the investment and guarantee haves ~~s~~ been properly structured under IRS or state tax provisions ~~rules~~ and the guarantee does not disqualify the reporting entity from obtaining ~~federal general business~~the tax credits.

17. Reporting entities shall annually obtain U.S. GAAP or U.S. tax basis audited financial statements on the investment fund. In the event audited U.S. GAAP or U.S. tax basis financial statements are not obtained or the audit receives an opinion other than unqualified, the asset shall be nonadmitted. If the audited financial statements are in-process but not completed as of the annual statement filing deadline, the reporting entity may admit the investment based on the results of the immediately preceding prior year audited financial statements. A lag in reporting shall be consistent from period to period.

a. Other tax credit investments – If the reporting entity has a tax credit investment which by virtue of its structure cannot be audited, the investment is exempt from the annual audit requirement. One example of this type of investments would be tax credit debt investments[4] which do not involve any amount of equity ownership as a component of the investment. This type of tax credit debt investment is exempt from the annual audit requirement, but the reporting entity is still required to obtain a clean tax opinion, in accordance with paragraph 16, to support admittance at initial investment.

Prospective Utilization Assessment

18. The prospective utilization assessment, as detailed below in paragraphs 19-21, must be performed annually by the reporting entity if any of the following circumstances exist in either the current or prior reporting period:

a. Reporting entity records a valuation allowance against a deferred tax asset (DTA) balance.

b. Reporting entity becomes aware of other facts and circumstances which indicate that it will, more likely than not, be unable to substantially utilize the unallocated tax credits. Such instances include, but are not limited to:

i. If the reporting entity holds an investment which allocates state premium tax credits and intends to decrease premium volume in that state, it may affect whether or not the unallocated tax credits in that state can be utilized.

ii. If the reporting entity holds an investment allocating state income tax credits and records a valuation allowance in its U.S. GAAP financial statements against state DTA balances, including the same state as the tax credit investment, it cannot ignore the circumstances that led to the valuation allowance, even though statutory accounting does not permit state DTAs.

[2] While not quantified or defined in either the Internal Revenue Code or state regulations, common industry standards consider a "should" opinion to be the minimum degree of confidence associated with a clean tax opinion. For the purposes of this statement, a "should" opinion must represent a probability of success no less 70%. Any tax credit investment which receives a tax opinion with a degree of confidence less than "should" is to be nonadmitted.

[3] A fund level tax opinion for the purposes of this statement is defined as a full IRS Circular 230 tax opinion which covers from the fund level through to the underlying assets generating the tax credit benefits. The fund level is defined as the entity, or level, at which the investor comes directly into the investment without any intermediaries.

[4] Common examples of tax credit debt investments are Tax Credit Strips derived from tax credit bonds, Qualified Tax Credit Bonds, and Build America Tax Credit Bonds. Tax opinions received on these tax credit investments are also referred to as "bond counsels." Tax Credit Strips derived from tax equity investments would not qualify for the paragraph 17.a carve out as the source of the stripped tax credits is auditable.

19. Prospective Utilization Assessment – ~~A r~~If any of the circumstances detailed in paragraph 18 exist, the reporting entity is required to ~~first~~ assess the future utilization of the investment's ~~current portion of~~ unallocated tax credits against ~~the~~ estimated tax liabilities ~~for both the tax year in which the tax credits can be initially utilized as well as any applicable carryback periods. Based on this assessment, if the reporting entity does not expect to substantially utilize the current portion of unallocated investment tax credits, the reporting entity shall perform an expanded assessment to~~and determine the extent to which it will be able to utilize the investment's unallocated tax credits over the life of the ~~investment~~tax credits. If assessment projections identify that the investment's unallocated tax credits ~~from investments in tax credit programs~~ will exceed what can be utilized under IRS or state tax provisions ~~(current and other applicable tax periods)~~, the reporting entity shall nonadmit investments as necessary so that investments in scope of this statement (in aggregate) are only admitted to the extent tax credits are expected to be utilized within current, carryback, and carryforward periods. ~~Additionally, if the assessment indicates that the next three years of investment tax credits cannot be substantially utilized within the carryforward periods then the entire investment shall be nonadmitted.~~ In making this assessment, the reporting entity is not permitted to assume increased operations (e.g., expanded product sales) beyond those allowed under prudent and feasible tax-planning strategies ~~actual experience~~ to conclude that additional federal or state tax liability will exist that would allow additional utilization of tax credits. A reporting entity ~~can~~ may subsequently admit a previously nonadmitted tax credit investment, based on subsequent assessments in which the reporting entity determines that they will be able to utilize the unallocated tax credits.

~~18.~~20. Additional Admittance to Prospective Utilization Assessment – If the tax credit investment allocates tax credits with the following features, the reporting entity may perform a secondary assessment to determine if additional amounts of the tax credit investment nonadmitted under paragraph 19 can be admitted:

a. Tax credit investments which allocate tax credits which are certificated or transferable in accordance with permitted IRS or state tax provisions ~~are~~ shall admit~~ted~~ up to the lesser of the proportional amortized cost~~,~~ or fair value of the unallocated tax credits. ~~If the fair market value is not determinable, then the reporting entity may only admit the amount calculated in paragraph 18.~~

b. Tax credit investments which allocate tax credits eligible for direct payment ~~are~~ shall admit~~ted~~ up to the lesser of the proportional amortized cost~~,~~ or the estimated proceeds from unallocated tax credits.

~~c. For all other tax credits, if a reporting entity does not expect to fully utilize investment tax credits in the upcoming tax year or for a carryback year, the reporting entity shall perform an assessment to determine the extent it will be able to utilize the tax credits over the life of the investment. If assessment projections identify that the tax credits from investments in tax credit programs will exceed what can be utilized under IRS or state tax provisions (current and other applicable tax periods), the reporting entity shall nonadmit investments as necessary so that investments in scope of this statement (in aggregate) are only admitted to the extent tax credits are expected to be utilized. Additionally, if the assessment indicates that the next three years of investment tax credits cannot be substantially utilized then the entire investment shall be nonadmitted. In making this assessment, the reporting entity is not permitted to assume increased operations (e.g., expanded product sales) beyond actual experience to conclude that additional federal or state tax liability will exist that would allow additional utilization of tax credits. A reporting entity can subsequently admit a previously nonadmitted tax credit investment, based on subsequent assessments in which the reporting entity determines that they will be able to utilize the tax credits.~~

~~19.~~21. For tax credit investments which have an amortization timeframe greater than the tax credit allocation timeframe (as demonstrated in ~~both examples within~~ Exhibit A), the reporting entity would still,

if required, perform the prospective utilization assessment ~~same assessment detailed in paragraph 18~~ but on the reporting entity's ability to utilize the remaining stream of anticipated tax benefits.

Future Contributions and Additional Tax Credits

~~20.~~22. Many tax credit investments require future contributions by the investor, that may be contingent on a variety of conditions, such as receiving representations, contract performance, meeting occupancy requirements, etc. A liability shall be recognized for delayed ~~equity~~ contributions which result in additional tax credits that are unconditional and legally binding, and a liability shall also be recognized for ~~equity~~ contributions which result in additional tax credits that are contingent upon a future event when that contingent event becomes probable pursuant to the loss contingency guidance in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. (ASC 323-740-25-3) Liabilities or loss contingencies recognized for future contributions which result in additional tax credits shall be reported as 'Payable for Securities' until remitted or until the obligation is otherwise eliminated.

~~21.~~23. If a commitment to provide future contributions is not required to be recognized pursuant to paragraph 22, the commitment shall be disclosed in the notes to the financial statements with other commitments.

~~22.~~24. Additional contributions that do not result in additional tax credits for the reporting entity investor shall be immediately expensed as a component of net investment income.

~~23.~~25. If additional contributions result in additional tax credits for the reporting entity, the proportional amortization method for the tax credit investment shall be adjusted, on a prospective basis, to reflect the increased cost with the revised expected ~~income~~ tax credits and ~~income~~ other tax benefits.

26. In the event a reporting entity obtains additional tax credits without the reporting entity making additional contributions, the reporting entity shall not adjust the book/adjusted carrying value of the tax credit investment. (The proportional amortization method shall not be adjusted to reflect the expected additional tax credits.) Rather, the tax credit shall be recognized when allocated pursuant to paragraph 14.

Impairment of Tax Credit Investments

~~24.~~27. Reporting entities with investments in tax credit programs shall complete and document an impairment analysis at each reporting period. For this analysis, the reporting entity shall compare the current book/-adjusted carrying value to the fair value of the investment. (~~In lieu of~~If fair value is not determinable, an entity can compare book/-adjusted carrying value to the present value of future tax credits and other tax benefits discounted at a risk-free rate of return.) If book-/adjusted carrying value is higher, the difference between book/-adjusted carrying value and fair value shall be recognized as an other-than-temporary impairment (INT 06-07) to the tax credit investment. This will result in a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries in fair value ~~(discounted value present value)~~.

~~25.~~28. An other-than-temporary impairment shall also be considered to have occurred if a previously allocated tax credit has been recaptured or if it is probable that future tax credits will not be allocated as expected. If a project no longer qualifies for tax credits, the entire investment, less any residual established at initial recognition, shall be written off as other-than-temporarily impaired. If the reporting entity experiences a tax credit recapture, the reporting entity shall assess whether future tax credits and other benefits will qualify for use by the reporting entity. If future credits will not be generated or will be subject to future recapture, then the reporting entity shall write-off the investment as other-than-temporarily impaired so that the resulting investment value only reflects expected qualifying tax credits and other benefits expected to be allocated. This will result in a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries or revision to tax credit expectations.

~~26.~~29. Certain tax credit programs allocate variable amounts of tax credits (for example, clean energy production tax credit programs) which will result in regular differences between actual allocated tax credits and estimated tax credit allocations as calculated upon acquisition of the investment. Variable tax credits allocated in excess of estimates should be accounted for in accordance with paragraph 26. If the allocated variable tax credits are less than estimates by more than 10% or consistently allocate less than the estimated amounts over multiple allocation periods, then the reporting entity must either recognize an other-than-temporary impairment or specifically address within its impairment analysis the reason why consistently diminished tax credit returns do not represent an impairment event. Note that if the company determines it is probable that the total amount of anticipated variable tax credits will not be received, it would still be considered an other-than-temporary impairment in accordance with paragraph 28.

Disclosures

~~27.~~30. A reporting entity shall disclose information that enables users of its financial statements to understand the following information about its ~~tax~~ investments in projects that generate tax credits and other tax benefits from tax programs captured in scope of this statement: (ASC 323-740-50-1)

a. The nature of its investments in projects that generate tax credits and other tax benefits.

b. The effect of the recognition and measurement of its investments in projects that generate tax credits and other tax benefits and the related tax credits on its financial position and results of operations.

~~28.~~31. To meet the objective of paragraph 30, a reporting entity shall disclose the following information about its ~~tax~~ investments in projects that generate tax credits and other tax benefits from a tax credit program in scope of this statement:

a. The amount of tax credits and other tax benefits recognized during the reporting period(s).

b. The balance of the investments recognized in the statement of financial position for the reporting period(s) presented.

c. The amount of investment amortization and non-income tax related activity recognized as a component of net investment income, and other returns allocated that were recognized outside of income tax expense.

d. An aggregate schedule of tax credits expected to be generated each year for the subsequent five years and thereafter, disaggregated by transferable/certificated and non-transferable.

e. Any commitment or contingent commitment (e.g., guarantees or commitments to provide additional capital contributions) including the amount of contributions that are contingent commitments related to tax credit investments and the year(s) that contingent commitments are expected to be paid shall be disclosed.

~~29.~~32. The following disclosures shall be included if applicable to tax credit investments:

a. If the underlying ~~property~~ project is currently subject to any regulatory reviews and the status of such review. (Example: Investigations by the housing authority.)

b. Significant modifications or events that resulted in a change in the nature of the investment or a change in the relationship with the underlying project for investments in scope. (ASC 323-740-50-1A)

~~30.~~33. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment and how fair value was determined.

34. The following disclosures pertain only to those tax credits allocated from tax credit investments and are unused as of the reporting period(s). For purposes of this disclosure, total unused tax credits represent the entire amount of tax credits available:

a. Carrying value of tax credits, disaggregated by transferable/certificated and non-transferable, gross of any related tax liabilities by jurisdiction and in total.

b. Total unused tax credits by jurisdiction, disaggregated by transferable/certificated and non-transferable.

c. Method of estimating utilization of remaining tax credits or other projected recovery of the current carrying value.

d. Impairment amount recognized in the reporting period(s), if any.

e. Identify tax credits by transferable/certificated and non-transferable classifications and identify the admitted and nonadmitted portions of each classification.

~~31.~~35. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

~~32.~~36. This statement adopts with modification *Accounting Standards Update (ASU) 2023-02, Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method*. The ASU is modified for the following statutory concepts:

a. This statement is applicable to all federal and state tax credit programs earned through any tax credit investment structure that meets the requirements in paragraph 2. Under the ASU, use of the proportional amortization method is an election and only pertains to income tax equity investment structures in which the reporting entity does not exercise significant influence. With this statement, the U.S. GAAP election to use the proportional amortization method is rejected and use of proportional amortization for investments within the scope of this statement is required. The guidance is expanded for state premium tax credits.

b. Investments that meet the criteria of this statement are required to use a proportional amortization method as prescribed in this statement. This method requires the tax credits and benefits to be recognized in proportion to the percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be allocated by the reporting entity over the life of the investment. This statement requires a gross presentation on the financial statements. Under the ASU, a practical expedient is allowed for the calculation of proportional amortization but has been rejected with this statement.

c. Federal tax credits shall be recognized in the income statement as an offset to federal income taxes in the tax reporting year in which the tax credit is utilized in accordance with SSAP No. 101. State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax reporting year in which the credit is utilized.

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d. Tax benefits allocated, other than tax credits, shall be accounted for pursuant to SSAP No. 101. Amortization shall be reported as a component of net investment income.

e. Reporting entities shall follow the guidance in paragraphs 22 and 23 regarding the recognition of contingent commitments from SSAP No. 5R to equity contributions.

f. This statement has specific impairment and nonadmittance requirements.

g. For statutory accounting purposes, deferred taxes are not reported as a component of income from continuing operations in the income statement; rather deferred taxes are recognized as a separate component of gains and losses in unassigned funds (surplus).

h. Disclosures should be followed as indicated in the disclosures section in this statement.

~~h.~~i. The examples detailed in Exhibit A were modified to better illustrate the statutory accounting method for tax credit investments.

Effective Date and Transition

~~33.~~37. This statement is effective for reporting periods beginning on or after January 1, 2006. Early adoption is permitted. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3–Accounting Changes and Corrections of Errors*. The guidance previously in paragraph 3 of this statement superseded paragraph 1 of SSAP No. 48. In 2011, this guidance was moved to SSAP No. 48 and deleted from this statement. The original guidance included in this standard is retained for historical purposes in Issue Paper No. 125. The guidance from ASU 2014-01 is effective for reporting periods beginning on or after January 1, 2015, with early adoption permitted.

38. In March 2024, new SAP concept revisions, as detailed in Issue Paper No. XXX, were adopted. These revisions, effective January 1, 2025, expanded the scope of SSAP No. 93 to include all federal and state tax credit investment structures and provide new guidance on the accounting, recognition, and reporting of tax credit investment structures. As of the effective date, reporting entities shall prospectively modify the recognition, accounting, and reporting of tax credit investment structures to reflect the guidance in the conceptual revisions. Additionally, all tax credit investment structures which fall within the scope of this statement not currently reported on Schedule BA are to be transferred to Schedule BA as of the effective date.

Glossary

39. The following definitions are provided for the purposes of this statement.

a. Unallocated tax credits – The portion of tax credits expected to be earned and allocated to the reporting entity through the tax credit investment structure.

~~i. Current portion – The tax credits to be allocated within one year of the reporting period.~~

b. Transferable/Certificated – The tax credits are certified for sale (certificated tax credits) or saleable through the execution of a state or federal transfer form (transferable tax credits).

c. More Likely Than Not – Refers to a likelihood of more than 50%.

REFERENCES

Relevant Issue Papers

- Issue Paper No. 125—Accounting for Low-Income Housing Tax Credit Property Investments
- Issue Paper No. XX—XXX

EXHIBIT A – APPLICATION OF PROPORTIONAL AMORTIZATION METHOD

Example 1: ~~Application of Proportional Amortization Method for Qualifying Investment~~Qualifying Tax Credit Investment Structure

~~This example is based on paragraph 323-740-55-5 of the Accounting Standards Codification which illustrates the application of a standard project. The amount and timing of amortization in the proportional amortization method is consistent with the statutory modifications; therefore, the table incorporated in this exhibit is based on the proportional amortization table. The statutory income statement requires a gross presentation on the income statement, with proportional amortization of the initial cost of the investment in investment income and the tax credits and benefits included in income tax expense.~~

~~Terms:~~
~~Date of Investment: January 1, 20X1~~
~~Purchase Price of Investment: $100,000~~
On January 1, 20X1, ABC Insurance Company purchases a 5% equity stake in a tax credit investment structure for $100,000. The allocated tax credits are transferable, and ABC anticipates that all tax credits received will be fully utilized prior to expiration of the tax credit carryover period.

Assumptions:

1. All cash flows (except initial investment) occur at the end of each year.

2. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).

3. The investor made a $100,000 investment for a 5% limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.

4. The partnership finances the project cost of $4,000,000 with 50% equity and 50% debt.

5. The annual tax credit allocation (equal to 4% of the project's original cost) will be received for a period of 10 years.

6. The investor's tax rate is 40%.

7. For simplicity, the project will operate with break-even pretax cash flows including debt service during the first 15 years of operations.

8. The project's taxable loss will be equal to depreciation expense. The cumulative book loss (and thus the cumulative depreciation expense) recognized by the investor is limited to the $100,000 investment.

9. It is assumed that all requirements are met to retain allocable tax credits so there will be no recapture of tax credits.

10. The investor expects that the estimated residual value of the investment will be zero.

Proportional Amortization Method with Statutory Modifications

Year	Net Investment (1)	Amortization of Investment (2)	Tax Credits (3)	Net Losses/Tax Depreciation (4)	Other Tax Benefits from Tax Depreciation (5)	Tax Credits and Other Tax Benefits (6)
	100,000					
1	90,909	9,091	8,000	7,273	2,909	10,909
2	81,818	9,091	8,000	7,273	2,909	10,909
3	72,727	9,091	8,000	7,273	2,909	10,909
4	63,636	9,091	8,000	7,273	2,909	10,909
5	54,545	9,091	8,000	7,273	2,909	10,909
6	45,454	9,091	8,000	7,273	2,909	10,909
7	36,363	9,091	8,000	7,273	2,909	10,909
8	27,272	9,091	8,000	7,273	2,909	10,909
9	18,181	9,091	8,000	7,273	2,909	10,909
10	9,090	9,091	8,000	7,273	2,909	10,909
11	6,666	2,424		7,273	2,909	2,909
12	4,242	2,424		7,273	2,909	2,909
13	1,818	2,424		7,273	2,909	2,909
14	0	1,818		5,451	2,183	2,183
15	0					0
Total		100,000	80,000	100,000	40,000	120,000

(1) End-of-year investment for a 5% limited liability interest in the project net of amortization in Column (2).

(2) Initial investment of $100,000 x (total tax benefits allocated during the year in Column (6) / total anticipated tax benefits over the life of the investment of $120,000).

(3) Annual 4% tax credit on $200,000 tax basis of the underlying assets.

(4) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.5 years up to the amount of the initial investment of $100,000.

(5) Column (4) x 40% tax rate.

(6) Column (3) + Column (5).

Initial Year

	Tax credit investment	100,000	
	Cash		100,000
	To record the purchase of tax credit investment		

Years 1-10

	Amortization expense	9,091	
	Tax credit investment		9,091
	Federal tax credits	8,000	
	Income tax expense		8,000
	To record annual receipt of allocated tax credits and proportional amortization of investment.		

	Income taxes payable	8,000	
	Federal tax credits		8,000
	To record annual utilization of allocated tax credits.		

Year 11-13

	Amortization expense	2,424	
	Tax credit investment		2,424
	To record annual proportional amortization of tax credit investment.		

Year 14

	Amortization expense	1,818	
	Tax credit investment		1,818
	To record annual proportional amortization of tax credit investment.		

Example 2: Qualifying Tax ~~Equity~~ Credit Investment~~s~~ Structure with Non-Income Tax Related Benefits

~~This example is based on paragraphs 323-740-55-11 through 323-740-55-14 of the Accounting Standards Codification and illustrates a tax equity investment that generates non-income-tax-related benefits in addition to tax credits and other income tax benefits.~~

~~The amount and timing of amortization in the proportional amortization method is consistent with the statutory modifications; therefore, the table incorporated in this exhibit is based on the proportional amortization table. The statutory income statement requires a gross presentation on the income statement, with proportional amortization of the initial cost of the investment in investment income and the tax credits and benefits included in income tax expense.~~

~~Terms:~~
~~Date of Investment: January 1, 20X1~~
~~Purchase Price of Investment: $100,000~~
On January 1, 20X1, T&A Insurance Company purchased a 5% equity stake in a tax credit investment structure for $100,000. The allocated tax credits are non-transferable, and T&A anticipates that all tax credits received will be fully utilized prior to expiration of the tax credit carryover period.

Assumptions:

1. All cash flows (except initial investment) occur at the end of each year.

2. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).

3. The investor made a $100,000 investment for a 5% limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.

4. The partnership will receive production tax credits based on the energy the project produces. The credits will be allocated over a four-year period.

5. The tax equity investor will receive cash proceeds based on 2% of the project's cash generated during the life of the ~~project~~investment.

6. The investor's tax rate is 40%.

7. All requirements are met to retain allocable income tax credits such that there will be no recapture of income tax credits.

~~8. The investor expects that the estimated residual value of the investment will be zero.~~

~~9.~~8. All of the conditions are met to require use of the proportional amortization method.

9. After 10 years, the tax equity investor has a right to require that the project sponsor purchase the tax equity investor's equity interest for a nominal amount. It is assumed that the Put option will be exercised and has a contractually agreed upon residual value of $1,000.

10. In Years 1-3 the investor is able to utilize all allocated tax credits in the same period they were received. In Year 4, the investor is only able to utilize half of that year's allocated tax credit and defers the remainder for utilization in Year 5.

Proportional Amortization Method with Statutory Modifications

Year	Net Investment (1)	Amortization of Investment (2)	Tax Credits (3)	Net Losses/Tax Depreciation (4)	Other Tax Benefits from Tax Depreciation (5)	Tax Credits and Other Tax Benefits (6)	Non-Tax Related Cash Returns (7)
	100,000						
1	~~79,399~~79,605	20,395~~601~~	20,000	8,300	3,320	23,320	58
2	~~58,799~~59,210	20,395~~601~~	20,000	8,300	3,320	23,320	58
3	~~38,198~~38,815	20,395~~601~~	20,000	8,300	3,320	23,320	58
4	~~17,597~~18,420	20,395~~601~~	20,000	8,300	3,320	23,320	58
5	~~14,664~~15,516	2,904~~33~~		8,300	3,320	3,320	58
6	~~11,731~~12,612	2,904~~33~~		8,300	3,320	3,320	58
7	~~8,799~~9,708	2,904~~33~~		8,300	3,320	3,320	58
8	~~5,866~~6,804	2,904~~33~~		8,300	3,320	3,320	58
9	~~2,933~~3,900	2,904~~33~~		8,300	3,320	3,320	58
10	~~0~~1,000	2,900~~33~~		8,300	3,320	3,320	58
Total	1,000	~~100~~99,000	80,000	83,000	33,200	113,200	580

(1) End-of-year investment for a 5% limited liability interest in the project net of amortization in Column (2).

(2) Initial investment, less residual value of $1,000, of $~~100~~99,000 x (total tax benefits allocated during the year in Column (6) / total anticipated tax benefits over the life of the investment of $113,200).

(3) These tax credits have been generated through the production of electricity, which generates production tax credits. The tax equity investor is not receiving renewable energy credits or carbon offsets.

(4) Depreciation /other tax losses passed on to the investor.

(5) Column (4) x 40% tax rate.

(6) Column (3) + Column (5).

(7) Non-income-tax-related benefits recognized in current-period pre-tax earnings when allocated. This represents the cash proceeds allocated by the tax equity investor based on the cash generated from the project~~.~~

Initial Year

Tax credit investment	100,000	
Cash		100,000
To record the purchase of tax credit investment		

Years 1-3

Amortization expense	20,395	
Tax credit investment		20,395
Federal tax credits	20,000	
Income tax expense		20,000
Cash	58	
Investment Income		58

	To record annual receipt of allocated tax credits, proportional amortization of investment, and receipt of non-tax cash returns.		
	Income taxes payable	20,000	
	Federal tax credits		20,000
	To record annual utilization of allocated tax credits.		

Year 4

	Amortization expense	20,395	
	Tax credit investment		20,395
	Federal tax credits	20,000	
	Income tax expense		20,000
	Cash	58	
	Investment Income		58
	To record annual receipt of allocated tax credits, proportional amortization of investment, and receipt of non-tax cash returns.		
	Income taxes payable	10,000	
	Federal tax credits		10,000
	Income tax expense	10,000	
	Deferred tax expense		10,000
	To record the portion of allocated tax credits utilized in the current year and defer the remainder. (Federal tax credit account should be mapped to the DTA reporting line as any balance remaining at year-end would be a DTA)		

Year 5

	Amortization expense	2,904	
	Tax credit investment		2,904
	Cash	58	
	Investment Income		58
	To record annual proportional amortization of tax credit investment and receipt of non-tax cash returns.		
	Income taxes payable	10,000	
	Federal tax credits		10,000
	Deferred tax expense	10,000	
	Income tax expense		10,000
	To record utilization of deferred tax credit.		

Years 6-9

	Amortization expense	2,904	
	Tax credit investment		2,904
	Cash	58	
	Investment Income		58
	To record annual proportional amortization of tax credit investment and receipt of non-tax cash returns.		

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Year 10

Amortization expense	2,900	
Tax credit investment		2,900
Cash	58	
Investment Income		58
To record annual proportional amortization of tax credit investment and receipt of non-tax cash returns.		
Cash	1,000	
Tax credit investment		1,000
To record sale of interest in tax credit investment at stated residual value.		

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Spring National Meeting Adoption: *Revisions to SSAP No. 94R made* ***after*** *the exposure on January 31, 2024, have been shown as tracked changes highlighted in grey. This document represents the final adopted version of SSAP No. 94R.*

Statements of Statutory Accounting Principles No. 94 - Revised

~~Transferable and Non-Transferable~~ State and Federal Tax Credits

STATUS

Type of Issue	Common Area
Issued	June 12, 2006; Substantively revised December 7, 2011~~,~~ Conceptually revised ~~-~~ March 16, 2024.
Effective Date	December 31, 2006; Substantive revisions detailed in Issue Paper No. 145 effective December 31, 2011; Conceptual revisions detailed in Issue Paper No. XXX effective XXX.
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS **1**
SCOPE OF STATEMENT **2**
SUMMARY CONCLUSION **2**
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SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for ~~transferable and non-transferable~~ state and federal tax credits that are purchased[1] by the reporting entity ~~without being an investor in the entity from which the tax credit were earned/purchased~~. Tax credits allocated from investments NOT within the scope of *SSAP 93R—Investments in Tax Credit Structures* should refer to this statement for tax credit accounting guidance. ~~Additionally, Tax credits that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).~~Tax credits which have been awarded[2] to the reporting entity are not within the scope of this statement and should refer to *SSAP No. 101—Income Taxes*.

2. Tax credits allocated from, and ~~I~~investments in, ~~Low-Income Housing Tt~~tax ~~Credits credits~~ credit structures,~~s~~ as discussed in SSAP No. 93R ~~SSAP No. 93R—*Low-Income Housing Tax Credit Property Investments*~~*Investments in Tax Credit Structures*~~,~~ which involve investments in projects or programs that generate general business federal tax credits or state tax credits, are not within the scope of this statement. ~~However, the tax credits received from tax credit investments are within the scope of this statement.~~

3. Investments in a CAPCO (Certified Capital Company), organized as a partnership or an LLC, which is a company, authorized by state statute that borrows from investors ~~(insurance companies)~~, in order to make venture capital investments in "qualified" businesses, are not within the scope of this statement. Although associated with tax credits, the insurance company is paid principal and interest on its investment with the CAPCO. Depending upon the terms of the CAPCO offering, principal and interest payments to the ~~insurance company~~investors will come from the CAPCO and/or the state. The CAPCO will make cash payments directly to the ~~insurance company~~investors while the state will make payments in the form of premium or income tax credits. Investments in a CAPCO shall be accounted for in accordance with *Interpretation (INT) 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)* and specific statutory accounting guidance addressing CAPCOs.

SUMMARY CONCLUSION

4. Both state and federal governments have enacted laws that create programs by which tax credits are granted to entities under certain specified conditions. The terms of these tax credits vary based on the issuing jurisdiction and from program to program.~~The criteria in paragraphs 5 and 6 are for transferable state tax credits (i.e., credits which may be sold or assigned). The criteria in paragraphs 7 and 8 are for non-transferable state tax credits (i.e., those which cannot be sold or assigned to other parties).~~

~~5. Some states have enacted laws that create programs by which transferable state tax credits are granted to entities under certain specified conditions (e.g., an entity makes an investment in a particular industry). The terms of these state tax credits vary from state to state and, within a state, from program to program. However, many of these transferable state tax credit programs share the following four characteristics:~~

~~a. The tax credit is nonrefundable;~~

[1] The process to purchase a tax credit typically involves the acquisition of a tax credit certificate (certificated tax credits) or the execution of a state or federal transfer form (transferable tax credits). Tax credits which have been received through other means are indicative of tax credits allocated from an investment (For example, if the tax credits are received through a schedule K-1) and may be within scope of SSAP No. 93.

[2] For the purposes of this statement, awarded tax credits are tax credits issued to the reporting entity which were neither purchased nor allocated from an investment structure. A common example of an awarded tax credit are Job Creation tax credits which are a type of performance-based tax credit program.

~~b. The holder of the transferable state tax credit may sell or otherwise transfer the transferable state tax credit to another entity, which can likewise resell or transfer the credit;~~

~~c. The transferable state tax credit will expire if not used by a predetermined date; and~~

~~d. The transferable state tax credit can be applied against either state income tax or state premium tax.~~

~~6. For purposes of this statement, such programs will be referred to as "transferable state tax credits." The criteria in paragraphs 5.b., 5.c. and 5.d. must be present in order for the transferable state tax credit to receive the accounting treatment described in this statement. When a reporting entity purchases a transferable state tax credit from another entity, the transaction does not result in a continuing investment in a business entity (i.e. limited partnership).~~

~~**Non-Transferable State Tax Credits**~~

~~7. If the original or subsequent holder of the transferable tax credit is not able to transfer the tax credit, then the admissibility criteria in paragraph 8 for non-transferable tax credits apply. These non-transferable state tax credits share the following characteristics:~~

~~a. The tax credit is nonrefundable;~~

~~b. The successive holder of a state tax credit must redeem the credit by April 15 of the subsequent year to the entity's acquisition of the state tax credit and is not permitted to carry over, carry back, obtain a refund, sell or assign the credit;~~

~~c. The non-transferable state tax credit will expire if not used by the predetermined date; and~~

~~d. The non-transferable state tax credit can be applied against either state income tax or state premium tax.~~

5. ~~The criteria in paragraphs 7.b., 7.c. and 7.d. must be present in order for the non-transferable state tax credit to receive the accounting treatment described in this statement.~~For the purposes of this statement, "tax credits" must be issued by either a federal or state governmental entity and must be refundable[3] or can be applied against income tax or premium tax in accordance with permitted IRS or state tax provisions. Tax credits which may be sold or otherwise transferred to another entity are referred to as "transferable tax credits" whereas all other tax credits are referred to as "non-transferable."

6. When a reporting entity purchases a transferable or certificated tax credit from another entity, the transaction does not result in a continuing investment in a business entity (i.e., limited partnership)~~.~~. Direct payment elections are non-revocable and supersede the transferability of tax credits, as such, once the election has been made the tax credit would be considered a non-transferable tax credit.

~~**Transferable and non-transferable state tax credits as defined within this SSAP held by reporting entities meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and**~~

[3] Direct payment tax credits are synonymous with refundable tax credits, as such the terms are used interchangeably within this statement.

~~are admissible assets to the extent that they comply with the requirements of this statement. If the criteria in paragraphs 6 or 8 are not met, the tax credits are nonadmitted.~~

~~Acquisition~~Accounting

7. All tax credits within the scope of the statement must be recognized in the period they are allocated to or purchased by the reporting entity for tax purposes and must be recorded at face value upon receipt. ~~Transferable and non-transferable state tax credits are recorded at cost at the date of acquisition.~~Tax credits acquired at a premium or discount to their face value must record the gain/loss as follows:

a. Tax credits acquired at a discount must defer the gain as a miscellaneous liability upon receipt of the tax credit.

b. Tax credits acquired at a premium must realize the loss within the income statement upon receipt of the tax credit.

8. Deferred g~~G~~ains on ~~transferable and nontransferable~~ tax credits are deferred until the value of the ~~state~~ tax credits utilized exceeds the initial acquisition cost of the tax credits, or until the ~~state~~ tax credits are transferred to other entities or the direct payment election is utilized and the payment(s) or refund ~~is greater than~~exceed the initial ~~carrying~~ acquisition ~~value~~cost.

~~Balance Sheet Treatment~~

9. Tax credits shall be recognized in the period that they are purchased or allocated to the reporting entity for tax purposes:

a. Federal tax credits that can be utilized in the year allocated or purchased shall be reported in the income statement as an offset to federal taxes in accordance with *SSAP No. 101—Income Taxes*. Federal tax credits that cannot be utilized in the year allocated or purchased and are carried forward to a future tax year shall be reported ~~net of~~as a deferred tax asset (DTA) in accordance with SSAP No. 101.

b. State tax credits that can be utilized in the year allocated or purchased shall be reported in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized. State tax credits that cannot be utilized in the year allocated or purchased and are carried forward to a future tax year shall be reported gross of any related state tax liabilities and reported in the category of other-than-invested-assets (not to be reported net).

10. Use of carried forward tax credits in a future period shall be reflected as an offset to the corresponding income or premium~~s~~ tax in the tax reporting year in which the tax credit is utilized.

~~8. Transferable and non-transferable state tax credits shall be established gross of any related state tax liabilities and reported in the category of other-than-invested assets (not reported net).~~

~~9. As transferable and non-transferable state tax credits are redeemed, the carrying value of the tax credits is reduced dollar for dollar by the amount of state tax credits applied toward the reporting entity's applicable state tax liability.~~

~~Income Statement Treatment~~

~~10. Gains on transferable and non-transferable state tax credits are deferred until the value of the state tax credits utilized exceeds the cost of the state tax credits or until the state tax credits are sold to other entities and the payment received is greater than the book value.~~

~~11. Losses on transferable and non-transferable state tax credits are recognized when known.~~

11. Gains and losses on ~~transferable and non-transferable state~~ tax credits are reflected in other income when realized.

12. A tax credit asset is considered purchased or allocated once the tax credit is received and available for use. If the reporting entity determines a commitment to purchase tax credits has met the definition of a liability, then the asset would be reported in other-than-invested assets as tax credits receivable.

Admittance

13. ~~Transferable and non-transferable t~~Tax credits as defined within this SSAP held by reporting entities meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement. The admissibility of tax credits ~~are~~is subject to SSAP No. 101.

Impairment

~~12.~~14. An impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to recover the book/-adjusted carrying value ~~amount~~ of the ~~transferable or non-transferable state~~ tax credits. T~~State t~~ax credits should be evaluated for impairment at each reporting date.

~~13.~~15. When there is a decline in the realizability of a ~~transferable or non-transferable state~~ tax credit owned by the reporting entity that is other- -than- -temporary(INT 06-07), the asset shall be written down to the expected realizable amount and the amount of the write down shall be accounted for as a realized loss. The expected realizable value is the new cost basis.

~~14.~~16. The new cost basis shall not be changed for subsequent recoveries in realizability.

Disclosures

~~15.~~17. The following disclosures shall be made in the financial statements for the reporting period(s) presented. For purposes of this disclosure, total unused ~~transferable and non-transferable state~~ tax credits represent the entire amount of ~~transferable and non-transferable state~~ tax credits available:

a. Carrying value of ~~transferable and non-transferable state~~ tax credits, disaggregated by transferable/certificated and non-transferable, gross of any related ~~state~~ tax liabilities by ~~state~~ jurisdiction and in total.~~,~~

b. Total unused ~~transferable and non-transferable state~~ tax credits by ~~state~~jurisdiction, disaggregated by transferable/certificated and non-transferable.~~;~~

c. Method of estimating utilization of remaining ~~transferable and non-transferable state~~ tax credits or other projected recovery of the current carrying value.

d. Impairment amount recognized in the reporting period(s), if any.

e. Identify ~~state~~ tax credits by transferable/certificated and non-transferable classifications~~,~~ and identify the admitted and ~~N~~nonadmitted portions of each classification.

~~16.~~18. Any commitment or contingent commitment to purchase tax credits shall be disclosed.

Effective Date and Transition

19. This statement is effective for reporting periods ending on or after December 31, 2006. Early adoption is permitted. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3. Substantive revisions to 1) revising the title; 2) incorporating the criteria for non-transferable state tax credits as described in paragraphs 7 and 8; 3) adding a disclosure; and 4) updating terminology throughout the document as appropriate, are effective for reporting periods ending on or after December 31, 2011.

20. In March 2024, new SAP concept revisions, as detailed in Issue Paper No. XXX, were adopted. These revisions, effective January 1, 2025, with early adoption permitted, expanded the scope of SSAP No. 94R to include all purchased, and certain allocated, state and federal income or premium tax credits and provide new guidance on the accounting, recognition, and reporting for state and federal tax credits within the scope of this statement. As of the effective date, reporting entities shall prospectively modify the recognition, accounting, and reporting of tax credits within the scope of this statement to reflect the guidance in the conceptual revisions. For unutilized tax credits which were carried forward from prior to the effective date:

a. Federal tax credits in other-than-invested assets are to be transferred and reported ~~net of~~as a ~~deferred tax asset (~~DTA~~)~~ in accordance with SSAP No. 101.

~~a.~~b. Tax credits previously recorded at acquisition cost should be adjusted to reflect the face value of the acquired tax credits with the corresponding loss immediately recognized or the gain deferred.

REFERENCES

Relevant Issue Papers

- Issue Paper No. 126—Accounting for Transferable State Tax Credits
- Issue Paper No. 145—Accounting for Transferable and Non-Transferable State Tax Credits
- Issue Paper No. XXX—XXX

EXHIBIT A – ACCOUNTING FOR TRANSFERABLE ~~STATE~~ TAX CREDITS

On 1/1/X1 SAM Insurance Company purchased transferable state tax credits for a cost of $100,000. The transferable state tax credits are redeemable for $160,000 and expire at the end of 12/31/X4. SAM initially expects to utilize the tax credits before expiration in their state of domicile in the amount of $40,000 per year. In year X4, SAM sells the remaining $30,000 in transferable state tax credits for $20,000.

1/1/x1	Transferable state tax credits	~~100~~160,000	
	Deferred gains on acquired tax credits		60,000
	Cash		100,000
	To record the purchase of the tax credits		
6/30/x1	Premium tax expense	40,000	
	Premium taxes payable to domiciliary state		40,000
	To record premium tax expense and accrue the liability in Year 1.		
10/1/x1	Premium tax payable	40,000	
	Transferable state tax credits		40,000
	To record the use of tax credits in Year 1. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x2	Premium tax expense	60,000	
	Premium taxes payable to domiciliary state		60,000
	To record premium tax expense and accrue the liability in Year 2.		
9/30/x2	Premium tax payable	60,000	
	Transferable state tax credits		60,000
	To record the use of taxes credits in Year 2. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x3	Premium tax expense	30,000	
	Premium taxes payable to domiciliary state		30,000
	To record premium tax expense and accrue the liability in Year 3.		
9/30/x3	Premium tax payable	30,000	
	Transferable state tax credits~~Other income~~		30,000
	Deferred gains on acquired tax credits	30,000	
	Other income		30,000
	To record the use of premium tax credits in excess of cost and recognize a gain on premium tax credits in other income. The Company intends to sell the remaining tax credits in year 4.		
6/30/x4	Cash	20,000	
	Other income	10,000	
	Transferable state tax credits		30,000
	Deferred gains on acquired tax credits	30,000	
	Other income		~~20~~30,000
	To record the sale of the remaining tax credits.		

EXHIBIT B – ACCOUNTING FOR NON-TRANSFERABLE ~~STATE~~ TAX CREDITS

On 7/1/X1 LJW Insurance Company purchased non-transferable ~~state~~ federal tax credits for a cost of $100,000. The ~~state~~ federal tax credits are redeemable for $110,000~~, are not transferable~~ and expire on, April 15, 20x2. LJW expects to utilize the tax credits before expiration ~~in their state of domicile~~ in the amount of $110,000. Tax credits are utilized pro-rata, approximately $36,666 every quarter, from acquisition date to expiration date. The illustration below assumes that LJW Insurance Company's quarterly income tax liability equals the amount of credits that were purchased.

7/1/x1	~~State~~ Federal tax credits	1~~1~~0,000	
	Deferred gains on acquired tax credits		10,000
	Cash		100,000
	To record the purchase of the tax credits		
9/30/x1	~~Premium~~ Income tax expense	~~200,000~~36,666	
	Income ~~Premium~~ taxes payable ~~to domiciliary state~~		~~200,000~~36,666
	To record quarterly ~~premium tax expense and accrue the~~income tax liability.		
10/1/x1	Income taxes payable	36,666	
	Federal tax credits		36,666
	To record the use of tax credits in the quarter.		
12/31/x1	Income tax expense	36,666	
	Income taxes payable		36,666
	To record quarterly income tax liability.		
1/1/x2	Income taxes payable	36,666	
	Federal tax credits		36,666
	To record the use of tax credits in the quarter.		
3/31/x2	Income tax expense	36,668	
	Income taxes payable		36,668
	To record quarterly income tax liability.		
~~3/15/x2~~	~~Premium tax payable~~	~~110,000~~	
4/1/x2	Income taxes payable	36,668	
	Deferred gains on acquired tax credits	10,000	
	Other Income		10,000
	Federal tax credits		36,668
	~~Other Income~~		~~10,000~~
	~~Federal tax credits~~		~~100~~110,000
	To record the use of ~~premium~~ tax credits in the quarter. ~~in excess of cost and recognize a gain on premium tax credits in other income. (The additional $90,000 of premium taxes payable would still be due.)~~		

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Other SSAPs

Spring National Meeting Adoption: *This document represents the final adopted version of the revisions to SSAP No. 34 and SSAP No. 48R. The changes shown to SSAP No. 48R have **not** been amended to reflect the proposed formatting changes proposed in agenda item #2024-08: Consistency Revisions for Residuals.*

Proposed revisions to ***SSAP No. 34—Investment Income Due and Accrued***

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investment income due and accrued. This statement does not address the accounting for tax credits allocated or purchased, which are discussed in SSAP No. 93R—*Investments in Tax Credit Structures* and *SSAP No. 94R—State and Federal Tax Credits*.

Proposed revisions to ***SSAP No. 48R—Joint Ventures, Partnerships and Limited Liability Companies***

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investments in any joint ventures, partnerships, and limited liability companies, including investments in certified capital companies (CAPCO) per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)*, whether or not it is considered to be controlled by or affiliated with the reporting entity. Single real estate property investments that are wholly-owned by an LLC that is directly and wholly-owned by the reporting entity, and that meet the criteria established in *SSAP No. 40R—Real Estate Investments*, are excluded from this statement. This statement does not address the accounting for investments in joint ventures, partnerships, and ~~and~~ limited liability companies that invest in tax credit programs ~~that~~ and are in the scope of~~hold an equity interest in either a tax syndication structure or tax equity fund invest in Low-Income Housing Tax Credit Properties as discussed in~~ *SSAP No. 93R~~—Low-Income Housing Tax Credit Property Investments~~*Investments in Tax Credit Structures*.

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: *ASU 2023-03—Amendments to SEC Paragraphs*

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
In July of 2023 FASB issued *ASU 2023-03, Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 120, SEC Staff Announcement at the March 24, 2022, EITF Meeting, and Staff Accounting Bulletin Topic 6.B, Accounting Series Release 280—General Revision of Regulation S-X: Income or Loss Applicable to Common Stock*, which amends SEC paragraphs from the Accounting Standards Codification based on the issuance of SEC Staff Accounting Bulletin (SAB) 120, the March 24, 2022 EITF meeting SEC staff announcement, and SAB Topic 6.B "Accounting Series Release No. 280 — General Revision of Regulation S-X: Income or Loss Applicable to Common Stock. This ASU updates various aspects of SEC guidance on stock compensation and equity-based payments.

Existing Authoritative Literature:
Historically, SEC guidance from ASUs have been rejected as not applicable for statutory accounting in Appendix D. Regardless, all ASUs are reviewed for statutory accounting purposes to determine if the guidance should be considered for statutory accounting.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2023-03, Amendments to SEC Paragraphs* as not applicable to statutory accounting. This item is proposed to be rejected as not applicable as the ASU is specific to amendment of SEC paragraphs, which are not applicable for statutory accounting purposes.

Staff Review Completed by: William Oden – October 2023

Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification and exposed revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2023-03—Amendments to SEC Paragraphs* as not applicable for statutory accounting.

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On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, the exposed revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2023-03, Amendments to SEC Paragraphs* as not applicable to statutory accounting.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/03-16-24 Spring National Meeting/Adoptions/23-25 - ASU 2023-03 - SEC Updates.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: *ASU 2023-04—Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 121*

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
In August of 2023 FASB issued *ASU 2023-04, Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 121*, which amends SEC paragraphs from the Accounting Standards Codification for the issuance of SEC Staff Accounting Bulletin (SAB) 121 which provides guidance on accounting for obligations to safeguard Crypto-Assets an entity holds for its platform users.

Existing Authoritative Literature:
Historically, SEC guidance from ASUs have been rejected as not applicable for statutory accounting in Appendix D. Regardless, all ASUs are reviewed for statutory accounting purposes to determine if the guidance should be considered for statutory accounting.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
In May 2021, the Working Group issued INT 21-01: Accounting for Cryptocurrencies, which provided guidance for the statutory accounting treatment of cryptocurrencies. INT 21-01 establishes that directly held cryptocurrencies have not been identified in the Accounting Practices and Procedures Manual (AP&P Manual) as an admitted asset, and do not meet the definition of any admitted asset that is defined in the AP&P Manual. Accordingly, by default they are a nonadmitted asset per *SSAP No. 4—Assets and Nonadmitted Assets*, paragraph 3, as they are not specifically identified in the Accounting Practices and Procedures Manual as an admitted asset.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2023-04, Amendments to SEC Paragraphs* as not applicable to statutory accounting. This item is proposed to be rejected as not applicable as the ASU is specific to amendment of SEC paragraphs, which are generally not applicable for statutory accounting purposes.

Staff Review Completed by: Jake Stultz – October 2023

Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification and exposed revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2023-04—Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 121* as not applicable for statutory accounting.

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On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, the exposed revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2023-04, Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 121* as not applicable to statutory accounting.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/03-16-24 Spring National Meeting/Adoptions/23-27 - ASU 2023-04 - SEC Updates - Crypto.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: IMR / AVR Preferred Stock

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☐	☒	☐
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to update guidance for the Interest Maintenance Reserve (IMR) and the Asset Valuation Reserve (AVR) in the Annual Statement (A/S) Instructions for perpetual preferred stock, which includes SVO-Identified Preferred Stock ETFs. The existing IMR/AVR guidance is based on measurement of preferred stock based on NAIC designation. However, statutory accounting revisions effective in 2021 revised the measurement method for perpetual preferred stock to always reflect fair value, not to exceed any currently effective call price, regardless of NAIC designation. Furthermore, with dedicated reporting lines established to separate redeemable and perpetual preferred stock, the reporting of NAIC designations was revised and no longer references an "RP" or "P." These revisions were incorporated as perpetual preferred stock is more akin to an equity instrument, as it is not required to be redeemed by the issuing entity or at the option of the investor. At the time of this measurement method change, corresponding revisions to the IMR/AVR instructions were not reflected. As such, the existing IMR/AVR guidance directs realized gains/loss treatment for all preferred stock based on the NAIC designation during the holding period and refers to the prior designation classifications.

This agenda item proposes to clarify that realized gains and losses on perpetual preferred stock shall not be added to the IMR, regardless of NAIC designation, and shall follow the same concepts that exist for common stock in reporting realized gains/losses to the AVR. This agenda item does not propose to change the concepts for redeemable preferred stock, which is more akin to a debt instrument, but proposes to clarify the guidance so application based on the type of structure is clear. Separate reporting of perpetual preferred stock and redeemable preferred stock is already included on Schedule D-2-1: Preferred Stock.

For the revisions proposed in this agenda item, the guidance for redeemable preferred stock will not be revised and will continue to classify realized gains/losses between the IMR and AVR based on NAIC designation. This guidance indicates that if the designation was a 4-6 at any time during the holding period, the realized gain or loss would go to AVR as non-interest related gains or losses. This agenda item does not intend to confirm that the allocation approach for redeemable preferred stock is appropriate and is strictly focused on ensuring that the current annual statement instructions for IMR/AVR corresponds with the current accounting and reporting guidance for perpetual preferred stocks. As detailed in the recommendation, discussion on whether use of NAIC designation for redeemable preferred stock is appropriate is proposed to occur as part of the long-term IMR project.

Existing Authoritative Literature:

- **SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve**

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for an asset valuation reserve (AVR) and an interest maintenance reserve (IMR) for life and accident and health insurance companies, excluding separate accounts. Separate account AVR/IMR reporting is addressed in *SSAP No. 56—Separate Accounts.*

SUMMARY CONCLUSION

2. Life and accident and health insurance companies shall recognize liabilities for an AVR and an IMR. The AVR is intended to establish a reserve to offset potential credit-related investment losses on all

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invested asset categories excluding cash, policy loans, premium notes, collateral notes and income receivable. The IMR defers recognition of the realized capital gains and losses resulting from changes in the general level of interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the investments sold. The IMR also applies to certain liability gains/losses related to changes in interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the liability released.

3. The IMR and AVR shall be calculated and reported as determined per guidance in the SSAP for the specific type of investment (e.g., SSAP No. 43R for loan-backed and structured securities), or if not specifically stated in the respective SSAP, in accordance with the NAIC *Annual Statement Instructions* for Life and Accident and Health Insurance Companies.

Effective Date and Transition

4. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

- **A/S Instructions – Life, Accident and Health / Fraternal Companies**

(This reflects 2023 guidance. Agenda item 2023-15 proposes revisions to address specific allocations to the IMR that may not reflect interest-related losses.)

Interest Maintenance Reserve (IMR)

Line 2 – Current Year's Realized Pre-tax Capital Gains (Losses) of $_____ Transferred into the Reserve Net of Taxes of $_____

Include interest-rate-related realized capital gains (losses), net of capital gains tax thereon. All realized capital gains (losses) transferred to the IMR are net of capital gains taxes thereon. Exclude non-interest-related (default) realized capital gains and (losses), realized capital gains (losses) on equity investments, and unrealized capital gains (losses).

All realized capital gains (losses), due to interest rate changes on fixed income investments, net of related capital gains tax, should be captured in the IMR and amortized into income (Column 2, Lines 1 through 31) according to Table 1 or the seriatim method. Realized capital gains (losses) must be classified as either interest (IMR) or non-interest (AVR) related, not a combination except as specified in *SSAP No. 43R—Loan-Backed and Structured Securities*. Purchase lots with the same CUSIP are treated as individual assets for IMR and Asset Valuation Reserve (AVR) purposes.

Exclude those capital gains and (losses) that, in accordance with contract terms have been used to directly increase or (decrease) contract benefit payments or reserves during the reporting period. The purpose of this exclusion is to avoid the duplicate utilization of such gains and (losses).

Capital gains tax should be determined using the method developed by the company to allocate taxes used for statutory financial reporting purposes. By capturing the realized capital gains (losses) net of tax, the capital gains tax associated with those capital gains (losses) due to an interest rate change is charged or credited to the IMR and amortized in proportion to the before-tax amortization.

Include realized capital gains (losses) on:

Debt securities (excluding loan-backed and structured securities) and preferred stocks whose National Association of Insurance Commissioners (NAIC)/Securities Valuation Office (SVO) designation at the end of the holding period is **NOT** different from its NAIC designation at the beginning of the holding period by more than one NAIC designation. Exclude any such gains (losses) exempt from the IMR.

Exchange Traded Funds (ETFs) as listed on the SVO Identified Bond ETF List (thereafter subject to bond IMR guidelines) and the SVO Identified Preferred Stock ETF List (thereafter subject to preferred stock IMR guidelines). Include any capital gains (losses) realized by the Company, whether from sale of the ETF or capital gains distributions by the ETF. If the ETF is removed from either SVO ETF list, the ETF is reported and treated as common stock, with any capital gains/(losses) excluded from the IMR.

SVO Identified Funds designated for systematic value

Called bonds, tendered bonds, and sinking fund payments.

Mortgage loans where:

- Interest is **NOT** more than 90 days past due, or
- The loan is **NOT** in process of foreclosure, or
- The loan is **NOT** in course of voluntary conveyance, or
- The terms of the loan have **NOT** been restructured during the prior two years.

Additional Provisions for Including/Excluding Gains (Losses) from IMR:

Mortgage loan prepayment penalties are not included in IMR. Treat them as regular investment income.

Interest-related gains (losses) realized on directly held capital and surplus notes reported on Schedule BA should be transferred to the IMR in the same manner as similar gains and (losses) on fixed income assets held on Schedule D. A capital gain (loss) on such a note is classified as an interest rate gain if the note is eligible for amortized-value accounting at both the time of acquisition and the time of disposition.

Determination of IMR gain (loss) on multiple lots of the same securities should follow the underlying accounting treatment in determining the gain (loss). Thus, the designation, on a purchase lot basis, should be compared to the designation at the end of the holding period to determine IMR or AVR gain or (loss).

Realized capital gains (losses) on any debt security (excluding loan-backed and structured securities) that has had an NAIC/SVO designation of 6 at any time during the holding period should be excluded from the IMR and included as a non-interest-related gain (loss) in the AVR.

Realized capital gains (losses) on any preferred stock that had an NAIC/SVO designation of RP4, RP5 or RP6 or P4, P5 or P6 at any time during the holding period should be reported as non-interest-related gains (losses) in the AVR.

The holding period for debt securities (excluding loan-backed and structured securities) and preferred stocks is defined as the period from the date of purchase to the date of sale. For the end of period classification, the most recent available designation should be used. For bonds acquired before Jan. 1, 1991, the holding period is presumed to have begun on Dec. 31, 1990. For preferred stocks acquired before Jan. 1, 1993, the holding period is presumed to have begun on Dec. 31, 1992. For SVO Identified ETFs, the holding period is defined as one calendar year to expected maturity. For SVO Identified Funds designated for systematic value, the holding period is the weighted-average life of the underlying bonds.

In accordance with *SSAP No. 26R—Bonds*, securities with other-than-temporary impairment losses shall be recorded entirely to either AVR or IMR and not bifurcated between interest and non-interest components.

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Asset Valuation Reserve (AVR)

Line 2 – Realized Capital Gains (Losses) Net of Taxes – General Account

Report all realized non-interest-related (default) and equity capital gains (losses), net of capital gains tax, applicable to the assets in each component and sub-component. All realized capital gains (losses) transferred to the AVR are net of capital gains taxes thereon. Exclude all interest rate-related capital gains (losses) from the AVR.

Capital gains tax should be determined using the method developed by the company to allocate taxes used for statutory financial reporting purposes.

Report all realized capital gains (losses), net of capital gains tax, on each debt security (excluding loan-backed and structured securities) whose NAIC/SVO designation at the end of the holding period is different from its NAIC/SVO designation at the beginning of the holding period by more than one NAIC/SVO designation. The holding period is defined as the period from the date of purchase to the date of sale. For end of period classification, the most recent available designation should be used. For bonds acquired before Jan. 1, 1991, the holding period is presumed to have begun on Dec. 31, 1990.

Determination of AVR gain (loss) on multiple lots of the same fixed income securities should follow the underlying accounting treatment in determining gain (loss). Thus, the designation, on a purchase lot basis, should be compared to the designation at the end of the holding period to determine IMR or AVR gain or (loss).

In accordance with *SSAP No. 26R—Bonds*, securities with other-than-temporary impairment losses shall be recorded entirely to either AVR or IMR and not bifurcated between interest and non-interest components.

In accordance with *SSAP No. 43R—Loan-Backed and Structured Securities*, for loan-backed and structured securities only:

- Other-Than-Temporary Impairment – Non-interest-related other-than-temporary impairment losses shall be recorded through the AVR. If the reporting entity wrote the security down to fair value due to the intent to sell or does not have the intent and ability to retain the investment for a period of time sufficient to recover the amortized cost basis, the non-interest-related portion of the other-than-temporary impairment losses shall be recorded through the AVR; the interest related other-than-temporary impairment losses shall be recorded through the IMR. The analysis for bifurcating impairment losses between AVR and IMR shall be completed as of the date when the other-than-temporary impairment is determined.

- Security Sold at a Loss Without Prior OTTI – An entity shall bifurcate the loss into AVR and IMR portions depending on interest- and non-interest-related declines in accordance with the analysis performed as of the date of sale. As such, an entity shall report the loss in separate AVR and IMR components as appropriate.

- Security Sold at a Loss with Prior OTTI – An entity shall bifurcate the current realized loss into AVR and IMR portions depending on interest- and non-interest-related declines in accordance with the analysis performed as of the date of sale. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

- Security Sold at a Gain with Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale. The bifurcation between AVR and IMR that

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occurs as of the date of sale may be different from the AVR and IMR allocation that occurred at the time of previous other-than-temporary impairments. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

- Security Sold at a Gain Without Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale.

In addition, all gains (losses), net of capital gains tax, on mortgage loans where:

- Interest is more than 90 days past due, or
- The loan is in the process of foreclosure, or
- The loan is in course of voluntary conveyance, or
- The terms of the loan have been restructured during the prior two years

Would be classified as non-interest-related gains (losses).

The gain (loss), net of capital gains tax, on any debt security (excluding loan-backed and structured securities) that has had an NAIC/SVO designation of "6" at any time during the holding period should be reported as a credit related gain (loss).

All capital gains (losses), net of capital gains tax, from preferred stock that had an NAIC/SVO designation of RP4, RP5 or RP6 or P4, P5 or P6 at any time during the holding period should be reported as on-interest-related gains (losses) in the AVR.

However, for a convertible bond or preferred stock purchased while its conversion value exceeds its par value, any gain (loss) realized from its sale before conversion must be included in the Equity Component of the AVR. Conversion Value is defined to mean the number of shares available currently or at next conversion date multiplied by the stock's current market price.

Report all realized equity capital gains (losses), net of capital gains tax, in the appropriate sub-components.

The following guidance pertains to instruments in Scope of *SSAP No. 86—Derivatives*:

- For derivative instruments used in hedging transactions, the determination of whether the capital gains (losses) are allocable to the IMR or the AVR is based on how the underlying asset is treated. Realized gains (losses), net of capital gains tax, on portfolio or general hedging instruments should be included with the hedged asset. Gains (losses), net of capital gains tax, on hedges used, as specific hedges should be included only if the specific hedged asset is sold or disposed of.

- For income generation derivative transactions, the determination of whether the capital gains (losses) are allocable to the IMR or the AVR is based on how the underlying interest (for a put) or covering asset (for a call, cap or floor) is treated. Realized gains (losses), net of capital gains tax should be included in the same sub-component where the realized gains (losses) of the underlying interest (for a put) or covering asset (for a call, cap or floor) is reported. Refer to *SSAP No. 86—Derivatives* for accounting guidance.

Realized gains (losses), net of capital gains tax, resulting from the sale of U.S. government securities and the direct or guaranteed securities of agencies which are backed by the full faith and credit of the U.S. government are exempt from the AVR. This category is described in the Investment Schedules General Instructions.

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Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

- Agenda item 2019-04: SSAP No. 32 – Investment Classification Project, resulted with revisions to update the preferred stock accounting and reporting guidance. These revisions resulted with all perpetual preferred stock being reported at fair value, not to exceed any currently effective call price, with unrealized gains and losses accounted for in accordance *with SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve.*

- Agenda Item 2023-14: *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve* establishes a broad project to capture accounting guidance for AVR and IMR in SSAP No. 7.

- Agenda Item 2023-15: IMR/AVR Specific Allocations considers revisions to the A/S instructions to address guidance that prescribes specific allocation to the IMR. These revisions were exposed in August 2023.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Recommendation:
NAIC staff recommend that the Working Group include this item on their maintenance agenda as a SAP clarification and expose this agenda item with proposed revisions to the A/S instructions to remove the guidance that directs all preferred stock to be allocated between IMR/AVR based on NAIC designation. This agenda item proposes new guidance that corresponds to the accounting and reporting differences for redeemable and perpetual preferred stock, with all perpetual preferred stock being treated as an equity instrument similar to common stock. With this approach, all unrealized gains or losses on perpetual preferred stock will reverse to realized gains or losses in the AVR formula. The revisions also clarify that SVO-Identified Preferred Stock ETFs shall be treated as perpetual preferred stock (equities) as that is consistent with the guidance in *SSAP No. 32R—Preferred Stock*.

(Note: This item is proposed as a SAP Clarification as the revisions to SSAP No. 32R to revise the measurement method for perpetual preferred stock was a new SAP Concept. The revisions proposed in this agenda item simply update the IMR/AVR A/S instructions to correspond to those adopted changes.)

As discussed in the introduction, this agenda item does not propose to alter the current process of using NAIC designations for redeemable preferred stock in determining whether realized gains or losses should be allocated to IMR or AVR. However, it should not be perceived that this agenda item confirms retention of this existing approach. Discussion on the approach to allocate gains/losses incurred from redeemable preferred stock is recommended for review as part of the long-term project on IMR/AVR. Any comments received on this dynamic will be addressed as part of that project. As detailed in the A/S instructions, for preferred stock, the determination for AVR is based on whether the preferred stock was an NAIC 4-6 at any time during the holding period and not based on a change in NAIC designation.

Staff Note: Shaded guidance reflects sections that have proposed revisions that were exposed in agenda item 2023-15: IMR/AVR Specific Allocations. These changes are accepted only for ease of readability and to prevent confusion on the proposed revisions related to this agenda item. Whether the revisions from agenda item 2023-15 are adopted will depend on the discussion and action by the Working Group. With the exception of the added 'redeemable' in the first shaded paragraph, all of the edits proposed in this agenda item are in separate paragraphs from agenda item 2023-15.

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Interest Maintenance Reserve (IMR)

Line 2 – Current Year's Realized Pre-tax Capital Gains (Losses) of $_____ Transferred into the Reserve Net of Taxes of $_____

Include interest-rate-related realized capital gains (losses), net of capital gains tax thereon. All realized capital gains (losses) transferred to the IMR are net of capital gains taxes thereon. Exclude non-interest-related (default) realized capital gains and (losses), realized capital gains (losses) on equity investments, and unrealized capital gains (losses).

All realized capital gains (losses), due to interest rate changes on fixed income investments, net of related capital gains tax, should be captured in the IMR and amortized into income (Column 2, Lines 1 through 31) according to Table 1 or the seriatim method. Realized capital gains (losses) must be classified as either interest (IMR) or non-interest (AVR) related, not a combination except as specified in *SSAP No. 43R—Loan-Backed and Structured Securities*. Purchase lots with the same CUSIP are treated as individual assets for IMR and Asset Valuation Reserve (AVR) purposes.

Exclude those capital gains and (losses) that, in accordance with contract terms have been used to directly increase or (decrease) contract benefit payments or reserves during the reporting period. The purpose of this exclusion is to avoid the duplicate utilization of such gains and (losses).

Capital gains tax should be determined using the method developed by the company to allocate taxes used for statutory financial reporting purposes. By capturing the realized capital gains (losses) net of tax, the capital gains tax associated with those capital gains (losses) due to an interest rate change is charged or credited to the IMR and amortized in proportion to the before-tax amortization.

Include realized capital gains (losses) on:

Debt securities (excluding loan-backed and structured securities) and redeemable preferred stocks where the realized capital gains (losses) more predominantly reflect interest-related changes. By default, debt instruments whose National Association of Insurance Commissioners (NAIC)/Securities Valuation Office (SVO) designation at the end of the holding period, or within a reasonable amount of time after the reporting entity has sold/disposed of the instrument, are different from its NAIC designation at the beginning of the holding period by more than one NAIC designation or NAIC designation category shall not be considered to reflect interest-related changes. Gains (losses) from those debt instruments shall NOT be reported in the IMR and shall be reported in the AVR

Exchange Traded Funds (ETFs) as listed on the SVO Identified Bond ETF List (thereafter subject to bond IMR guidelines) ~~and the SVO Identified Preferred Stock ETF List (thereafter subject to preferred stock IMR guidelines)~~. ~~I~~include any capital gains (losses) realized by the Company, whether from sale of the ETF or capital gains distributions by the ETF. If the ETF is removed from either SVO ETF list, the ETF is reported and treated as common stock, with any capital gains/(losses) excluded from the IMR. (Investments on the SVO-Identified Preferred Stock List are captured as perpetual preferred stock and treated as equity investments, with gains and losses excluded from IMR.)

SVO Identified Funds designated for systematic value

Called bonds, tendered bonds, and sinking fund payments.

Mortgage loans where the realized gains (losses) more predominantly reflect interest-related changes. By default, mortgage loans that meet any of the following criteria shall not

be considered to reflect interest-related losses. Realized gains (losses) from mortgage loans with these characteristics shall be reported in the AVR:

- Any mortgage loan sold/disposed with an established valuation allowance under SSAP No. 37, or
- Interest is more than 90 days past due, or
- The loan is in process of foreclosure, or
- The loan is in course of voluntary conveyance, or
- The terms of the loan have been restructured during the prior two years.

Additional Provisions for Including/Excluding Gains (Losses) from IMR:

Mortgage loan prepayment penalties are not included in IMR. Treat them as regular investment income.

Interest-related gains (losses) realized on directly held capital and surplus notes reported on Schedule BA should be transferred to the IMR in the same manner as similar gains and (losses) on fixed income assets held on Schedule D. A capital gain (loss) on such a note is classified as an interest rate gain if the note is eligible for amortized-value accounting at both the time of acquisition and the time of disposition.

Determination of IMR gain (loss) on multiple lots of the same securities should follow the underlying accounting treatment in determining the gain (loss). Thus, the designation, on a purchase lot basis, should be compared to the designation at the end of the holding period to determine IMR or AVR gain or (loss).

Realized capital gains (losses) on any debt security (excluding loan-backed and structured securities) that has had an NAIC/SVO designation of 6 at any time during the holding period should be excluded from the IMR and included as a non-interest-related gain (loss) in the AVR.

Realized capital gains (losses) on ~~any~~ redeemable preferred stock that had an NAIC/SVO designation of 4-6 ~~RP4, RP5 or RP6 or P4, P5 or P6~~ at any time during the holding period should be reported as non-interest-related gains (losses) in the AVR.

The holding period for debt securities (excluding loan-backed and structured securities) and redeemable preferred stocks is defined as the period from the date of purchase to the date of sale. For the end of period classification, the most recent available designation should be used. For bonds acquired before Jan. 1, 1991, the holding period is presumed to have begun on Dec. 31, 1990. For redeemable preferred stocks acquired before Jan. 1, 1993, the holding period is presumed to have begun on Dec. 31, 1992. For SVO Identified Bond ETFs, the holding period is defined as one calendar year to expected maturity. For SVO Identified Bond ETFs ~~Funds~~ designated for systematic value, the holding period is the weighted-average life of the underlying bonds.

In accordance with *SSAP No. 26R—Bonds*, securities with other-than-temporary impairment losses shall be recorded entirely to either AVR or IMR and not bifurcated between interest and non-interest components.

Asset Valuation Reserve (AVR)

Line 2 – Realized Capital Gains (Losses) Net of Taxes – General Account

Report all realized non-interest-related (default) and equity capital gains (losses) (which includes, but is not limited to, common stock, perpetual preferred stock and SVO-Identified Preferred Stock ETFs), net of capital gains tax, applicable to the assets in each component and sub-component. All realized capital gains (losses) transferred to the AVR are net of capital gains taxes thereon. Exclude all interest rate-related capital gains (losses) from the AVR.

Capital gains tax should be determined using the method developed by the company to allocate taxes used for statutory financial reporting purposes.

Report all realized capital gains (losses), net of capital gains tax, on each debt security (excluding loan-backed and structured securities) where the realized capital gains (losses) more predominantly reflect non-interest-related changes. By default, debt instruments whose NAIC/SVO designation at the end of the holding period, or within a reasonable amount of time after the reporting entity has sold/disposed of the instrument, is different from its NAIC/SVO designation at the beginning of the holding period by more than one NAIC designation or NAIC designation category shall be considered to reflect non-interest-related changes. Gains (losses) from those debt instruments shall be reported in the AVR.

Determination of AVR gain (loss) on multiple lots of the same fixed income securities should follow the underlying accounting treatment in determining gain (loss). Thus, the designation, on a purchase lot basis, should be compared to the designation at the end of the holding period to determine IMR or AVR gain or (loss).

In accordance with *SSAP No. 26R—Bonds*, securities with other-than-temporary impairment losses shall be recorded entirely to either AVR or IMR and not bifurcated between interest and non-interest components.

In accordance with *SSAP No. 43R—Loan-Backed and Structured Securities*, for loan-backed and structured securities only:

- Other-Than-Temporary Impairment – Non-interest-related other-than-temporary impairment losses shall be recorded through the AVR. If the reporting entity wrote the security down to fair value due to the intent to sell or does not have the intent and ability to retain the investment for a period of time sufficient to recover the amortized cost basis, the non-interest-related portion of the other-than-temporary impairment losses shall be recorded through the AVR; the interest related other-than-temporary impairment losses shall be recorded through the IMR. The analysis for bifurcating impairment losses between AVR and IMR shall be completed as of the date when the other-than-temporary impairment is determined.

- Security Sold at a Loss Without Prior OTTI – An entity shall bifurcate the loss into AVR and IMR portions depending on interest- and non-interest-related declines in accordance with the analysis performed as of the date of sale. As such, an entity shall report the loss in separate AVR and IMR components as appropriate.

- Security Sold at a Loss with Prior OTTI – An entity shall bifurcate the current realized loss into AVR and IMR portions depending on interest- and non-interest-related declines in accordance with the analysis performed as of the date of sale. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

- Security Sold at a Gain with Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale. The bifurcation between AVR and IMR that occurs as of the date of sale may be different from the AVR and IMR allocation that occurred at the time of previous other-than-temporary impairments. An entity shall not

adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

- Security Sold at a Gain Without Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale.

In addition, all gains (losses), net of capital gains tax, on mortgage loans where the realized gains (losses) more predominantly reflect non-interest-related changes. By default, mortgage loans that meet any of the following criteria shall be considered to reflect non-interest-related changes and realized gains (losses) from mortgage loans with these characteristics shall be reported in the AVR:

- Any mortgage loan sold/disposed with an established valuation allowance under SSAP No. 37, or
- Interest is more than 90 days past due, or
- The loan is in the process of foreclosure, or
- The loan is in course of voluntary conveyance, or
- The terms of the loan have been restructured during the prior two years

The gain (loss), net of capital gains tax, on any debt security (excluding loan-backed and structured securities) that has had an NAIC/SVO designation of "6" at any time during the holding period should be reported as a credit related gain (loss).

All capital gains (losses), net of capital gains tax, from redeemable preferred stock that had an NAIC/SVO designation of 4-6 ~~RP4, RP5 or RP6 or P4, P5 or P6~~ at any time during the holding period should be reported as non-interest-related gains (losses) in the AVR.

However, for a convertible bond or redeemable preferred stock purchased while its conversion value exceeds its par value, any gain (loss) realized from its sale before conversion must be included in the Equity Component of the AVR. Conversion Value is defined to mean the number of shares available currently or at next conversion date multiplied by the stock's current market price.

Report all realized equity capital gains (losses), net of capital gains tax, in the appropriate sub-components.

The following guidance pertains to instruments in Scope of *SSAP No. 86—Derivatives*:

- For derivative instruments used in hedging transactions, the determination of whether the capital gains (losses) are allocable to the IMR or the AVR is based on how the underlying asset is treated. Realized gains (losses), net of capital gains tax, on portfolio or general hedging instruments should be included with the hedged asset. Gains (losses), net of capital gains tax, on hedges used, as specific hedges should be included only if the specific hedged asset is sold or disposed of.

- For income generation derivative transactions, the determination of whether the capital gains (losses) are allocable to the IMR or the AVR is based on how the underlying interest (for a put) or covering asset (for a call, cap or floor) is treated. Realized gains (losses), net of capital gains tax should be included in the same sub-component where the realized gains (losses) of the underlying interest (for a put) or covering asset (for a call, cap or floor) is reported. Refer to *SSAP No. 86—Derivatives* for accounting guidance.

Realized gains (losses), net of capital gains tax, resulting from the sale of U.S. government securities and the direct or guaranteed securities of agencies which are backed by the full faith

and credit of the U.S. government are exempt from the AVR. This category is described in the Investment Schedules General Instructions.

Staff Review Completed by: Julie Gann - NAIC Staff, September 2023

Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification and exposed revisions, as illustrated above, to the annual statement instructions to remove the guidance that directs all preferred stock to be allocated between IMR/AVR based on NAIC designation, and clarify that perpetual preferred stock, which includes SVO-Identified Preferred Stock ETFs shall reported as equities through AVR.

On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, the proposed revisions to the annual statement instructions to remove the guidance that directs all preferred stock to be allocated between IMR/AVR based on NAIC designation, and clarify that perpetual preferred stock, which includes SVO-Identified Preferred Stock ETFs, as well as all mandatorily convertible preferred stock (regardless of redeemable or perpetual) shall reported through the AVR. The adopted revisions are shown below. (Revisions from the exposure pertain to inclusion of guidance for mandatorily convertible preferred stock.) The proposed revisions will be considered by the Blanks (E) Working Group for year-end 2024. This agenda item did not result in SAP revisions.

Adopted Revisions:
Staff Note: Shaded guidance reflects sections with revisions discussed under agenda item 2023-15: IMR/AVR Specific Allocations. Agenda item 2023-15 should be reviewed for the adopted revisions to those sections. With the exception of the added 'redeemable' in the first shaded paragraph, all of the edits in this agenda item are in separate paragraphs from agenda item 2023-15.

Interest Maintenance Reserve (IMR)

Line 2 – Current Year's Realized Pre-tax Capital Gains (Losses) of $_____ Transferred into the Reserve Net of Taxes of $_____

Include interest-rate-related realized capital gains (losses), net of capital gains tax thereon. All realized capital gains (losses) transferred to the IMR are net of capital gains taxes thereon. Exclude non-interest-related (default) realized capital gains and (losses), realized capital gains (losses) on equity investments, and unrealized capital gains (losses).

All realized capital gains (losses), due to interest rate changes on fixed income investments, net of related capital gains tax, should be captured in the IMR and amortized into income (Column 2, Lines 1 through 31) according to Table 1 or the seriatim method. Realized capital gains (losses) must be classified as either interest (IMR) or non-interest (AVR) related, not a combination except as specified in *SSAP No. 43R—Loan-Backed and Structured Securities*. Purchase lots with the same CUSIP are treated as individual assets for IMR and Asset Valuation Reserve (AVR) purposes.

Exclude those capital gains and (losses) that, in accordance with contract terms have been used to directly increase or (decrease) contract benefit payments or reserves during the reporting period. The purpose of this exclusion is to avoid the duplicate utilization of such gains and (losses).

Capital gains tax should be determined using the method developed by the company to allocate taxes used for statutory financial reporting purposes. By capturing the realized capital gains (losses) net of tax, the capital gains tax associated with those capital gains (losses) due to an interest rate change is charged or credited to the IMR and amortized in proportion to the before-tax amortization.

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Include realized capital gains (losses) on:

Debt securities (excluding loan-backed and structured securities) and redeemable preferred stocks where the realized capital gains (losses) more predominantly reflect interest-related changes. By default, debt instruments whose National Association of Insurance Commissioners (NAIC)/Securities Valuation Office (SVO) designation at the end of the holding period, or within a reasonable amount of time after the reporting entity has sold/disposed of the instrument, are different from its NAIC designation at the beginning of the holding period by more than one NAIC designation or NAIC designation category shall not be considered to reflect interest-related changes. Gains (losses) from those debt instruments shall NOT be reported in the IMR and shall be reported in the AVR

Exchange Traded Funds (ETFs) as listed on the SVO Identified Bond ETF List (thereafter subject to bond IMR guidelines) ~~and the SVO Identified Preferred Stock ETF List (thereafter subject to preferred stock IMR guidelines)~~. ~~I~~include any capital gains (losses) realized by the Company, whether from sale of the ETF or capital gains distributions by the ETF. If the ETF is removed from either SVO ETF list, the ETF is reported and treated as common stock, with any capital gains/(losses) excluded from the IMR. (Mandatory convertible preferred stocks (regardless of if redeemable or perpetual) and investments on the SVO-Identified Preferred Stock List are captured as perpetual preferred stock and treated as equity investments, with gains and losses excluded from IMR.)

SVO Identified Funds designated for systematic value

Called bonds, tendered bonds, and sinking fund payments.

Mortgage loans where the realized gains (losses) more predominantly reflect interest-related changes. By default, mortgage loans that meet any of the following criteria shall not be considered to reflect interest-related losses. Realized gains (losses) from mortgage loans with these characteristics shall be reported in the AVR:

- Any mortgage loan sold/disposed with an established valuation allowance under SSAP No. 37, or
- Interest is more than 90 days past due, or
- The loan is in process of foreclosure, or
- The loan is in course of voluntary conveyance, or
- The terms of the loan have been restructured during the prior two years.

Additional Provisions for Including/Excluding Gains (Losses) from IMR:

Mortgage loan prepayment penalties are not included in IMR. Treat them as regular investment income.

Interest-related gains (losses) realized on directly held capital and surplus notes reported on Schedule BA should be transferred to the IMR in the same manner as similar gains and (losses) on fixed income assets held on Schedule D. A capital gain (loss) on such a note is classified as an interest rate gain if the note is eligible for amortized-value accounting at both the time of acquisition and the time of disposition.

Determination of IMR gain (loss) on multiple lots of the same securities should follow the underlying accounting treatment in determining the gain (loss). Thus, the designation, on

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a purchase lot basis, should be compared to the designation at the end of the holding period to determine IMR or AVR gain or (loss).

Realized capital gains (losses) on any debt security (excluding loan-backed and structured securities) that has had an NAIC/SVO designation of 6 at any time during the holding period should be excluded from the IMR and included as a non-interest-related gain (loss) in the AVR.

Realized capital gains (losses) on ~~any~~ redeemable preferred stock that had an NAIC/SVO designation of 4-6 ~~RP4, RP5 or RP6 or P4, P5 or P6~~ at any time during the holding period should be reported as non-interest-related gains (losses) in the AVR.

The holding period for debt securities (excluding loan-backed and structured securities) and redeemable preferred stocks is defined as the period from the date of purchase to the date of sale. For the end of period classification, the most recent available designation should be used. For bonds acquired before Jan. 1, 1991, the holding period is presumed to have begun on Dec. 31, 1990. For redeemable preferred stocks acquired before Jan. 1, 1993, the holding period is presumed to have begun on Dec. 31, 1992. For SVO Identified Bond ETFs, the holding period is defined as one calendar year to expected maturity. For SVO Identified Bond ETFs ~~Funds~~ designated for systematic value, the holding period is the weighted-average life of the underlying bonds.

In accordance with *SSAP No. 26R—Bonds*, securities with other-than-temporary impairment losses shall be recorded entirely to either AVR or IMR and not bifurcated between interest and non-interest components.

Asset Valuation Reserve (AVR)

Line 2 – Realized Capital Gains (Losses) Net of Taxes – General Account

Report all realized non-interest-related (default) and equity capital gains (losses) (which includes, but is not limited to, common stock, perpetual preferred stock, mandatory convertible preferred stocks (regardless of if redeemable or perpetual) and SVO-Identified Preferred Stock ETFs), net of capital gains tax, applicable to the assets in each component and sub-component. All realized capital gains (losses) transferred to the AVR are net of capital gains taxes thereon. Exclude all interest rate-related capital gains (losses) from the AVR.

Capital gains tax should be determined using the method developed by the company to allocate taxes used for statutory financial reporting purposes.

Report all realized capital gains (losses), net of capital gains tax, on each debt security (excluding loan-backed and structured securities) where the realized capital gains (losses) more predominantly reflect non-interest-related changes. By default, debt instruments whose NAIC/SVO designation at the end of the holding period, or within a reasonable amount of time after the reporting entity has sold/disposed of the instrument, is different from its NAIC/SVO designation at the beginning of the holding period by more than one NAIC designation or NAIC designation category shall be considered to reflect non-interest-related changes. Gains (losses) from those debt instruments shall be reported in the AVR.

Determination of AVR gain (loss) on multiple lots of the same fixed income securities should follow the underlying accounting treatment in determining gain (loss). Thus, the designation, on a purchase lot basis, should be compared to the designation at the end of the holding period to determine IMR or AVR gain or (loss).

In accordance with *SSAP No. 26R—Bonds*, securities with other-than-temporary impairment losses shall be recorded entirely to either AVR or IMR and not bifurcated between interest and non-interest components.

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In accordance with *SSAP No. 43R—Loan-Backed and Structured Securities*, for loan-backed and structured securities only:

- Other-Than-Temporary Impairment – Non-interest-related other-than-temporary impairment losses shall be recorded through the AVR. If the reporting entity wrote the security down to fair value due to the intent to sell or does not have the intent and ability to retain the investment for a period of time sufficient to recover the amortized cost basis, the non-interest-related portion of the other-than-temporary impairment losses shall be recorded through the AVR; the interest related other-than-temporary impairment losses shall be recorded through the IMR. The analysis for bifurcating impairment losses between AVR and IMR shall be completed as of the date when the other-than-temporary impairment is determined.

- Security Sold at a Loss Without Prior OTTI – An entity shall bifurcate the loss into AVR and IMR portions depending on interest- and non-interest-related declines in accordance with the analysis performed as of the date of sale. As such, an entity shall report the loss in separate AVR and IMR components as appropriate.

- Security Sold at a Loss with Prior OTTI – An entity shall bifurcate the current realized loss into AVR and IMR portions depending on interest- and non-interest-related declines in accordance with the analysis performed as of the date of sale. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

- Security Sold at a Gain with Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale. The bifurcation between AVR and IMR that occurs as of the date of sale may be different from the AVR and IMR allocation that occurred at the time of previous other-than-temporary impairments. An entity shall not adjust previous allocations to AVR and IMR that resulted from previous recognition of other-than-temporary impairments.

- Security Sold at a Gain Without Prior OTTI – An entity shall bifurcate the gain into AVR and IMR portions depending on interest and non-interest factors in accordance with the analysis performed as of the date of sale.

In addition, all gains (losses), net of capital gains tax, on mortgage loans where the realized gains (losses) more predominantly reflect non-interest-related changes. By default, mortgage loans that meet any of the following criteria shall be considered to reflect non-interest-related changes and realized gains (losses) from mortgage loans with these characteristics shall be reported in the AVR:

- Any mortgage loan sold/disposed with an established valuation allowance under SSAP No. 37, or
- Interest is more than 90 days past due, or
- The loan is in the process of foreclosure, or
- The loan is in course of voluntary conveyance, or
- The terms of the loan have been restructured during the prior two years

The gain (loss), net of capital gains tax, on any debt security (excluding loan-backed and structured securities) that has had an NAIC/SVO designation of “6” at any time during the holding period should be reported as a credit related gain (loss).

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All capital gains (losses), net of capital gains tax, from redeemable preferred stock that had an NAIC/SVO designation of 4-6 ~~RP4, RP5 or RP6 or P4, P5 or P6~~ at any time during the holding period should be reported as non-interest-related gains (losses) in the AVR.

However, for a convertible bond or redeemable preferred stock purchased while its conversion value exceeds its par value, any gain (loss) realized from its sale before conversion must be included in the Equity Component of the AVR. Conversion Value is defined to mean the number of shares available currently or at next conversion date multiplied by the stock's current market price.

Report all realized equity capital gains (losses), net of capital gains tax, in the appropriate sub-components.

The following guidance pertains to instruments in Scope of *SSAP No. 86—Derivatives*:

- For derivative instruments used in hedging transactions, the determination of whether the capital gains (losses) are allocable to the IMR or the AVR is based on how the underlying asset is treated. Realized gains (losses), net of capital gains tax, on portfolio or general hedging instruments should be included with the hedged asset. Gains (losses), net of capital gains tax, on hedges used, as specific hedges should be included only if the specific hedged asset is sold or disposed of.

- For income generation derivative transactions, the determination of whether the capital gains (losses) are allocable to the IMR or the AVR is based on how the underlying interest (for a put) or covering asset (for a call, cap or floor) is treated. Realized gains (losses), net of capital gains tax should be included in the same sub-component where the realized gains (losses) of the underlying interest (for a put) or covering asset (for a call, cap or floor) is reported. Refer to *SSAP No. 86—Derivatives* for accounting guidance.

Realized gains (losses), net of capital gains tax, resulting from the sale of U.S. government securities and the direct or guaranteed securities of agencies which are backed by the full faith and credit of the U.S. government are exempt from the AVR. This category is described in the Investment Schedules General Instructions.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Admissibility Requirements of Investments in Downstream Holding Companies

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item is the result of regulator comments received on the existing guidance in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*, paragraph 24, and is intended to update the language in paragraph 24 on audits and admissibility to better align with guidance in paragraphs 26 and 27 on the look-through methodology. The current SSAP No. 97, paragraph 24 guidance states "if the downstream noninsurance holding company does not meet the requirements of paragraph 26, **audited GAAP financial statements, as described in paragraph 23, are required for the downstream noninsurance holding company and its SCA and non-SCA investments** in order for the investment in the downstream noninsurance holding company to be classified as an admitted asset."

The issue with the existing paragraph 24 guidance is that as it summarizes other guidance it could be perceived as contradicting guidance provided in paragraph 27 related to the "look through" process. This process allows admitting audited investments in entities owned by an **unaudited downstream noninsurance holding company** SCA entity.

Existing Authoritative Literature:

***SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* (bolding added for emphasis)**

Admissibility Requirements of Investments in Downstream Holding Companies

23. To meet the admissibility requirements of this statement, unless the limited exception to the audited financial statements requirement discussed in paragraphs 26 and 27 applies, an annual audit of the financial statements of SCA entities, including the downstream holding company valued under paragraphs 8.b.i through 8.b.iv. must be obtained. The requirement for audited financial statements may be met by utilizing any one of the following methods:

a. Audited US GAAP financial statements of the downstream SCA holding company. (Consolidated or combined financial statements are allowed encompassing one or more downstream holding companies, including such holding companies that directly own U.S. insurance entities, provided that the statutory financial statements of such U.S. insurance entities are audited. Annual consolidated or combined audits are allowed for insurance entities if completed in accordance with the Model Regulation Requiring Annual Audited Reports as adopted by the SCA's domiciliary state.) The audited financial statements of the downstream holding company shall include as other financial information, consolidating or combining balance sheet schedule(s) showing the equity of all relevant SCA entities and non-SCA SSAP No. 48 entities, and any required intercompany eliminations. The consolidating or combining balance sheet schedule shall separately present those entities owned directly by the downstream holding company. The consolidating or combining balance sheet shall then be adjusted for GAAP to SAP differences for paragraph 8.b.i., 8.b.ii. and 8.b.iv. entities owned directly or indirectly by the downstream holding company. The adjusted amount would then be the reported value of the investment in the downstream holding company at the higher-level reporting entity; or

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b. Audited foreign GAAP-basis financial statements of the downstream SCA holding company. (Consolidated or combined financial statements are allowed encompassing one or more downstream holding companies, including such holding companies that directly own U.S. insurance entities, provided that the statutory financial statements of such U.S. insurance entities are audited. Annual consolidated or combined audits are allowed for insurance entities if completed in accordance with the Model Regulation Requiring Annual Audited Reports as adopted by the SCA's domiciliary state.) The audited foreign GAAP basis financial statements shall include an audited footnote disclosure within the financial statements that reconciles each consolidated entity's net income and equity on a foreign basis of accounting to a U.S. GAAP basis. The audited financial statements of the downstream holding company shall include as other financial information, consolidating or combining balance sheet schedule(s) showing the equity of all relevant SCA entities non-SCA SSAP No. 48 entities, and any required intercompany eliminations. The consolidating or combining balance sheet schedule shall separately present those entities owned directly by the downstream holding company. The consolidating or combining balance sheet shall then be adjusted for GAAP to SAP differences of the insurance entities and paragraph 8.b.ii. and paragraph 8.b.iv. entities owned directly or indirectly by the downstream holding company. The adjusted amount would then be the reported value of the investment in the downstream holding company at the higher-level reporting entity; or

c. Individual audits of the downstream holding company and the downstream holding company's investments in individual SCA entities.

24. If the downstream noninsurance holding company does not meet the requirements of paragraph 26, audited GAAP financial statements, as described in paragraph 23, are required for the downstream noninsurance holding company and its SCA and non-SCA investments in order for the investment in the downstream noninsurance holding company to be classified as an admitted asset.

25. A purchased downstream holding company is valued in accordance with the provisions of paragraphs 22-25 and the provisions of SSAP No. 68.

Limited Exceptions to the Audit Requirements for Downstream Noninsurance Holding Companies

26. This statement requires that investments in SCA entities be recorded using one of the valuation methods described in paragraph 8 in order to be admitted assets. Each of the paragraph 8.b. valuation methods require the financial statements of SCA entities, including downstream noninsurance holding companies, to be audited in order for the investments in SCA entities to be admitted assets. Likewise, SSAP No. 48 requires the financial statements of joint ventures, partnerships, and/or limited liability companies in which the downstream noninsurance holding company has a minor ownership interest or otherwise lacks control, i.e., ownership interest is less than 10% to be audited (U.S. GAAP) in order to be admitted assets. **There is a limited exception to the requirement to have audited financial statements of a downstream noninsurance holding company, provided that the entities owned by the downstream noninsurance holding company (paragraph 8.b.iii. entity) have audited financial statements as described in paragraphs 26 and 27.**

27. The process of admitting audited investments in entities owned by an unaudited downstream noninsurance holding company SCA entity will be known as a "look through." In order to admit the investments in audited SCAs or the audited non-SCA SSAP No. 48 entities owned by an unaudited downstream noninsurance holding company, a reporting entity may apply the look through approach, provided all of the following conditions are met:

a. The downstream noninsurance holding company is an 8.b.iii entity, and

b. The downstream noninsurance holding company does not own any other assets which are material to the downstream holding company other than the audited SCA entities and/or audited non-SCA SSAP No. 48 entities, and

d. The downstream noninsurance holding company is not subject to liabilities, commitments, contingencies, guarantees or obligations which are material to the downstream noninsurance holding company.

If an investment in a downstream noninsurance holding company meets the requirements set forth above, the reporting entity can admit the individual audited SCA entities and/or audited non-SCA SSAP No. 48 entities; however, unaudited immaterial assets of the downstream noninsurance holding company are to be carried at the lesser of the paragraph 8 valuation or nonadmitted (e.g. some equity method investments are required to be carried at a negative value due to either statutory adjustments or to parental obligations to keep funding the subsidiary). If a holding company structure has more than one downstream non-insurance holding company, each downstream non-insurance holding company may be looked through, provided each downstream non-insurance holding company meets all of the conditions in paragraph 27.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation: NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *SSAP No. 97—Subsidiary, Controlled and Affiliated Entities* to revise paragraph 24 language to better align it with the existing guidance provided in paragraphs 26 and 27.

Proposed edits to SSAP No. 97:

24. If the downstream noninsurance holding company does not meet the requirements of paragraph 26, audited GAAP financial statements, as described in paragraph 23, are required~~. for the downstream noninsurance holding company and its SCA and non-SCA investments~~ in order for the investment in the downstream noninsurance holding company or individual SCAs to be classified as an admitted asset.

Staff Review Completed by: Jason Farr– NAIC Staff, November 2023

Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and exposed consistency revisions to *SSAP No. 97—Subsidiary, Controlled and Affiliated Entities* to revise paragraph 24 language to better align it with the existing guidance provided in paragraphs 26 and 27.

On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, the exposed revisions to SSAP No. 97, paragraph 24 with modification to remove the previously exposed revision "or individual SCAs" language as suggested by interested parties as not necessary. The adopted revisions better align it with the existing guidance provided in paragraphs 26 and 27.

Adopted edits to SSAP No. 97:

24. If the downstream noninsurance holding company does not meet the requirements of paragraph 26, audited GAAP financial statements, as described in paragraph 23, are required~~. for the downstream~~

~~noninsurance holding company and its SCA and non-SCA investments~~ in order for the investment in the downstream noninsurance holding company to be classified as an admitted asset.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/03-16-24 Spring National Meeting/Adoptions/23-30 - SSAP 97 Admissibility Requirements.docx

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Revisions to the
As of March 2024 Accounting Practices and Procedures Manual

On **May 15, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2023-16	Schedule BA	Schedule BA Categories *SAP Clarification* No SSAP revisions	Adopted agenda item summarizing key revisions in the modified blanks proposal 2023-12BWG sponsored by the SAPWG, which is proposed to be effective January 1, 2025. This agenda item did not result in any SSAP revisions.
2024-13	SSAP No. 107	Update SSAP No. 107 Disclosures *SAP Clarification* Effective Year End 2024	Adopted revisions to SSAP No. 107 remove the transitional reinsurance program disclosures and the risk corridor disclosures as both programs have expired. In addition, the roll-forward illustration in Exhibit B was revised to remove the portion for the transitional reinsurance program and the risk corridors program.

https://naiconline.sharepoint.com/teams/frsstatutoryaccounting/national meetings/a. national meeting materials/2024/05-15-24/adoptions/00 - adoptions toc.docx

Statutory Accounting Principles (E) Working Group
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Issue: Schedule BA Reporting Categories

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to incorporate more detailed definitions for the annual statement reporting categories of *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* (SSAP No. 48) and residual interests on Schedule BA: Other Long-Term Invested Assets. These investments are reported on designated lines divided by the reporting entity's classification as to the underlying asset characteristics:

- Bonds/Fixed-Income Instruments*
- Common Stocks
- Real Estate
- Mortgage Loans
- Other

** Bond /fixed-income instruments reported in scope of SSAP No. 48 as non-registered private funds, joint ventures, partnerships, or limited liability companies is divided between investments that have an NAIC designation assigned by the SVO and those that do not have an NAIC designation assigned by the SVO.*

The recent residual discussions have further identified that variations exist across industry on the types of investments that should be captured within each category. It has also been noted that the Annual Statement Instructions are limited with guidance and examples for determining reporting classification.

This agenda item has been drafted to propose revisions to the reporting category descriptions in the Annual Statement Instructions to improve consistency in reporting for both ease of industry classifications and for regulator assessment of the type and volume of investment types. The proposed revisions from the Statutory Accounting Principles (E) Working Group will be used to sponsor a blanks annual statement instruction change. The revisions within this agenda item will not result in statutory accounting revisions.

Existing Authoritative Literature:
A/S Instructions – Life, Accident and Health/Fraternal Companies

Reporting Categories on Schedule BA:

Non-Registered Private Funds with Underlying Assets Having Characteristics of:
- Bonds
  - NAIC Designation Assigned by the Securities Valuation Office (SVO)
    - Unaffiliated 0799999
    - Affiliated 0899999
  - NAIC Designation Not Assigned by the Securities Valuation Office (SVO)
    - Unaffiliated 0999999
    - Affiliated 1099999
- Mortgage Loans
  - Unaffiliated 1199999

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Affiliated 1299999

Other Fixed Income Instruments

Unaffiliated 1399999
Affiliated 1499999

Joint Venture, Partnership or Limited Liability Company Interests with Underlying Assets Having the Characteristics of:

Fixed Income Instruments

NAIC Designation Assigned by the Securities Valuation Office (SVO)

Unaffiliated 1599999
Affiliated 1699999

NAIC Designation Not Assigned by the Securities Valuation Office (SVO)

Unaffiliated 1799999
Affiliated 1899999

Common Stocks

Unaffiliated 1999999
Affiliated 2099999

Real Estate

Unaffiliated 2199999
Affiliated 2299999

Mortgage Loans

Unaffiliated 2399999
Affiliated 2499999

Other

Unaffiliated 2599999
Affiliated 2699999

Residual Tranches or Interests with Underlying Assets Having Characteristics of:

Fixed Income Instruments

Unaffiliated 4699999
Affiliated 4799999

Common Stock

Unaffiliated 4899999
Affiliated 4999999

Preferred Stock

Unaffiliated 5099999
Affiliated 5199999

Real Estate

Unaffiliated 5299999
Affiliated 5399999

Mortgage Loans

Unaffiliated 5499999
Affiliated 5599999

Other

Unaffiliated 5699999
Affiliated 5799999

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Schedule BA Classification Instructions/Guidance:

Non-Registered Private Funds with Underlying Assets Having Characteristics of a Bond, Mortgage Loan or Other Fixed Income Instrument

Include: Fixed income instruments that are not corporate or governmental unit obligations (Schedule D) or secured by real property (Schedule B).

Any investments deemed by the reporting entity to possess the underlying characteristics of a bond or other fixed income instrument that has been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 0799999 and 0899999.

Any investments deemed by the reporting entity to possess the underlying characteristics of a bond or other fixed income investment that has not been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 0999999, 1099999, 1199999, 1299999, 1399999 and 1499999.

Joint Ventures, Partnership or Limited Liability Company Interests with Underlying Assets Having the Characteristics:

Fixed Income Instruments

Include: Leveraged Buy-out Fund.

A fund investing in the “Z” strip of Collateralized Mortgage Obligations.

Any investments deemed by the reporting entity to possess the underlying characteristics of fixed income instruments that has been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 1599999 and 1699999.

Any investments deemed by the reporting entity to possess the underlying characteristics of fixed income instruments that has not been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 1799999 and 1899999.

Common Stocks

Include: Venture Capital Funds.

Real Estate

Include: Real estate development interest. Reporting should be consistent with the detailed property analysis appropriate for the corresponding risk-based capital factor for this investment category. If the requisite details are not available for reporting, report under “Other” subcategory.

Mortgage Loans

Include: Mortgage obligations. Reporting should be consistent with the detailed property analysis appropriate for the corresponding risk-based capital factor for this investment category. If the requisite details are not available for reporting, report under “Other” subcategory.

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Other

Include: Limited partnership interests in oil and gas production.

Forest product partnerships.

Investments within the Joint Venture and Partnership Interests category that do not qualify for inclusion in the "Fixed Income Instruments," "Common Stocks," "Real Estate" or "Mortgage Loans" subcategories.

Reporting should be consistent with the corresponding risk-based capital factor for this investment category (i.e., Other Long-Term Assets).

Residual Tranches or Interests with Underlying Assets Having Characteristics of:

Investment in Residual Tranches or Interests should be assigned to the subcategory with the highest underlying asset concentration. There shouldn't be any bifurcation of the underlying assets among the subcategories.

Include: Residual tranches or interests captures securitization tranches and beneficial interests as well as other structures captured in scope of *SSAP No. 43R – Loan-Backed and Structured Securities*, that reflect loss layers without any contractual payments, whether interest or principal, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. See SSAP No. 43R for accounting guidance.

Fixed Income Instruments

Include: Investments with underlying collateral which, if held individually, would be reported on *Schedule D – Part 1 – Long-Term Bonds*

Common Stocks

Include: Investments with underlying collateral which, if held individually, would be reported on *Schedule D – Part 2 – Section 2 – Common Stocks*

Preferred Stocks

Include: Investments with underlying collateral which, if held individually, would be reported on *Schedule D – Part 2 – Section 1 – Preferred Stocks*

Real Estate

Include: Investments with underlying collateral which, if held individually, would be reported on *Schedule A – Real Estate Owned*

Mortgage Loans

Include: Investments with underlying collateral which, if held individually, would be reported on *Schedule B – Mortgage Loans*

Other

Include: Items that do not qualify for inclusion in the above subcategories.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

- Bond Project: Under the principle-based bond definition project, revisions are proposed to combine the non-registered provide funds within the reporting category for joint ventures, partnerships and limited

liability companies as those items would also be in scope of SSAP No. 48. With that change the category of "fixed income instruments" would be retained.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): NA

Recommendation:
NAIC staff recommend that the Working Group include this item on their maintenance agenda as a SAP clarification/potential blanks reporting change and expose this agenda item with a request for industry and regulator feedback to further define and provide examples for the investments captured as non-registered private funds, joint ventures, partnerships or limited liability companies, or residual interests and reported based on the underlying characteristics of assets. Specifically, comments are requested on what should be captured as investments with underlying asset characteristics of:

- Fixed-Income Instruments
- Common Stocks
- Real Estate
- Mortgage Loans
- Other

As detailed in the current A/S instructions, descriptions are included for non-registered private funds, joint ventures, partnerships, and limited liability companies, whereas references to the SSAP the underlying assets would be captured in are included for residual interests.

This agenda item is only intended to improve the annual statement instructions and examples for the allocation of investments based on the above underlying characteristics of assets. If needed, and preferred by the Working Group, this agenda item could be expanded to propose new reporting lines (structural changes) to Schedule BA. As noted within 'Activity to Date,' revisions are currently being considered to combine and rearrange broad reporting lines under the bond project. Those revisions currently do not expand on the instructions for reporting based on underlying characteristics of assets. The proposed revisions from the Statutory Accounting Principles (E) Working Group will be used to sponsor a blanks annual statement instruction change. The revisions within this agenda item will not result in actual statutory accounting revisions.

Staff Review Completed by: Julie Gann - NAIC Staff, May 2023

Status:
On August 13, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification and exposed this agenda item to further define for consistency purposes the investments captured as non-registered private funds, joint ventures, partnerships or limited liability companies, or residual interests and reported based on the underlying characteristics of assets.

On December 1, 2023, the Statutory Accounting Principles (E) Working Group exposed additional revisions, as detailed below, to further define the investments captured on Schedule BA along with the continued proposed to combine non-registered private funds within the proposed reporting lines for joint ventures, partnerships, or limited liability companies. The Working Group also requested additional regulator and industry feedback on whether more specificity is needed since the existing Schedule BA descriptions are fairly broad.

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Proposed Interested Parties' Edits to the Schedule BA Instructions from Separate Attachment:

Non-Registered Private Funds with Underlying Assets Having Characteristics of a Bond, Mortgage Loan or Other Fixed Income Instrument

Include: Fixed income instruments that are not corporate or governmental unit obligations (Schedule D) or secured by real property (Schedule B).

Any investments deemed by the reporting entity to possess the underlying characteristics of a bond or other fixed income instrument that has been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 0799999 and 0899999.

Any investments deemed by the reporting entity to possess the underlying characteristics of a bond or other fixed income investment that has not been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 0999999, 1099999, 1199999, 1299999, 1399999 and 1499999.

Joint Ventures, Partnership or Limited Liability Company Interests with Underlying Assets Having the Characteristics:

Fixed Income Instruments

Include: Investments with underlying collateral which include contractual principal and/or interest payments, excluding mortgage loans~~Leveraged Buy-out Fund~~.

~~A fund investing in the "Z" strip of Collateralized Mortgage Obligations.~~

Any investments deemed by the reporting entity to possess the underlying characteristics of fixed income instruments that has been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 1599999 and 1699999.

Any investments deemed by the reporting entity to possess the underlying characteristics of fixed income instruments that has not been assigned an NAIC designation by the Securities Valuation Office (SVO) pursuant to the policies in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* for this category. Report these investments on Lines 1799999 and 1899999.

Common Stocks

Include: Venture Capital Funds or other underlying equity investments.

Real Estate

Include: Real estate development interest. Reporting should be consistent with the detailed property analysis appropriate for the corresponding risk-based capital factor for this investment category. If the requisite details are not available for reporting, report under "Other" subcategory.

Mortgage Loans

Include: Mortgage obligations. Reporting should be consistent with the detailed property analysis appropriate for the corresponding risk-based capital

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factor for this investment category. If the requisite details are not available for reporting, report under "Other" subcategory.

Other

Include: Limited partnership interests in oil and gas production.

Forest product partnerships.

Investments within the Joint Venture and Partnership Interests category that do not qualify for inclusion in the "Fixed Income Instruments," "Common Stocks," "Real Estate" or "Mortgage Loans" subcategories.

~~Reporting should be consistent with the corresponding risk-based capital factor for this investment category (i.e., Other Long-Term Assets).~~

Residual Tranches or Interests with Underlying Assets Having Characteristics of:

Investment in Residual Tranches or Interests should be assigned to the subcategory with the highest underlying asset concentration. There shouldn't be any bifurcation of the underlying assets among the subcategories.

Include: Residual tranches or interests from securitization tranches and beneficial interests as well as other structures captured in scope of *SSAP No. 43R – Loan-Backed and Structured Securities* Investments in joint ventures, partnerships and limited liability companies captured in scope of *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* that represent residual interests or that predominantly hold residual interests.

This category shall also include residual interests or residual security tranches within investment structures that are not captured in scope of SSAP No. 43R or SSAP No. 48 but that reflect, in substance, residual interests or residual security tranches.

Fixed Income Instruments

Include: ~~-~~Investments with underlying collateral which include contractual principal and/or interest payments, excluding mortgage loans~~, if held individually, would be reported on *Schedule D – Part 1 – Long-Term Bonds*~~.

Common Stocks

Include: Investments with underlying collateral which are securities that represent a subordinate equity ownership.~~, if held individually, would be reported on *Schedule D – Part 2 – Section 2 – Common Stocks*~~

Preferred Stocks

Include: Investments with underlying collateral which is a security that represents ownership of a corporation and gives the holder a claim prior to the claim of common stockholders on earnings and also generally on assets in the event of liquidation.~~, if held individually, would be reported on *Schedule D – Part 2 – Section 1 – Preferred Stocks*~~

Real Estate

Include: Investments with underlying collateral which is defined as directly-owned real estate properties and single real estate property investments that are directly and wholly-owned through a limited liability company~~. if held individually, would be reported on *Schedule A – Real Estate Owned*~~

Mortgage Loans

Include: Investments with underlying collateral which is secured by a mortgage on real estate. ~~, if held individually, would be reported on *Schedule B – Mortgage Loans*~~

Other

Include: Items that do not qualify for inclusion in the above subcategories.

On February 20, 2024, the Statutory Accounting Principles (E) Working Group reviewed the comments received on this item as well as comments received on the exposed blanks proposal 2023-12BWG. After the discussion, the Working Group exposed this agenda item and directed a modified SAPWG-sponsored blanks proposal (2023-12BWG) to recommend for exposure during the February 21, 2024, Banks (E) Working Group conference call. (This agenda item does not propose any SSAP revisions.)

The following key modifications are reflected in the modified Schedule BA blanks proposal and for documentation within this agenda item:

1) Schedule BA has a clear statement that all investments shall be reported in the dedicated reporting line. Investments that do not fit within any specific reporting line shall be captured as an "Any Other Class of Asset."

2) The Schedule BA reporting category for investments in "Joint Ventures, Partnerships and Limited Liability Companies" has been clarified to identify that investments captured within this reporting category shall be in scope of SSAP No. 48. With this clarification, the revisions proposed by industry to clarify the "underlying characteristics of bonds" subcategory to include "collateral that has contractual principal and/or interest payments, excluding mortgage loans," as well as the other proposed industry descriptions for other subcategories, has been retained. One exception to the SSAP No. 48 restriction has been included to reference structured settlement payment rights in scope of *SSAP No. 21R—Other Admitted Assets* that have an SVO-Assigned designation. This inclusion is consistent with the guidance in SSAP No. 21R. The Schedule BA blanks proposal maintains the recommendation to eliminate the "non-registered private fund" reporting category as those items shall be reported in the "joint ventures, partnerships and limited liabilities companies" reporting category if in scope of SSAP No. 48.

3) The Schedule BA reporting category for residuals has been modified to refer to SSAP No. 21R for the residual definition, pursuant to agenda item 2019-21. As such, the proposed revisions offered by industry in their January 22, 2024, comment letter have not been reflected. Beginning Jan. 1, 2025, all residuals shall be captured in scope of SSAP No. 21R, regardless of the investment form.

On May 15, 2024, the Statutory Accounting Principles (E) Working Group reviewed the comments received on this item as well as comments received on the exposed blanks proposal 2023-12BWG, which is proposed to be effective on January 1, 2025. After the discussion, the Working Group adopted this agenda item, resulting in no SSAP revisions, the adoption is to communicate support for the adoption of 2023-12BWG with the following three additional modifications to the blanks proposal:

1) Rename "Fixed Income Instruments" to "Bonds":

   Residual Tranches or Interests with Underlying Assets Having Characteristics of:
   Investment in Residual Tranches or Interests should be assigned to the subcategory with the highest underlying asset concentration. There should not be any bifurcation of the underlying assets among the subcategories.

   Include: Residual tranches or interests captured in scope of *SSAP No. 21R – Other Admitted Assets.* The scope of SSAP No. 21R includes all in-substance residuals regardless of the investment form. Therefore, this category shall include investments that reflect in-substance residuals in the form of 1) an investment in a securitization

tranche or beneficial interest, 2) an investment in a joint venture, partnership or limited liability company, 3) an investment in preferred stock 4) an investment in common stock, or 5) any other investment structure.

~~**Fixed Income Instruments**~~**Bonds**

Include: Investments with underlying collateral which, if held individually, would be reported as issuer credit obligations on *Schedule D – Part 1 – ~~Long-Term Bonds~~Section 1,* or as asset-backed securities on *Schedule D – Part 1 – Section 2.* Residual tranches from collateralized loan obligations (CLOs) shall be captured within this reporting line.

Other

Include: Items that do not qualify for inclusion in the above subcategories. Examples include, but are not limited to, residual tranches from investments with underlying assets of student loans, auto loans, aircraft leases or train car leases.

2) Clarify Guidance for Schedule BA, Column 26 – Maturity Date

Column 26 – Maturity Date

The maturity date shall be reported for all investments on Schedule BA that have a stated maturity date. This is anticipated to include, but not be limited to, all investments captured as non-bond debt securities, surplus notes, capital notes, collateral loans, non-collateral loans, and investments in tax credits. However, this list should not be considered all-inclusive for investments captured on other reporting lines with stated maturity dates.

~~Use only for securities included in the following subtotal lines.~~

~~State the date the mortgage loan matures.~~

3) Correct Joint Venture, Partnerships and LLCs Reporting Line. (Change from exposure is shaded.)

As Exposed: Interests in Joint Ventures, Partnerships or Limited Liability ~~Company~~ Companies (Including Non-Registered Private Funds) ~~Interests with Underlying Assets Having the Characteristics of~~:

With Correction: Interests in Joint Ventures, Partnerships or Limited Liability ~~Company~~ Companies (Including Non-Registered Private Funds) ~~Interests~~ with Underlying Assets Having the Characteristics of:

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
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Issue: Update SSAP No. 107 Disclosures

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
This agenda item recommends updates to disclosure requirements in *Statement of Statutory Accounting Principles No. 107—Risk-Sharing Provisions of the Affordable Care Act* to remove disclosures related to transitional reinsurance and for the risk corridors programs which have expired.

In December 2014, the NAIC Statutory Accounting Principles (E) Working Group (SAPWG) issued SSAP No. 107 to provide accounting and disclosure guidance for the three risk-sharing provision programs of the Affordable Care Act (the "3Rs programs"). SSAP No. 107 covers the three risk sharing programs that were initially part of the Affordable Care Act, a permanent risk adjustment program, a transitional reinsurance program, and a temporary risk corridors program. Since that time, the 3Rs programs have changed significantly. Most notably, the temporary transitional reinsurance and risk corridors programs terminated at the end of 2016.

SSAP No. 107 introduced significant financial statement disclosure requirements for the 3Rs programs. The disclosures are required by SSAP No. 107, paragraphs 60-62. Exhibit B of SSAP No. 107 illustrates the roll-forward disclosure required by paragraph 61. These disclosure requirements are currently satisfied through detailed data tables included in Footnote 24E of the quarterly and annual financial statements.

Despite the passage of time and the termination of two of the 3Rs programs, the disclosure requirements outlined in SSAP No. 107 and the disclosure instructions for footnote 24E have not been updated or modified since inception. As a result, companies originally subject to the 3Rs programs are still required by SSAP No. 107 to include several tables in Footnote 24E, even though the majority of the information disclosed is either zero or blank because two of the programs were terminated several years ago. This agenda item proposal removal of the disclosures for the expired programs and also removal of the related roll-forward illustration in Exhibit B of SSAP No. 107 for the expired programs.

Existing Authoritative Literature:

SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act
Disclosures

60. The financial statements shall disclose on an annual and quarterly basis beginning in the first quarter of 2014, the assets, liabilities and revenue elements by program regarding the risk-sharing provisions of the Affordable Care Act for the reporting periods which are impacted by the programs including the listing in paragraphs 60.a. through 60.c. Reporting entities shall also indicate if they wrote any accident and health insurance premium, which is subject to the Affordable Care Act risk-sharing provisions. In the event that the balances are zero, the reporting entity should provide context to explain the reasons for the zero balances, including insufficient data to make an estimate, no balances or premium was excluded from the program, etc. Asset balances shall reflect admitted asset balances. The disclosure shall include the following:

a. ACA Permanent Risk Adjustment Program

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i. Premium adjustments receivable due to ACA Risk Adjustment (including high-cost risk pool payments)

ii. Risk adjustment user fees payable for ACA Risk Adjustment

iii. Premium adjustments payable due to ACA Risk Adjustment (including high-cost risk pool ceded premium)

iv. Reported as revenue in premium for accident and health contracts (written/collected) due to ACA Risk Adjustment

v. Reported in expenses as ACA risk adjustment user fees (incurred/paid)

b. ACA Transitional Reinsurance Program

i. Amounts recoverable for claims paid due to ACA Reinsurance

ii. Amounts recoverable for claims unpaid due to ACA Reinsurance (contra-liability)

iii. Amounts receivable relating to uninsured plans for contributions for ACA Reinsurance

iv. Liabilities for contributions payable due to ACA Reinsurance - not reported as ceded premium

v. Ceded reinsurance premiums payable due to ACA Reinsurance

vi. Liability for amounts held under uninsured plans contributions for ACA Reinsurance

vii. Ceded reinsurance premiums due to ACA Reinsurance

viii. Reinsurance recoveries (income statement) due to ACA Reinsurance payments or expected payments

ix. ACA Reinsurance Contributions – not reported as ceded premium

c. ACA Temporary Risk Corridors Program

i. Accrued retrospective premium due from ACA Risk Corridors

ii. Reserve for rate credits or policy experience rating refunds due to ACA Risk Corridors

iii. Effect of ACA Risk Corridors on net premium income (paid/received)

iv. Effect of ACA Risk Corridors on change in reserves for rate credits

61. In addition, beginning in annual 2014 and both quarterly and annual thereafter, a roll forward of prior year ACA risk-sharing provisions specified asset and liability balances shall be disclosed in the annual statutory Notes to Financial Statements, as illustrated in Exhibit B. Note for the roll-forward illustration, assets shall be reflected gross of any nonadmission. The reasons for adjustments to prior year balances (i.e. federal audits, revised participant counts, information which impacted risk score projections, etc.) shall also be disclosed. For year-end 2014, all columns and rows are expected to be zero since 2014 is the first year that a receivable or liability will be recorded. For reporting periods on or after March 31, 2016, the risk corridors roll forward is amended to require disclosure of the risk corridors asset and liability balances and subsequent adjustments by program benefit year. The beginning receivable or payable in the roll forward will reflect the prior year-end balance for the specified benefit.

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62. For reporting periods ending on or after March 31, 2016, for both quarterly and annual reporting, the following information is required for risk corridors balances by program benefit year:

a. Estimated amount to be filed or final amounts filed with federal agency

b. Amounts impaired or amounts not accrued for other reasons (not withstanding collectability concerns)

c. Amounts received from federal agency

d. Asset balance gross of nonadmission

e. Nonadmitted amounts

f. Net admitted assets

Exhibit B of SSAP No. 107 illustrates the roll forward required by the SSAP No. 107. paragraph 61 of the disclosures.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:

Convergence with International Financial Reporting Standards (IFRS):Not Applicable

Sponsor Recommendation
We are respectfully requesting SAPWG to re-evaluate and amend the disclosure requirements of SSAP No. 107 and request BWG to update the quarterly and annual financial statement instructions for Footnote 24E to eliminate certain tables, or portions of tables, that are no longer applicable. Specifically, we are requesting elimination of the portions of each table related to the transitional reinsurance and risk corridors programs that are no longer valid.

Sherry Gillespie, Senior Director - Regulatory Finance
UnitedHealthcare
2884 School Ln, Green Bay, WI 54313
February 1, 2024

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act* as illustrated below. The revisions will remove the transitional reinsurance program disclosures and the risk corridor disclosures as both programs have expired. In addition, the roll-forward illustration in Exhibit B is also proposed to be updated to remove the portion for the transitional reinsurance program and the risk corridors program. NAIC staff recommends that the Working Group direct a Blanks proposal, allowing for concurrent consideration, to allow for the disclosures to be removed beginning with the year-end 2024 financial statements.

NAIC staff is aware that some states have federal waivers to operate reinsurance programs, but not all of the federal reinsurance waivers operate the same as the original transition program. To the extent the Working Group decides that new disclosures are needed for these reinsurance waiver programs, a future disclosure can be developed separately.

Staff Review Completed by: Robin Marcotte - NAIC Staff

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Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act* which would remove the transitional reinsurance program disclosures and the risk corridor disclosures as both programs have expired. In addition, the roll-forward illustration in Exhibit B is also proposed to be updated to remove the portion for the transitional reinsurance program and the risk corridors program. The Working Group also directed NAIC staff to prepare a Blanks proposal, allowing for concurrent consideration, to allow for the disclosures to be removed beginning with the year-end 2024 financial statements.

Proposed Revisions:
SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act Disclosures

60. The financial statements shall disclose on an annual and quarterly basis beginning in the first quarter of 2014, the assets, liabilities and revenue elements ~~by~~ for the permanent risk adjustment program regarding the risk-sharing provisions of the Affordable Care Act for the reporting periods which are impacted by the programs including the listing in paragraph~~s~~ 60.a. ~~through 60.c~~. Reporting entities shall also indicate if they wrote any accident and health insurance premium, which is subject to the Affordable Care Act risk-sharing provisions. In the event that the balances are zero, the reporting entity should provide context to explain the reasons for the zero balances, including insufficient data to make an estimate, no balances or premium was excluded from the program, etc. Asset balances shall reflect admitted asset balances. The disclosure shall include the following:

a. ACA Permanent Risk Adjustment Program

i. Premium adjustments receivable due to ACA Risk Adjustment (including high-cost risk pool payments)

ii. Risk adjustment user fees payable for ACA Risk Adjustment

iii. Premium adjustments payable due to ACA Risk Adjustment (including high-cost risk pool ceded premium)

iv. Reported as revenue in premium for accident and health contracts (written/collected) due to ACA Risk Adjustment

v. Reported in expenses as ACA risk adjustment user fees (incurred/paid)

~~b. ACA Transitional Reinsurance Program~~

~~i. Amounts recoverable for claims paid due to ACA Reinsurance~~

~~ii. Amounts recoverable for claims unpaid due to ACA Reinsurance (contra-liability)~~

~~iii. Amounts receivable relating to uninsured plans for contributions for ACA Reinsurance~~

~~iv. Liabilities for contributions payable due to ACA Reinsurance - not reported as ceded premium~~

~~v. Ceded reinsurance premiums payable due to ACA Reinsurance~~

~~vi. Liability for amounts held under uninsured plans contributions for ACA Reinsurance~~

~~vii. Ceded reinsurance premiums due to ACA Reinsurance~~

~~viii. Reinsurance recoveries (income statement) due to ACA Reinsurance payments or expected payments~~

~~ix. ACA Reinsurance Contributions – not reported as ceded premium~~

~~c. ACA Temporary Risk Corridors Program~~

~~i. Accrued retrospective premium due from ACA Risk Corridors~~

~~ii. Reserve for rate credits or policy experience rating refunds due to ACA Risk Corridors~~

~~iii. Effect of ACA Risk Corridors on net premium income (paid/received)~~

~~iv. Effect of ACA Risk Corridors on change in reserves for rate credits~~

61. In addition, beginning in annual 2014 and both quarterly and annual thereafter, a roll forward of prior year ACA risk-sharing provisions for the risk adjustment program specified asset and liability balances shall be disclosed in the annual statutory Notes to Financial Statements, as illustrated in Exhibit B. Note for the roll-forward illustration, assets shall be reflected gross of any nonadmission. The reasons for adjustments to prior year balances (i.e. federal audits, revised participant counts, information which impacted risk score projections, etc.) shall also be disclosed. ~~For year-end 2014, all columns and rows are expected to be zero since 2014 is the first year that a receivable or liability will be recorded. For reporting periods on or after March 31, 2016, the risk corridors roll forward is amended to require disclosure of the risk corridors asset and liability balances and subsequent adjustments by program benefit year.~~ The beginning receivable or payable in the roll forward will reflect the prior year-end balance for the specified benefit.

62. For reporting periods ending on or after March 31, 2016, for both quarterly and annual reporting, the following information is required for risk ~~corridors~~ adjustment balances by program benefit year:

a. Estimated amount to be filed or final amounts filed with federal agency

b. Amounts impaired or amounts not accrued for other reasons (not withstanding collectability concerns)

c. Amounts received from federal agency

d. Asset balance gross of nonadmission

e. Nonadmitted amounts

f. Net admitted assets

EXHIBIT B – ACA RISK-SHARING PROVISIONS ROLL-FORWARD ILLUSTRATION

Receivables are reflected gross of any nonadmission for this illustration.

	Accrued During the Prior Year on Business Written Before December 31 of the Prior Year		Received or Paid as of the Current Year on Business Written Before December 31 of the Prior Year		Differences		Adjustments			Unsettled Balances as of the Reporting Date	
					Prior Year Accrued Less Payments (Col 1 – 3)	Prior Year Accrued Less Payments (Col 2 – 4)	To Prior Year Balances	To Prior Year Balances		Cumulative Balance from Prior Years (Col 1 – 3 + 7)	Cumulative Balance from Prior Years (Col 2 – 4 + 8)
	1	2	3	4	5	6	7	8	9	10	11
	Receivable	(Payable)	Receivable	(Payable)	Receivable	(Payable)	Receivable	(Payable)	Ref	Receivable	(Payable)
a. Permanent ACA Risk Adjustment Program											
1. Premium adjustments receivable	4,000,000		3,000,000		1,000,000		-800,000		A	200,000	0
2. Premium adjustments (payable)		8,000,000		9,000,000		-1,000,000		1,000,000	B		0
3. ~~Sub~~Total ACA Permanent Risk Adjustment Program	**4,000,000**	**8,000,000**	**3,000,000**	**9,000,000**	**1,000,000**	**-1,000,000**	**-800,000**	**1,000,000**		**200,000**	**0**
~~b. Transitional ACA Reinsurance Program~~											
~~1. Amounts recoverable for claims paid~~	~~22,000,000~~		~~15,000,000~~		~~7,000,000~~		~~-7,000,000~~		~~C~~	~~0~~	
~~2. Amounts recoverable for claims unpaid (contra liability)~~	~~8,000,000~~		~~9,000,000~~		~~-1,000,000~~		~~990,000~~		~~D~~	~~-10,000~~	
~~3. Amounts receivable relating to uninsured plans~~	~~3,000,000~~		~~2,800,000~~		~~200,000~~		~~-100,000~~		~~E~~	~~100,000~~	
~~4. Liabilities for contributions payable due to ACA Reinsurance – not reported as ceded premium~~		~~90,000~~		~~75,000~~		~~15,000~~		~~-14,000~~	~~F~~		~~1,000~~
~~5. Ceded reinsurance premiums payable~~		~~100~~		~~200~~		~~-100~~		~~100~~	~~G~~		~~0~~
~~6. Liability for amounts held under uninsured plans~~		~~125,000~~		~~15,000~~		~~110,000~~		~~90,000~~	~~H~~		~~200,000~~
~~**7. Subtotal ACA Transitional Reinsurance Program**~~	~~**33,000,000**~~	~~**215,100**~~	~~**26,800,000**~~	~~**90,200**~~	~~**6,200,000**~~	~~**124,900**~~	~~**-6,110,000**~~	~~**76,100**~~		~~**90,000**~~	~~**201,000**~~
~~c. Temporary ACA Risk Corridors Program~~											
~~1. Accrued retrospective premium~~	~~12,000,000~~		~~14,000,000~~		~~-2,000,000~~		~~1,750,000~~		~~I~~	~~-250,000~~	
~~2. Reserve for rate credits or policy experience rating refunds~~		~~150,000~~		~~250,000~~		~~-100,000~~		~~100,000~~	~~J~~		~~0~~
~~**3. Subtotal ACA Risk Corridors Program**~~	~~**12,000,000**~~	~~**150,000**~~	~~**14,000,000**~~	~~**250,000**~~	~~**-2,000,000**~~	~~**-100,000**~~	~~**1,750,000**~~	~~**100,000**~~		~~**-250,000**~~	~~**0**~~
~~**d. Total for ACA Risk Sharing Provisions**~~	~~**49,000,000**~~	~~**8,365,100**~~	~~**43,800,000**~~	~~**9,340,200**~~	~~**5,200,000**~~	~~**-975,100**~~	~~**-5,160,000**~~	~~**1,176,100**~~		~~**40,000**~~	~~**201,000**~~

Explanation of adjustments:

A. Adjusted due to federal audit.

B. Adjusted because of revised participant count.

C. Adjusted due to poor experience of other participants in the reinsurance pool.

D. Revised risk score information in the state of substantially impacted risk scores.

On May 15, 2024, the Statutory Accounting Principles (E) Working Group incorporated additional revisions into what was exposed which also deleted SSAP No. 107, paragraph 62 as recommended by interested parties. The adopted revisions, which are effective for year-end 2024 reporting, are reflected below. Similar revisions will be recommended to the Blanks (E) Working Group proposal 2024-10BWG in the May meeting. The deletion of SSAP No. 107, paragraph 62 will also result in the deletion of Note 24E/F (2) and 24E/F (3) tables on the proposal 2024-10BWG.

Adopted SSAP No. 107 revisions:

SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act Disclosures

60. The financial statements shall disclose on an annual and quarterly basis beginning in the first quarter of 2014, the assets, liabilities and revenue elements ~~by~~ for the permanent risk adjustment program regarding the risk-sharing provisions of the Affordable Care Act for the reporting periods which are impacted by the programs including the listing in paragraph~~s~~ 60.a. ~~through 60.c~~. Reporting entities shall also indicate if they wrote any accident and health insurance premium, which is subject to the Affordable Care Act risk-sharing provisions. In the event that the balances are zero, the reporting entity should provide context to explain the reasons for the zero balances, including insufficient data to make an estimate, no balances or premium was excluded from the program, etc. Asset balances shall reflect admitted asset balances. The disclosure shall include the following:

a. ACA Permanent Risk Adjustment Program

i. Premium adjustments receivable due to ACA Risk Adjustment (including high-cost risk pool payments)~~–~~

ii. Risk adjustment user fees payable for ACA Risk Adjustment~~–~~

iii. Premium adjustments payable due to ACA Risk Adjustment (including high-cost risk pool ceded premium)~~–~~

iv. Reported as revenue in premium for accident and health contracts (written/collected) due to ACA Risk Adjustment

v. Reported in expenses as ACA risk adjustment user fees (incurred/paid)

~~b. ACA Transitional Reinsurance Program~~

~~i. Amounts recoverable for claims paid due to ACA Reinsurance~~

~~ii. Amounts recoverable for claims unpaid due to ACA Reinsurance (contra-liability)~~

~~iii. Amounts receivable relating to uninsured plans for contributions for ACA Reinsurance~~

~~iv. Liabilities for contributions payable due to ACA Reinsurance - not reported as ceded premium~~

~~v. Ceded reinsurance premiums payable due to ACA Reinsurance~~

~~vi. Liability for amounts held under uninsured plans contributions for ACA Reinsurance~~

~~vii. Ceded reinsurance premiums due to ACA Reinsurance~~

~~viii. Reinsurance recoveries (income statement) due to ACA Reinsurance payments or expected payments~~

~~ix. ACA Reinsurance Contributions - not reported as ceded premium~~

~~c. ACA Temporary Risk Corridors Program~~

~~i. Accrued retrospective premium due from ACA Risk Corridors~~

~~ii. Reserve for rate credits or policy experience rating refunds due to ACA Risk Corridors~~

~~iii. Effect of ACA Risk Corridors on net premium income (paid/received)~~

~~iv. Effect of ACA Risk Corridors on change in reserves for rate credits~~

61. In addition, beginning in annual 2014 and both quarterly and annual thereafter, a roll forward of prior year ACA risk-sharing provisions for the risk adjustment program specified asset and liability balances shall be disclosed in the annual statutory Notes to Financial Statements, as illustrated in Exhibit B. Note for the roll-forward illustration, assets shall be reflected gross of any nonadmission. The reasons for adjustments to prior year balances (i.e. federal audits, revised participant counts, information which impacted risk score projections, etc.) shall also be disclosed. ~~For year-end 2014, all columns and rows are expected to be zero since 2014 is the first year that a receivable or liability will be recorded. For reporting periods on or after March 31, 2016, the risk corridors roll forward is amended to require disclosure of the risk corridors asset and liability balances and subsequent adjustments by program benefit year.~~ The beginning receivable or payable in the roll forward will reflect the prior year-end balance for the specified benefit.

~~62. For reporting periods ending on or after March 31, 2016, for both quarterly and annual reporting, the following information is required for risk corridors balances by program benefit year:~~

~~a. Estimated amount to be filed or final amounts filed with federal agency~~

~~b. Amounts impaired or amounts not accrued for other reasons (not withstanding collectability concerns)~~

~~c. Amounts received from federal agency~~

~~d. Asset balance gross of nonadmission~~

~~e. Nonadmitted amounts~~

~~f. Net admitted assets~~

EXHIBIT B – ACA RISK-SHARING PROVISIONS ROLL-FORWARD ILLUSTRATION

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					Prior Year Accrued Less Payments (Col 1 – 3)	Prior Year Accrued Less Payments (Col 2 – 4)	To Prior Year Balances	To Prior Year Balances		Cumulative Balance from Prior Years (Col 1 – 3 + 7)	Cumulative Balance from Prior Years (Col 2 – 4 + 8)
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	Receivable	(Payable)	Receivable	(Payable)	Receivable	(Payable)	Receivable	(Payable)	Ref	Receivable	(Payable)
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2. Premium adjustments (payable)		8,000,000		9,000,000		-1,000,000		1,000,000	B		0
3. ~~Sub~~T~~total~~ ACA Permanent Risk Adjustment Program	**4,000,000**	**8,000,000**	**3,000,000**	**9,000,000**	**1,000,000**	**-1,000,000**	**-800,000**	**1,000,000**		**200,000**	**0**
~~b. Transitional ACA Reinsurance Program~~											
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~~2. Amounts recoverable for claims unpaid (contra liability)~~	~~8,000,000~~		~~9,000,000~~		~~-1,000,000~~		~~990,000~~		~~D~~	~~-10,000~~	
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~~7. Subtotal ACA Transitional Reinsurance Program~~	**~~33,000,000~~**	**~~215,100~~**	**~~26,800,000~~**	**~~90,200~~**	**~~6,200,000~~**	**~~124,900~~**	**~~-6,110,000~~**	**~~76,100~~**		**~~90,000~~**	**~~201,000~~**
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~~2. Reserve for rate credits or policy experience rating refunds~~		~~150,000~~		~~250,000~~		~~-100,000~~		~~100,000~~	~~J~~		~~0~~
~~3. Subtotal ACA Risk Corridors Program~~	**~~12,000,000~~**	**~~150,000~~**	**~~14,000,000~~**	**~~250,000~~**	**~~-2,000,000~~**	**~~-100,000~~**	**~~1,750,000~~**	**~~100,000~~**		**~~-250,000~~**	**~~0~~**
~~d. Total for ACA Risk Sharing Provisions~~	**~~49,000,000~~**	**~~8,365,100~~**	**~~43,800,000~~**	**~~9,340,200~~**	**~~5,200,000~~**	**~~-975,100~~**	**~~-5,160,000~~**	**~~1,176,100~~**		**~~40,000~~**	**~~201,000~~**

Explanation of adjustments:

A. Adjusted due to federal audit.

B. Adjusted because of revised participant count.

C. Adjusted due to poor experience of other participants in the reinsurance pool.

D. Revised risk score information in the state of substantially impacted risk scores.

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Revisions to the
As of March 2024, Accounting Practices and Procedures Manual

On **August 13, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2019-21	**Issue Paper No. 169**	Principles-Based Bond Definition *New SAP Concept* Issue Papers are Not Authoritative	Adopted Issue Paper No. 169 documents the discussions and decisions related to the principles-based bond project. The adopted SSAPs impacted by the principles-based bond definition are effective January 1, 2025, and should be used as the source of authoritative guidance.
2022-12	SSAP No. 25 SSAP No. 63 **INT 03-02**	Review of *INT 03-02: Modification to an Existing Intercompany Pooling Arrangement* *SAP Clarification* Effective Immediately (August 13, 2024)	Adopted revisions to SSAP No. 25 and SSAP No. 63 address transfers of assets when modifying intercompany pooling agreements. This agenda item also nullifies INT 03-02.
2023-26	SSAP No. 15 SSAP No. 86	*ASU 2023-06, Disclosure Improvements* *SAP Clarification* Effective Immediately (August 13, 2024)	Adopted revisions in SSAP No. 15 and SSAP No. 86 adopt, with modification, certain disclosures from ASU 2023-06. The ASU 2023-06 disclosures originally recommended for inclusion in SSAP No. 103R are to be added to agenda item 2024-04: Conforming Repurchase Agreements for further consideration as part of the larger project looking at statutory guidance for repurchase agreements and secured lending.
2024-02	SSAP No. 19 SSAP No. 73	*ASU 2023-01, Leases (Topic 842), Common Control Arrangements* *SAP Clarification* Effective Immediately (August 13, 2024)	Adopted revisions in SSAP No. 19 and SSAP No. 73 adopt, with modification, ASU 2023-01.

Ref #	SSAP/ Appendix	Title	Summary
2024-03	SSAP No. 20 **INT 21-01**	*ASU 2023-08, Accounting for and Disclosure of Crypto Assets* *SAP Clarification* Effective Immediately (August 13, 2024)	Adopted revisions in SSAP No. 20 adopt, with modification, ASU 2023-08 and nullify *INT 21-01: Accounting for Cryptocurrencies*.
2024-08	SSAP No. 26R SSAP No. 30R SSAP No. 32R SSAP No. 43R SSAP No. 48	Residual Consistency Revisions *SAP Clarification* Effective January 1, 2025	Adopted revisions result with identified SSAPs referring to SSAP No. 21 for the formal residual definition and for accounting and reporting guidance.
2024-09	SSAP No. 2	SSAP No. 2 Clarification *SAP Clarification* Effective January 1, 2025	Adopted revisions eliminate lingering references implying that asset-backed securities, mortgage loans, or other Schedule BA items are permitted to be reported as cash equivalents or short-term investments.
2024-14EP	Various	Spring 2024 Editorial Revisions Effective Immediately (August 13, 2024)	Adopted editorial revisions to the *Accounting Practices and Procedures Manual* remove "Revised" and "R" identifiers from SSAP titles and SSAP references throughout the Manual.

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Statutory Issue Paper No. 169

Principles-Based Bond Definition

STATUS
Adopted –August 13, 2024

Original SSAP: SSAP No. 26 and SSAP No. 43

Current Authoritative Guidance: SSAP No. 21, SSAP No. 26 and SSAP No. 43

Type of Issue:
Common Area

SUMMARY OF ISSUE

1. The guidance within this issue paper details the new statutory accounting concept revisions to *SSAP No. 26—Bonds* (SSAP No. 26), *SSAP No. 43—Loan-backed and Structured Securities* (SSAP No. 43) and *SSAP No. 21—Other Admitted Assets* (SSAP No. 21) pursuant to the Statutory Accounting Principles (E) Working Group's (Working Group) Investment Classification Project as well as in response to expanding investment structures that have been reported on Schedule D-1: Long-Term Bonds. The revisions and discussions detailed within reflects a comprehensive review, referred to as the "Principles-Based Bond Project," to establish principal concepts for determining whether a debt security qualifies for reporting as a bond. Although SSAP No. 26 was previously revised pursuant to the Investment Classification Project in 2017, it was identified that some entities were classifying securities issued from special purpose vehicles (SPVs) in scope of SSAP No. 26 instead of SSAP No. 43. As the focus of this Principles-Based Bond Project is on the substance of investments, regardless of whether they include an SPV for issuance, this project includes all debt securities and encompasses both SSAP No. 26 and SSAP No. 43.

SUMMARY CONCLUSION

2. Investments eligible for reporting as bonds on Schedule D-1[1] shall comply with the principles-based definition of a bond or be specifically noted in scope of SSAP No. 26 or SSAP No. 43. Revisions to reflect the principles-based bond definition have been incorporated to SSAP No. 26, with SSAP No. 43 revised for accounting and reporting guidance for investments that qualify as asset-backed securities under the SSAP No. 26 bond definition. SSAP No. 21 has been revised to detail accounting and reporting guidance for debt securities that do not qualify as bonds under SSAP No. 26 and to provide guidance for the accounting and reporting of residual interests. Lastly, various revisions to other SSAPs have been incorporated to update guidance and/or references to the bond guidance. The final adopted SSAPs and other revisions are shown in the exhibits to this issue paper.

DISCUSSION

3. The discussion of this issue originally began in August 2019 with agenda item 2019-21: SSAP No. 43 – Equity Investments. This agenda item was drafted to consider clarification to SSAP No. 43 particularly with regards to collateralized fund obligations and similar structures that reflect underlying equity interests. In response to the discussion of comment letters in January 2020, this project was expanded to include a

[1] Pursuant to reporting changes adopted in response to the principles-based bond definition, issuer credit obligations (ICO) in scope of *SSAP No. 26—Bonds* will be reported *on Schedule D-1-1: Bonds* and asset-backed security (ABS) investments that qualify as bonds under SSAP No. 26 but follow *SSAP No. 43—Asset-Backed Securities* for accounting and reporting will be reported on *Schedule D-1-2: Asset-Backed Securities*. Throughout this issue paper, these bond investments (both ICO and ABS) are collectively referred to as bonds reported on Schedule D-1.

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comprehensive review of SSAP No. 43 under the Working Group's Investment Classification Project, with NAIC staff directed to prepare a discussion document for subsequent review.

4. A preliminary discussion document was exposed for comment on March 18, 2020. Although there were no proposed recommendations in that exposed document, it captured the following:

a. History of the definition / scope development of SSAP No. 43. (This history has been retained in this issue paper, beginning with paragraph 124.)

b. Definitions of asset backed securities (ABS) from the Code of Federal Regulations (CFR), the Securities Exchange Act of 1934 and NAIC Model 280, Investments of Insurers Model Act (Defined Limits Version).

c. Potential options for the accounting and reporting of ABS based on whether they were considered traditional securitizations in accordance with the Code of Federal Regulations (CFR) (17 CFR 229.1101(c)) definition of an ABS or non-traditional securitizations that did not comply with the CFR definition.

5. In response to this initial exposure, a detailed comment letter dated July 31, 2020, was received from interested parties. Although a variety of elements were noted, two key issues were the primary focus:

a. Separation between SSAP No. 26 and SSAP No. 43: Pursuant to the comments, it was identified that many insurers had different interpretations of the adopted 2010 revisions that separated investments between SSAP No. 26 and SSAP No. 43 due to the presence of a "trust" or an "SPV" structure. As such, investment designs that had been identified as concerning due to the underlying investments in the SPV (e.g., equity-driven investments) believed by some to be limited to SSAP No. 43 were, under some interpretations, eligible to be captured in scope of SSAP No. 26.

b. Defining an asset backed security: The comments received focused heavily on whether the 17 CFR definition captured securities within the 1933 or 1934 Securities Act. The proposed use of the 17 CFR definition, which is the ABS definition used by the SEC as a nationally recognized statistical ratings organization (NRSRO) registered for asset-backed securities, was intended to allow consistency in ABS items permitted for NRSRO designations. Furthermore, it was only the first "broad brush" in determining whether an investment would be initially captured in scope of SSAP No. 43. Regardless, based on the comments received, which noted variations between the 1933 and 1934 Securities Act, differences of assessments based on whether an entity is the issuer or acquirer, the legal scrutiny that may be required in determining whether an investment complies with the definition, as well as a recommendation for independent principles for determining an investment as an asset backed security, it was identified that further discussion should occur before utilizing the CFR definition of an asset-backed security.

6. After considering the interested parties' July 31, 2020, comments, the Working Group directed that a small group of industry work with Iowa representatives and NAIC staff to define what should be considered a bond for reporting on Schedule D-1. It was identified that some investment designs, which have been previously captured on Schedule D-1 or are proposed for inclusion on that schedule, may be well-performing assets, but are not bonds and should not be captured on Schedule D-1. It was also noted that regulators are not anticipating these sorts of investment structures when reviewing D-1 and assessing investment risk. These small group discussions began December 1, 2020, and continued until the bond proposal was initially exposed for public comment on May 20, 2021.

7. After considering the comment letters from the May 2021 exposure, on August 26, 2021, the Working Group affirmed the direction of the principle-based bond concepts and directed NAIC staff to

utilize those concepts in proposing statutory accounting revisions. With this explicit direction, it was noted that all elements of the principles-based bond proposal, and the reflection of those concepts in statutory accounting guidance, is subject to continued discussion and deliberation. Revised guidance for Schedule D-1 investment classification will not be considered authoritative statutory guidance until the specific effective date detailed in adopted authoritative SSAP. With the direction to proceed with the development of statutory guidance to reflect the principle-based concepts, the Working Group directed that NAIC staff continue to work with the small group of regulators and industry to discuss concepts, review proposed language and consider innovating investment designs. (During this meeting, the small group was repurposed and referred to as the "study" group with additional regulators participating.)

8. From September 2021 through January 2022, the study group of regulators and industry met to continue discussions on the bond proposal definition. Key elements discussed during this timeframe included 1) the requirement for a credit enhancement that puts the holder of an ABS in a different economic position from holding the underlying collateral directly, 2) the contractual stapling restriction, and 3) guidance for when a debt instrument is issued from an SPV that owns a portfolio of equity interests. Revisions from these discussions, as well as other aspects to clarify the definition and an initial issue paper were presented to the Statutory Accounting Principles (E) Working Group on March 2, 2022, and exposed. Subsequently, the full Working Group discussed and exposed revisions to the draft guidance until adoption.

9. This issue paper intends to provide information on discussions that occurred when considering the principles-based bond definition and the statutory accounting revisions to specify the types of investments that shall be reported on Schedule D-1: Long-Term Bonds. A summary of the exposure periods and adoption actions are detailed below:

a. On March 2, 2022, this issue paper, along with the principles-based bond definition, was exposed, with comments due May 6, 2022. The Working Group heard comments on July 18, 2022, and directed limited edits to be reflected while also deciding not to incorporate revisions for a number of industry-proposed comments.

b. On August 10, 2022, this issue paper, along with the principles-based bond definition, and proposed revisions to SSAP No. 26 and SSAP No. 43 was exposed, with comments due October 7, 2022. Comments were received from Interested Parties, Fermat Capital and the industry Lease-Backed Securities Working Group. After considering comments, the Working Group incorporated certain revisions.

c. On November 16, 2022, after considering comments from the August 2022 exposure, the Working Group exposed revisions to SSAP No. 26 and SSAP No. 43. The Working Group also exposed revisions to other SSAPs that will be impacted with the bond project revisions. These edits included revisions to detail the short-term and cash equivalent restriction for ABS in *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments* as well as guidance for debt securities that do not qualify as bonds in SSAP No. 21. This guidance was exposed until February 10, 2023.

d. On March 22, 2023, during the 2023 Spring National Meeting, the Working Group considered comments received and exposed updated guidance, with a comment period ending June 9, 2023, to reflect most of the interested party comments.

e. On August 13, 2023, during the 2023 Summer National Meeting, the Working Group adopted the exposed revisions to SSAP No. 26, SSAP No. 43 and the document detailing revisions to other SSAPs with an effective date of January 1, 2025. With this action, it was noted that no comments had been received on these exposed items. Also on August 13, 2023, the Working Group considered comments on the exposed SSAP No. 21 on the guidance for non-bond debt securities that do not qualify as bonds and on residual interests and exposed a revised SSAP No. 21 until September 29, 2023.

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f. On December 1, 2023, during the 2023 Fall National Meeting, the Working Group considered comments received on SSAP No. 21, predominantly focused on the accounting and measurement of residual interests and exposed an updated SSAP No. 21 until January 22, 2024.

g. On February 20, 2024, the Working Group received a revised SSAP No. 21 that was updated to reflect interested parties' comments during the interim. The Working Group exposed the revised SSAP No. 21 for a shortened comment period ending March 7, 2024, to allow for possible adoption consideration during the 2024 Spring National Meeting.

h. On March 16, 2024, during the 2024 Spring National Meeting, the Working Group adopted new statutory accounting guidance within SSAP No. 21 for "Debt Securities That Do Not Qualify as Bonds" and for "Residual Tranches or Interests/Loss Positions." The new sections are effective January 1, 2025, but reporting entities may elect to adopt the residual guidance for year-end 2024. With this action, all planned statutory accounting guidance for the principles-based bond definition was adopted.

Discussion of Principles-Based Bond Concepts

10. Pursuant to the "small group" discussions comprised of industry, Iowa regulators and NAIC staff, the broad principle-based bond concepts discussed on August 26, 2021, reflected the following key concepts:

a. Definition of a bond requires a security structure, representing a creditor relationship, that is considered an Issuer Credit Obligation (ICO) or an Asset Backed Security (ABS).

b. The assessment of whether a security represents a creditor relationship requires consideration of the substance, rather than the legal form of the document, as well as consideration of other investments owned in the investee and other contractual arrangements. A security that possesses equity-like characteristics or that represents an ownership interest in the issuer in substance does not represent a creditor relationship.

c. An ABS is a bond issued by an entity created for the primary purpose of raising debt capital backed by financial assets or cash generating non-financial assets owned by the ABS Issuer, whereby repayment is primarily derived from the cash flows associated with the underlying defined collateral rather than the cash flows of an operating entity.

d. There are two defining characteristics that must be present for a security to meet the definition of an ABS: 1) The holder of a debt instrument issued by an ABS issuer is in a different economic position than if the holder owned the ABS Issuer's assets directly, and 2) When the assets owned by the ABS are non-financial assets, the assets are expected to generate a meaningful level of cash flows towards repayment of the bond other than through the sale or refinancing of the non-financial assets.

11. Various discussions and components were addressed in the establishment of these broad concepts and throughout the development of the principles-based bond definition. Specific elements and discussion points are detailed within this issue paper.

Security Structure Representing a Creditor Relationship

12. Similar to long-standing guidance in defining a bond, the principles-based bond concepts only permit security structures to be considered eligible for Schedule D-1 reporting. Although the concepts continue reference to the adopted security definition from U.S. GAAP, the guidance is expanded to require

that the evaluation of the structure under the security definition considers the substance of the instrument rather than solely its legal form.

13. The consideration of whether a structure reflects a "security" is a key factor in determining the appropriate SSAP for accounting and reporting. A structure with one or more future payments that qualifies as a security has historically been captured as a bond, with measurement and risk-based capital (RBC) charges based on the NAIC designation. Under the prior SSAP guidance, bond securities did not require additional provisions for admittance and would likely only be subject to nonadmittance based on state investment limits. This treatment is distinctly different than a "non-security' structure considered to be a loan under SSAP No. *20—Nonadmitted Assets* or SSAP No. 21. For these structures, the ability to admit the loan under the SSAP provisions is contingent on the nature of the loan and qualifying collateral or related party assessments. (State investment limits may have additional loan-to-value requirements that impact admittance.) Loans (other than mortgage loans) are captured on Schedule BA: Other Long-Term Invested Assets and are likely limited by state investment limits along with other invested assets reported on Schedule BA. Although the RBC charge for admitted collateral loans is lower than other Schedule BA investments, the RBC charge is still higher than Schedule D-1 investments with most NAIC designations.

14. Over time, since the codification of statutory accounting principles, various industry comments have been received questioning the difference between loans and securities (e.g., bonds), particularly with the different reporting outcomes. This discussion was also revisited as part of the principles-based bond proposal, and it was concluded that structures must meet the security definition to be captured as a bond on Schedule D-1. Although industry requested "loans with recourse" to be added to the bond scope paragraph as well as an explicit reference to "loans" as a type of investment captured in the bond definition, these proposals were not supported for inclusion. This discussion highlighted that the security definition is not a high threshold to meet, and direct loans should not be reflected as bonds if they do not qualify as securities. With this discussion it was noted that an investment could meet the definition of a bond regardless of the legal form (paper) it was written on and/or how it was described (such as a bond, note, obligation, etc.). Although an instrument could be described as a "loan," if it meets the security definition requirements and other principle concepts, it shall be captured as a bond. The same concept would be true for instruments named as a "bond" but that do not meet the security or other principle-based bond requirements, as they would not be permitted for reporting as a bond on Schedule D-1.

15. The statutory accounting guidance in SSAP No. 26 and *SSAP No. 37—Mortgage Loans* adopts the U.S. GAAP definition of a security as it is used in FASB Codification Topic 320 and 860:

a. Security: A share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:

i. It is either represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.

ii. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.

iii. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

16. The "security/non-security" discussion highlighted that the naming convention of an investment (as a "note," "bond," "obligation," "loan," or other such term) does not determine the correct underlying SSAP or reporting location. Non-security structures (other than mortgage loans) shall be captured as collateral or non-collateral loans pursuant to SSAP No. 20 or SSAP No. 21 as applicable. To prevent incorrect assumptions that all loans could be captured as issuer credit obligations, the group agreed not to

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include explicit reference to loan structures within the principles-based bond concepts and instead refer to the substance of the investment structure. Additionally, the following existing guidance was noted as support for this conclusion and to further highlight that the naming convention does not override the structural design of an investment when it comes to reporting or the application of statutory accounting principles.

a. Existing guidance in SSAP No. 21 states that if an instrument meets the definition of a bond, but has supporting collateral, then the investment is not classified as a collateral loan. This concept was affirmed as part of the principles-based bond discussion, noting that investments that qualify for bond reporting on Schedule D-1 shall not be classified as collateral loans regardless of whether there is collateral backing the investment.

b. Guidance in *SSAP No. 25—Affiliates and Other Related Parties* applies to all transactions, regardless of the SSAP that governs the underlying accounting and reporting. As such, the provisions in SSAP No. 25 that require assessment of "loans or advances (including debt, public or private)" are intended to apply to all forms of lending from a reporting entity to a related party. As such, this guidance applies regardless of the naming convention of the agreement (e.g., loan, bond, note, obligation, etc.). Investments reported as bonds on Schedule D-1 that reflect related party transactions shall only be admitted if the requirements in SSAP No. 25 are met. In addition to having a specific due date and written agreements, these requirements include specific assessments based on whether the arrangement is with a parent or principal owner or to other related parties.

17. After determining whether a structure represents a security, the next component for the principle-based bond definition is assessing whether the security represents a creditor relationship. Although the reference to a "creditor relationship" may seem very similar to prior guidance in SSAP No. 26, that prior guidance did not explicitly detail the intended meaning of a "creditor relationship" but simply identified that such structures have a fixed schedule for one or more future payments. This prior guidance resulted with interpretations that structures qualified as "bonds" strictly on legal form. With the focus of the principles-based definition, it is explicit that the assessment of a whether a security represents a creditor relationship requires consideration of the substance, rather than just the legal form, along with consideration of other investments owned in the investee and other contractual arrangements.

18. Original regulator concerns with the historical guidance and reporting were in part due to the identification of investments with underlying equity interests that were structured to resemble bond instruments. Discussions that occurred as part of the principles-based bond project identified that there is a significant incentive for insurers to characterize equity exposures, which would traditionally be captured on Schedule BA, as bonds due to the favorable capital treatment. Transferring or acquiring them as debt issued by an SPV (such as through a collateralized fund obligation (CFO) structure) is a mechanism to reclassify these equity instruments and characterize them as bonds. These discussions noted that the lack of historical safeguards in existing SSAPs also provides significant opportunity for these reclassifications.

19. Equity investments differ from other types of financial assets in that they generally do not have contractual pre-determined principal or interest payments. Distributions are typically at the discretion of whichever decision maker has control of the entity. However, certain types of entities have greater likelihood and predictability of cash flows than others. For example, private equity and debt funds are often designed to have finite lives that begin with a capital raising and investment phase, and once the portfolio is built and seasoned, investments are monetized, returns are realized, and distributed to investors. Therefore, while there can be variability in timing and amounts of cash flows, distributions can be expected with some level of predictability compared to other types of equity investments (e.g., publicly traded companies). Private debt funds are more predictable still given that the underlying investments of the fund have contractual cash flows. If a large, diversified pool of seasoned funds are securitized, (often in the form of a CFO), there can be a level of predictable cash flows that is suited to support a bond, when coupled with the overcollateralization, liquidity facilities, and other protections that are built into the structure.

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20. Regulator concerns arise when features that facilitate the production of predictable cash flows are not present. In such situations, when there are not predictable cash flows equipped to service the debt, repayment may rely on sale or refinancing of the underlying equity investments at maturity in order to satisfy the debt. In that case, equity valuation risk may be the primary risk for the non-payment of the issued debt. If repayment predominantly relies on a point-in-time equity valuation (such as at maturity), then the substance of the risk is not consistent with what is expected of a bond reported on Schedule D-1.

21. Although the full disallowance of equity-backed debt would prevent these regulator concerns, there is a position that there are CFO securitizations (or other investments) of well-diversified, seasoned funds for which there is compelling evidence that there will be sufficient cash distributions to amortize the debt and structure protections that minimize the residual equity exposure. The approach to allow such CFO securitizations/investments to be reported as bonds only works when there are appropriate safeguarding principles established, which require a relatively high standard of proof.

22. An investment for which the primary non-payment risk is equity devaluation is not consistent with the substance-intent for what is expected to be reported as a bond on Schedule D-1 under the principles-based definition. Allowing such investments to be reported as bonds on Schedule D-1 could result with the regulatory arbitrage that regulators are concerned about without any real mitigants. This could ultimately result in a situation where industry has taken on significantly more equity risk that they have historically, all while characterizing the investment as a bond exposure. As such, it was noted as critical that appropriate safeguards be incorporated into the principles-based bond definition to address this concern. This is why the guidance reflects a rebuttable presumption that equity-backed ABS do not qualify to be reported as bonds on Schedule D-1 unless a documented analysis supporting the predictability of cash flows is completed that demonstrates bond-like cashflows that supports different treatment from that presumption.

23. The principles-based bond definition is clear that a security that possesses equity-like characteristics or that represents an ownership interest in the issuer in substance does not represent a creditor relationship. Examples of equity investments, equity holdings and equity-like interests include any security ultimately reflecting an ownership or membership interest in an entity (such as common stock, preferred stock, private equity holdings, investments in joint ventures, partnerships, and LLCs) as well as any structure that reflects the performance of an entity (such as dividends or capital gains). Furthermore, examples of equity instruments also include any debt instrument where the risk/reward profile is substantially similar to an equity interest.

24. With the prohibition of equity-like structures or items that represent ownership interests, there is a rebuttable presumption that debt instruments collateralized by equity interests do not qualify as bonds because they do not reflect a creditor relationship in substance. Notwithstanding this rebuttable presumption, it is possible for such a debt instrument to represent a creditor relationship if the characteristics of the underlying equity interests lend themselves to the production of predictable cash flows and the underlying equity risks have been sufficiently redistributed through the capital structure of the issuer.

25. With the establishment of the principles-based bond definition, this rebuttable presumption was specifically discussed, and it was concluded that the determination of whether debt instruments collateralized by equity interests qualify as bonds inherently requires significant judgment and analysis. Unlike debt instruments collateralized with contractual cash flows, or debt instruments collateralized by cash-generating non-financial assets, debt instruments collateralized by equity interests may be dependent on cash flow distributions that are not contractually required to be made, predetermined, and/or may not be controlled by the issuer of the debt. In some instances, sale or refinancing of the underlying equity interests may be the only means of generating cash flows to service the debt instruments. If this is the situation, then it is expected that compensating factors from other characteristics of the structure will be present that supports classifying the investment as a bond. For example, if the source of cash flows is driven from the sale or refinancing, then an appropriate, compensating level of overcollateralization would be required to overcome the presumption that the structure does not qualify as a bond.

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26. For debt instruments that are collateralized by equity interests, various factors should be considered in determining whether debt collateralized by equity interests qualify as bonds. Additionally, to overcome the presumption that the structure does not qualify as a bond, it is presumed that reporting entities will have sufficient documentation supporting this conclusion. Factors to consider include, but are not limited to, the following:

a. Number and diversification of the underlying equity interests

b. Characteristics of the equity interests

c. Liquidity facilities

d. Overcollateralization

e. Waiting period for the distributions / paydowns to begin

f. Capitalization of interest

g. Covenants (e.g., loan-to-value trigger provisions)

h. Reliance on ongoing sponsor commitments

i. Source(s) of expected cash flows to service the debt (i.e., dividend distributions from the underlying collateral vs. sale of the underlying collateral)

27. The assessment of equity-backed securities should be looked at, not only in form, but in substance. For example, a common arrangement exists where debt is issued from a feeder fund, and the feeder fund has an equity interest in another fund which predominantly holds debt instruments. The fund passes those fixed-income cash flows through the structure to the ultimate feeder fund debt holder(s), in a way that produces substantially the same risk profile to the debt holders as a collateralized loan obligation (CLO). Accordingly, such an arrangement may have its substance aligned with a debt investment rather than a single equity investment, despite the direct holding being a fund investment. This conclusion would be supported if the terms of the structure ensure that the underlying fixed-income cash flows are passed through. Factors that add additional uncertainty as to the timing and/or amount of the pass-through of cash flows from the underlying debt instruments may call into question a conclusion that a feeder fund structure is a debt-backed structure in substance. For example, discretion of an underlying fund manager to withhold distribution of the underlying cash flows passed through from underlying debt instruments may create uncertainties as to the timing and/or amount of cash flows in such a manner that is more characteristic of an equity investment. Likewise, a feeder fund structure that is not expected to provide for regular cash interest payments would also call into question the substance as a debt-backed investment. Features that are customary to CLOs and other asset-backed securities would not ordinarily call the investment's substance into question on its own. For example, a waterfall structure dictating the pass-through and order of payments or retaining sufficient funds for covering contractual underlying fund level payments (e.g., investment management fees, legal costs, and other customary fund level expenses) are common to CLOs and other ABS, as are customary payment in kind (PIK) features designed to address temporary liquidity issues where the PIK then gets prioritized in the waterfall structure. These customary features do not constitute manager discretion that would call into question a conclusion that a feeder fund structure is a debt-backed structure in substance.

28. Conversely, if the feeder fund debt ultimately relies on equity interests for repayment (the final fund holds equity interests that generate the pass-through cash flows), the held debt instrument from the feeder fund would have to meet the requirements of paragraph 26 while looking at the substance of equity interests supporting the debt. Regardless of the underlying collateral, feeder fund arrangements would have to meet the other relevant parts of the standard (e.g., have a substantive credit enhancement, etc.) to qualify for bond reporting. Investments that resemble feeder fund structures will require entity review to determine the

underlying source of cash flows and identify the uncertainties or vulnerabilities that could impact the cash flows that will be passed through to the reporting entity holder. Ultimately, the conclusion that a structure represents a feeder fund shall not automatically qualify the structure for bond classification but shall not automatically preclude bond classification. Substance over form should be the determining factor in these and similar situations.

Determination of Issuer Credit Obligation or Asset Backed Security (ABS)

29. Security structures that qualify as creditor relationships are divided between ICO and ABS. The initial distinction between ICO and an ABS is a key factor with the principle-based bond concepts. Given their differing characteristics, investments that qualify as ICO are not required to complete assessments for qualifying credit enhancements or meaningful cash flow generation. As such, it is critical to ensure that structures which should be considered ABS or that reflect non-qualifying Schedule D-1 structures, are not classified as ICO to avoid those detailed assessments.

30. Determining whether an investment reflects an ICO or an ABS focuses on the issuer and the primary source of repayment of the instrument. An ICO represents a bond structure where the repayment is supported primarily[2] by the general creditworthiness of an operating entity or entities. The support for this structure consists of direct or indirect recourse to an operating entity or entities. An "operating entity" can be any sort of business entity, not-for-profit organization, or other provider of goods or services, but cannot be a natural person or an Asset Backed Security (ABS) Issuer. An ABS is a bond issued by an entity (an ABS Issuer) created for the primary purpose of raising debt capital backed by financial assets or cash generating non-financial assets owed by the ABS Issuer, whereby repayment is primarily derived from the cash flows associated with the underlying defined collateral rather than the cash flows of an operating entity.

31. The prior assessments to divide structures between SSAP No. 26 and SSAP No. 43 seemed to focus primarily on legal form (issued by trust/SPV that held pledged assets) or on the basis of prepayment risk within the structure (meaning, that the expected timing of cash flows may vary, impacting the effective interest rate). Under the principle-based bond definition, neither of these components shall be used as a determinant in concluding whether a structure represents an ICO or an ABS.

a. The prior guidance which focused on the use of an SPV relied more on legal form than the substance of the transaction. Although it is common that many ABS Issuers are in the form of a trust or SPV, the presence or lack of a trust or SPV is not a definitive criterion in determining that a security meets the definition of bond intended as a Schedule D-1 investment, or that it is limited to a classification as an ABS. A key component of the principles-based bond definition is that it will not be possible for insurers to classify a non-qualifying investment as a bond simply by moving it to a debt-issuing SPV that resembles a creditor relationship with a future payment obligation. Furthermore, the guidance does not preclude the use of SPVs in ICO structures. Such structures are commonly utilized in project finance arrangements to separate business operations that support specific debt instruments, or to facilitate efficient marketing of an specific ICO design (e.g., funding agreement backed notes). Although packaging investments together in an SPV, with an

[2] To clarify the phrase "supported primarily by the general creditworthiness of an operating entity," this means that the full repayment is expected to come from cash flows generated by the operating entity, not from collateral, although secondary recourse to collateral may be present. If it is expected that a majority of repayment will come from operating entity cash flows, but it is expected that some cash flows will come from collateral, this investment does not qualify as an issuer credit obligation and shall be assessed as an asset-backed security. The expectation must be that full repayment will be generated from operating entity cash flows. For asset-backed securities, the expectation is that the source of cash flows will come from collateral, even though there may be secondary recourse to an operating entity.

SPV-issued note may currently result with better RBC charges due to the current ability to report such items as bonds, structures that simply reflect a pass-through of cash flows or performance from the underlying collateral and provide no economic difference than if holding the underlying collateral items directly shall not be characterized as bonds under the principles-based bond definition.

b. With regards to the prior interpretation that SSAP classification was based on the presence of prepayment risk, which was not an interpretation based on any explicit guidance to that effect, under the principles-based bond definition, the presence or absence of prepayment risk will continue to play no role in SSAP classification. Classification is based on whether the investment has the substance of an ICO or ABS. This distinction aligns the accounting and measurement with the characteristics of the bond structure. As ABS rely on the cash flows of underlying collateral, the measurement method described in SSAP No. 43, which requires a quarterly review of underlying cash flow assumptions, is appropriate regardless of whether variations in timing of cash flows impact the effective yield. This methodology captures variations in both timing and amount of the underlying cash flows.

32. Whether an issuer of debt represents an operating entity or ABS Issuer is expected to be clear in most instances, but certain instances may be less clear. Ultimately, for an ICO, it comes down to whether support for repayment consists of direct or indirect recourse to an operating entity or entities. In addition to "traditional bond" structures previously included in SSAP No. 26, examples of issuer credit obligations include:

a. Investments in the form of securities for which repayment is fully supported by an underlying contractual obligation of a single operating entity. Examples can include credit tenant loans (CTLs), equipment trust certificates (ETCs), other lease backed securities, Funding Agreement Backed Notes (FABNs), etc. For purposes of applying this principle concept, repayment is fully-supported by the underlying operating entity obligation if it provides cash flows for the repayment of all interest and at least 95% of the principal of the security.

b. Bonds issued by real estate investment trusts (REITS) or similar property trusts.

c. Bonds issued by business development corporations, closed-end funds or similar operating entities, in each case registered under the 1940 Act. With this inclusion, it is important to highlight that the intent is specific to bonds issued from SEC-registered entities. The reference to "similar entities" is not intended to capture items issued from collateralized fund obligations (CFOs), feeder funds or other such structures. Although some may consider CFOs to be similar to closed-end funds, that assessment is not supported for classification as an ICO. Instruments considered to reflect CFOs (and other like structures) are required to be assessed as ABS for inclusion as a bond reported on Schedule D-1. Paragraphs 27-28 also detail the assessment expected in classifying feeder funds, and the requirement to determine the source of the underlying cash flows in determining classification and if the structure qualifies for reporting as a bond on Schedule D-1.

Note: Paragraph 32.c. will be revised with adoption of agenda item 2024-01.

d. Project finance debt issued by operating entities. These investments reflect financing of a single asset or "operation" (such as a toll road or power generation facility) that collateralizes a debt issuance and the cash flows produced by the asset/operation service the debt, where the issuer may also represent an operating entity. These designs have characteristics of both ICO, as the operation constitutes a stand-alone business, as well as characteristics of ABS, as they are formed for the purpose of raising debt capital backed

by the cash flows from collateral held by a bankruptcy-remote entity. When viewed holistically, these issuing entities are typically used to facilitate the financing of an operating component of a project sponsor or municipality. Although the use of a bankruptcy-remote entity (e.g., SPV) facilitates the efficient raising of debt as a source of financing, the primary purpose is to finance an operating project. Therefore, when the issuing entity represents a stand-alone business producing its own operating revenues and expenses, where the primary purpose is to finance an operating project, the issuing entity shall be considered an operating entity despite certain characteristics that resemble ABS issuances.

i. It is important to highlight that the guidance for project finance is strictly for instruments issued by operating entities, similar to other instruments that qualify as ICO under the principles-based bond definition. Consistent with other concepts, the naming convention (e.g., referring to an instrument as project finance) or the presence or absence of an SPV/trust structure are not definitive components in determining whether an investment qualifies for reporting as a bond on Schedule D-1, or is classified as an ICO or ABS. Instruments (even if identified as "project finance") that do not qualify as ICO as they are not issued by operating entities, shall be assessed for qualification for reporting on Schedule D-1 as ABS. If the instruments do not qualify for reporting as ABS, they shall not be reported on Schedule D-1.

e. U.S. Treasury Inflation-Protected Securities (TIPs): The inclusion of U.S. TIPs specifically as an ICO intends to highlight a specific exception to the determination as a creditor relationship as the variation is due to plain-vanilla inflation adjustment mechanisms. Although U.S. TIPs are specific as ICO, under the bond definition, in order for a debt instrument to represent a creditor relationship for both ICO and ABS, it must have pre-determined principal and interest payments (whether fixed interest or variable interest) with contractual amounts that do not vary based on the appreciation or depreciation (e.g., performance) of any underlying collateral value or other non-debt variable[3]. For example, an issued security that has varying principal and interest payments based on the appreciation of referenced equity, real estate or other non-debt variables are precluded from bond treatment as they do not reflect creditor relationships. Although US TIPS are indexed to the consumer price index and grow with inflation, these securities shall be captured as ICO on Schedule D-1-1.

33. This principles-based bond project is not expected to reconsider certain investments previously considered by the Working Group and explicitly permitted for bond reporting on Schedule D-1. As such, unless subsequently addressed, the following investment types are expected to continue to qualify as Schedule D-1 investments, classified as ICO. (By including these investments as ICO, these investments are not subject to the assessments of sufficient credit enhancement or meaningful cash flow generation required for ABS securities.)

[3] The principles-based bond definition requirement for pre-determined principal and interest payments with contractual payments that do not vary based on the performance of an underlying collateral value or other non-debt variable does not intend to encompass nominal interest rate adjustments. Nominal interest rate adjustments are those that are too small to be taken into consideration when assessing the investment's substance as a bond. Nominal adjustments are not typically influential factors in an investors' evaluation of investment return and are often included to incentivize certain behavior of the issuer. An example would include sustainability-linked bonds where failure to achieve performance metrics could cause interest rate adjustments. In general, interest rate adjustments that adjust the total return from interest by more than 10% (e.g., >0.4% for a 4% yielding bond), would not be considered nominal. Further, any such adjustments that cause an investment to meet the definition of a structured note would not be considered nominal.

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a. Certificates of deposit that have a fixed schedule of payments and a maturity date in excess of one year from the date of acquisition.

b. Bank loans that are obligations of operating entities, issued directly by a reporting entity or acquired through a participation, syndication or assignment.

c. Debt instruments in a certified capital company (CAPCO).

d. SVO-Identified Bond ETFs.

34. The investment structures explicitly permitted for Schedule D-1 reporting no longer includes a generic reference to "hybrid securities." Under prior guidance in SSAP No. 26, hybrid securities, defined in the annual statement instructions as securities with characteristics of both debt and equity securities, were included and captured on a specific Schedule D-1 reporting line. Examples in the annual statement instructions included Trust Preferred Securities and Yankee Tier 1 bonds, however, both types of securities are no longer overly prevalent, although some insurers may continue to have them in their portfolios. Pursuant to the intent of the principle-based bond definition, a broad exception for securities that have characteristics of both debt and equity is not viable. Rather, to ensure that securities are classified and reported based on the substance of the investments, securities with characteristics of both debt and equity shall be assessed for inclusion as a bond for reporting on Schedule D-1 in accordance with the principal-based bond definition. If the securities qualify as ICO or ABS, then they can be reported on Schedule D-1.

a. Trust Preferred Securities – With these securities, there is a trust funded by debt where shares of the trust are then sold to investors in the form of preferred stock. The shares held are referred to as "trust preferred" securities. These securities have characteristics of both stock and debt. While the trust is funded with debt, the shares are considered to be preferred stocks and pay dividends like preferred stock. However, since the trust holds the bank's debt as the funding vehicle, the payments received by investors are considered interest payments. These securities are considered equities under U.S. GAAP but are taxed as debt obligations by the IRS. With the Dodd-Frank reforms, the incentives for banks to issue trust-preferred securities decreased, resulting in a significant reduction in the issuance of these securities. If these securities continue to be held by insurers, they should be assessed for reporting as a bond on Schedule D-1 under the principal-based bond definition. If these securities do not qualify as a bond for reporting on Schedule D-1, presumably, these securities would be reported as preferred stock on Schedule D-2-1.

b. Yankee Bond – A Yankee bond is one issued by a foreign bank or company but that is traded in the U.S and priced in U.S. dollars. Yankee bonds are normally issued in tranches, with a large debt structure financing arrangement, with each tranche having different levels of risk, interest rates and maturities. The non-U.S. issuers have to register Yankee bonds with the SEC before offering the bond for sale. If these securities are held by insurers, they should be assessed for reporting as a bond on Schedule D-1 under the principal-based bond definition.

c. Other Hybrid Securities – From information received, it was noted that some reporting entities have previously reported securities on Schedule D-1 as hybrids due to a code in Bloomberg that identified the security as having characteristics of both debt and equity. Such securities shall be reviewed in accordance with the principles-based bond definition and reported as a bond on Schedule D-1 only if they qualify.

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35. For securities that represent principal-protected securities and structured notes that have been previously captured within SSAP No. 26 or SSAP No. 43, the principles-based bond definition will no longer permit these security structures to be reported as bonds on Schedule D-1. Fundamentally, these structures have the potential for variable principal or interest / returns, or both, due to appreciation or depreciation (i.e., performance) of an underlying collateral value or other non-debt variable. This structural characteristic precludes these investments from being captured as ICO or ABS as the investment does not represent a creditor relationship in substance. It should be clear that the principles-based bond definition is intended to require a structural assessment inclusive of all investment components, therefore it is not permissible to segregate components within a structure, such as bond collateral supporting principal and interest payments to determine bond reporting on Schedule D-1 when the structure also includes other collateral with the potential to generate additional interest or returns. Such structures must be viewed holistically within the principles-based bond definition, with all potential returns considered in determining whether the structure qualifies as a creditor relationship.

a. A principal-protected security is defined in *the Purposes and Procedures Manual of the NAIC Investment Analysis Office*, but generally includes a high-quality traditional bond (such as a U.S. Treasury) that is used to safeguard principal repayment at the structure's maturity, along with performance components where payments originate from, or are determined by, non-fixed-income securities. These returns, often based on underlying equity factors, prevent these structures from qualifying as a creditor relationship. In addition to the traditional design of principal-protected notes, other designs have been identified that may provide "interest" payments in the form of tax-credits based on underlying equity exposures. (So, a high-quality bond safeguards principal returns, but the structure includes equity elements that provide tax credits to the note holder as a form of interest.) Although the classification of a creditor-relationship may not be as clear in this example, such designs would further be disqualified from reporting as a bond on Schedule D-1 as they would not qualify as ICO due to the different forms of collateral within the structure (considering both the bond and equity items) and such structures would not qualify as ABS as there is generally no credit enhancement. These investments shall follow the guidance for non-bond debt securities in *SSAP No. 21—Other Admitted Assets*.

b. A structured note is a security that otherwise meets the definition of a bond, but for which the contractual amount of the instrument to be paid at maturity (or the original investment) is at risk for other than failure of the borrower to pay the principal amount due. These instruments, although in the form of a debt instrument, incorporate the risk of an underlying variable in the terms of the agreement, and the issuer obligation to return the full principal is contingent on the performance of the underlying variable. These investments are addressed in *SSAP No. 86—Derivatives.* Mortgage-referenced securities issued by a government sponsored enterprise are explicit inclusions in scope of SSAP No. 43. Foreign-denominated bonds subject to variation as a result of foreign current fluctuations are not structured notes.

36. The guidance in the principles-based bond definition requires "assessment at origination" in determining whether a security qualifies for reporting as a bond on Schedule D-1. This provision intends to reflect the reporting entity's understanding of the intent and ultimate structure of the security's focus at origination, not simply what a structure holds on the day of origination. It is not permissible to conclude that a principal-protected security is an ICO at origination (when the structure includes only a US Treasury and cash) and disregard the intended use of the cash in the structure to subsequently acquire other investments to generate additional returns. The determination of whether an investment qualifies as a

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creditor-relationship, and then as an ICO or ABS (as applicable), requires an assessment by the reporting entity of the full structure at the time of acquisition as it was ultimately intended by the issuer at the time of origination.

37. Consistent with prior guidance in SSAP No. 26, mortgage loans and other real estate lending activities, which are not securities, made in the ordinary course of business are excluded from bond classification on Schedule D-1. Those investments shall follow the applicable statutory accounting guidance in SSAP No. 37 and *SSAP No. 39—Reverse Mortgages*.

Asset Backed Securities and Required Components

38. An ABS is a bond issued by an entity (an ABS Issuer) created for the primary purpose of raising debt capital backed by financial assets or cash generating non-financial assets owed by the ABS Issuer, whereby repayment is primarily derived from the cash flows associated with the underlying defined collateral rather than the cash flows of an operating entity. In most instances, the ABS Issuer is not expected to continue functioning beyond the final maturity of the debt initially raised by the ABS Issuer. As previously noted, ABS Issuers are often in the form of a trust or special purpose vehicle, though the presence or lack of a trust or special purpose vehicle is not a definitive criterion for determining that a security meets the definition of an asset backed security.

39. To qualify for bond reporting on Schedule D-1 as an ABS, there are two defining characteristics that must be present. If the structure is a not an ICO or identified for specific inclusion on Schedule D-1, and does not meet these ABS requirements, the instrument is not permitted to be reported as a bond. Assessment on these aspects is investment specific, with determination at origination by the reporting entity based on the overall intent and ultimate expected holdings of the structure:

a. Substantive Credit Enhancement: The holder of the debt obligation issued by the ABS Issuer is in a different economic position than if the holder owned the ABS Issuer's assets directly.

b. Cash Generating Collateral Assets: The assets owed by the ABS Issuer are either financial assets or cash-generating non-financial assets. Cash-generating non-financial assets are defined as assets that are expected to generate a meaningful source of cash flows for repayment of the bond through use, licensing leasing, servicing or management fees, or other similar cash flow generation other than through the sale or refinancing of the assets.

40. Substantive Credit Enhancement: The component for substantive credit enhancement is required for all ABS structures. There are no practical expedients or thresholds that can be applied in determining whether a structure reflects substantive credit enhancement. Although certain structures may only require a limited analysis (such as agency-backed mortgage-backed securities—MBS), and insurers may benefit from prior analysis when acquiring similar subsequent structures, an automatic assessment is not permitted for this requirement.

41. To qualify as an ABS, the holder of the debt obligation is required to be in a different economic position than if the holder owned the ABS issuer's assets directly. For purposes of this assessment, the holder of the instrument is considered to be in a different economic position if the instrument benefits from substantive credit enhancement through guarantees (or other similar forms of recourse), subordination and/or overcollateralization. This element is required for all ABS designs, regardless of the collateral that is backing the ABS.

42. The requirement for substantive credit enhancement is intended to address investment designs crafted to appear as a debt / bond structure for reporting and RBC purposes, but for which the holder does

not have a "more than nominal" change to the risk or reward profile than if they held the underlying investment directly. This guidance prevents using a specifically designed legal form (such as transferring assets to an SPV and acquiring an SPV-issued note), but which lacks any economic substance, to obtain favorable measurement and RBC impact or to avoid nonadmittance that would occur if the assets were directly held by the reporting entity.

43. The intent of the "substantive" threshold requiring the holder to be in a different economic position is to distinguish qualifying bonds from instruments with equity-like characteristics or where the substance of the transaction is more closely aligned with that of the underlying collateral. To qualify as a bond under this standard, there is a requirement that there are substantive credit enhancements within the structure that absorb losses before the debt instrument being evaluated would be expected to absorb losses. This is inherent in the context of an ICO as the owners of the equity in the operating entity are the first to absorb any variability in performance of the operating entity. The same concept applies to ABS. If substantive credit enhancement did not exist, the substance of the investment would be more closely aligned with that of the underlying collateral than that of a bond. Credit enhancement that is merely nominal or lacks economic substance does not put a holder in a different economic position.

44. The original exposure (May 2021) detailed this ABS requirement as a "sufficient" credit enhancement and detailed the provision as the level of credit enhancement a market participant (i.e., reasonable investor) would conclude is expected to absorb losses (or decreases in cash flows) to the same degree as other debt instruments of similar quality, under a range of stress scenarios (i.e., scenarios are similar to stress scenarios performed for other debt instruments of the same quality). This original proposal noted that losses are those a market participant would estimate with consideration of historical losses (including loss recoveries) on similar collateral, current market conditions, reasonable and supportable forecasts, and prepayment assumptions associated with the collateral. Excluded from the estimate of expected losses are historical gains on similar collateral and expected market appreciation on the collateral. After further discussion of this concept, it was identified that the term sufficient and its proposed definition implied a quantitative assessment of credit quality was required. As a result, the proposed concept could be interpreted to mean that a reperformance of the credit underwriting process would be needed to support accounting classification, which is not the intent and could be seen to violate the policy that credit ratings do not determine accounting classification, as well as introduce an administrative reporting burden that is both duplicative and lacking any added value. Further, a misinterpretation could occur that would permit satisfaction of this component if a credit rating or NAIC designation was obtained. The intent of the concept is not to address credit quality. Rather, the intent is to require that there must be economic substance to support the transformation of the underlying collateral risk, to bond risk. As a result of these discussions, revisions were incorporated to revise the terminology and related definition to reflect a "substantive credit enhancement." In addition to eliminating a perception that reporting entities could use credit ratings to support this distinction, this guidance incorporates principle concepts to ensure that the provision cannot be satisfied with structural elements that are merely nominal or lack economic substance.

45. Substantive credit enhancement can come in various forms, including but not limited to, subordination/overcollateralization, guarantees, or other forms of recourse. In whatever form the credit enhancement comes in, it must be of a level of significance that the holder of the debt instrument is in a substantively different position than owning the underlying collateral directly. Assessment of whether a credit enhancement has substance may involve an evaluation of the level of overcollateralization (loan-to-value or LTV) or the capacity of whatever form of subordination, guarantee or recourse to absorb collateral losses. The guidance intends to be specific that an NAIC designation, obtained from either the NAIC Securities Valuation Office (SVO) or from a Credit Rating Provider (CRP) does not provide standalone evidence to support a conclusion that the structure includes a substantive credit enhancement. Although the presence of independent market validation may provide evidence supporting the substance of a credit enhancement, that provision shall not be interpreted to indicate that the presence of an NRSRO rating is automatic validation that the substantive threshold has been met.

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46. The following elements were specifically discussed with regards to the requirement for a substantive credit enhancement:

a. Agency-Backed Pass-Through Structures (e.g., RMBS/CMBS): These structures, when they have an agency guarantee, are expected to meet the substantive credit enhancement requirement with little analysis. Although the reporting entity participates on a proportional basis in the cash flows from the underlying mortgage loans held by the SPV, the reporting entity is in a different economic position than if it owned the underlying mortgages directly because the credit risk has been redistributed and assumed by the agencies.

b. Non-Agency Backed Pass-Through Structures: Unlike the above agency-backed example, a pass-through MBS without a credit enhancement, if one were to exist, would not put the holder in a different economic position as owning the mortgage loans directly as they would participate proportionally in the first dollar of losses on the underlying loans. Pursuant to the intent of the overall principles-based bond / Schedule D-1 project and required substantive credit enhancement, the guidance does not permit use of an SPV to recharacterize an asset to qualify for reporting as a bond on Schedule D-1 if the holder is in the same economic position as holding the underlying investments directly. This would apply to any type of underlying asset. In contrast, if a debt instrument represents a senior interest in the pool of loans, through existence of a subordinated tranche for example, the holder may conclude that it is in a different economic position from holding the loans directly, provided the subordination is determined to be substantive.

c. Loan-To-Value (LTV) Assessments: An assessment of LTV at origination may provide evidence of substantive credit enhancement through overcollateralization. The review should be a holistic assessment, evaluating the expected LTV over the life of the transaction, in conjunction with the liquidity and market value volatility of the underlying collateral, particularly in points in time when the underlying equipment is expected to be off-lease or at the time of maturity if refinancing or sale is required. It is appropriate to consider any expected economic depreciation, but it is not appropriate to factor in any expected economic appreciation. Although an expected decline in the LTV ratio may support the presence of a credit enhancement, a declining LTV is not required, and an increasing LTV is not prohibited, as long as the structure continues to provide a substantive credit enhancement. An expected high LTV at maturity, relative to the market value volatility of the underlying collateral, is considered to lack substantive overcollateralization and would require other forms of credit enhancement in order to meet the substantive credit enhancement criteria.

d. The first loss position may be issued as part of an ABS structure in the form of debt or equity interest, or it may be retained by the sponsor and not be issued as part of the structure. The holder of the loss position, regardless of if it is issued as a tranche or retained by the issuer, does not impact the determination of whether the loss position provides substantive credit enhancement. Rather, the assessment focuses on whether the holder of the debt instrument is in a substantively different position than owning the underlying collateral directly. This assessment includes consideration on the first loss position (or more senior positions, if the first loss position is not sufficient) regardless of the holder of the loss positions. If the first loss position (or a more senior position(s), if the first loss position(s) lacks substantive credit enhancement) is issued as part of the structure and does not have substantive credit enhancement and is held by a reporting entity, the investment(s) does not qualify for reporting as a bond as it is a residual interest. All residual interests shall follow the accounting and reporting guidance in SSAP No 21.

47. Meaningful Level of Cash Flows to Service Debt: The element for meaningful cash flow generation is only a requirement for ABS that are backed by non-financial assets. ABS designs backed by financial

assets, when there is no future performance obligation outside of default risk that could impact the ability to generate cash flows to service the debt, are not required to be assessed under the meaningful cash flow requirement.

48. To qualify as an ABS, there must be a meaningful level of cash flows generated from non-financial assets backing an ABS to service the debt, other than through the sale or refinancing of the assets. The evaluation is specific to each transaction and should consider the market volatility and remarketing potential of the underlying collateral, the variability of the cash flows produced, as well as the diversification of the source of cash flows within the structure. The main intent of this guidance is to ensure that non-financial assets supporting structures reported as bonds on Schedule D-1 encompass a level of "cash generation" that is conducive to servicing traditional bond-like cash flows.

49. Consistent with the substance theme of the principles-based bond proposal, this guidance intends to prohibit situations in which the legal form of an investment is utilized to receive favorable accounting and reporting treatment, while the primary non-payment risk is the point-in-time valuation of an underlying asset. The prior guidance in SSAP No. 43 that focused on placing collateral assets in trust, with the SPV issuing a debt instrument, enabled situations in which non-cash generating structures could be reported as bonds on Schedule D-1. As a simple example, this guidance prevents artwork from being captured as the collateral backing a debt instrument issued by an SPV, with the reporting entity then reporting the SPV-issued note as a bond investment that reflects the expected future value that will be received upon the ultimate sale of the artwork.

50. The guidance requires meaningful cash generation to satisfy the debt instrument throughout the duration of the debt term. The timing of the cash generation, at points prior to maturity of the investment, is a key element as it intends to specifically exclude transactions in which the underlying assets must be sold or refinanced at maturity to produce cash to meet the meaningful requirement. However, this restriction is not intended to automatically exclude all structures that may incorporate collateral asset sales or refinancing throughout the debt duration as part of the expected cash generation. An example could be the securitization of short-term rental car receivables. Such a design could encompass both the rental car lease payments as well as periodic sales of the rental cars as the means to generate meaningful cash flows to service the debt. This design, with planned periodic sales of the non-financial collateral assets over the debt term, is distinctly different than a structure in which cash flows are not meaningfully generated over the course of the debt term and would rely predominantly on the sale or refinancing of the underlying collateral at maturity to satisfy the debt obligation. This restriction also does not exclude all structures that have any amount of sales or refinancing at the end of the debt term. Such investments can qualify for reporting as a bond on Schedule D-1 if they meet the meaningful cash generation criteria throughout the term of the instrument other than through the sale/refinancing at maturity.

51. The assessment of meaningful cash flows may require detailed evaluations as it is not permissible to conclude that the presence of any cash flows generated within the structure will result with the investment reaching the "meaningful" threshold. It is also not expected to commonly see ABS structures that include both financial and non-financial collateral. Such designs shall be reviewed to determine that the structure is in line with the principle intent of the bond definition and has not been developed to circumvent separate assessment or reporting of non-financial asset components. As a simplistic example, including mortgage-backed securities and artwork in a single structure, and identifying that the cash flows of the MBS satisfies the meaningful threshold with the artwork representing a minimal residual element, with a conclusion that the full structure qualifies for reporting as a bond on Schedule D-1 is not reflective of the intent of the principles-based standard. If there are instances in which financial asset and non-financial asset collateral are combined in a single ABS structure, consideration should occur on the intent of commingling these collateral elements pursuant to the intent of the principles-based bond definition and in assessing the meaningful cash flow requirements. Structures identified that have been developed to circumvent the provisions of the principle-based bond definition are not permitted to be reported as a bond on Schedule D-1 and shall be captured as a non-bond debt security in scope of SSAP No. 21.

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52. The assessment of meaningful cash flows is specific to each transaction, determined at origination, and should consider various factors collectively in determining if the meaningful threshold is met. For this assessment, it is noted that an increase in price volatility or variability of cash flows requires a greater percentage of cash flows generated to service the debt from sources other than the sale or refinancing of the underlying collateral. On the flip side, as liquidity, diversification or overcollateralization increase, the required percentage of cash flows generated to service the debt from sources other than the sale or refinancing of the underlying collateral is permitted to decrease. The following factors should be considered with the assessment of meaningful cash flows:

a. Price volatility in the principal market in the underlying collateral.

b. Liquidity in the principal market for the underlying collateral.

c. Diversification characteristics of the underlying collateral (i.e., types of collateral, geographic locations, sources of cash flows within the structure, etc.,)

d. Overcollateralization of the underlying collateral relative to the debt obligation.

e. Variability of cash flows, from sources other than sale or refinancing, expected to be generated from the underlying collateral.

53. The assessment of meaningful cash flows does permit a practical expedient under the principles-based bond definition. A reporting entity may consider an asset for which less than 50% of the original principal relies on sale or refinancing to meet the meaningful cash-flow generating criteria. (A structure with contractual cash flows that does not satisfy all of the interest stipulated in the structure does not qualify under the practical expedient.) In applying this practical expedient, only contractual cash flows of the non-financial asset may be considered. This practical expedient should not be construed to mean that assets cannot meet the meaningful criteria if they rely on the sale or refinancing to service any interest, an amount greater than 50% of the original principal or if they rely on cash flows that are not contracted at origination. Rather, such instances do not qualify under the practical expedient and would require a complete analysis of the noted factors in determining whether the meaningful cash-generating criteria has been met.

Additional Elements for Asset Backed Securities

54. When establishing the ABS definition and required components, various aspects were discussed to improve clarity on the application of the guidance.

55. Determination of "Assets" Backing Securities: Although the definition of an asset detailed in *SSAP No. 4—Assets and Nonadmitted Assets*, is applied throughout statutory accounting principles, the question was raised as to where the asset definition would be applied in determining a qualifying ABS. For example, an entity that expects to have subsequent receivables from future operations does not have recognized "assets" from those expectations as the requirements of the asset definition have not been met. However, if that entity were to sell the rights to future cash flows from expected operations, the selling entity would receive cash (a qualifying asset), and the acquiring entity would also have a recognized asset from the acquired right to future cash flows.

56. For purposes of qualifying as an "asset" permitted in an ABS structure, the definition of an asset must be met by the ABS Issuer. In some situations, particularly when the asset represents a right to future cash flows, the asset may not be in a form that could be liquidated to provide payment towards the debt obligations. (For example, if the asset represents acquired rights to future royalties, those royalty rights would have to materialize to have liquid assets available toward the debt obligations.) The ability to liquidate the backing collateral asset at a single point in time does not impact the structural determination of whether the issued security meets the definition of an ABS provided that the assets are expected to produce meaningful cash flows to service the debt terms. Additionally, the inability to liquidate the assets

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backing the instrument may impact the assessment of what constitutes substantive credit enhancement. Failure of cash flows to materialize may impact recoverability and require impairment of an ABS.

57. There is no requirement for a collateral asset backing an ABS structure to qualify as an admitted asset under statutory accounting. Assessing whether the underlying asset qualifies for admittance is not necessary as non-financial assets backing ABS must meet the meaningful cash-generating criteria. If the structure fails to meet the meaningful cash-generating requirement, the instrument does not qualify for reporting as a bond on Schedule D-1. Statutory accounting has not historically restricted bonds backed by inadmissible assets from being admissible, nor has it included any kind of evaluation of the cash flow producing ability of underlying assets. The principles-based bond definition adds a requirement to evaluate the cash flow producing ability of the underlying collateral, but continues to recognize that assets that may not be admissible if held individually on an insurer's balance sheet, may be well suited to support bond-like cash flows when securitized in large numbers with appropriate structuring (e.g. prioritization of cash flows).

58. Determining Whether the Structure Reflects "Financial" or "Non-Financial" Assets: The definition of a "financial asset" has previously been adopted from U.S. GAAP and is reflected in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* as cash, evidence of an ownership interest in an entity, or a contract that conveys to one entity a right 1) to receive cash or another financial instrument from a second entity or 2) to exchange other financial instruments on potentially favorable terms with the second entity.

59. For purposes of excluding financial assets from the ABS meaningful cash generation criteria, the financial asset definition was clarified, for the avoidance of doubt, to not include assets for which the realization of benefits from the rights to receive or exchange financial assets depends on the completion of a performance obligation such as with a lease, mortgage servicing right, royalty rights, etc. For purposes of applying the ABS guidance, when there is a performance obligation required before the cash flows are generated, the assets represent non-financial assets, or a means through which non-financial assets produce cash flows, until the performance obligation has been satisfied. As another way to assess this clarification, if the assets backing the ABS are only subject to default risk (meaning the risk of nonpayment is solely based on failure of the underlying payer to satisfy its unconditional promise to pay), then the asset is a financial asset. If the asset is subject to any other risk in addition to default risk, then the assets represent non-financial assets. As simple illustrative examples:

a. A mortgage-backed security (MBS), where the underlying mortgages have been securitized into a structure, the mortgage receivables represent unconditional promises to pay, with no further performance obligation of the lender or any other party. This structure is considered to be backed by financial assets. Although this structure is excluded from the meaningful cash flow assessment, it must still comply with the substantive credit enhancement requirement.

b. A structure that represents the securitization of rental car leases is contingent on the lessor performing its side of the transaction (providing the car for use) before the lessee is obligated to pay. Therefore, a lease is a non-financial asset due to the performance obligation that must be satisfied in order for payment to become unconditional. Additionally, as is the case with short-term car rentals, the lease (rental agreement) may not be in place and the structure may represent a securitization of the rights to future rental payments, which adds an additional performance condition. This structure combines performance risk with default risk, resulting with the structure not qualifying for classification as being backed by financial assets. For this structure, the reporting entity would have to complete assessments that 1) the structure results with substantive credit enhancement and 2) the structure produces meaningful cash flows over the term of the instrument to satisfy the debt obligation other than through the sale or refinancing at maturity. If at origination, the contractual cash flows from the underlying collateral (leased

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rental cars) would be sufficient to satisfy all of the interest and at least 50% of the original principal, then the meaningful criteria would be met through the practical expedient. That means, as discussed in SSAP No. 26, paragraph 9.b., that the practical expedient can only be used if less than 50% of the principal relies upon sale or refinancing.

60. Whole-Business Securitizations: In most ABS structures, the assets backing the cash flows are specified and limited to a distinct collateral pool. For example, dedicated cash flows from specific lease arrangements, or specific receivables from credit cards or mortgages. However, ABS structures can exist that represent an entire range of operating revenues or cash flows generated by the business. These structures are often referred to as "whole business" or "operating asset" securitizations. These structures, which could only include cash flows from certain operating segments, and not necessarily the entire business of a company's operations, transfer the cash flows from the dedicated operations first to the investment holders, with the operating entity receiving their "operation proceeds" after the investment holders have been paid. This is different from a traditional bond structure where the operating entity first receives the proceeds from their operations and has discretion on how it uses those proceeds to continue operations and pay expenses and then ultimately pay the bond holders according to the debt terms. Further, debt holders in a whole-business securitization generally only have recourse to the cash flow streams pledged to support the debt, unlike a general credit obligation of the operating entity.

61. For the principles-based bond definition, structures that refer to whole-business securitizations, or that refer to operation proceeds as the collateral for the source of debt repayment still meet the definition as an ABS and do not reflect ICO. For these structures, the dedicated operational cash flows represent the defined collateral pool and should not be classified as ICO based on an interpretation that the proceeds represent the cash flows of an operating entity as they are not supported by the general creditworthiness of an operating entity, but rather only on referenced cash flow streams from the entity's operations.

62. Residual Tranches / "Equity" Components of Schedule D-1 Qualifying Structures: The assessment of qualifying Schedule D-1 investments has to consider the overall investment structure but focuses primarily on the specific instrument held by the reporting entity. Structures, particularly ABS, may include residual tranches that provide payment after pre-determined principal and interest payments have been made to other tranches or interests based on remaining available funds. Although payments to residual note holders could occur throughout an investment's duration, and not just at maturity, such instances still reflect the residual amount permitted to be distributed after other holders have received interest and principal payments. In all instances, despite whether other tranches of the investment structure qualify for reporting as a bond on Schedule D-1 reporting, residual tranches do not qualify for bond reporting on Schedule D-1.

63. Under prior guidance in SSAP No. 43, there was no exclusion that restricted residual tranches of qualifying securitizations from being captured in scope and being reported as bonds. From the outreach performed in developing the principles-based bond definition, it was identified that several insurers have historically reported these residual tranches on Schedule BA: Other Long-Term Invested Assets. However, it was noted that some reporting entities have reported these items as a bond on Schedule D-1 as a component of the securitization or as a beneficial interest in scope of SSAP No. 43. Although residual tranches (first loss tranches) do not receive CRP ratings or NAIC SVO designations, when reported on Schedule D-1, an NAIC designation is required. From information obtained, entities reporting residual tranches on Schedule D-1 have either been reporting as self-assigned 6* or they applied the NAIC 5GI concept to self-designate these securities. Under the 5GI concept, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) permits self-designation as an NAIC 5 if the documentation necessary for a full SVO credit analysis does not exist, the issuer is current on all principal and interest payments, and the reporting entity has an expectation that they will receive all contracted interest and principal. The use of the NAIC 5GI concept to self-designate residual tranches on Schedule D-1 is a misapplication of this guidance. It is faulty to conclude that an investment is current and will provide all contractual interest and principal payments when the investment provides payments based on remaining funds after obligations to other issued debt instruments from the structure are satisfied. Furthermore, the

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5GI provision was intended to prevent an NAIC 6 designation simply because the documentation for a full credit analysis could not be provided or reviewed, such as situations involving foreign securities when the supporting documents are in a foreign language. The NAIC 5GI provision was not intended to permit self-assignment of an NAIC 5 designation to securities that would not qualify as a fixed-income instrument eligible for an NAIC designation under the P&P Manual.

64. With the identification that residual tranches are inconsistently reported, with some entities reporting as bonds on D-1 and others reporting on Schedule BA, the Working Group drafted and exposed agenda item 2021-15: SSAP No. 43 – Residual Tranches in September 2021 as an interim action prior to the conclusion of the bond project. The guidance within that agenda item clarified that residual tranches shall be reported on Schedule BA at lower of amortized cost or fair value. The guidance also clarified that the reference to residual tranches intends to capture securitization tranches and beneficial interests, as well as other structures captured in scope of SSAP No. 43 that reflect loss layers where failing to remit contractual interest or principal payments does not result in an act of default. Payments to holders of residual interests occur after contractual interest and principal payments have been made to holders of other tranches or interests and are based on the remaining available funds. Although payments can occur throughout an investment's duration, such instances still reflect the residual amount permitted to be distributed after other holders have received contracted interest and principal payments.

65. On November 10, 2021, the Statutory Accounting Principles (E) Working Group adopted agenda item 2021-15, clarifying that residual tranches are required to be reporting on Schedule BA: Other Long-Term Assets beginning December 31, 2022, with early adoption permitted. The effective date of this action allowed time for reporting entities to implement this change and to correspond with a Blanks (E) Working Group proposal to incorporate separate reporting lines for residuals, based on underlying characteristics of the structure, on Schedule BA. With the adoption of this guidance, the Working Group noted that reporting entities may elect to reclassify residual tranches or interests to Schedule BA in advance of the effective date. As of the effective date, residual tranches or interests previously reported on Schedule BA shall be reclassified to the appropriate residual tranche Schedule BA reporting line based on the underlying characteristics of the investment structure.

66. Along with the action to specify the Schedule BA reporting for residuals, the Statutory Accounting Principles (E) Working Group and the Valuation of Securities (E) Task Force provided a joint memorandum to the Blanks (E) Working Group to specifically identify that application of the NAIC 5GI process to residuals is an inaccurate application. Residual tranches or interests reported on Schedule D-1 for year-end 2021 shall be reported with an NAIC 6. The Task Force also received a referral requesting clarification of the NAIC 5GI process so future misapplications could be mitigated. The Task Force considered specific changes to address residuals and adopted those revisions during the 2021 Fall National Meeting.

67. Subsequent to the guidance adopted in agenda item 2021-15, additional revisions were adopted to *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* (agenda item 2023-12) and to *SSAP No. 30—Unaffiliated Common Stock* and *SSAP No. 32R—Preferred Stock* (agenda item 2023-23) to clarify that all residuals, regardless of legal form of the investment, shall be reported on the dedicated residual reporting lines on Schedule BA.

68. The adoption of SSAP No. 21 in accordance with the principles-based bond project, incorporated guidance for non-bond debt securities and residual interests. The residual guidance includes the definition, common traits in identifying residuals as well as accounting and reporting guidance. Although adopted with a January 1, 2025 effective date consistent with the bond project, reporting entities are permitted to early-adopt the residual guidance in 2024.This SSAP No. 21 residual guidance has the following key aspects:

a. Residuals are permitted to be admitted assets if debt securities from the same securitization qualify (or would qualify) as admitted assets. If a debt security held from the same structure is (or would be) nonadmitted, then any residual interests or first loss positions held from the same structure do not qualify as admitted assets. Residuals in the legal form of a SSAP

No. 48 investment are not subject to the SSAP No. 48 audit requirements for admittance as they are captured in scope of SSAP No. 21 and not SSAP No. 48.

b. Residuals shall be initially reported at cost, or allocated cost (using proportional fair values) if acquired along with debt tranches from the securitization. Subsequent to initial acquisition, residuals shall be reported at either 1) the lower of adjusted cost or fair value under the Allowable Earned Yield method, with temporary reductions in fair value reported as unrealized losses, or 2) at the calculated practical expedient method permitted in SSAP No. 21. For the residual guidance, amortized cost is defined as the cost the residual reduced for distributions in excess of the Allowable Earned Yield and other-then-temporary impairments (OTTI). The Allowable Earned Yield is established at acquisition as the discount rate that equates the initial best estimate of the residual's cash flows to its acquisition cost. With this approach, interest income is recorded under the effective yield method using the Allowable Earned Yield, capped by the amount of cash distributions received. Amounts received in excess of the Allowable Earned Yield reduces amortized cost. The practical expedient calculates book/adjusted carrying value (BACV) such that all distributions received are treated as a reduction in BACV. With this approach, the reporting entity will not recognize any interest or investment income until the residual tranche has a BACV of zero.

c. Residuals shall be assessed for OTTI on an ongoing basis, with required assessment anytime that fair value is less than the reported value. For residuals measured using the Allowable Earned Yield method, an OTTI is considered to have occurred if the present value of expected cash flows discounted by the Allowable Earned Yield is less than amortized cost. For residuals measured under the practical expedient, an OTTI shall be considered to have occurred if the fair value of the residual is less than the BACV.

d. The residual guidance is adopted prospectively and includes transition guidance in applying the revised measurement method for securities previously captured in scope of another SSAP. This guidance mirrors concepts from the transition of the principles-based bond definition.

69. Stapling of Investments: The original exposure of the principles-based bond definition (May 2021) included an initial example detailing a situation where "equity interests" from a tranche (such as residuals) were required to be held by a reporting entity when holding debt tranches. That language identified situations where the reporting entity would be restricted from selling, assigning, or transferring the unsecured debt investment without also selling, assigning or transferring the equity interest to the same party. This restriction is often referred to as the "stapling" of investments. Pursuant to the guidance in the initial example, although the debt instrument would separately qualify as a creditor relationship for bond reporting, when considering the entirety of the holdings (both the residual/equity interests and debt tranches combined), the investment would be considered an equity instrument in substance. Although the debt instrument would appear to have a higher priority of payment, that priority would be supported by the residual/equity interest the reporting entity has to hold. Ultimately, the reporting entity would be subordinate to themselves as they would recognize a loss on the residual/equity tranche to safeguard payment under the debt tranche. Under that initial proposed example, all holdings under such situations, including the debt tranches, would not qualify as creditor relationships and would not qualify for bond reporting.

70. After considering comments from the first exposure period, as well as discussing within the small group of industry and regulators, this example was eliminated from the principles-based bond definition. These discussions ultimately concluded that tranches that separately qualify as bonds should be reported as bonds even if other tranches from a structure that do not qualify as bonds are also held by the reporting entity. Elements noted as part of the decision to remove the stapling restriction include:

a. A key element in the initial proposal to require all of the holdings as equity was to ensure that the risk of the holdings was properly captured. It was noted that recent developments to tranche investments that were previously reported as investments in LLCs or joint ventures could result in RBC arbitrage. This is because the risk of the investment would be concentrated in a specific tranche intended to absorb losses, and only that limited tranche would be reported on Schedule BA with higher RBC charges. This would allow the debt tranches (as they are subordinated by the equity tranche) to likely qualify as bonds with Schedule D-1 reporting and lower RBC charges. However, because risk has been concentrated into the smaller equity tranche as a result of leverage, and because Schedule BA RBC charges are fixed and insensitive to leverage, there is a lowering of risk-based capital in total despite no change in risk. The subsequent discussions highlighted that this is an RBC issue for the equity tranche and is not an accounting classification issue. As consideration on appropriate risk charges for residual tranches has been requested to the Financial Condition (E) Committee and is a discussion item for the RBC Investment Risk and Evaluation (E) Working Group, this issue is not within the focus of the Statutory Accounting Principles (E) Working Group. It was also noted that consideration of statutory accounting provisions (such as nonadmittance) to achieve a desired risk assessment would be an inappropriate use of the accounting guidance. It was also noted that the investments within scope of these discussions are likely permitted for admittance under state law and incorporating statutory guidance different from state law would only result with identification of prescribed practices as domiciliary state laws and statutes are the ultimate authority for the application of SAP.

b. It was also identified that the initial exposed example was specific to investments that were "stapled" under contractual terms. This guidance would have only been applicable to dynamics in which there was an explicit restriction in the sale, assignment, or transfer of the residual/equity tranche separately from a debt tranche. It was identified that without an active market for residual/equity tranches (which is common) the explicit restrictions would not be necessary to achieve a similar result. Structures would only need to be designed to require initial acquisition of residual/equity tranches when acquiring debt tranches (with removal of the explicit disposal restrictions) to avoid the proposed stapling guidance. Since the proposed guidance could be easily avoided, the guidance would not address the underlying concern.

c. This discussion noted that it is quite common for acquisitions to require purchases of a vertical slice of a structure and for investments to be stapled for a short duration of time. These provisions are generally made for easier marketing and for easier compliance with conflict-of interest provisions. The short-term aspect of some stapled investments raised concerns as to how bond-qualifying debt tranches would be reported if stapling provisions to a residual/equity tranche were subsequently eliminated. This was identified as likely requiring a schedule move (from BA to D-1) with potential other accounting and reporting impacts (such as with NAIC designations and measurement method). This discussion noted that an issuer's stapling of investments may reflect a legitimate business purpose, and not intend for RBC arbitrage, and the elimination of such components after the stated timeframe could cause confusion or unnecessary noise in the financial statements from the reclassification of investments. This discussion further supported that the acquisition of different tranches, even if explicitly stapled, should not prevent separate debt (bond) and residual/equity recognition based on the characteristics of the specific tranche.

71. ABS as Short-Term or Cash Equivalent: With the required assessments and requirements for a security to qualify as ABS, as well as dedicated reporting based on the underlying collateral assets, ABS will no longer be permitted to be reported as short-term or cash equivalents. All qualifying ABS will be required to be reported on Schedule D-1-2, even if acquired within one year or less from the maturity date,

to allow for full assessment of ABS held by a reporting entity by regulators. Investments captured in scope of SSAP No. 2R are intended to reflect situations in which limited risk remains, either from changes in credit-quality or interest rates, due to the short-duration until maturity. As ultimate cash flows from ABS may have other risks beyond default risk or interest rate risk (such as performance factors, balloon payments, collateral quality), reporting as a cash equivalent or short-term investment is not permitted to prevent inappropriate assumptions of the investment's remaining potential risk.

Key Discussions / Aspects in Developing the Definition

72. Refinancing Risk / Residual Risk Exposure: Discussion of refinancing risk (where there is outstanding debt owed at maturity that will need to be refinanced for the remaining principal to be received by the note holder) was a key element discussed in accordance with the meaningful cash flow requirement for non-financial ABS. This discussion highlighted that traditional refinancing risk is accepted in the context of corporate debt but is viewed differently when assessing the cash flows of non-financial assets in an ABS structure. This differentiation was confirmed, with identification that there are concerns unique to non-financial ABS.

73. The requirement for a non-financial ABS to produce meaningful cash flows to service the debt other than through the sale or refinancing of the collateral assets ensures that structures captured as a bond on Schedule D-1 actually reflect bond-like cash flows. Structures that rely on the sale or refinancing at maturity to generate cash flows to repay debt obligations ultimately reflect a point-in-time reliance on the underlying collateral asset values that does not reflect the intent of Schedule D-1 reporting of bond-like cash flows. These structures are more reflective of the underlying collateral risk, ultimately contingent on the market at a future point in time and whether the underlying assets can be sold or refinanced in accordance with original expectations at the time of the structure origination.

74. A key comment raised by industry with regards to the meaningful cash flow requirement, and the restriction against relying on the sale/refinancing at maturity to produce meaningful cash flows, is that consideration should be given to the level of overcollateralization that exists in a structure if the meaningful requirement will not be met without sale or refinancing. These industry comments take the position that as the level of overcollateralization to the debt obligation increases, then there is a greater likelihood that the debt issuer will be successful in refinancing or selling the assets and generate the means to repay the debt obligation. Although overcollateralization is a factor in securities for bond classification, allowing overcollateralization to override the requirement for meaningful cash flows other than the refinancing / sale at maturity is not permitted for the following reasons:

a. The intent of the principles-based bond definition is to clarify what shall be reported as bonds on Schedule D-1. Non-financial ABS that do not generate meaningful cash flows and rely on the refinancing or sale of the underlying assets do not reflect bond-like cash flows and are not characteristic of bond investments. These structures ultimately reflect equity (point-in-time) valuation risks of the assets held as collateral.

b. The industry position that overcollateralization safeguards the asset performance is an argument that supports the quality of the structure, but not the substance of the investment design. The principles-based bond definition does not factor in investment or credit quality within the determination of whether a structure qualifies for reporting as a bond on Schedule D-1. Permitting an assessment based on overcollateralization would introduce a concept that credit quality determines bond / Schedule D-1 reporting, and that is not an accurate conclusion in line with the principle concepts of bond classification.

75. Consistent with prior conclusions, reporting an investment as a bond on Schedule D-1 is not indicative of the quality of the investment, but rather reflects securities expected to generate bond-like cash flows. Securities reported as bonds on Schedule D-1 may be of high-quality or low-quality, but the reporting is based on the substance of the structure, which ultimately requires bond-like cash flows for all

investments. This includes a requirement that non-financial ABS must produce meaningful cash flows through the use of the underlying collateral assets other than through the sale or refinancing of the assets.

76. Additionally, through the small group discussions around the refinancing restriction, it was noted that even if a debt instrument meets all of the criteria to be reported as a bond on Schedule D-1, there will still be a potential for unintentional RBC arbitrage related to securitizations, because the residual tranches absorb all of the redistributed risk of the underlying collateral, but receives a fixed RBC charge that is not in any way risk-rated. While this could be the case in any type of securitization, it is particularly pronounced if the underlying collateral is equity investments. Equity investments generally receive a base 30% RBC charge for life companies. If equity investments are securitized, the bond tranches will get low bond charges (<2%), while the residual tranche will continue to receive a flat 30% base charge. This will have the effect of bringing the overall weighted-average capital charge on the underlying investments from 30% to approximately 10-15%. This will occur even if the bond tranches have all of the substance associated with a bond. Following these discussions, it was identified that this regulatory concern may not be appropriate to address through the accounting standards but may warrant discussion under the Capital Adequacy (E) Task Force. Subsequent discussions from the Financial Condition (E) Committee directed the new RBC working group (the RBC Investment Risk and Evaluation (E) Working Group) to evaluate this and any other investment-related RBC items. Subsequent to these discussions, the RBC Investment Risk and Evaluation (E) Working Group assumed a project to assess RBC factors for residual interests. An interim approach was adopted to include a 30% base RBC factor with a 15% sensitivity test for year-end 2023, with a 45% base RBC factor and 0% sensitivity for year-end 2024. Continued discussion is expected under a long-term project.

77. Use of NAIC Designation / SVO Review in Determining Bond / Schedule D-1 Reporting: The accuracy of the financial statements, and compliance with statutory accounting provisions, is the responsibility of the reporting entity. Assessment and compliance with key concepts, such as the "meaningful cash flow generation" and "substantive credit enhancement" concepts for ABS are also the responsibility of the reporting entity, along with appropriate documentation of these assessments for regulator review when requested. Consistent with the existing *NAIC Policy Statement on Coordination of the Accounting Practices and Procedures Manual and the Purposes and Procedures Manual of the NAIC Investment Analysis Office*, a reporting entity cannot utilize an NAIC designation to conclude on the substance of an investment or the resulting reporting schedule. Pursuant to the policy statement, obtaining an NAIC designation does not change an investment's applicable SSAP, annual or quarterly statement reporting schedule, or override SSAP guidance required for an investment to be an admitted asset.

78. Questions have been received whether an NAIC designation in the AVS+ product or an assessment of an investment from a "Regulatory Treatment Analysis Service" (RTAS) submission from the SVO can be utilized as support that an investment qualifies as a bond for Schedule D-1 reporting. These are inaccurate interpretations on the use of NAIC designations within those products. The assignment of an NAIC designation (either from the SVO or CRP) reflects the credit quality of an investment. An assessment of credit quality does not provide assurances that the investment qualifies for reporting as a bond on Schedule D-1 as an ICO or an ABS. As part of this principles-based bond project, consideration is planned to expand the ability to report and use NAIC designations on Schedule BA so that investments that do not qualify as bonds can have appropriate risk assessments that factor in the credit quality of the investment. This capability would ultimately depend on action by the Capital Adequacy (E) Task Force.

79. Although the NAIC designation and RTAS processes cannot be used in determining Schedule D-1 compliance, it is envisioned that a small group of regulators and NAIC staff could be formed to review specific investment structures under the principle-based concepts to assist in assessments of complex new investment designs. If formed, it is anticipated that NAIC staff on the statutory accounting side and within the SVO would assist this small group.

80. Interest Only / Principal Only Strips: Discussion occurred on whether specific guidance should direct the reporting of interest only (IO) and principal only (PO) strips. The resulting conclusion from this

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discussion was that the principle concepts from the bond definition should continue to be applied to these investments. If the strips qualify within the definition as ICO, they would be captured in scope of that guidance. If the strips qualified as ABS, they would be captured in scope of that guidance. It was noted that interest-only strips shall also be assessed in accordance with the residual guidance. If the interest-only strip reflects excess interest (e.g., remaining differential spread from interest collected from interest paid), these investments would be akin to a residual investment without contractual interest or principal payments and shall be captured in scope of that guidance. (Residuals are in scope of SSAP No. 21 and required to be reported on Schedule BA. Residuals are not permitted to be reported on Schedule D-1.)

81. The discussion of IO/PO strips with industry representatives identified that they are not overly prevalent investments with insurance reporting entities. It was also noted that IO/PO based on RMBS are relatively rare due to the prepayment risk, however those based on CMBS generally have contractual provisions that prohibit prepayments, thus ensuring that they act more akin to typical bonds. This discussion further highlighted that changes to the principal-based bond definition are not justified for IO/PO investments, and insurers should document their accounting policies for these investments to demonstrate compliance with the bond definition.

82. The discussion of IO/PO strips focused on U.S. Treasury strips and mortgage-backed securities as likely investments, but it was noted that the application of the overall bond definition concepts should be applied to any future design of these investments. Specific elements noted for the two general designs:

a. U.S. Treasury Strips: Treasury Strips are created when a bond's coupons are separated from the bond. The coupons separated from the bond are sold individually (IO), becoming separate securities from the principal payments due at maturity (PO). U.S. Treasury Strips are backed by the U.S. government. U.S. Treasury strips (IO and PO) are considered U.S. government issues and would be captured with other securities backed by the U.S. government as ICO. Specific identification of U.S. Treasury strips as a separate reporting line of ICO investments, captured within the U.S. government category, was noted to be repetitive and not necessary.

b. Mortgage-Backed Securities and Other Non-Treasury Strips: Other IO and PO strips are required to be assessed in accordance with the principle concepts of the bond definition. It is anticipated that non-U.S. strips (including mortgage-backed security strips) would not qualify as ICO and shall be reviewed in accordance with the ABS concepts to determine whether the strip qualifies for reporting as a bond on Schedule D-1. The separation of the principal and interest components into separate securities does not change the application of the principle concepts for determining whether a security qualifies as a bond. It was noted that IO strips could be high in the capital structure (supported by subordination) or could represent residual interests (reflecting the spread between proceeds collected and contractual interest). The specific details of the individual IO/PO security shall determine the appropriate accounting and reporting.

83. The discussion of IO/PO strips identified that there is no current need to have separate reporting lines to identify these items within the investment schedules. However, it was identified that the ability to identify these investments with a code (or other feature) would allow for future aggregation and assessment. This was requested to be considered as part of the reporting revisions.

84. Embedded Derivatives / Underlying Variables: Discussion occurred on the language that precludes bond reporting based on the appreciation or depreciation of an underlying collateral value or other variable. Although industry comments noted that the intent of the language was understood, it was identified that the language could be interpreted to mean that amounts in both the magnitude and timing of principal and interest payments must be known in advance, and it could also be interpreted to mean the amounts need to be contractual in nature but can still vary as long as the variability is not dependent on the appreciation or depreciation of an asset or variable. It was also noted that the reference to "other variable" could be

interpreted to mean interest is not allowed to vary based on any variable or just the appreciation or depreciation of the variable. After discussing these comments, revisions were drafted to clarify that the exclusion is not intended to restrict variables that are commonly related to debt instruments, such as but not limited to, plain vanilla inflation or benchmark interest rate adjustments (such as with U.S. TIPs or SOFR-Linked coupons), scheduled interest rate step-ups, or credit-quality related interest rate adjustments. Furthermore, as detailed in footnote 3, this exclusion is not intended to encompass nominal interest rate adjustments. This guidance has also been incorporated within the provisions for determining whether a debt instrument represents a creditor relationship and is applicable for debt instruments structured as ICO and ABS.

Accounting for Debt Securities That Do Not Qualify as Bonds

85. Securities that reflect debt instruments that do not qualify for bond reporting as an ICO or an ABS shall follow specific guidance captured in SSAP No. 21 and be reported on Schedule BA. Investments in scope of this guidance are limited to items that would be in scope of SSAP No. 26, but that do not qualify for bond reporting as they reflect:

a. Debt securities for which the investment does not reflect a creditor relationship in substance.

b. Debt securities that do not qualify for bond reporting due to a lack of substantive credit enhancement.

c. Debt securities that do not qualify for bond reporting due solely to a lack of meaningful cash flows.

86. The debt securities captured in the SSAP No. 21 guidance meet the definition of assets as defined in SSAP No. 4 and are admitted assets to the extent they conform to the requirements within SSAP No. 21. The provisions are specific that the guidance for non-bond debt securities in SSAP No. 21 shall not be inferred to other securities or investment structures.

87. Debt securities in scope of SSAP No. 21 that do not qualify as bonds under SSAP No. 26 and for which the primary source of repayment is derived through rights to underlying collateral, qualify as admitted assets if the underlying collateral primarily qualify as admitted invested assets. As detailed in the SSAP No. 21 guidance pertaining to residual tranches, any residual tranches or first loss positions held from the same securitization that did not qualify as a bond under SSAP No. 26 also only qualify as admitted assets to the extent the underlying collateral primarily qualifies as admitted invested assets.

88. Debt securities in scope of the SSAP No. 21 guidance shall be reported at acquisition at cost, including brokerage and other related fees on Schedule BA. Subsequent measurement shall reflect the lower of amortized cost or fair value. Changes in measurement to reflect the lower value or to reflect changes in fair value shall be recorded as unrealized gains or losses. Debt securities in scope of SSAP No. 21 shall then follow the guidance in SSAP No. 43 for calculating amortized cost, for determining and recognizing other-than-temporary impairments and for allocating unrealized and realized gains and losses between the asset valuation reserve (AVR) and the interest maintenance reserve (IMR).

89. During the SSAP No. 21 discussion, industry inquired on the direction to utilize SSAP No. 43 for the components detailed in paragraph 88, and not separately assess securities to determine if they are more akin to ICO or ABS and using either SSAP No. 26 or SSAP No. 43 based on those assessments for the calculation of amortized cost, OTTI and allocating AVR/IMR. With this discussion, it was noted that investments that fail the creditor relationship test are identified before determining whether the security would be an ICO or ABS, and as the components of SSAP No. 43 are more relevant for debt securities that do not qualify as bonds, and to ensure consistency for all non-bond debt securities in scope of SSAP No. 21, the decision to utilize SSAP No. 43 for all debt securities that do not qualify as bonds was retained.

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Transition Guidance

90. At the time of transition to apply the guidance adopted to reflect the principles-based bond definition, reporting entities shall make their best efforts to assess investments to determine whether they qualify within the bond definition for reporting on Schedule D-1. The bond definition requires assessments at the time of acquisition (as of the origination date), and it is recognized that reporting entities may not have the means to complete historical assessments for securities held at the time of transition. For these instances, if information is not readily available for reporting entities to assess a security as of the date at origination, reporting entities may utilize current or acquisition information in concluding that a security qualifies for reporting as a bond as either an ICO or ABS.

91. Investments that were reported as a bond on Schedule D-1: Long-Term Bonds as of December 31, 2024, that do not qualify under the principle-based bond definition shall be reported as a disposal from that schedule, with a reacquisition on the appropriate reporting schedule as of January 1, 2025. These investments shall be accounted for in accordance with the resulting SSAP that addresses the specific investment structure. For securities that are reported at the lower of amortized cost or fair value under the guidance in SSAP No. 21 for non-bond debt securities, this could result with an unrealized loss in the measurement of the investment at the time of the reclassification. Although the adoption of this guidance is considered a change in accounting principle under *SSAP No. 3—Accounting Changes and Corrections of Errors*, the following transition guidance shall be applied on January 1, 2025, to ensure consistency in reporting and to allow investment schedules to roll appropriately:

a. Securities reclassified from Schedule D-1 as they no longer qualify under the bond definition shall be reported as a disposal from Schedule D-1 at amortized cost. Although no proceeds are received, amortized cost at the time of disposal shall be reported as consideration on Schedule D-4.

   i. For securities held at amortized cost at the time of disposal, BACV and amortized cost shall agree, preventing gain or loss recognition at the time of reclassification.

   ii. For securities held at fair value under the lower of amortized cost or fair value measurement method, previously reported unrealized losses shall be reversed on January 1, 2025, prior to disposal, resulting with a reported value that mirrors amortized cost at the time of disposal. This action prevents realized loss recognition at time of reclassification.

b. Securities reclassified from Schedule D-1 shall be recognized on the subsequent schedule (e.g., Schedule BA) with an actual cost that agrees to the disposal value (amortized cost). Immediately subsequent to recognition on the resulting schedule, the securities shall be reported in accordance with the measurement method prescribed by the applicable SSAP:

   i. For securities previously reported at fair value on Schedule D-1 (under a lower of amortized cost or fair value measurement method), the reporting entity will recognize an unrealized loss to match the previously reported BACV. Subsequently, the security will continue to reflect a lower of amortized cost or fair value measurement method.

   ii. For securities previously reported at amortized cost on Schedule D-1, if the subsequent applicable SSAP guidance requires a lower of amortized cost or fair value measurement method, then the reporting entity shall recognize an unrealized loss to the extent fair value is less than amortized cost.

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c. After application of the transition guidance all securities shall reflect either the same reported value as of December 31, 2024 (amortized cost or fair value) or a lower reported value (if the security is subject to the lower of amortized cost or fair value measurement method). There should be no instances that result with a security having a greater reported value than what was presented on December 31, 2024. Subsequent to transition, securities reported at fair value may incur unrealized gains or losses due to fair value fluctuations, but should never have unrealized gains that result with a BACV that exceeds amortized cost.

92. With this transition guidance, changes in measurement for securities reclassified under the bond definition will be reported as a change in unrealized capital gains (losses) in the first quarter 2025 financial statements (unless sold in the interim with a realized gain or loss) and not as a change in accounting principle. To enable regulators the ability to identify the impact of securities reclassified under the bond definition, the following disclosure for the 2025 first quarter financial statement is required:

a. Aggregate BACV for all securities reclassified off Schedule D-1.

b. Aggregate BACV after transition for all securities reclassified off Schedule D-1 that resulted with a change in measurement basis. (This shall be a subset of the aggregate BACV reclassified off Schedule D-1 and captures the securities that moved from an amortized cost to a fair value measurement method under the lower of amortized cost or fair value approach.)

c. Aggregate surplus impact for securities reclassified off Schedule D-1. This shall include the difference between BACV as of December 31, 2024 and BACV after transition for those securities that moved from an amortized cost to a fair value measurement method under the lower of amortized cost or fair value approach.

93. ABS that were previously reported as short-term (Schedule DA) or as a cash equivalent (Schedule E2) shall be reclassified to be reported on Schedule D-1-2 on January 1, 2025. Similar to the process detailed above, the securities shall be removed from Schedule DA and E2 at amortized cost, with reversal of any unrealized loss prior to the reclassification. The amortized cost shall be reported as "consideration received on disposals' on Schedule DA – Verification Between Years or Schedule E-2 – Verification Between Years, as applicable based on the prior reporting location. The security shall be recognized as an ABS acquired on Schedule D-3 at amortized cost. Immediately after initial recognition, if the security was required to be held at fair value, under the lower of amortized cost or fair value measurement method, the reporting entity shall recognize an unrealized loss.

94. The transition guidance shall be applied prospectively beginning with the first year of adoption (January 1, 2025). For disclosures that provide comparative information, reporting entities shall not restate the prior year's information in the 2025 disclosure.

Investment Examples – Securities That Do Not Represent Creditor Relationship Despite Legal Form

95. As detailed in the principles-based bond definition, an initial determinant is whether the investment is a security that represents a creditor relationship in substance. Examples included intend to identify scenarios that do not reflect an in-substance creditor relationship.

96. Example 1: Debt Instrument from SPV with Large Number of Diversified Equity Interests: A reporting entity invests in a debt instrument issued by a SPV that holds a large number of diversified equity interests with characteristics that support the production of predictable cash flows. The structure contains sufficient overcollateralization and liquidity provisions to ensure the production of adequate cash flows to service both principal and interest payments without significant reliance on refinancing or sale of the

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underlying equity investments. The debt instrument's periodic principal or interest payments, or both, contractually vary based on the appreciation or depreciation of the equity interests held in the SPV.

97. Example 1 Rationale: Because the instrument's principal or interest payments, or both, contractually vary with the appreciation or depreciation of the underlying equity interests, it contains an equity-like characteristic that is not representative of a creditor relationship. It would be inappropriate to conclude that a security with any variation in principal or interest payments, or both, due to underlying equity appreciation or depreciation, or an equity-based derivative, is a bond under the principles-based bond definition as such security would contain equity-like characteristics.

98. Example 2: Debt Instrument from SPV with Few Equity Interests, Not an Issuer Credit Obligation: A reporting entity invests in a debt instrument issued from a SPV that owns a portfolio of equity interests, and the debt instrument does not meet the definition of an ICO.

99. Example 2 Rationale: Determining whether debt instruments collateralized by equity interests qualify as bonds under the principles-based bond definition inherently requires significant judgment and analysis. Unlike debt instruments collateralized by assets with contractual cash flows, or debt instruments collateralized by cash-generating non-financial assets, debt instruments collateralized by equity interests may be dependent on cash flow distributions that are not contractually required to be made and/or may not be controlled by the issuer of the debt. In some instances, sale or refinancing of the underlying equity interests may be the only means of generating cash flows to service the debt instruments. As a result, there is a rebuttable presumption that a debt instrument collateralized by equity interests does not qualify as a bond. Notwithstanding this rebuttable presumption, it is possible for such debt instruments to qualify as bonds, if the characteristics of the underlying equity interests lend themselves to the production of predictable cash flows and the underlying equity risks have been sufficiently redistributed through the capital structure of the issuer. Factors to consider in making this determination include but are not limited to:

a. Number and diversification of the underlying equity interests

b. Characteristics of the underlying equity interests (vintage, asset-types, etc.)

c. Liquidity facilities

d. Overcollateralization

e. Waiting period for distributions/paydowns to begin

f. Capitalization of interest

g. Covenants (e.g., loan-to-value trigger provisions)

h. Reliance on ongoing sponsor commitments

i. Source(s) of expected cash flows to service the debt (i.e., dividend distributions from the underlying collateral vs. sale or refinancing of the underlying collateral)

100. While reliance on the sale of underlying equity interests or refinancing at maturity does not preclude the rebuttable presumption from being overcome, it does require that other characteristics mitigate the inherent reliance on equity valuation risk to support the transformation of underlying equity risk to bond risk. As reliance on sale or refinancing increases, the more compelling the other factors needed to overcome the rebuttable presumption become.

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101. The analysis of the underlying structure should be conducted and documented by a reporting entity at the time such an investment is acquired. The level of documentation and analysis required will vary based on the characteristics of the individual debt instrument, as well as the level of third-party and/or non-insurance company market validation to which the issuance has been subjected. For example, a debt instrument collateralized by fewer, less diversified equity interests would require more extensive and persuasive documented analysis than one collateralized by a large and diversified portfolio of equity interests. Likewise, a debt instrument that has been successfully marketed to unrelated and/or non-insurance company investors may provide enhanced market validation of the structure compared to one held only by related party and/or insurance company investors where capital relief may be the primary motivation for the securitization.

Investment Examples – Analysis of ABS Under the Meaningful Cash Flows and Substantive Credit Enhancement Concepts

102. All ABS structures are required to provide substantive credit enhancement to qualify for bond reporting on Schedule D-1. Furthermore, ABS structures that are backed by non-financial assets must generate meaningful cash flows to service the debt without reliance on the sale or refinancing at the maturity of the investment. The following provides examples of analysis under these criteria:

103. Example 3 – Agency Mortgage-Backed Securities: A reporting entity invests in debt instruments issued from a SPV sponsored by the Government National Mortgage Association (GNMA), the Federal National Mortgage Association (FNMA) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, "Agency or Agencies"). These debt instruments pass through principal and interest payments received from underlying mortgage loans held by the SPV to the debtholders proportionally, with principal and interest guaranteed by the Agencies. While there is prepayment and extension risk associated with the repayment of the underlying mortgage loans, the credit risk associated with the mortgage loans is assumed by the Agencies.

104. Example 3 Rationale: Although the reporting entity participates on a proportional basis in the cash flows from the underlying mortgage loans held by the SPV, the reporting entity is in a different economic position than if it owned the underlying mortgage loans directly because the credit risk has been redistributed and assumed by the Agencies. This is a substantive credit enhancement because a market participant (i.e., knowledgeable investor transacting at arm's length) would conclude the Agency guarantee is expected to absorb all losses from the debt instrument. Therefore, the holder of the debt instrument is in a substantively different economic position than if the holder owned the ABS Issuer's unguaranteed assets directly. When guarantees do not cover 100% of principal and interest as the Agency guarantees do in this example, it is still appropriate to determine if the guarantee is substantive in accordance with the requirements of the principles-based bond definition to determine if the holder is in a substantively different economic position than if the holder held the underlying assets directly.

105. Example 4 – Debt Instrument Issued by an SPV: A reporting entity invested in a debt instrument issued by a SPV. Payments under the instrument are secured by a note, a legal assignment from the borrower of a lease for real property and an assignment of the lease payments from an operating entity tenant. Additional security is provided by a mortgage on the leased property (the "underlying collateral"). The leased property is owned by the borrower under the note and the SPV does not have any ownership interest in the underlying collateral, though it has legal recourse to it through the mortgage. The tenant makes contractually-fixed payments over the life of the lease to the borrower, who has assigned both the lease and the lease payments to the SPV as security for the debt. While the debt is outstanding, the lease, the lease payment, and the mortgage all serve as security for the debtholders. Should a default occur, the debtholders can foreclose on and liquidate the real property as well as submit an unsecured lease claim in the lessee's bankruptcy for any defaulted lease payments. The loan-to-value (LTV) (as a percentage of property value) at origination is 100%.

106. The existing lease payments are sufficient to cover all interest payments and all scheduled debt amortization payments over the life of the debt instrument. However, at debt maturity, there is a balloon payment due, totaling 50% of the original outstanding debt principal amount. The corresponding lease has no balloon payment due at lease maturity, so the SPV will either need to refinance the debt or sell the underlying collateral to service the final debt balloon payment. The property has a high probability of appreciating in value over the term, however, ignoring any potential for appreciation, the 50% loan-to-value at maturity is the expected figure at the end of the debt term based solely on scheduled amortization payments. The real property is expected to be subject to some market value volatility and periods of lower liquidity at certain points in time but has a predictable value range and ready market over a longer period of time, such that the property could be liquidated over a reasonable period of time, if necessary.

107. Example 4 Rationale: The reporting entity determined that as a debtholder, they are in a fundamentally different position than if the real estate was owned directly. The lease is a cash generating non-financial asset which is expected to generate a meaningful level of cash flows for the repayment of the bonds which covers all interest payments and 50% of the principal payments. The level of reliance on the collateral value for sale or refinancing is just over the cutoff for using the practical expedient (greater than 50%), so a full analysis is required. In reaching its determination, the reporting entity considered the predictable nature of the cash flows, which are contractually fixed for the life of the debt instrument, as well as the ability of the underlying collateral value to provide for the balloon payment through sale or refinancing in light of its characteristics. While the real property may have some market value volatility and periods of lower liquidity at points in time, the cash flows produced by the lease were concluded to reduce the loan balance to a level (50% loan-to-value) that would be able to be recovered by sale or refinancing at the maturity of the loan.

108. The reporting entity also determined that the structure provides substantive credit enhancement in the form of overcollateralization to conclude that investors are in a different economic position than holding the real property directly, in accordance with the requirements of the principles-based bond definition. In reaching this conclusion, the reporting entity noted that although the debt instrument starts with a 100% loan-to-value (not including the value of the contractually required lease payments), contractual fixed payments from the lease provide additional security such that the reporting entity is in a different economic position than owning the property directly. Lease cash flows are sufficient to cover the payment of all interest and 50% of the outstanding principal over the term of the lease. In the context of the predictable nature of the cash flows and collateral value range over time, the reporting entity concluded that a market participant (i.e., a knowledgeable investor transacting at arm's length) would consider this level of overcollateralization to put the investor in a substantially different economic position than owning the underlying property directly.

109. For the purpose of determining whether there is substantive overcollateralization, it is appropriate to consider any expected economic depreciation, if it is reasonably expected, but it is not appropriate to consider any expected economic appreciation. Note that a debt instrument with a LTV that is expected to decrease over time is not necessarily deemed to have substantive overcollateralization.

110. Example 5 – Debt Instrument Issued by an SPV With Lease Term Less than Debt Instrument: A reporting entity invested in a debt instrument with the same characteristics as described in Example 4, except that the existing lease at the time of origination has a contractual term that is shorter than that of the debt instrument. It is expected with a high degree of probability that the lease will be renewed, and a substantial leasing market exists to replace the lessee should they not renew. However, in the unlikely circumstance that the property cannot be re-leased, there would not be enough cash flows to service the scheduled principal and interest payments, and the property would have to be liquidated to pay off the debt upon default.

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111. Example 5 – Rationale: All details of this example, including the expected collateral cash flows, are consistent with those in Example 4, except that the cash flows in Example 4 are contractually fixed for the duration of the debt while the cash flows in this example are subject to re-leasing risk. Notwithstanding the involvement of re-leasing risk, the reporting entity concluded that the ability to re-lease the property was highly predictable and supported the conclusion that the underlying collateral was expected to produce meaningful cash flows to service the debt.

112. This distinction is to highlight that the expected cash flows of a cash-generating non-financial asset may or may not be contractually fixed for the term of the bond. Certain securitized cash flow streams may not by their nature lend themselves to long-term contracts (e.g., single-family home rentals), but may nevertheless lend themselves to the production of predictable cash flows. While the non-contractual nature of the cash flows is an important consideration in determining whether a non-financial asset is expected to produce meaningful cash flows to service the debt, it does not, in and of itself, preclude a reporting entity from concluding that the assets are expected to produce meaningful cash flows.

113. Example 6 – Lease in SPV with 80% Balloon Payment: A reporting entity invested in a debt instrument issued by a SPV that owns equipment which is leased to an equipment operator. The equipment operator makes lease payments to the SPV, which are passed through to service the SPV's debt obligation. While the debt is outstanding, the equipment and lease are held in trust and pledged as collateral for the debtholders. Should a default occur, the debtholders can foreclose on and liquidate the equipment as well as submit an unsecured lease claim in the lessee's bankruptcy for any defaulted lease payments. The LTV at origination is 70%.

114. The existing lease payments are sufficient to cover all interest payments and all scheduled debt amortization payments over the life of the debt instrument. However, at maturity, there is a balloon payment due, totaling 80% of the original outstanding principal amount. The corresponding lease has no balloon payment due at lease maturity, so the SPV will either need to refinance the debt or sell the underlying equipment to service the final debt balloon payment. The LTV at maturity is expected to increase to 95% considering the scheduled principal amortization payments net of the expected economic depreciation in the equipment value over the term of the debt. The equipment is expected to be subject to some market value volatility and periods of lower liquidity at certain points in time but has a predictable value range and ready market over a longer period of time, such that the equipment could be liquidated over a reasonable period of time, if necessary.

115. Example 6 Rationale: The equipment is a cash generating non-financial asset which is not expected to generate a meaningful level of cash flows for the repayment of the issued debt via the existing lease that covers all interest payments and 20% of principal payments. In reaching this determination, the reporting entity considered that, while the cash flows being produced are predictable, the ability to recover the principal of the debt investment is almost entirely reliant on the equipment retaining sufficient value to sell or refinance to satisfy the debt.

116. The reporting entity also determined that the structure lacks a substantive credit enhancement to conclude that investors are in a different economic position than holding the equipment directly, in accordance with the requirements of the principles-based bond definition. In reaching this conclusion, the reporting entity noted that the debt starts with a 70% LTV, but the overcollateralization is expected to deteriorate over the term of the debt as the equipment economically depreciates more quickly than the debt amortizes. This results in a high LTV (i.e., 95%) at maturity, relative to the market value volatility of the underlying collateral. Despite the predictable nature of the cash flows, the reporting entity concluded that the debt instrument lacked a substantive level of overcollateralization to conclude that the investor is in a different economic position than owning the underlying equipment directly. It was determined that the level of overcollateralization, as determined by a market participant (i.e., a knowledgeable investor transacting

at arm's length), is nominal. Therefore, the reporting entity concluded that it was in a substantively similar position as if it owned the equipment directly.

117. For the purposes of determining whether there is substantive overcollateralization, it is appropriate to consider any expected economic depreciation, if it is reasonably expected, but it is not appropriate to factor in any expected economic appreciation. Note that a debt instrument with a LTV that is expected to increase over time is not necessarily deemed to have nominal overcollateralization.

Reflecting the Principles-Based Bond Proposal in SAP

118. The principles-based bond definition and the specific accounting guidance for bonds, including ICO and ABS, and the guidance for debt securities that do not qualify as bond be captured as new SAP concepts to existing SSAPs:

a. *SSAP No. 26—Bonds (Exhibit 1)*

b. *SSAP No. 43—Asset-Backed Securities* (renamed from Loan-Backed and Structured Securities) (Exhibit 2)

c. *SSAP No. 21—Other Admitted Assets (Exhibit 3)*

119. For SSAP No. 26, the revisions capture the full bond definition, and the guidance for determining whether a security qualifies as either an ICO or an ABS. The accounting guidance for ICO is retained within SSAP No. 26 and is not changed with the inclusion of the bond definition. Other key revisions include transition guidance to reclassify debt securities that do not qualify as bonds from Schedule D-1 to the subsequent schedule and to delete the glossary as no longer necessary.

120. For SSAP No. 43, in addition to revising the name to "Asset-Backed Securities," revisions reorder and streamline the existing guidance. Although the broad measurement concepts and requirements to assess cash flows have not changed, the guidance specific to whether collection of cash flows is probable, not probable, and pertains to beneficial interests has been eliminated. The guidance has been rewritten to provide consistent guidance for the assessment of cash flows and considering the impact of prepayments. These revisions are not expected to result in significant deviations from past practice as the resulting guidance is believed to be reflective of prominent past industry interpretations. Clarifications have been included to ensure recognition of an other-than-temporary impairment whenever a security is in an impaired state (fair value is less than amortized cost, regardless of if an unrealized loss has been recognized) and there is an adverse change in cash flows expected to be collected. Other key revisions include transition guidance to reclassify debt securities that do not qualify as bonds from Schedule D-1 to the subsequent schedule as well as to incorporate guidance that prohibits reporting ABS as cash equivalents or short-term investments and the process to reclassify any securities reported as such as of the effective date.

121. For SSAP No. 21, revisions incorporate new guidance for the accounting and reporting for debt securities that do not qualify as bonds as well as residual interests. For both sections, the revisions specify new measurement and admittance concepts for these securities and specify reporting on Schedule BA in designated reporting lines. For residuals, guidance is included for the recognition of other-than-temporary impairments and transition guidance for situations where the residual had a different measurement method prior to the effective date.

122. In addition, Exhibit 4, details "revisions to other SSAPs" adopted in accordance with the principles-based bond definition. This section identifies all SSAPs that have modified guidance, which predominantly

reflects updated terms and references, but includes the revisions to SSAP No. 2R to restrict ABS from being in scope.

Discussion of Comments Received and Exposures

123. This section details key comments received from exposures of the principles-based bond definition revisions and the Working Group's consideration for potential edits.

a. Per the exposure of the issue paper and principles-based bond definition on March 2, 2022, with comments due May 6, 2022. The Working Group heard comments on July 18, 2022, and directed limited edits to be reflected as followed:

i. Revise the guidance related to U.S. Treasury Inflation Protected Securities (TIPs) and to clarify the guidance regarding variable contractual principal and interest payments. These revisions clarified that securities with plain-vanilla inflation adjustment mechanisms are not intended to be captured within the provisions that restrict bond classification due to varying principal or interest payments, as well as clarified that other variances in contractual amounts due to reference variables (and not just equity interests) are intended to be precluded from bond treatment.

ii. Revise guidance describing substantive credit enhancements, particularly to revise reference to the first loss "tranche" as the first loss "position" and clarify that securitization tranches that do not have contractual principal and interest payments along with substantive credit enhancement do not qualify as a Schedule D Bond and shall be reported on Schedule BA. (Tranches without contractual principal and interest payments are considered residual tranches shall be on Schedule BA.) (Subsequent to these edits further discussion and updates to the residual guidance were adopted. These revisions improve the guidance and remove specific references to contractual principal and interest payments.)

iii. Document the outcome of small group discussions around the application of the bond principles, particularly the equity-backed example, to feeder fund structures. Feeder fund structures shall not automatically be assumed to qualify for bond classification (even if the ultimate collateral is fixed income), nor be automatically precluded bond classification. The substance of the investment should be the determining factor in these and other similar situations. In particular, the assessment of feeder fund structures should evaluate whether the structure ensures the pass through of the underlying cash flows, or whether uncertainty as to the timing or amount of cash flows is introduced by the structure.

iv. Requested interested parties to work with NAIC staff in proposing revisions to capture the elements that may introduce equity-like characteristics into the main components of the bond definition.

b. In addition to the revisions incorporated from the July 18, 2022, call, the Working Group also heard comments and elected not to incorporate revisions for the following items:

i. The Working Group identified that non-bond items that are specifically scoped into SSAP No. 26 will not be identified in the bond definition. The Working Group was explicit that the inclusion of an investment in-scope of SSAP No. 26 did not make the investment a "bond" and such a distinction is necessary to prevent scope-creep or inference of other investments into the bond definition. For example, although SVO-Identified Bond ETFs, SVO-Identified CTLs and certificates of

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deposit that exceed one year are explicit inclusions to SSAP No. 26 and reported on Schedule D-1, these investments are not bonds.

ii. The Working Group did not incorporate industry-proposed edits to limit guidance that requires the consideration of all returns to equity-backed ABS. Rather, the Working Group clarified that all investments that have contractual principal and interest that can fluctuate due to a referenced variable shall consider all returns in excess of principal repayment as interest when determining whether the investment qualifies for bond reporting under the principles-based definition.

iii. The Working Group did not agree with comments supporting ABS to be reported as cash equivalents or short-term investments even if acquired with a maturity date that is less than 90-days or 1-year away. To ensure proper assessment under the bond definition, and reporting based on the underlying components of the investments, the Working Group retained the provisions that all ABS shall be captured within SSAP No. 43 and be reported on Schedule D-1-2.

iv. The Working Group did not direct changes to the bond definition or issue paper after considering the industry "Lease-Backed Securities Working Group" May 5, 2022, comment letter. That letter, which is consistent with their prior comments, proposes to capture securities as ICO if they pass-through cash flows unaltered (such as with certain lease-backed structures) and are supported primarily by a single rated credit payor, though principal repayment is not fully supported by the obligation of that payor. The discussion noted that these securities shall follow the guidance for ABS if they are not fully supported by an underlying contractual obligation of a single operating entity, including the criteria for substantive credit enhancement and meaningful cash flows. The Working Group identified that these structures are not based on the credit worthiness of a single operating entity and rely on the underlying collateral for repayment, which is why they should be considered ABS rather than ICO. The comment letter also raised concerns around the guidance for evaluating project finance debt noting a perception that inconsistent classification may occur for investments with similar characteristics. As a result of the discussion, there were no changes to the exposed bond definition. Working Group members and other interested parties noted during the discussion that the guidance pertaining to project finance is intended to provide guidance for evaluating issuers that share characteristics of both operating entities and ABS Issuers (i.e., the middle of the spectrum). Nevertheless, the guidance is clear that issuers of project finance debt must themselves have the characteristics of operating entities in order for the debt instrument to qualify as an ICO. As such, project finance bonds issued by operating entities and other municipal revenue bonds will be retained as ICO as the design of these structures are supported by the credit worthiness of a single operating entity and are therefore different than the investment structures presented by the industry Lease-Backed Securities Working Group.

c. Per the exposure of the principles-based bond definition, and proposed revisions to SSAP No. 26 and SSAP No. 43 on August 10, 2022, with comments due October 7, 2022, comments were received from Fermat Capital, the industry Lease-Backed Securities Working Group and Interested Parties. After considering the comments, the following key revisions were incorporated:

i. Revisions to incorporate the entire bond definition within SSAP No. 26, with a deletion of bond definition guidance from SSAP No. 43. With this change, securities that qualify as ABS after application of the bond definition will follow

the measurement and reporting guidance within SSAP No. 43. This edit prevents unintended inconsistencies in the guidance that could occur if aspects of the bond definition are in both SSAPs.

ii. Revisions to incorporate the guidance for determining a creditor relationship, which was in an exhibit, into the body of guidance within SSAP No. 26.

iii. Revisions to the examples for ABS analysis, which were moved to SSAP No. 26, to reflect a scenario in which payments under the instrument are secured by a note, a legal assignment from the borrower of a lease for real property and the assignment of the lease payments from an operating entity tenant. This revision was in response to comments from the industry Lease-Backed Security Working Group and detail that the SPV does not need to have ownership interest in the underlying collateral for the security to qualify as an ABS.

iv. Revisions to SSAP No. 26 to clarify that investments with specific guidance and reporting lines (such as surplus notes, working capital finance investments (WCFI) and structured settlements) shall follow the guidance in their specific SSAP and be reported on designated reporting lines. This edit was made in response to the comments from Fermat Capital, who identified that WCFI meet the definition of ICO. These investments shall follow the guidance *in SSAP No. 105R—Working Capital Finance Investments* and be reported on their specific reporting lines on Schedule BA.

v. Revisions to SSAP No. 26, and the addition of a new footnote, to clarify that the general creditworthiness of an entity can be direct or indirect recourse and is the primary source of repayment for issuer credit obligations.

vi. Revisions to SSAP No. 26 to clarify application when interest and principal vary based on the performance of an underlying value or variable. The revised guidance adds language to clarify that the exclusion is not intended to restrict variables that are commonly linked to debt instruments, such as plain-vanilla inflation or benchmark interest rates.

vii. Revisions to SSAP No. 26 to delete the proposed glossary, with the inclusion of the bank loan definition into a footnote. Other definitions were identified as not being necessary for retained inclusion in the statement.

viii. Revisions to SSAP No. 43 to identify Freddie-Mac When Issued Trust Certificates, pursuant to *INT 22-01: Freddie Mac When Issued K-Deal (WI Trust) Certificates*, as an explicit scope inclusion.

ix. Revisions to SSAP No. 43 to clarify the guidance for prospective adjustment method for high-credit quality investments, and on the assessment of cash flows. This guidance clarifies that if a security is in an unrealized loss position, and there is an adverse change in cash flow, the entity shall recognize an other-than-temporary impairment.

x. Revisions to both SSAP No. 26 and SSAP No. 43 to provide specialized transition and disclosure guidance for the reclassification of securities previously reported that will no longer qualify for reporting as bonds.

xi. Revision to the issue paper to clarify the application of the principles-based bond definition to feeder funds.

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d. Per an exposure on November 16, 2022 of SSAP No. 26, SSAP No. 43 and other SSAPs that will be impacted under the bond project, until February 10, 2023, revisions were incorporated to reflect most of the interested party comments. The revised documents were discussed and exposed at the 2023 Spring National Meeting. Most of the edits were minor, but the following elements are specifically noted:

i. Revisions to SSAP No. 26 incorporated an exception for nominal interest rate adjustments. The guidance defines the exception as being too small to be taken into consideration when assessing an investment's substance as a bond. This revision was added based on industry's comments on inadvertent impact to sustainability-linked bonds, but the exception guidance is not limited to those specific bonds.

ii. Revisions clarify that replication (synthetic asset) transactions are addressed in *SSAP No. 86—Derivatives* and are not impacted by the principles-based bond definition.

iii. Revisions to SSAP No. 26 to explicitly identity that residuals, including first loss positions, do not qualify as bonds and shall be captured in *SSAP No. 21—Other Admitted Assets*.

iv. Revisions specific to transition that clarify that investment assessments are required as of origination and to permit current or acquisition information in determining whether investments qualify as bonds at the time of transition. The guidance was also clarified that the transition guidance shall be applied prospectively beginning with the first year of adoption. For disclosures that provide comparable information, reporting entities shall not restate the prior year's information in the 2025 disclosure.

v. With an exposure of the revised documents, an updated SSAP No. 21 was also exposed to update guidance for the measurement of debt securities at the lower of amortized cost or fair value and to incorporate proposed accounting and reporting guidance for residuals.

e. The Statutory Accounting Principles (E) Working Group received comments on June 9, 2023, from the 2023 Spring National Meeting exposure. No comments were received on SSAP No. 26, SSAP No. 43 or the document that detailed revisions to other SSAPs. The Working Group adopted the SSAP revisions reflected in these documents on August 12, 2023, during the 2023 Summer National Meeting, effective January 1, 2025.

f. During the 2023 Summer National Meeting, the Working Group considered comments on SSAP No. 21 pertaining to the guidance for debt securities that do not qualify as bonds and for residual interests and exposed a revised SSAP No. 21 until September 29, 2023. The revisions for debt securities that do not qualify as bonds reflect a majority of interested parties' comments.

i. For debt securities that do not qualify as bonds, revisions clarify that if the primary source of repayment is derived through underlying collateral, the investment shall only be admitted if the underlying collateral qualifies as admitted invested assets. For residuals, revisions clarify that if the reporting entity holds a debt tranche from the same securitization, and the debt tranche does not qualify as a bond (either an ICO or ABS), and the debt security does not qualify as an admitted asset under SSAP No. 21, then the residual does not qualify as an admitted asset.

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ii. Revisions proposed new measurement methods for residuals. This guidance is different from what was proposed by interested parties but intends to reflect the highly uncertain amount and timing of residual cashflows. This proposed guidance will require all cash flows received to be treated as a return of principal until the BACV is zero. At that point, all cashflows received would be treated as interest income. This proposed guidance was noted to best suit how residuals work conceptually. The reporting BACV will reflect the potential risk of loss prior to recovering the initial investment, rather than requiring an assessment of potential loss over the entire life of the securitization.

g. During the 2023 Fall National Meeting, the Working Group considered comments and exposed an updated SSAP No. 21 until January 22, 2024. No comments were received on the section for non-bond debt securities, but comments focused on the guidance for residual interests. Revisions reflected in the 2023 Fall National Meeting exposure:

i. Revisions capture an Allowable Earned Yield method for the measurement of residuals. This guidance will limit the extent interest income can be recognized without recognizing cash flows as return of principal. Provisions were also included to permit a practical expedient to allow all cash flows received to be taken as a reduction of BACV. Under the practical expedient, interest income would not be recognized until BACV was zero.

ii. Revisions clarified the treatment of reductions in fair value as unrealized losses and updated OTTI guidance to be consistent with SSAP No. 43 and the assessment of the present value of expected cash flow to the BACV.

h. On February 22, 2024, an updated SSAP No. 21 reflecting a variety of edits from working with industry throughout the interim was exposed until March 7, 2024. The shortened comment period was proposed to allow for adoption consideration during the 2023 Spring National Meeting.

i. Revisions for residual incorporate the definition and characteristics captured in other SSAPs to make SSAP No. 21 the location for all residual guidance. All residuals shall follow the accounting, admittance and reporting guidance detailed in SSAP No. 21.

ii. Revisions clarified that residuals shall be accounted for at the lower of Allowable Earned Yield method or fair value, or under the practical expedient.

iii. Revisions eliminated the guidance that directed reclassification of residuals to other SSAPs and reporting schedules in situations when the residual tranches cease to meet the definition of residual tranches. With the deletion, once classified as a residual, an investment would retain that classification and reporting until it is disposed by the reporting entity.

iv. Revisions separate the OTTI calculation between items measured at the Allowable Earned Yield method and those that follow the practical expedient.

v. Revisions incorporate transition guidance for residuals that were accounted for under a different SSAP prior to the effective date.

vi. Revisions prescribe a January 1, 2025, effective date, but permit early adoption of the residual guidance.

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History of Definition / Scope Development of SSAP No. 43 – Before the Principles-Based Definition

The following section details the historical development of SSAP No. 43 along with the prior benefits for reporting investments in scope of SSAP No. 43 and key issues from the prior guidance. Due to various revisions that have been reflected since its original adoption, this information is retained for historical reference on the SSAP No. 43 guidance prior to the reflection of the principles-based bond proposal.

124. *SSAP No. 43—Loan-backed and Structured Securities* was originally effective with the SAP codification and resulted with separate guidance for "bonds" (in SSAP No. 26) and "loan-backed and structured securities" (in SSAP No. 43). (The initial guidance indicated that investments in scope of SSAP No. 43 met the definition of a bond in *SSAP No. 26—Bonds, excluding Loan-backed and Structured Securities*.) Although most of the guidance between the original SSAP No. 26 and SSAP No. 43 was the same, the guidance in SSAP No. 43 recognized the need to review (at least quarterly) the assumptions and resulting cash flows of the underlying loans, as changes in assumptions could necessitate a recalculation of the effective yield or other-than-temporary impairment.

125. The original issue paper to SSAP No. 43 (Issue Paper No. 43) cited guidance originally contained in Chapter 1, *Bonds and Loaned Backed and Structured Securities*, from the *Accounting Practices and Procedures Manual of the Life and Accident and Health Insurance Companies*. The issue paper identified that the *Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies* contained similar guidance. In this Issue Paper No. 43, and the original SSAP No. 43, loan-backed securities were defined as "pass-through certificates, collateralized mortgage obligations (CMOs) and other securitized loans…" The reference to "securitized loans" was a key aspect of this original definition.

126. Original definition / scope guidance for SSAP No. 43:

> 2. Loan-backed securities are defined as pass-through certificates, collateralized mortgage obligations (CMOs), and other securitized loans not included in structured securities, as defined below, for which the payment of interest and/or principal is directly proportional to the interest and/or principal received by the issuer from the mortgage pool or other underlying securities.
>
> 3. Structured securities are defined as loan-backed securities which have been divided into two or more classes for which the payment of interest and/or principal of any class of securities has been allocated in a manner which is not proportional to interest and/or principal received by the issuer from the mortgage pool or other underlying securities.
>
> 4. Loan-backed securities are issued by special-purpose trusts (issuer) established by a sponsoring parent organization. Mortgage loans or other securities securing the loan-backed obligation are acquired by the issuer and pledged to an independent trustee under the issuer's obligation has been fully satisfied. The investor can only look to the issuer's assets (primarily the trusteed assets or third parties such as insurers or guarantors) for repayment of the obligation. As a result, the sponsor and its other affiliates may have no financial obligation under the instrument, although one of those entities may retain the responsibility for servicing the underlying mortgage loans. Some sponsors do guarantee the performance of the underlying loans.
>
> 5. Loan-backed securities meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted asset to the extent they conform to the requirements of this statement.

127. In agenda item 2007-26, *FAS 156: Accounting for Servicing of Financial Assets an amendment of FASB Statement No. 140,* the Working Group adopted with modification FAS 156 in *SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, revising the terminology for "retained interests" to "interests that continue to be held by the transferor." This action also clarified that beneficial interests from the sale of loan-backed and structured securities shall be accounted for in accordance with SSAP No. 43. This initial adoption identified that the holder of a beneficial interest in securitized financial assets should recognize the excess of all cash flows attributed to the beneficial

interest estimated at the acquisition date over the initial investment as interest income over the life of the beneficial interest using the effective yield method.

128. In 2009, the Working Group adopted a substantively-revised SSAP No. 43 (effective September 30, 2009). The focus of the substantive revisions was to revise the valuation and impairment requirements based on the cash flows expected to be collected for the securities, rather than fair value. Although the focus of the revisions was inclusion of impairment guidance based on whether an entity has an intent to sell, whether an entity does not have the intent and ability to hold a security, and when there is a non-interest related decline if there is no intent to sell and the entity has the intent and ability to hold, the revisions resulted in a significant rewrite of the guidance in SSAP No. 43, including the guidance for beneficial interests. This guidance expanded the prior scope inclusion from "beneficial interests from the sale of LBSS," to include "purchased beneficial interests in securitized financial assets."

129. In agenda item 2010-12, Clarify Definitions of Loan-Backed and Structured Securities, the Working Group received a regulator-sponsored, nonsubstantive Form A with a proposal to revise the definitions of a loan-backed and structured security (LBSS). As a result of this proposal, the definition was revised to eliminate the reference to "securitized loans" and instead refer to "securitized assets." These revisions were adopted with an effective date of January 1, 2011.

a. Although the agenda item simply identifies that this item was exposed in August 2010, and then adopted after a single exposure in October 2010, with an effective date of January 1, 2011, there were significant comments received during the exposure period. In short summary, these comments highlighted that the scope of the changes were intended to move fixed-income assets that had been accounted for as bonds under SSAP No. 26 to SSAP No. 43 as LBSS. Particularly, the comments noted concerns with the movement of equipment trust certificates and credit tenant loans from the accounting provisions of SSAP No. 26 to the accounting rules of SSAP No. 43. These comments stated that "instruments with radically different sources of cash flows and risk characteristics utilize trust structures, and not all should be classified as loan-backed." There were no changes incorporated to the proposed guidance as a result of these comments, and the revisions were adopted as exposed.

130. In 2019, revisions to the definition and scope section were also adopted to clarify the identification of affiliate/related party transactions (agenda item 2019-03) as well as to explicitly capture mortgage-referenced securities issued from a government sponsored enterprise in scope of SSAP No. 43 (agenda item 2018-17). The inclusion of mortgage-referenced securities was a distinct departure from the "trust" structure required in determining inclusion within scope of SSAP No. 43, but was incorporated as the securities (with the referenced pool of assets), functions similarly to the securities held in trust and the referenced pool of assets can be assessed for the underlying credit risk

131. Between the adoption of agenda item 2010-12 and the items adopted in 2019, there were several revisions to SSAP No. 43, but those revisions did not impact the definition / scope of the statement. Those revisions included changes to incorporate price-point NAIC designations, guidance for interim financials for RMBC/CMBS, clarification of disclosures, updating Q/A guidance, and guidance for prepayment fees.

132. Definition of loan-backed and structured securities in the "As of March 2020" AP&P Manual:

> 2. Loan-backed securities are defined as securitized assets not included in structured securities, as defined below, for which the payment of interest and/or principal is directly proportional to the payments received by the issuer from the underlying assets, including but not limited to pass-through securities, lease-backed securities, and equipment trust certificates.
>
> 3. Structured securities are defined as loan-backed securities which have been divided into two or more classes for which the payment of interest and/or principal of any class of securities has

been allocated in a manner which is not proportional to payments received by the issuer from the underlying assets.

4. Loan-backed securities are issued by special-purpose corporations or trusts (issuer) established by a sponsoring organization. The assets securing the loan-backed obligation are acquired by the issuer and pledged to an independent trustee until the issuer's obligation has been fully satisfied. The investor only has direct recourse to the issuer's assets, but may have secondary recourse to third parties through insurance or guarantee for repayment of the obligation. As a result, the sponsor and its other affiliates may have no financial obligation under the instrument, although one of those entities may retain the responsibility for servicing the underlying assets. Some sponsors do guarantee the performance of the underlying assets.

a. In determining whether a loan-backed structure is a related party investment, consideration shall be given to the substance of the transaction, and the parties whose action or performance materially impacts the insurance reporting entity holding the security. For example, although a loan-backed security may be acquired from a non-related issuer, if the assets held in trust predominantly[4] reflect assets issued by affiliates of the insurance reporting entity, and the insurance reporting entity only has direct recourse to the assets held in trust, the transaction shall be considered an affiliated investment, and the transaction shall also subject to the accounting and reporting provisions in *SSAP No. 25—Affiliates and Other Related Parties*.

5. Mortgage-referenced securities do not meet the definition of a loan-backed or structured security but are explicitly captured in scope of this statement. In order to qualify as a mortgage-referenced security, the security must be issued by a government sponsored enterprise[5] in the form of a "credit risk transfer" in which the issued security is tied to a referenced pool of mortgages. These securities do not qualify as "loan-backed securities" as the pool of mortgages are not held in trust and the amounts due under the investment are not backed or secured by the mortgage loans. Rather, these items reflect instruments in which the payments received are linked to the credit and principal payment risk of the underlying mortgage loan borrowers captured in the referenced pool of mortgages. For these instruments, reporting entity holders may not receive a return of their full principal as principal repayment is contingent on repayment by the mortgage loan borrowers in the referenced pool of mortgages. Unless specifically noted, the provisions for loan-backed securities within this standard apply to mortgage-referenced securities.

6. Investments within the scope of this statement are also subject to the provisions and disclosure requirements of SSAP No. 25 if the SSAP No. 43 transaction is a related party arrangement[6]. Loan-backed and structured securities meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement and SSAP No. 25.

[4] In applying this guidance, a reporting entity is not required to complete a detailed review of the assets held in trust to determine the extent, if any, the assets were issued by related parties. Rather, this guidance is a principle concept intended to prevent situations in which related party transactions (particularly those involving affiliates) is knowingly captured in a SSAP No. 43 structure and not identified as a related party transaction (or not reported as an affiliated investment on the investment schedule) because of the involvement of a non-related trustee or SSAP No. 43 security issuer. As identified in *SSAP No. 25—Affiliates and Other Related Parties*, it is erroneous to conclude that the inclusion of a non-related intermediary, or the presence of non-related assets in a structure predominantly comprised of related party investments, eliminates the requirement to identify and assess the investment transaction as a related party arrangement.

[5] Currently, only Fannie Mae and Freddie Mac are the government sponsored entities that issue qualifying mortgage-referenced securities. However, this guidance would apply to mortgage-referenced securities issued by any other government sponsored entity that subsequently engages in the transfer of residential mortgage credit risk.

[6] As discussed in paragraph 4.a. of this statement, a SSAP No. 43 security may still be considered a related party transaction even if the asset trustee or security issuer is a non-related party.

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7. The scope of this statement encompasses all types of loan-backed and structured securities, including, but not limited to, the following:

a. Loan-backed and structured securities acquired at origination,

b. Loan-backed and structured securities acquired subsequent to origination for which it is probable, at acquisition, that the reporting entity will be able to collect all contractually required payments receivable, and are accounted for at acquisition under SSAP No. 103R,

c. Loan-backed and structured securities for which it is probable, either known at acquisition or identified during the holding period[7], that the reporting entity will be unable to collect all contractually required payments receivable, and

d. Transferor's beneficial interests in securitization transactions that are accounted for as sales under SSAP No. 103R and purchased beneficial interests in securitized financial assets[8].

Benefits of Reporting in Scope of SSAP No. 43 – Before the Principles-Based Definition

133. There are a variety of benefits for reporting investments as bonds on Schedule D-1. Also, with regards to bifurcated impairment, capturing an investment in scope of SSAP No. 43 may be more advantageous than capturing in scope of *SSAP No. 26—Bonds*. These benefits include:

a. Capturing an investment in scope of SSAP No. 26 or SSAP No. 43 results with reporting the investment on Schedule D-1, Long-Term Bonds. By reporting on this bond schedule, the investment is generally not subject to investment limitations, the asset is admitted and the investment has the benefit of lower risk-based capital (RBC) charges based on NAIC designation. (Moving held equity instruments from Schedule BA into a SSAP No. 43 trust has been particularly noted as providing "regulatory capital relief.")

b. Capturing an investment in scope of SSAP No. 26 or SSAP No. 43 may result in amortized cost reporting and a delay in recognizing decreases in value or other-than-temporary impairments than if the assets held in trust were reported separately on the statutory financial statements.

i. Under the SSAP No. 43 bifurcated impairment model, an entity is not required to recognize an OTTI or deviate from an amortized cost measurement as long as the entity can assert that they have the intent and ability to hold the SSAP No. 43 security to recover the amortized cost basis and there is no non-interest related decline. (This has been a key factor in the PPN design, as a high-quality bond is placed in trust (along with other assets), and the bond – over several years – will single-handedly satisfy the contractual requirements of the 43 issued security, preventing any recognition of OTTI or a reduction of NAIC designation even when the other securities held in trust could completely default to zero.)

ii. The SSAP No. 43 bifurcated impairment can be considered an advantage over SSAP No. 26 as under SSAP No. 43, if there is an intent and ability to hold the asset, a reporting entity only has to recognize an OTTI for the portion of the non-

[7] Securities classified within the type of paragraph 7.a. or 7.b. may be required to change classification to type 6.c. when it becomes probable that the reporting entity will be unable to collect all contractually required payments receivable.

[8] The accounting requirements related to these types of securities included in paragraphs 22-25 shall be determined at acquisition or initial transfer.

interest related loss. Under SSAP No. 26, if there is any assessed OTTI (despite if interest or credit related), a reporting entity must recognize an OTTI down to the then-current fair value for the security.

iii. Prior to the principles-based bond project, guidance in SSAP No. 43 did not differentiate between different types of tranches or payment streams for the issued securities. This is easiest to illustrate through the "equity" tranche of a SSAP No. 43 investment but could be a factor if payments are provided sequentially. (Sequential payments are used to pay the senior notes first, until paid in full, before payments are allocated to junior notes.) For the "equity" tranche, which is a term that refers to the junior-most layer of issued SSAP No. 43 securities, this tranche is the first-loss position and only receives payment after all other layers have been satisfied. Without prior guidance in SSAP No. 43 for this layer, entities were able to classify these residual tranches as "bonds" on Schedule D-1, which did not properly reflect the nature of those investments.

c. SSAP No. 43 permits admittance of the security without any verification to the assets held in trust. As such, if a reporting entity was to derecognize a joint venture or LLC from Schedule BA and reacquire through the ownership of a SSAP No. 43 security, the reporting entity would be permitted to admit the security without any verification of the joint venture or LLC held in trust. Under *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, assets must have audited support (audited U.S. GAAP financials, audited reconciliation to U.S. GAAP, audited IFRS financials or audited U.S. tax basis equity) in order to be admitted in the statutory financial statements.

Key Issues with Scope / Definition Application of SSAP No. 43 – Before the Principles-Based Definition

134. With the existing guidance in SSAP No. 43, there are no restrictions to the assets that can be placed in trust and used to support securities issued from the trust structure. Although these structural designs are referred to as "securitizations" and reported as debt instruments, these investment structures may not reflect actual securitizations in which cash flows from multiple contractual debt obligations held in trust are used to pay principal and interest payments on the trust-issued security. The assets being securitized may include assets that are not cash flow producing, creating reliance on an underlying collateral valuation risk. Or, there may be no economic substance to the use of the securitization structure, such that the insurer is in the same economic position as owning the underlying assets directly. As a result, there is a regulatory concern that assets being represented as bonds may contain unidentifiable risks that regulators would not traditionally associate with bond risk.

135. As an additional issue of the existing guidance, questions have been raised on whether securities captured in scope of SSAP No. 43 would be "asset-backed securities" as defined by the Code of Federal Regulations (17 CFR 229.1101(c)). These questions have arisen as an SEC identified nationally recognized statistical rating organization (NRSRO) must be specifically approved to provide ratings of "asset-backed securities." Since the CFR definition is different than what is permitted in scope of SSAP No. 43, a rating from an NRSRO approved as a credit rating provider (CRP) that may not be approved by the SEC for "asset-backed securities" could provide a valid rating for a SSAP No. 43 instrument permitted as "filing exempt" if that asset was not an "asset-backed security." This has caused questions as regulators have identified designations given by CRPs not SEC approved to provide "ABS" designations and have questioned the use of these CRP ratings in determining the NAIC designation.

Issue Paper Exhibits:

Staff Note: Although not captured, the final issue paper retained for historical purposes will include the following Exhibits reflecting the adopted guidance to initially reflect the principles-based bond definition.

Exhibit 1 – SSAP No. 26—Bonds

Exhibit 2 – SSAP No. 43—Asset-Backed Securities

Exhibit 3 – SSAP No. 21—Other Admitted Assets

Exhibit 4 – Revisions to Other SSAPs

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/Bond IP - Adopted 2024 Summer.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Review of *INT 03-02: Modification to an Existing Intercompany Pooling Arrangement*

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
This agenda item provides a review of Interpretation (INT) 03-02*: Modification to an Existing Intercompany Pooling Arrangement*, because of conflicts between INT 03-02 and *SSAP No. 25—Affiliates and Other Related Parties.* This agenda item was prompted by the recent focus of Statutory Accounting Principles (E) Working Group on related party transactions, recent queries to NAIC about how broadly to apply the guidance in INT 03-02 and the review of the SSAP No. 62R, paragraph INT 03-02 addresses the valuation of bonds in instances when bonds are used instead of cash for the payment among affiliates for amounts due on modifications to existing intercompany reinsurance pooling contracts. The discrepancy between the INT 03-02 and SSAP No. 25 has been identified through recent discussions evaluating related party transactions. Key excerpts of INT 03-02 are in the Authoritative Literature section below.

The primary accounting question that is a concern for this agenda item is INT 03-02, paragraph 11b which asks, "What is the appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement?" The response provided in INT 03-02, paragraph 13 is, "The appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement is statutory book value for assets and statutory value for liabilities. Book value is defined in the glossary of the *Accounting Practices and Procedure Manual*."

INT 03-02 states that it is an interpretation of the following three reinsurance statements: *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*, *SSAP No. 62R—Property and Casualty Reinsurance* and *SSAP No. 63—Underwriting Pools. SSAP No. 25—Affiliates and Other Related Parties* is not listed as an interpreted statement. However, as described below, the consensus in INT 03-02, paragraph 13 is not consistent with the guidance in SSAP No. 25 regarding economic transactions between related parties.

The result of the consensus in INT 03-02, paragraph 13 allows assets used in affiliated payments for reinsurance contracts, which modify existing intercompany reinsurance pooling agreements, to be transferred using statutory book value. Note that in most cases, this means that bonds, which are likely the primary assets that would be used, would typically have a statutory book value that reflects amortized cost. The valuation of assets using statutory book value on transfer to an affiliate can result in substantial differences from the cash equivalent (fair value) for the payment due. For example, bonds reported at amortized cost book value could have a corresponding fair value that is materially higher or lower. This difference in valuation can result in an unacknowledged dividend or with the passing on of an investment loss.

SSAP No. 25 describes economic transactions and non-economic transactions (See Authoritative Literature). Economic transactions are defined as arm's-length transactions which results in the transfer of the risks and rewards of ownership and represents a consummated act thereof, i.e., "permanence." SSAP No. 25, paragraph 18 indicates that economic transactions between related parties shall be recorded at fair value at the date of the transaction and also notes that to the extent that the related parties are affiliates under common control, the controlling reporting

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entity shall defer the effects of such transactions that result in gains or increases in surplus until such time that the asset is sold outside the group.

It is quite possible, by using transfers at book value instead of fair value, to design a transaction with a very significant economic effect. The following example illustrates the concern with the results of the guidance in INT 03-02. For this example, $100 million is due on an existing intercompany reinsurance pooling agreement. INT 03-02 would allow bonds to be settled using statutory book value which may not be reflective of the fair value equivalent of a cash settlement.

Asset Used to Settle	Book Value (millions) Measurement for Settlement	Fair Value (millions)	Result	Consistent with SSAP No. 25 for an Economic Transaction?
Cash	$100	$100	No difference in basis	Yes
Bonds	$100	$ 85	$15 difference in fair value means the paid party received an amount less than what is actually owed. This approach could allow reporting entities to transfer impaired assets to affiliates in lieu of assessing OTTI.	No
Bonds	$100	$110	$10 difference in fair value means the paid party has received an asset greater than what was owed. This dynamic could result in an unrecognized gain or dividend.	No

The INT 03-02 direction to use statutory book value for the transfer of bonds between affiliated entities in most instances would conflict with the primary guidance on affiliated transactions contained in *SSAP No. 25—Affiliates and Other Related Parties.* For example, economic transactions between related parties are valued using fair value. (There are more nuances in SSAP No. 25 when payments have the possibility of being economic for one entity and noneconomic for an upper-level parent). NAIC staff recommends that the treatment of transfers of assets between affiliates should be consistent for all intercompany transactions and there is not a compelling need to be different if assets are transferred instead of cash for intercompany reinsurance.

Under INT 03-02, for intercompany reinsurance transactions, takes an approach that either SSAP No. 25 or SSAP No. 62R may apply, but multiple Working Group discussions have noted that SSAP No. 25 provides the overarching guidance that is relevant in evaluating all related party transactions. INT 03-02, paragraph 8 indicates that the statutory accounting intention is to avoid surplus gains for the ceding entity as a result of implementing a modification to an intercompany pooling arrangement. However, the guidance in SSAP No, 62R, paragraph 37 uses a more punitive method of accounting if there is a gain in surplus to the ceding entity as a result of the intercompany reinsurance transaction. Therefore, NAIC staff would characterize the SSAP No. 62R guidance as imposing an accounting penalty if there is a gain, rather than seeking to avoid recognizing such a gain. The INT also characterizes SSAP No. 25 as being for isolated transactions, which is inconsistent with discussions of the Working Group on the applicability of SSAP No. 25.

SSAP No. 62R, paragraph 36d (see Authoritative Literature) includes an exception to retroactive reinsurance accounting which allows prospective accounting treatment for intercompany reinsurance agreements and any amendments thereto, among companies 100% owned by a common parent or ultimate controlling person provided there is no gain in surplus as a result of the transaction. Paragraph 37 provides that if there is a gain to the ceding entity that a more restrictive method of accounting is required which is less beneficial to the financial statements. Whereas the INT tries to argue that statutory intent is to avoid surplus gain, NAIC staff would note that the goal is not to avoid gain as a result of the reinsurance transaction, but to impose a different accounting if there is a gain. NAIC staff would characterize evaluating reinsurance agreements for SSAP No. 62R, paragraph 36d or paragraph

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37 as using the cash flows or corresponding equivalent fair value (cash equivalent) of the amounts payable or receivable in the reinsurance transactions to determine if there is a gain or loss to the ceding entity. The reinsurance cash flows evaluated should be the same as if the bond was sold for fair value and resulting cash equivalent obligation was paid. The fact that the bond sold has a gain or loss is not part of the reinsurance contract evaluation, the reinsurance contract that is an economic transaction evaluation is based on the cash equivalent value of the assets transferred less the liabilities transferred. The evaluation of gain or loss on the intercompany reinsurance transaction should give the same answer if either cash or assets were transferred.

Existing Authoritative Literature:

03-02*: Modification to an Existing Intercompany Pooling Arrangement* is attached in full. The following excerpts are from INT 03-02:

> 8. Therefore, based on the foregoing guidance and background, the statutory accounting intent is to avoid surplus gains for the ceding entity as a result of implementing a modification to an intercompany pooling arrangement. On that basis, such a modification does not represent an economic transaction to the insurance group or to the impacted companies. As such, the transfer of both the assets and the liabilities valued at statutory book value ensures that there is no impact to surplus as a result of implementing a modification to an existing pooling arrangement.
>
> 11. The accounting issues are:
>
> a. What is the relevant guidance for modifications to intercompany pooling arrangements?
>
> b. What is the appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement?
>
> The Working Group reached a consensus as follows:
>
> 12. SSAP No. 62R provides accounting for property and casualty reinsurance agreements including specific guidance on intercompany pooling agreements. SSAP No. 62R provides two methods of accounting for changes in intercompany pooling agreements, depending on whether or not the pooling results in a gain in surplus.
>
> 13. The appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement is statutory book value for assets and statutory value for liabilities. Book value is defined in the glossary of the *Accounting Practices and Procedure Manual*.

SSAP No. 25—Affiliates and Other Related Parties

> **Transactions Involving the Exchange of Assets or Liabilities**
>
> 14. An arm's-length transaction is defined as a transaction in which willing parties, each being reasonably aware of all relevant facts and neither under compulsion to buy, sell, or loan, would be willing to participate. A transaction between related parties involving the exchange of assets or liabilities shall be designated as either an economic transaction or non-economic transaction. An economic transaction is defined as an arm's-length transaction which results in the transfer of the risks and rewards of ownership and represents a consummated act thereof, i.e., "permanence." The appearance of permanence is also an important criterion in assessing the economic substance of a transaction. In order for a transaction to have economic substance and thus warrant revenue (loss) recognition, it must appear unlikely to be reversed. If subsequent events or transactions reverse the effect of an earlier transaction prior to the issuance of the financial statements, the reversal shall be considered in determining whether economic substance existed in the case of the original transaction. Subsequent events are addressed in SSAP No. 9—Subsequent Events. An economic transaction must represent a bonafide business purpose demonstrable in measurable

terms. A transaction which results in the mere inflation of surplus without any other demonstrable and measurable betterment is not an economic transaction. The statutory accounting shall follow the substance, not the form of the transaction.

15. In determining whether there has been a transfer of the risks and rewards of ownership in the transfer of assets or liabilities between related parties, the following—and any other relevant facts and circumstances related to the transaction—shall be considered:

a. Whether the seller has a continuing involvement in the transaction or in the financial interest transferred, such as through the exercise of managerial authority to a degree usually associated with ownership;

b. Whether there is an absence of significant financial investment by the buyer in the financial interest transferred, as evidenced, for example, by a token down payment or by a concurrent loan to the buyer;

c. Whether repayment of debt that constitutes the principal consideration in the transaction is dependent on the generation of sufficient funds from the asset transferred;

d. Whether limitations or restrictions exist on the buyer's use of the financial interest transferred or on the profits arising from it;

e. Whether there is retention of effective control of the financial interest by the seller.

16. A transaction between related parties may meet the criteria for treatment as an economic transaction at one level of financial reporting but may not meet such criteria at another level of financial reporting. An example of such a transaction is a reporting entity purchasing securities at fair value from an affiliated reporting entity that carried the securities at amortized cost. This transaction meets the criteria of an economic transaction at this level of financial reporting, and therefore, the selling reporting entity would record a gain and the acquiring reporting entity would record the securities at their cost (fair value on the transaction date). At the common parent level of reporting, this transaction has resulted in the mere inflation of surplus, and therefore, is a non-economic transaction. The parent reporting entity shall defer the net effects of any gain or increase in surplus resulting from such transactions by recording a deferred gain and an unrealized loss. The deferred gain shall not be recognized by the parent reporting entity unless and until arms-length transaction(s) with independent third parties give rise to appropriate recognition of the gain.

17. A non-economic transaction is defined as any transaction that does not meet the criteria of an economic transaction. Similar to the situation described in paragraph 16, transfers of assets from a parent reporting entity to a subsidiary, controlled or affiliated entity shall be treated as non-economic transactions at the parent reporting level because the parent has continuing indirect involvement in the assets.

18. When accounting for a specific transaction, reporting entities shall use the following valuation methods:

a. Economic transactions between related parties shall be recorded at fair value at the date of the transaction. To the extent that the related parties are affiliates under common control, the controlling reporting entity shall defer the effects of such transactions that result in gains or increases in surplus (see paragraph 16);

b. Non-economic transactions between reporting entities, which meet the definition of related parties above, shall be recorded at the lower of existing book values or fair values at the date of the transaction;

c. Non-economic transactions between a reporting entity and an entity that has no significant ongoing operations other than to hold assets that are primarily for the direct or indirect benefit or use of the reporting entity or its affiliates, shall be recorded at the fair value at the date of the transaction; however, to the extent that the transaction results in a gain, that gain shall be deferred until such time as permanence can be verified;

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d. Transactions which are designed to avoid statutory accounting practices shall be reported as if the reporting entity continued to own the assets or to be obligated for a liability directly instead of through a subsidiary.

Examples of transactions deemed to be non-economic include security swaps of similar issues between or among affiliated companies, and swaps of dissimilar issues accompanied by exchanges of liabilities between or among affiliates.

Transactions Involving Services

19. Transactions involving services between related parties can take a variety of different forms. One of the significant factors as to whether these transactions will be deemed to be arm's length is the amount charged for such services. In general, amounts charged for services are based either on current market rates or on allocations of costs. Determining market rates for services is difficult because the circumstances surrounding each transaction are unique. Unlike transactions involving the exchange of assets and liabilities between related parties, transactions for services create income on one party's books and expense on the second party's books, and therefore, do not lend themselves to the mere inflation of surplus. These arrangements are generally subject to regulatory approval.

20. Transactions involving services provided between related parties shall be recorded at the amount charged[1]. Regulatory scrutiny of related party transactions where amounts charged for services do not meet the fair and reasonable standard established by Appendix A-440, may result in (a) amounts charged being recharacterized as dividends or capital contributions, (b) transactions being reversed, (c) receivable balances being nonadmitted, or (d) other regulatory action. Expenses that result from cost allocations shall be allocated subject to the same fair and reasonable standards, and the books and records of each party shall disclose clearly and accurately the precise nature and details of the transaction. See *SSAP No 70—Allocation of Expenses* for additional discussion regarding the allocation of expenses.

SSAP No. 62R—Property and Casualty Reinsurance provides the following (**bolding added for emphasis**):

36. The accounting principles for retroactive reinsurance agreements in paragraph 34 shall not apply to the following types of agreements (which shall be accounted for as prospective reinsurance agreements unless otherwise provided in this statement):

a. Structured settlement annuities for individual claims purchased to implement settlements of policy obligations;

b. Novations (i.e., (i) transactions in which the original direct insurer's obligations are completely extinguished, resulting in no further exposure to loss arising on the business novated or (ii) transactions in which the original assuming entity's obligations are completely extinguished) resulting in no further exposure to loss arising on the business novated, provided that (1) the parties to the transaction are not affiliates (or if affiliates, that the transaction has the prior approval of the domiciliary regulators of the parties) and (2) the accounting for the original reinsurance agreement will not be altered from retroactive to prospective;

c. The termination of, or reduction in participation in, reinsurance treaties entered into in the ordinary course of business;

[1] The amount charged shall be reviewed when there are any modifications or waivers subsequent to the establishment of the contract terms. If waivers or modifications to amounts charged occur, the related party transaction shall be reassessed to determine whether the contract continues to reflect fair and reasonable standards. If the transaction was with a parent or other stockholder and the charge for services has been fully waived, then the guidance in SSAP No. 72 for recognition as contributed capital (forgiveness of reporting entity obligation) or as a dividend (forgiveness of amount owed to the reporting entity) shall apply.

d. Intercompany reinsurance agreements, and any amendments thereto, among companies 100% owned by a common parent or ultimate controlling person provided there is no gain in surplus as a result of the transaction; or

e. Reinsurance/retrocession agreements that meet the criteria of property/casualty run-off agreements described in paragraphs 102-105.

37. **Retroactive reinsurance agreements resulting in surplus gain to the ceding entity (with or without risk transfer)** entered into between affiliates or between insurers under common control (as those terms are defined in Appendix A-440) shall be reported as follows:

a. The consideration paid by the ceding entity shall be recorded as a deposit and reported as a nonadmitted asset; and

b. No deduction shall be made from loss and loss adjustment expense reserves on the ceding entity's balance sheet, schedules, and exhibits.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

INT 03-02 was exposed in March of 2003 and adopted in June 2003. The interpretation was not subsequently amended. The final vote on this consensus had three members opposed. The March 2003 exposure received six different comment letters to the Emerging Accounting Issues (E) Working Group from: 1) Ohio (EAIWG member); 2) New Hampshire (EAIWG member); 3) Interested parties, 4) Liberty Mutual and 5) PricewaterhouseCoopers (one of the very few letters ever submitted directly by the firm.) and 6) CNA. Five out of the six commenters noted concerns that the proposed guidance (which was ultimately adopted) would conflict with SSAP No. 25 guidance regarding economic transactions. While the interested parties' comment letter was more neutral, the verbal comments provided supported the use of SSAP No. 25.

Several commenters recommended not adopting the guidance regarding the use of book value and instead following SSAP No. 25 guidance for economic and non-economic transactions. The commenters noted that SSAP No. 25 directs the use of fair value when such transactions meet the definition of an economic transaction and that tax regulations would provide a result similar to SSAP No. 25. Multiple comments noted concerns similar to those highlighted in the illustration above. Commenters also noted that intercompany pooling reinsurance transactions are economic transactions. They noted that when assets (such as bonds valued at amortized cost) are transferred, if the assets have a different fair value than book value, that difference should be recognized since the transferor no longer controls the assets. Commenters also noted that treatment for reinsurance transactions for asset transfers should not be different than the treatment for other intercompany transactions.

CNA comments were supportive of adopting the exposed consensus, the comment letter provided illustrations and noted that intercompany reinsurance agreements were subject to regulatory approval. The comments tried to illustrate concerns possibly having premature gain / surplus recognition.

The June 2003 minutes Emerging Accounting Issues (E) Working Group discussion on the INT 03-02 are excerpted below.

> The working group was referred to INT 03-02: *Modification to an existing intercompany pooling arrangement* (Attachment D). Written comments were received from Ohio, New Hampshire and interested parties. Ohio and New Hampshire believe that the transfer of assets and liabilities in an intercompany pooling arrangement constitute an economic transaction and the accounting guidance in SSAP No. 25—*Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties* (SSAP No. 25), should be followed. As such, the assets should be transferred at fair value and the ceding entity should record a realized gain or loss. Keith Bell (Travelers) spoke on behalf of interested parties. Interested parties commented that if the transaction was considered to be an economic transaction, SSAP No. 25 should be followed. If the modification of an intercompany pooling arrangement is considered a noneconomic transaction, the guidance in SSAP No.62—*Property and Casualty Reinsurance*(SSAP No. 62) is applied,

as such, statutory book value should be used for assets and statutory value should be used for liabilities. Jeff Alton (CNA) presented his comments by summarizing the statements made in his comment letter. Mr. Alton stated that no revenue recognition should occur and suggested using a modified statutory book value for transferring assets and liabilities. Mr. Clark stated that the Statutory Accounting Principles Working Group must address the recommended transfer at modified statutory book value as this recommendation would require substantive adjustments to statutory accounting principles. Shelly Zimmerman (Liberty Mutual) provided comments which supported that intercompany pooling changes should follow the accounting guidance in SSAP No. 25 as these are economic transactions between affiliates. Jean Connelly (PriceWaterhouseCoopers) provided comments that summarize those outlined in the comment letter. Ms. Connelly stated that intercompany pooling arrangements are economic transactions and that INT 03-01 provides a substantive change to SSAP No. 25.

Mr. Johnson then stated that he believes there is a stronger case for non-economic transaction treatment and as such, statutory book value is appropriate for valuation purposes. Additionally, all these transactions are subject to regulatory review under the Insurance Holding Company Act, affording regulators some control over the approval of these transactions. Mr. Fritsch commented that if this guidance is not adopted in the form of a new interpretation, SSAP No. 25 should be followed. Mr. Alton stated that he believes the current guidance in effect for intercompany pooling arrangements exists in SSAP No. 62, paragraph 30d which supports surplus neutrality: hence, the need is for an interpretation of paragraph 30d. Mr. Johnson stated that language clarification in SSAP No.61—*Life, Deposit-Type and Accident and Health Reinsurance*(SSAP No. 61) and SSAP No. 62 should be addressed as a project of the reinsurance subgroup of the SAPWG. Mr. Johnson made a motion to adopt Interpretation 03-02 with deletion of the first two sentences in paragraph 11. Mr. Stolte seconded the motion. Mr. Johnson requested a roll call vote. There were 9 yeas from Alabama, Connecticut, Florida, Illinois, Louisiana, Michigan, Texas, Pennsylvania and Virginia. There were 3 nays from New York, Ohio, and Wisconsin. Therefore, the working group adopted Interpretation 03-02 by consensus. Mr. Johnson also made a motion to refer to the Reinsurance Subgroup of the SAPWG, review of the current guidance in SSAP No. 61, SSAP No. 62 and SSAP No. 63—*Underwriting Pools and Associations Including Intercompany Pools.* Mr. Ford seconded the motion. The working group unanimously adopted the referral.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): Not Applicable

Staff Review Completed by: Robin Marcotte – NAIC Staff, July - 2022

Staff Recommendation: NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose the intent to nullify INT 03-02, as it is inconsistent with SSAP No. 25 guidance regarding economic and non-economic transactions between related parties. The guidance in INT 03-02 can result with in essence, unrecognized gains (dividends) or losses through the using the statutory book valuation when using assets (bonds) to make payments to affiliates for modifications to existing intercompany reinsurance pooling agreements. Treatment of transfers of assets between affiliates should be consistent for all intercompany transactions and there is not a compelling need to be different when valuing assets for intercompany reinsurance transactions.

Status:
On August 10, 2022, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and exposed the intent to nullify INT 03-02.

On December 13, 2022, the Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and re-exposed the intent to nullify INT 03-02. This re-exposure requested industry to provide comments on specific instances in which the interpretation was being applied. In addition, the following key points were noted for consideration during the exposure in response to some of the comments received.

1. In the current interest rate environment, the fair value of many bonds is below book value. For example, a bond with an amortized cost of 100 with a fair value of 85. The way INT 03-02 is written a bond with a fair value of 85 could be used to settle an intercompany reinsurance pooling obligation of 100. If the reporting entity paid with cash, they would be required to pay $100. The actual cash value of obligations when they are extinguished is a relevant measure of the transaction.

2. Using book value for measurement of payments between affiliates can result in either unrecognized or in effect dividend or losses. SSAP No. 25 requires such transfers of assets between affiliates to use fair value. If a subsidiary can pay the parent with assets that have a lower fair value than book value (ex, owes $100 but pays with a bond of 85), this has a similar effect as an unrecognized capital contribution to the subsidiary. SSAP No. 72 requires a capital contribution to be valued using fair value.

3. At the ultimate parent level such transfer of assets (in accordance with SSAP No. 25 guidance) may be noneconomic in that the parent continues to hold an interest in the same assets. Therefore, at the parent level, such transfers of assets may result in the deferral of gains. Staff believes that losses would not be deferred at the ultimate parent level.

4. While it may be more expedient to pay intercompany reinsurance pooling transactions with assets, the valuation used should be similar to if the obligation was extinguished with cash. Therefore, an entity can still choose to pay with assets, they just need to be valued consistently with SSAP No. 25 guidance.

5. SSAP No. 62R, paragraph 36d provides an exception to retroactive reinsurance accounting guidance which allows for prospective accounting treatment for intercompany reinsurance among 100% owned affiliated provided there is no gain to the ceding entity. If there is again to the ceding entity, there is guidance in SSAP No. 62R, paragraph 37 which requires a more punitive method of accounting than either prospective or retroactive reinsurance accounting. Therefore, NAIC staff comment is that the statutory accounting objective is to provide different treatment for retroactive reinsurance contracts if there is a gain to the ceding entity. This is another reason that the guidance in INT 03-02 is problematic. The object is to correctly measure the effects of the contract, which drives the accounting. The objective is not to obscure whether there is a gain to the ceding entity, which can happen in the event that the assets used in payment are not measured correctly.

6. Interested parties noted that modifications to intercompany pooling arrangements are typically effective retroactive to the beginning of the year. Staff notes that the payment value when the transaction is settled should be equivalent to the cash value of what is owed on the date of extinguishment of the liability.

7. Many of the interested parties' comments regarding GAAP use of book value are more relevant to consolidated basis accounting which is not consistent with the legal entity basis of statutory accounting.

8. Interested parties' comments noted that there is a difference in treatment for intercompany pooling participants who are not 100% owned by a common parent. NAIC staff notes that retroactive pooling agreement changes with participants that are not 100% under common control do not meet the exception to retroactive accounting provided in SSAP No. 62R, paragraph 36d. NAIC staff notes that SSAP No. 62R, paragraph 37 provides guidance for retroactive reinsurance agreements among affiliates where there is a gain to the ceding entity. Therefore, the regulatory objective is not to avoid gain but to properly account for intercompany retroactive contracts that include gains.

On March 22, 2023, the Working Group re-exposed the intent to nullify INT 03-02, effective December 31, 2023. The nullification is proposed as INT 03-02 is inconsistent with SSAP No. 25 guidance regarding economic and non-economic transactions between related parties. The guidance in INT 03-02 can result with, in essence, unrecognized gains (dividends) or losses through the using the statutory book valuation when using assets (bonds) to make payments to affiliates for modifications to existing intercompany reinsurance pooling agreements.

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Treatment of transfers of assets between affiliates should be consistent for all intercompany transactions and there is not a compelling need to be different when valuing assets for intercompany reinsurance transactions.

On August 13, 2023, the Statutory Accounting Principles (E) Working Group re-exposed the intent to nullify INT 03-02 and directed NAIC staff to work with industry regarding some of their comments and examples to be submitted by industry.

On December 1, 2023, the Statutory Accounting Principles (E) Working Group deferred action on this agenda item and directed NAIC staff to continue working with interested parties on the proposal.

On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed its intent to nullify INT 03-02, and exposed revisions to *SSAP No. 25—Affiliates and Other Related Parties* and *SSAP No. 63—Underwriting Pools* to address transfers of assets when modifying intercompany pooling agreements. The exposed revisions were based on interested parties' comments with minor edits proposed by NAIC staff.

Exposed Revisions to SSAP No. 25 and SSAP No. 63 are illustrated below.

SSAP No. 25—Affiliates and Other Related Parties

4. If a company transfers assets or liabilities to effectuate a modification to an existing intercompany pooling arrangement, the transaction, including the transfer of assets, shall be accounted for and valued in accordance with the guidance in *SSAP No. 63—Underwriting Pools*. The guidance in SSAP No. 63 regarding the transfers of assets or liabilities to effectuate a modification of an intercompany pooling arrangements shall not be applied or analogized to other transactions involving transfers of assets and liabilities.

SSAP No. 63—Underwriting Pools (only impacted paragraph are reflected.)

1. This statement establishes statutory accounting principles for underwriting pools and associations, including intercompany pooling arrangements.

8. Insurance groups that utilize intercompany pooling arrangements often modify these arrangements from time to time for various business reasons. These business reasons commonly include mergers, acquisitions, dispositions, or a restructuring of the group's legal entity structure. In order to effectuate a relatively simple modification, such as changing pooling participation percentages without changing the pool participants, companies often simply amend the existing pooling agreement. Alternatively, in order to effectuate a more complex modification, such as changing (by adding or removing) the number of pool participants, a company may commute the existing pooling agreement and execute a new pooling agreement(s). In conjunction with executing the appropriate intercompany pooling agreements, a transfer of assets and liabilities amongst the impacted affiliates may also be required in order to implement the new pooling agreement(s). The following subparagraphs provide guidance specific to modifications of intercompany pooling arrangements and shall not be applied to an analogous transaction or event.

a. The appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new intercompany pooling agreement(s) that serves to substantively modify an existing intercompany pooling arrangement is statutory book value for assets and statutory value for liabilities.

b. The net amount of the assets and liabilities being moved among entities as a result of a modification to an intercompany pooling shall be used to settle the intercompany payable/receivable (i.e., the assets that are transferred in conjunction with the modification) to minimize the amount of assets transferred in the modification.

12. Note that other applicable reinsurance guidance from *SSAP No. 61R—Life, Deposit Type and Accident and Health Reinsurance* or *SSAP No. 62R—Property and Casualty Reinsurance*, depending on

the type of business, applies to intercompany pooling arrangements and voluntary and involuntary pools. This includes the SSAP No. 62R guidance in paragraphs 33 through 39 regarding retroactive reinsurance.

New disclosure in paragraph 13

13.i For modifications to an existing intercompany pooling arrangement that involve the transfer of assets with fair values that differ from cost or amortized cost, the statement value and fair value of assets received or transferred by the reporting entity.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted as final, revisions to *SSAP No. 25—Affiliates and Other Related Parties* and *SSAP No. 63—Underwriting Pools* to address transfers of assets when modifying intercompany pooling agreements. Effective upon adoption, this agenda item also nullifies *INT 03-02: Modification to an Existing Intercompany Pooling Arrangement*. The exposed disclosure to SSAP No. 63, paragraph 13i, was modified from the exposure to incorporate revisions suggested by interested parties.

Adopted revisions are illustrated below.
SSAP No. 25—Affiliates and Other Related Parties

4. If a company transfers assets or liabilities to effectuate a modification to an existing intercompany pooling arrangement, the transaction, including the transfer of assets, shall be accounted for and valued in accordance with the guidance in *SSAP No. 63—Underwriting Pools*. The guidance in SSAP No. 63 regarding the transfers of assets or liabilities to effectuate a modification of an intercompany pooling arrangements shall not be applied or analogized to other transactions involving transfers of assets and liabilities.

SSAP No. 63—Underwriting Pools (only impacted paragraphs are reflected.)

1. This statement establishes statutory accounting principles for underwriting pools and associations, including intercompany pooling arrangements.

8. Insurance groups that utilize intercompany pooling arrangements often modify these arrangements from time to time for various business reasons. These business reasons commonly include mergers, acquisitions, dispositions, or a restructuring of the group's legal entity structure. In order to effectuate a relatively simple modification, such as changing pooling participation percentages without changing the pool participants, companies often simply amend the existing pooling agreement. Alternatively, in order to effectuate a more complex modification, such as changing (by adding or removing) the number of pool participants, a company may commute the existing pooling agreement and execute a new pooling agreement(s). In conjunction with executing the appropriate intercompany pooling agreements, a transfer of assets and liabilities amongst the impacted affiliates may also be required in order to implement the new pooling agreement(s). The following subparagraphs provide guidance specific to modifications of intercompany pooling arrangements and shall not be applied to an analogous transaction or event.

a. The appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new intercompany pooling agreement(s) that serves to substantively modify an existing intercompany pooling arrangement is statutory book value for assets and statutory value for liabilities.

b. The net amount of the assets and liabilities being moved among entities as a result of a modification to an intercompany pooling shall be used to settle the intercompany payable/receivable (i.e., the assets that are transferred in conjunction with the modification) to minimize the amount of assets transferred in the modification.

13. Note that other applicable reinsurance guidance from *SSAP No. 61R—Life, Deposit Type and Accident and Health Reinsurance* or *SSAP No. 62R—Property and Casualty Reinsurance*, depending on

the type of business, applies to intercompany pooling arrangements and voluntary and involuntary pools. This includes the SSAP No. 62R guidance in paragraphs 33 through 39 regarding retroactive reinsurance.

New disclosure in paragraph 13 as modified after exposure:

13.i The statement value and fair value of assets received or transferred by the reporting entity for modifications to an existing intercompany pooling arrangement that involved the transfer of assets with fair value that differ from statement value.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/22-12 - Review INT 03-02.docx

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Interpretation of the Emerging Accounting Issues (E) Working Group

INT 03-02: Modification to an Existing Intercompany Pooling Arrangement

NULLIFIED BY AGENDA ITEM 2022-12

INT 03-02 Dates Discussed

March 9, 2003; June 22, 2003; August 10, 2022; December 13, 2022; March 22, 2023; August 13, 2023; December 1, 2023; March 16, 2024; August 13, 2024

INT 03-02 References

Current:
SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance
SSAP No. 62R—Property and Casualty Reinsurance
SSAP No. 63—Underwriting Pools

INT 03-02 Issue

1. Insurance groups that utilize intercompany pooling arrangements often modify these arrangements from time to time for various business reasons. These business reasons commonly include mergers, acquisitions, dispositions or a restructuring of the group's legal entity structure. As an insurance group's business objectives and strategies evolve, it may be necessary for the insurance group's legal entity structure to similarly evolve in order to address the insurance group's business needs.

2. SSAP No. 63, paragraphs 5 and 7, defines and describes intercompany pooling as an arrangement among affiliated entities whereby "all of the pooled business is ceded to the lead entity and then retroceded back to the pool participants in accordance with their stipulated shares." This arrangement is established through "a conventional quota share reinsurance agreement…" Arrangements whereby there is one lead company that retains 100% of the pooled business and all or some of the affiliated companies have a 0% net share of the pool may qualify as intercompany pooling."

3. Therefore, in order to effectuate a modification to the existing intercompany pooling arrangement, companies must either 1) amend the existing reinsurance agreement, or 2) execute new agreements. The latter scenario may entail executing at least two agreements: a commutation of the existing agreement, and a new quota share agreement(s) that covers both past and future periods.

4. To illustrate, in order to effectuate a relatively simple modification, such as changing pooling participation percentages without changing the pool participants, companies often simply amend the existing pooling agreement. Alternatively, in order to effectuate a more complex modification, such as changing (by adding or removing) the number of pool participants, a company must commute the existing pooling agreement and execute a new quota share agreement(s). In conjunction with executing the appropriate reinsurance agreements, a transfer of assets and liabilities amongst the impacted affiliates is also required in order to implement the new reinsurance agreement(s). At issue is the appropriate valuation basis to be used for assets and liabilities that are transferred pursuant to the new reinsurance agreement(s).

5. Since SSAP No. 63 does not specifically address modifications to intercompany pooling arrangements, insurance groups that modify their intercompany pooling arrangements must refer elsewhere in Statutory Accounting Principles (SAP) for relevant guidance. The obvious guidance for such transactions is SSAP No. 62R since an intercompany pooling arrangement is, by definition, affiliated reinsurance. There is, however, a minority opinion that *SSAP No. 25—Affiliates and Other Related*

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Parties appears to apply due to the affiliated nature of these transactions. Since the guidance and intent of SSAP No. 62R and SSAP No. 25 provide for different valuation bases, this interpretation serves to provide definitive guidance as to which SSAP is relevant for these transactions and, therefore, clarify the appropriate valuation basis to be used for assets and liabilities transferred pursuant to a modification to an intercompany pooling arrangement.

SSAP No. 62R Approach:

6. This approach refers to the guidance and statutory accounting intent from SSAP No. 62R since intercompany pooling arrangements are defined and established through reinsurance. Further, since modifications to intercompany pooling agreements typically involve the transfer of net liabilities incurred since the inception of the existing pooling agreement (i.e., prior to the effective date of the new agreement), the retroactive reinsurance accounting guidance in paragraphs 33-39 of SSAP No. 62R is applicable. Paragraph 33 states that this special accounting treatment is warranted "due to the potential abuses involving the creation of surplus to policyholders and the distortion of underwriting results…" However, paragraph 36.d. specifically applies to intercompany reinsurance arrangements, and amendments to intercompany reinsurance agreements, since the reinsurance agreement is among companies 100% owned by a common parent. This paragraph allows prospective accounting treatment for intercompany reinsurance agreements that do not result in a gain in surplus as a result of the transaction.

7. To provide historical perspective, prior to the adoption (with modification) of FASB *Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts* (FAS 113) as SAP, paragraph 36.d. was added as one of the SAP modifications. The intent of adding paragraph 36.d. was to specifically exclude intercompany reinsurance agreements among entities 100% owned by a common parent from retroactive reinsurance accounting requirements as a result of amending or modifying these agreements, provided there is no surplus gain. The presumption in this intent was that there would be no gains to the ceding entity resulting from implementing amendments or modifications to these types of reinsurance agreements.

8. Therefore, based on the foregoing guidance and background, the statutory accounting intent is to avoid surplus gains for the ceding entity as a result of implementing a modification to an intercompany pooling arrangement. On that basis, such a modification does not represent an economic transaction to the insurance group or to the impacted companies. As such, the transfer of both the assets and the liabilities valued at statutory book value ensures that there is no impact to surplus as a result of implementing a modification to an existing pooling arrangement.

SSAP No. 25 Approach:

9. An approach different from that which refers to reinsurance accounting guidance is to refer to the guidance in SSAP No. 25 since some may view a modification to an intercompany pooling agreement as a related party transaction involving the exchange of assets or liabilities. In this case, paragraphs 14-18 of SSAP No. 25 would appear applicable. This guidance specifies differing valuation bases, depending on whether the transaction is considered an economic or a non-economic transaction. SSAP No. 25, paragraph 14, states that "…The appearance of permanence is also an important criterion is assessing the economic substance of a transaction. In order for a transaction to have economic substance and thus warrant revenue (loss) recognition, it must appear unlikely to be reversed …" Since insurance groups often modify intercompany pooling arrangements, this type of transaction is not permanent, and may be construed as a non-economic transaction. SSAP No. 25, paragraph 18.b., states that "non-economic transactions … shall be recorded at the lower of existing book value or fair value at the date of the transaction."

10. It appears that this guidance is intended to address matters involving discrete or isolated transfers of assets and/or liabilities between affiliates rather than transfers of assets and liabilities effected in relation to executing reinsurance transactions (the guidance for which is SSAP No. 62R). Additionally,

application of this guidance would result in a change to the surplus of the insurance group as a result of implementing a modification to an existing intercompany pooling arrangement. As previously stated, the statutory accounting intent is to avoid surplus gains for the insurance group as a result of implementing a modification to an intercompany pooling arrangement.

11. The accounting issues are:

    a. What is the relevant guidance for modifications to intercompany pooling arrangements?

    b. What is the appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement?

INT 03-02 Discussion

The Working Group reached a consensus as follows:

12. SSAP No. 62R provides accounting for property and casualty reinsurance agreements including specific guidance on intercompany pooling agreements. SSAP No. 62R provides two methods of accounting for changes in intercompany pooling agreements, depending on whether or not the pooling results in a gain in surplus.

13. The appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement is statutory book value for assets and statutory value for liabilities. Book value is defined in the glossary of the *Accounting Practices and Procedure Manual*.

INT 03-02 Status

14. No further discussion is planned.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/22-12a INT 03-02.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: ASU 2023-06, Disclosure Improvements

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In October 2023, FASB issued *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative*, in response to a referral from SEC Release No. 33-10532, Disclosure Update and Simplification, issued August 17, 2018. The changes detailed in the ASU seek to clarify or improve disclosure and presentation requirements of a variety of Topics. Many of the amendments allow users to more easily compare entities subject to the SEC's existing disclosures with those entities that were not previously subject to the SEC's requirements, while others represent miscellaneous clarifications or technical corrections of the current disclosure requirements. Two of the more significant items from the SEC referral is the requirement for companies to disclose their the weighted-average interest rate of debt and provide repurchase agreement (repo) counterparty risk disclosures. FASB elected to only require the weighted-average interest rate disclosure for publicly traded companies due to concerns regarding the complexity of the calculation for private companies. It was also noted by Staff that the effective date of ASU 2023-06 is unusual as both its timing, and ultimately its implementation within the Codification, is dependent on whether the SEC removes the related disclosures from Regulation S-X, or Regulation S-K becomes effective, prior to June 30, 2027. For this agenda item, Staff believes that the occurrence, or non-occurrence, of future SEC actions is not relevant to discussion concerning the proposed disclosures' merits for inclusion in the statutory accounting framework. If needed, the Working Group will address the effective date of adoption at a later stage.

Existing Authoritative Literature:
The table starting on page six summarizes the updates in this ASU, as well as defines the recommended actions for statutory accounting.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
Agenda item 2024-04: Conforming Repurchase Agreements was developed in in response to the American Council of Life Insurers (ACLI) request to modify the treatment of repurchase agreements in the life risk-based capital (RBC) formula to converge with treatment for securities lending programs.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None.

Convergence with International Financial Reporting Standards (IFRS):
None.

Staff Recommendation – Spring National Meeting:
NAIC staff recommends that the Working Group expose revisions to adopt, with modification, certain disclosures from *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative,* for statutory accounting within *SSAP No. 15—Debt and Holding Company Obligations* and *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. The disclosures revisions we have recommended are:

- Certain disclosures for unused commitments and lines of credit, disaggregated by short-term and long-term.

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- Disclosure of accrued interest from repos and securities borrowing, separate disclosure of significant (10% of admitted assets) reverse repos, and counterparty disclosures for significant (10% of adjusted capital and surplus) repos and reverse repos.

NAIC staff also requests regulator and interested party input on whether the accounting policy disclosure for cash flows associated with derivatives, ASC 230-10-50-9, should also be adopted for statutory accounting purposes. This would require companies to provide an accounting policy disclosure for where cash flows associated with derivative instruments and their related gains and losses are presented in the statement of cash flows.

Staff Recommendation – Summer National Meeting:
NAIC staff recommends that the Working Group adopt, with modification, certain disclosures from *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative,* for statutory accounting within *SSAP No. 15—Debt and Holding Company Obligations* and *SSAP No. 86—Derivatives*. The disclosure revisions we have recommended are:

- Certain disclosures for unused commitments and lines of credit, disaggregated by short-term and long-term.
- Disclosure of the derivative cash flow accounting policy

In addition, NAIC staff recommend that the previously exposed revisions to adopt, with modification, certain disclosures from ASU 2023-06 within *No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* be combined with agenda item 2024-04: Conforming Repurchase Agreements. These disclosures revisions include:

- Disclosure of accrued interest from repos and securities borrowing, separate disclosure of significant (10% of admitted assets) reverse repos, and counterparty disclosures for significant (10% of adjusted capital and surplus) repos and reverse repos.

Agenda item 2024-04 is intended to review and revise current statutory guidance for repos and secured lending, as such adoption of additional repo disclosures should be considered as a part of that project.

Staff Review Completed by:
NAIC Staff – William Oden, February 2024

Status:
On December 1, 2023, the Statutory Accounting Principles (E) Working Group deferred exposure of this agenda item as some items were noted which require further consideration.

On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to adopt, with modification, certain disclosures from *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative*, for statutory accounting within *SSAP No. 15—Debt and Holding Company Obligations* and *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. The Working Group also requested input from regulators and interested parties on whether the derivative cash flow accounting policy disclosure, described in ASC 230-10-50-9, would provide useful information to regulators.

Exposed Revisions to SSAP No. 15—Debt and Holding Company Obligations – Adopted

22. For unused commitments and lines of credit, the reporting entity shall separately disclose the following, disaggregated by short-term and long-term, in the notes to financial statements:

a. The amount and terms of unused commitments for financing arrangements (including commitment fees and the conditions under which commitments may be withdrawn).

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~~a.~~b. The amount and terms of unused lines of credit for financing arrangements (including commitment fees and the conditions under which lines may be withdrawn) and the amount of those lines of credit that support commercial paper borrowing arrangements or similar arrangements.

Relevant Literature

32. This statement adopts, with modification, *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative.* Statutory modifications include:

a. Extending the disclosure requirements to both short-term and long-term unused commitments and lines of credit, whereas ASU 2023-06 only required these disclosures for long-term unused commitments and short-term lines of credit.

b. The requirement to disclose the weighted-average interest rate of short-term borrowings was rejected for statutory accounting purposes.

Exposed revisions to SSAP No. 86—Derivatives – Adopted

Disclosure Requirements

63. Reporting entities shall disclose the following for all derivative contracts used:

a. General disclosures:

i. A description of the reporting entity's objectives for using derivatives, i.e., hedging, income generation or replication;

ii. A description of the context needed to understand those objectives and its strategies for achieving those objectives;

iii. The description for hedging objectives shall identify the category, e.g., fair value hedges, cash flow hedges, or foreign currency hedges, and for all objectives, the type of instrument(s) used;

iv. A description of the accounting policies for derivatives including the policies for recognizing (or reasons for not recognizing) and measuring the derivatives used, and when recognized, where those instruments and related gains and losses are reported;

v. Identification of whether the reporting entity has derivative contracts with financing premiums. (For purposes of this term, this includes scenarios in which the premium cost is paid at the end of the derivative contract or throughout the derivative contract.);

vi. The net gain or loss recognized in unrealized gains or losses during the reporting period representing the component of the derivative instruments' gain or loss, if any, excluded from the assessment of hedge effectiveness; ~~and~~

vii. The net gain or loss recognized in unrealized gains or losses during the reporting period resulting from derivatives that no longer qualify for hedge accounting. For portfolio layer method hedges, disclose circumstances that led to the breach; and

~~vii.~~viii. The reporting entity shall disclose its accounting policy for where cash flows associated with derivative instruments and their related gains and losses are presented in the statement of cash flow.

Relevant Literature

74. This statement adopts, with modification, *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative*. The adopted guidance requires the reporting entity to disclose its accounting policy for where cash flows associated with derivative instruments are presented in the statement of cash flow.

Not adopted -* The following Revisions to were exposed SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities – *Are To be Combined with Agenda Item 2024-04 (not adopted in August 2024)

28. A reporting entity shall disclose the following[fn]:

a. For Repurchase and Reverse Repurchase Agreements:

i. If the entity has entered into repurchase or reverse repurchase agreements, information regarding the company policy or strategies for engaging in repo programs, policy for requiring collateral, as well as whether transactions have been accounted for as secured borrowings or as sale transactions. This disclosure shall include the terms of reverse repurchase agreements whose amounts are included in borrowing money. The following information shall be disclosed by type of agreement:

(a) Whether repo agreements are bilateral and/or tri-party trades;

(b) Maturity time frame divided by the following categories: open or continuous term contracts for which no maturity date is specified, overnight, 2 days to 1 week, from 1 week to 1 month, greater than 1 month to 3 months, greater than 3 months to 1 year, and greater than 1 year[fn];

(c) Aggregate narrative disclosure of the fair value of securities sold and/or acquired that resulted in default. (This disclosure is not intended to capture "failed trades," which are defined as instances in which the trade did not occur as a result of an error and was timely corrected. Rather, this shall capture situations in which the non-defaulting party exercised their right to terminate after the defaulting party failed to execute.)

(d) If as of the date of the most recent balance sheet the aggregate carrying amount of reverse repurchase agreements (securities or other assets purchased under agreements to resell) exceeds 10% of total admitted assets, the assets shall be separately disclosed. The entity shall also disclose whether there are any provisions, beyond the collateral requirements in paragraph 113, to ensure that the market value of the underlying assets remains sufficient to protect the entity in the event that the counterparty defaults and, if so, the nature of those provisions.

Staff Note 2: *The Supplemental Investment Risks Interrogatories (Appendix A-001) does require reporting of the amount and percentage of admitted assets subject to reverse repurchase agreements. Staff is of the opinion that if the assets subject to reverse repurchase agreements exceeded 10% then this fact is significant enough to also be included in the notes the financial statements.*

ii. For repurchase transactions accounted for as secured borrowings[fn], the maximum amount and end balance as of each reporting period (quarterly and annual) for the following:

(a) Fair value of securities sold. (Book adjusted carrying value shall be provided as an end balance only.) This information is required in the aggregate, and by type of security categorized by NAIC designation, with identification of nonadmitted assets. Although legally sold as a secured borrowing, these assets are still reported by the insurer and shall be coded as restricted pursuant to the annual

statement instructions, disclosed in accordance with *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*, reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for restricted assets.

(b) Cash collateral and the fair value of security collateral (if any) received. This information is required in the aggregate and by type of security categorized by NAIC designation with identification of collateral securities received that do not qualify as admitted assets.

(1) For collateral received, aggregate allocation of the collateral by the remaining contractual maturity of the repurchase agreements (gross): overnight and continuous, up to 30 days, 30-90 days, greater than 90 days. This disclosure shall also include a discussion of the potential risks associated with the agreements and related collateral received, including the impact arising changes in the fair value of the collateral received and/or the provided security and how those risks are managed.

(2) For cash collateral received that has been reinvested, the total reinvested cash and the aggregate amortized cost and fair value of the invested asset acquired with the cash collateral. This disclosure shall be reported by the maturity date of the invested asset: under 30 days, 60 days, 90 days, 120 days, 180 days, less than 1 year, 1-2 years, 2-3 years and greater than 3 years. To the extent that the maturity dates of the liability (collateral to be returned) does not match the invested assets, the reporting entity shall explain the additional sources of liquidity to manage those mismatches.

(c) Liability recognized, including accrued interest, to return cash collateral, and the liability recognized to return securities received as collateral as required pursuant to the terms of the secured borrowing transaction.

iii. For reverse repurchase transactions accounted for as secured borrowings[fn], the maximum amount and end balance as of each reporting period (quarterly and annual) for the following:

(a) Fair value of securities acquired. This information shall be reported in the aggregate, and by type of security categorized by NAIC designation, with identification of whether acquired assets would not qualify as admitted assets.

(b) Cash collateral and the fair value of security collateral (if any) provided. (If security collateral was provided, book adjusted carrying value shall be provided as an end balance only.) Disclosure shall identify the book adjusted carrying value of any nonadmitted securities provided as collateral. For collateral pledged, the aggregate allocation of the collateral by the remaining contractual maturity of the reverse-repurchase agreements (gross): overnight and continuous, up to 30 days, 30-90 days, greater than 90 days. This disclosure shall also include a discussion of the potential risks associated with the agreements and related collateral pledged, including obligations arising from a decline in the fair value of the collateral pledged and how those risks are managed.

(c) Recognized receivable for the return of collateral. (Generally cash collateral, but including securities provided as collateral as applicable under the terms of the secured borrowing transaction. Receivables are not recognized for securities provided as collateral if those securities are still reported as assets of the reporting entity.)

(d) Recognized liability, including accrued interest, to return securities acquired under the reverse-repurchase agreement as required pursuant to the secured borrowing transaction. (Generally, a liability is required if the acquired securities are sold.)

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iv. For repurchase transactions accounted for as a sale[fn], the maximum amount and end balance as of each reporting period (quarterly and annual) for the following:

(a) Fair value of securities sold (derecognized from the financial statements). (Book adjusted carrying value shall be provided as an end balance only, reflecting the amount derecognized from the sale transaction.) This information is required in the aggregate, and by type of security categorized by NAIC designation, with information on the book adjusted carrying value of nonadmitted assets sold.

(b) Cash and the fair value of securities (if any) received as proceeds and recognized in the financial statements. This information is required in the aggregate and by type of security categorized by NAIC designation, with identification of received assets nonadmitted in the financial statements. All securities received shall be coded as restricted pursuant to the annual statement instructions, disclosed in accordance with SSAP No. 1, reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for restricted assets.

(c) The forward repurchase commitment recognized to return the cash or securities received. Amount reported shall reflect the stated repurchase price under the repurchase transaction.

v. For reverse repurchase transactions accounted for as sale[fn], the maximum amount and end balance as of each reporting period (quarterly and annual):

(a) Fair value of securities acquired and recognized on the financial statements. (Book adjusted carrying value shall be provided as an end balance only.) This information shall be reported in the aggregate, and by type of security categorized by NAIC designation. The disclosure also requires the book adjusted carrying value of nonadmitted assets acquired.

(b) Cash collateral and the fair value of security collateral (if any) provided. (If security collateral was provided, book adjusted carrying value shall be provided as an end balance only.) Disclosure shall also identify whether any nonadmitted assets were provided as collateral (derecognized from the financial statements).

vi. If as of the date of the most recent balance sheet the amount at risk under repurchase agreements or the amount at risk under reverse repurchase agreements with any individual counterparty or group of related counterparties exceeds 10% of adjusted capital and surplus, an entity shall disclose the name(s) of those counterparties or group of related counterparties, the amount at risk with each, and the weighted-average maturity of the repurchase agreements or reverse repurchase agreements with each.

(a) For the purposes of this statement, the amount at risk under repurchase agreements is the excess of the carrying amount (or market value, if higher than the carrying amount or if there is no carrying amount) of the securities or other assets sold under agreement to repurchase, including accrued interest plus any cash or other assets on deposit to secure the repurchase obligation, over the amount of the repurchase liability (adjusted for accrued interest).

~~(a)~~(b) For the purposes of this statement, the amount at risk under reverse repurchase agreements is the excess of the carrying amount of the reverse repurchase agreements over the market value of assets delivered in accordance with the agreements by the counterparty to an entity (or to a third-party agent that has affirmatively agreed to act on behalf of the entity) and not returned to the counterparty, except in exchange for their approximate market value in a separate transaction.

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Relevant Literature

135. This statement adopts, with modification, *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative*. Statutory modifications include:

a. It is not feasible to require separate reporting of assets subject to reverse repurchase agreements in excess of 10% of total assets. Instead, this was modified to require separate disclosure and the threshold was modified to be "10% of total admitted assets."

b. The disclosure threshold for the amount at risk under repurchase agreements or reverse repurchase agreements was modified to be 10% of adjusted capital and surplus, rather than 10% of total equity.

c. The requirement to disclose the weighted-average interest rate of repurchase liabilities and related repurchase liabilities was rejected for statutory accounting purposes.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted, with modification, as final, certain disclosures from *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative,* for statutory accounting within *SSAP No. 15—Debt and Holding Company Obligations* and *SSAP No. 86—Derivatives*. The partial adoption of ASU 2023-06 only includes the previously exposed disclosures on unused commitments, lines of credit, and derivative cash flows accounting policy. The Working Group also directed NAIC staff to incorporate the previously exposed disclosures from ASU 2023-06 concerning repos, reverse repos and securities borrowing into agenda item 2024-04: Conforming Repurchase Agreements for further consideration as part of the ongoing project looking at the statutory accounting treatment of repos and securities lending. The adopted revisions are reflected below.

Adopted Revisions to SSAP No. 15—Debt and Holding Company Obligations – Adopted

22. For unused commitments and lines of credit, the reporting entity shall separately disclose the following, disaggregated by short-term and long-term, in the notes to financial statements:

a. The amount and terms of unused commitments for financing arrangements (including commitment fees and the conditions under which commitments may be withdrawn).

~~a.~~b. The amount and terms of unused lines of credit for financing arrangements (including commitment fees and the conditions under which lines may be withdrawn) and the amount of those lines of credit that support commercial paper borrowing arrangements or similar arrangements.

Relevant Literature

32. This statement adopts, with modification, *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative.* Statutory modifications include:

a. Extending the disclosure requirements to both short-term and long-term unused commitments and lines of credit, whereas ASU 2023-06 only required these disclosures for long-term unused commitments and short-term lines of credit.

b. The requirement to disclose the weighted-average interest rate of short-term borrowings was rejected for statutory accounting purposes.

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Proposed revisions to SSAP No. 86—Derivatives – Adopted

Disclosure Requirements

63. Reporting entities shall disclose the following for all derivative contracts used:

b. General disclosures:

i. A description of the reporting entity's objectives for using derivatives, i.e., hedging, income generation or replication;

ii. A description of the context needed to understand those objectives and its strategies for achieving those objectives;

iii. The description for hedging objectives shall identify the category, e.g., fair value hedges, cash flow hedges, or foreign currency hedges, and for all objectives, the type of instrument(s) used;

iv. A description of the accounting policies for derivatives including the policies for recognizing (or reasons for not recognizing) and measuring the derivatives used, and when recognized, where those instruments and related gains and losses are reported;

v. Identification of whether the reporting entity has derivative contracts with financing premiums. (For purposes of this term, this includes scenarios in which the premium cost is paid at the end of the derivative contract or throughout the derivative contract.);

vi. The net gain or loss recognized in unrealized gains or losses during the reporting period representing the component of the derivative instruments' gain or loss, if any, excluded from the assessment of hedge effectiveness; ~~and~~

vii. The net gain or loss recognized in unrealized gains or losses during the reporting period resulting from derivatives that no longer qualify for hedge accounting. For portfolio layer method hedges, disclose circumstances that led to the breach; and

~~vii.~~viii. The reporting entity shall disclose its accounting policy for where cash flows associated with derivative instruments and their related gains and losses are presented in the statement of cash flow.

Relevant Literature

74. This statement adopts, with modification, *ASU 2023-06, Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative*. The adopted guidance requires the reporting entity to disclose its accounting policy for where cash flows associated with derivative instruments are presented in the statement of cash flow.

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The last column lists the status of the GAAP source literature for statutory accounting and the recommended action.

Topic	Codification	Abbreviated Summary of Change	Related Paragraphs	SAP Status/Recommendation
Statement of Cash Flows—Overall	230-10	Requires an accounting policy disclosure in annual periods of where cash flows associated with derivative instruments and their related gains and losses are presented in the statement of cash flows.	50-9	NAIC staff noted that this disclosure may be duplicative of *SSAP No. 86—Derivatives*, paragraph 63a.iv. However, this disclosure does not specifically require disclosure of the accounting policy for the presentation of cash flows from derivatives and the statutory statement of cash flows does not currently break out cash flows from derivatives. No comments were received from regulators and Interested Parties had no comments on adoption of this disclosure. **Staff recommends adoption of this disclosure for statutory accounting purposes.**
Accounting Changes and Error Corrections—Overall	250-10	Requires that when there has been a change in the reporting entity, the entity disclose any material prior-period adjustment and the effect of the adjustment on retained earnings in interim financial statements.	50-6	This disclosure is duplicative of *SSAP No. 3—Accounting Changes and Corrections of Errors*, paragraph 13. **This update is not applicable – no action required.**
Earnings Per Share—Overall	260-10	Requires disclosure of the methods used in the diluted earnings-per-share computation for each dilutive security and clarifies that certain disclosures should be made during interim periods. Amends illustrative guidance to illustrate disclosure of the methods used in the diluted earnings-per-share computation.	50-1 55-51 55-52	**This update is not applicable – no action required.**

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Topic	Codification	Abbreviated Summary of Change	Related Paragraphs	SAP Status/Recommendation
Interim Reporting—Overall	270-10	Conforms to the amendments made to Topic 250.	45-12 45-19 50-1	**This update is not applicable – no action required.**
Commitments—Overall	440-10	Requires disclosure of assets mortgaged, pledged, or otherwise subject to lien and the obligations collateralized.	50-1	This disclosure is duplicative of *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*, paragraph 23b. **This update is not applicable – no action required.**
Debt—Overall	470-10	Requires disclosure of amounts and terms of unused lines of credit and unfunded commitments and the weighted-average interest rate on outstanding short-term borrowings. Entities that are not public business entities are not required to provide information about the weighted-average interest rate.	15-1 50-6 5-7	Staff do not recommend adoption of the weighted-average interest rate calculation for statutory accounting purposes. Due to the complexity of this computation, this this disclosure is only required for public entities under GAAP. As SAP does not have the public/private entity distinction, adoption of this disclosure would be applicable to all insurance entities. This disclosure is not considered necessary in light of existing debt SAP disclosures and does not provide enough benefit to offset the cost of implementing such a potentially complex calculation. **We recommend adoption, with modification, of the disclosures unused LOC and commitment disclosures.**
Equity—Overall	505-10	Requires entities that issue preferred stock to disclose preference in involuntary liquidation if the liquidation preference is other than par or stated value.	50-4	This disclosure is duplicative of *SSAP No. 72—Surplus and Quasi-Reorganizations*, paragraph 22b. **This update is not applicable – no action required.**

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Topic	Codification	Abbreviated Summary of Change	Related Paragraphs	SAP Status/Recommendation
Derivatives and Hedging—Overall	815-10	Adds inter-codification reference to 230-10-50-9 for disclosure of cash flows associated with derivative instruments.	50-8C	**This update is not applicable – no action required.**
Transfers and Servicing—Secured Borrowing and Collateral	860-30	Requires: a. That accrued interest be included in the disclosure of liabilities incurred in securities borrowing or repurchase or resale transactions. b. Separate presentation of the aggregate carrying amount of reverse repurchase agreements on the face of the balance sheet if that amount exceeds 10 percent of total assets. c. Disclosure of the weighted-average interest rates of repurchase liabilities for public business entities. d. Disclosure of amounts at risk with an individual counterparty if that amount exceeds more than 10 percent of stockholder's equity. e. Disclosure for reverse repurchase agreements that exceed 10 percent of total assets on whether there are any provisions in a reverse repurchase agreement to ensure that the market value of the underlying assets remains sufficient to protect against counterparty default and, if so, the nature of those provisions.	15-1 45-2 45-2A 45-3 50-7 50-9 thru 12 55-4	**We recommend adoption, with modification, of the disclosures in bullets a., b., d., and e. (see Abbreviated Summary of Changes)** **The disclosure in bullet c. is not recommended for adoption within SAP – no action required.**
Extractive Activities—Oil and Gas—Notes to Financial Statements	932-235	Requires that paragraphs 932-235-50-3 through 50-36 be applicable for each annual period presented in the financial statements.	50-2A	**This update is not applicable – no action required.**
Financial Services—Investment Companies—Investment Company Activities	946-20	Requires that investment companies disclose the components of capital on the balance sheet.	50-11 50-12	**This update is not applicable – no action required.**
Real Estate—Real Estate Investment Trusts—Overall	974-10	Requires disclosure for annual reporting periods of the tax status of distributions per unit (for example, ordinary income, capital	50-1	**This update is not applicable – no action required.**

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Topic	Codification	Abbreviated Summary of Change	Related Paragraphs	SAP Status/Recommendation
		gain, and return of capital) for a real estate investment trust.		
Generally Accepted Accounting Principles—Overall	105-10	Adds in transition and open effective date information.	65-7 65-8	**This update is not applicable – no action required.**

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: ASU 2023-01, Leases (Topic 842), Common Control Arrangements

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In March 2023, the Financial Accounting Standards Board (FASB) issued *Accounting Standard Update (ASU) 2023-01, Leases (Topic 842), Common Control Arrangements*. This ASU was issued as part of FASB's post-implementation review to address issues that have been found during the implementation of the new lease guidance from *ASU 2016-02, Leases (Topic 842)*. As a reminder, ASU 2016-02 was rejected for statutory accounting and the operating lease treatment was retained.

ASU 2023-01 focuses on two issues that are both related to private company stakeholders' concerns about applying Topic 842 to related party arrangements between entities under common control. The first issue provides a practical expedient for private companies and not-for-profit entities that are not conduit bond obligors to use the written terms and conditions of a common control arrangement to determine 1) whether a lease exists and, if so, 2) the classification of and accounting for that lease. The practical expedient may be applied on an arrangement-by-arrangement basis. If no written terms and conditions exist (including in situations in which an entity does not document existing unwritten terms and conditions in writing upon transition to the practical expedient), an entity is prohibited from applying the practical expedient and must evaluate the enforceable terms and conditions to apply Topic 842. The new U.S. GAAP guidance for this issue is only applicable to non-public entities.

The second issue involves the accounting for leasehold improvements associated with a lease between entities under common control. U.S. GAAP guidance for life of leasehold improvements prior to this update generally agrees to statutory accounting. It was noted in the ASU that private company stakeholders were concerned that amortizing leasehold improvements associated with arrangements between entities under common control determined to be leases (hereinafter referred to as common control leases) over a period shorter than the expected useful life of the leasehold improvements might result in financial reporting that do not faithfully represent the economics of those leasehold improvements, particularly in common control leases with short lease terms. While this issue originally came from private company stakeholder comments, the guidance for this issue is applicable for all lessees that are party to a lease between entities under common control in which there are leasehold improvements.

Existing Authoritative Literature:
The ASUs related to Topic 842 have previously been rejected in *SSAP No. 22R—Leases*. Guidance for leasehold improvements is included in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* and *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Heath Care Facilities*, and guidance for related parties is included in *SSAP No. 25—Affiliates and Other Related Parties*.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): ASC Topic 842 was the result of a joint project between FASB and the International Accounting Standards Board.

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Staff Recommendation:
NAIC staff recommends the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP clarification and expose revisions to adopt, with modification, ASU 2023-01 in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* and *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Heath Care Facilities*, as illustrated in the Form A. The proposed revisions reject the practical expedient for private companies and not-for-profit entities but recommend adoption of the leasehold improvement guidance from the ASU, with modification to the language to align with existing guidance in SSAP No. 19 and SSAP No. 73.

SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements

5. Leasehold improvements that increase the value and enhance the usefulness of the leased asset meet the definition of assets established in SSAP No. 4. Within that definition, such items also meet the criteria defining nonadmitted assets. Accordingly, such assets shall be reported as nonadmitted assets and charged against surplus. These nonadmitted assets shall be amortized against net income over the shorter of their estimated useful life or the remaining lease term as defined in SSAP No. 22R. Leasehold improvements associated with a lease between entities under common control shall be amortized over the useful life of those improvements to the holding company group as long as the lessee controls the use of the underlying asset through a lease. If the lessor obtained the right to control the use of the underlying asset through a lease with another entity not within the same holding company group, the amortization period shall not exceed the amortization period of the holding company group. Leasehold improvements that do not meet the definition of assets shall be charged to expense when acquired. The amortization of leasehold improvements (including property improvements and integral equipment) shall cease, with any remaining amount immediately expensed, in any event in which the lease is terminated in advance of the lease term. This includes situations in which leased real estate is acquired by the reporting entity lessee. Such improvements related to the functionality of health care delivery assets shall follow the accounting, reporting and impairment guidance in *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities*, and an exception to the application of this guidance to leasehold improvements necessary for the functionality of health care delivery assets is included in SSAP No. 73. If leased real estate is acquired, recognition of the real estate shall follow the provisions in *SSAP No. 40R—Real Estate Investments*.

20. This statement adopts, with modification, *ASU 2023-01, Leases (Topic 842), Common Control Arrangements*. The practical expedient for private companies and not-for-profit entities that are not conduit bond obligors to use the written terms and conditions of a common control arrangement is rejected for statutory accounting. The guidance for lessees that are a party to a lease between entities under common control in which there are leasehold improvements is adopted, with modification to align with existing statutory guidance.

SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities

9. Furniture, medical equipment and fixtures, and leasehold improvements shall be depreciated over their estimated useful lives but for a period not to exceed three years, except for a leasehold improvement which shall be amortized against net income over the shorter of its estimated useful life or the remaining lease term, using methods detailed in SSAP No. 19. Leasehold improvements associated with a lease between entities under common control shall be amortized over the useful life of those improvements to the holding company group as long as the lessee controls the use of the underlying asset through a lease. If the lessor obtained the right to control the use of the underlying asset through a lease with another entity not within the same holding company group, the amortization period shall not exceed the amortization period of the holding company group. The amortization of leasehold improvements (including property improvements and integral equipment) shall cease, with any remaining amount immediately expensed, in any event in which the lease is terminated in advance of the lease term. This includes situations in which leased real estate is acquired by the reporting entity lessee but excludes situations where the real estate lease agreement has a purchase option that contains language that allows leasehold improvements necessary for the functionality of specific health care delivery assets to be excluded from the purchase cost of the real estate. Upon acquisition, such leasehold improvements necessary for the functionality of healthcare delivery assets shall follow the guidance for health care delivery assets in this statement. If

leased real estate is acquired, recognition of the real estate shall follow the provisions in *SSAP No. 40R—Real Estate Investments*.

13. This statement adopts, with modification, *ASU 2023-01, Leases (Topic 842), Common Control Arrangements*. The practical expedient for private companies and not-for-profit entities that are not conduit bond obligors to use the written terms and conditions of a common control arrangement is rejected for statutory accounting. The guidance for lessees that are a party to a lease between entities under common control in which there are leasehold improvements is adopted, with modification to align with existing statutory guidance.

Staff Review Completed by: Jake Stultz, NAIC Staff – February 2024

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to adopt, with modification, *ASU 2023-01, Leases (Topic 842), Common Control Arrangements* in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* and *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Heath Care Facilities*, as illustrated above. The proposed revisions reject the practical expedient for private companies and not-for-profit entities but recommend adoption of the leasehold improvement guidance from the ASU, with modification to the language to align with existing guidance in SSAP No. 19 and SSAP No. 73.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed revisions which adopt with modification, as final, *ASU 2023-01, Leases (Topic 842), Common Control Arrangements* in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* and *SSAP No. 73—Health Care Delivery Assets and Leasehold Improvements in Heath Care Facilities.*

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/24-02 - ASU 2023-01 Leases.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: ASU 2023-08, Accounting for and Disclosure of Crypto Assets

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In December 2023, the Financial Accounting Standards Board (FASB) issued *Accounting Standard Update (ASU) 2023-08, Intangibles—Goodwill and Other—Crypto Assets (Subtopic 350-60), Accounting for and Disclosure of Crypto Assets*. This ASU establishes the accounting and reporting for crypto assets, which are defined in U.S. GAAP as assets that:

1. Meet the definition of intangible assets as defined in the Codification.
2. Do not provide the asset holder with enforceable rights to or claims on underlying goods, services, or other assets.
3. Are created or reside on a distributed ledger based on blockchain or similar technology.
4. Are secured through cryptography.
5. Are fungible.
6. Are not created or issued by the reporting entity or its related parties.

ASU 2023-08 also clarified the disclosure of crypto assets in the financial statements, which note that crypto assets are to be reported at fair value, are reported separately from the other intangible assets, describe how they are to be disclosed in the income statement and statement of cash flows, and includes a rollforward of activity and balances on an annual basis.

As background, on May 20, 2021, the Working Group adopted *Interpretation (INT) 21-01: Accounting for Cryptocurrencies*, which established statutory accounting for crypto assets. At that time, NAIC staff had received several questions on the proper treatment of cryptocurrencies, so with the absence of U.S. GAAP guidance, the Working Group adopted INT 21-01. The INT established that directly held cryptocurrencies have not been identified in the *Accounting Practices and Procedures Manual* (AP&P Manual) as an admitted asset, and do not meet the definition of any admitted asset that is defined in the AP&P Manual. Accordingly, by default they are a nonadmitted asset per *SSAP No. 4—Assets and Nonadmitted Assets*, paragraph 3, as they are not specifically identified in the AP&P Manual as an admitted asset. Additionally, a disclosure for crypto assets was added to the general interrogatories of the Annual Statement blanks and instructions.

This agenda item intends to codify the guidance that was adopted in INT 21-01, and formally establish that crypto assets are nonadmitted assets for statutory accounting.

Existing Authoritative Literature:
Accounting for cryptocurrencies is currently addressed by *INT 21-01 Accounting for Cryptocurrencies*, and the Annual Statement blanks included a disclosure in the general interrogatories.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

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Convergence with International Financial Reporting Standards (IFRS): None

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP clarification and expose revisions to adopt, with modification ASU 2023-08 for statutory accounting. The agenda item proposes to adopt the definition of crypto assets from the ASU but establishes that directly held crypto assets are nonadmitted assets for statutory accounting. The recommendation is to add guidance to *SSAP No. 20—Nonadmitted Assets* that clarifies that directly-held crypto assets are nonadmitted assets for statutory accounting and to define crypto assets using the definition from ASU 2023-08. This agenda item does not intend to modify the general interrogatory disclosures that had previously been added to the Annual Statement blanks and instructions. Additionally, NAIC staff recommends that the Working Group expose the intent to nullify *INT 21-01, Accounting for Cryptocurrencies*, upon the adoption of this agenda item. The revisions to SSAP No. 20 are illustrated below.

SSAP No 20—Nonadmitted Assets

Paragraph 4:

> f. Crypto assets are defined as intangible digital assets in which transactions are created or reside on a distributed ledger based on blockchain or similar technology and are verified with records maintained by a decentralized system using cryptography, rather than by a centralized authority, and do not provide the asset holder with enforceable rights to or claims on underlying goods, services, or other assets. Directly held crypto assets do not meet the definition of cash in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments*, and due to the volatile nature of the assets and liquidity issues, the assets shall not be considered available to satisfy policyholder obligations.

5. This statement adopts with modification *FASB Emerging Issues Task Force No. 08-7: Accounting for Defensive Intangible Assets* to nonadmit defensible intangible assets. This statement rejects Chapters 3A and 11 of *Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins*. This statement adopts, with modification, *ASU 2023-08, Intangibles—Goodwill and Other—Crypto Assets (Subtopic 350-60), Accounting for and Disclosure of Crypto Assets*, which adopts the definition of crypto assets from the ASU and establishes that directly held crypto assets are nonadmitted assets for statutory accounting.

Staff Review Completed by: Jake Stultz, NAIC Staff—February 2024

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to adopt, with modification *ASU 2023-08, Accounting for and Disclosure of Crypto Assets* for statutory accounting. The revisions propose to adopt the definition of crypto assets from the ASU but establishes within *SSAP No. 20—Nonadmitted Assets* that directly held crypto assets are nonadmitted assets for statutory accounting. Additionally, the exposure includes the intent to nullify *INT 21-01, Accounting for Cryptocurrencies*. This agenda item does not intend to modify the general interrogatory disclosures that had previously been added to the Annual Statement blanks and instructions.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed revisions to SSAP No. 20 which with modification, *ASU 2023-08, Accounting for and Disclosure of Crypto Assets* for statutory accounting. Upon adoption, this agenda also nullifies *INT 21-01, Accounting for Cryptocurrencies*.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 21-01: Accounting for Cryptocurrencies

GUIDANCE NULLIFIED AUGUST 13, 2024

INT 21-01 Dates Discussed

March 15, 2021; May 20, 2021; August 13, 2024

INT 21-01 References

SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments

INT 21-01 Issue

1. This interpretation is to address questions regarding statutory accounting treatment for cryptocurrencies, which are defined as a digital currency in which transactions are verified and records maintained by a decentralized system using cryptography, rather than by a centralized authority. Cryptocurrencies are purchased and exchanged using a limited number of unregulated digital currency exchanges and are not held or offered by major banks.

2. The most valuable cryptocurrency as of February 2021 is Bitcoin, which has been in circulation since 2009, and there are approximately 4,000 different cryptocurrencies available on 200 different cryptocurrency exchanges. Cryptocurrencies have seen significant price volatility and have experienced an extreme increase in value over the past year, with the value of the total outstanding cryptocurrencies nearing $1 trillion as of February 2021. The total market value and increased popularity has led to increased interest in the market by traditional financial institutions and insurance companies.

3. No NAIC Committees or groups have taken any action or established a position on cryptocurrencies. Currently, auditors must rely on guidance provided by the American Institute of Certified Public Accountants through a nonauthoritative practice guide.

4. This Interpretation intends to clarify that directly held cryptocurrencies are nonadmitted assets for statutory accounting.

INT 21-01 Discussion

5. Directly held cryptocurrencies have not been identified in the *Accounting Practices and Procedures Manual* (AP&P Manual) as an admitted asset, and do not meet the definition of any admitted asset that is defined in the AP&P Manual. Accordingly, by default they are a nonadmitted asset per *SSAP No. 4—Assets and Nonadmitted Assets,* paragraph 3, as they are not specifically identified in the *Accounting Practices and Procedures Manual* as an admitted asset.

6. Cash is defined in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* as a "medium of exchange that a bank or other similar financial institution will accept for deposit and allow an immediate credit to the depositor's account." Cryptocurrencies are currently not accepted by major banks and do not operate like a traditional currency, and as such do not meet the definition of cash in SSAP No. 2R.

INT 21-01 Consensus

7. The Statutory Accounting Principles (E) Working Group reached a consensus that directly held cryptocurrencies do not meet the definition of an admitted asset and are therefore considered to be a nonadmitted asset for statutory accounting. The Working Group intends to rely on this interpretation for statutory accounting and will address cryptocurrencies further once FASB has provided definitive guidance.

INT 21-01 Status

8. No further discussion is planned.

9. The Statutory Accounting Principles (E) Working Group will continue to monitor the evolution of cryptocurrencies and subsequently review this interpretation as appropriate as part of the normal maintenance process.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Consistency Revisions for Residuals

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to incorporate consistency revisions for residual tranches and residual security interests. Over the last couple of years, a variety of revisions have been incorporated for residual interests. These began with revisions to clarify the reporting on Schedule BA (instead of Schedule D-1) along with the residual definition and guidance within each investment SSAP to highlight that residuals shall be captured on Schedule BA. Although these revisions were necessary to immediately address the reporting of residuals, the discussion that accompanied these revisions have noted that conforming revisions would be needed coinciding with the effective date of the principles-based bond definition guidance to have consistency of guidance location, terminology and definitions.

With the revisions to *SSAP No. 21R—Other Admitted Assets* to provide the accounting and reporting for residuals, all residuals, regardless of investment structure, shall follow the guidance detailed in SSAP No. 21R and be reported on Schedule BA.

To ensure consistency in definitions and guidance, this agenda item proposes to centralize the guidance in SSAP No. 21R and use a consistent approach in the other investment SSAPs to exclude residuals from scope and direct to SSAP No. 21R.

Existing Authoritative Literature: - Key references **bolded** for emphasis.

- ***SSAP No. 21R—Other Admitted Assets (Effective 2025) – Adopted March 16, 2024***

  Residual Tranches or Interests/Loss Positions

  28. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.

  29. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a residual should be based on the substance

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of the investment and how cash flows to the holder are determined. Additionally, it would be expected that the equity position in an ABS Issuer, as defined in SSAP 26R, would be classified as a residual tranche.

a. Residuals often do not have contractual principal or interest.

b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance, and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.

c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.

d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.

e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.

30. Residual tranches or interests do not qualify for bond reporting. Residuals shall follow the accounting and admittance guidance within this statement and are required to be reported on Schedule BA: Other Long-Term Invested Assets.

31. As stated in paragraph 22, residuals are permitted to be admitted assets if debt securities from the same structure qualify (or would qualify) as admitted assets. If the debt security from a structure is (or would be) nonadmitted due to the requirements under paragraph 22, then any residual interests or first loss positions held from the same structure also do not qualify as admitted assets and shall be reported as nonadmitted assets.

32. Residuals shall be initially reported at cost, or allocated cost (using proportional fair values if acquired along with debt tranches from the securitization). Subsequent to initial acquisition, residuals shall be reported at either 1) the lower of amortized cost or fair value under the Allowable Earned Yield method detailed in paragraphs 33-34, with temporary reductions in fair value reported as an unrealized loss, or 2) at the calculated practical expedient method detailed in paragraph 35.

33. For purposes of this statement for residuals only, amortized cost shall be defined as the cost to acquire the residual reduced for distributions in excess of the Allowable Earned Yield and other-then-temporary impairments (OTTI). The Allowable Earned Yield shall be established at acquisition as the discount rate that equates the initial best estimate of the residual's cash flows to its acquisition cost. The Allowable Earned Yield is not to be updated after acquisition.

34. Interest income shall be recorded under the effective yield method using the Allowable Earned Yield, capped by the amount of cash distributions received. To the extent that the Allowable Earned Yield, applied to the current amortized cost, exceeds the cash distributions received, such unrecognized interest income may be carried forward to future periods to be recognized when sufficient cash distributions are received. To the extent cash distributions exceed the Allowable Earned Yield (including any unrecognized interest carried forward), the amortized cost shall be reduced by the excess. As a result of this method, the amortized cost shall not be increased unless there is a subsequent investment (i.e., an additional purchase with additional consideration remitted).

35. Reporting entities may elect a practical expedient in lieu of the Allowable Earned Yield detailed in paragraphs 33-34 and calculate Book/Adjusted Carrying Value (BACV) such that all distributions received are treated as a reduction in BACV. With this approach, the reporting entity will not recognize any interest or investment income until the residual tranche has a BACV of zero. Once the residual has a zero BACV, distributions received shall be recognized as interest income.

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a. Reporting entities applying the practical expedient shall continue to report residuals on Schedule BA, including those with a zero BACV. Any subsequent distributions shall be reported as interest income until the structure matures/terminates, is unwound, or no longer meets the definition of a residual.

b. Reporting entities are required to apply the practical expedient to all residuals held.

c. Reporting entities that wish to discontinue use of the practical expedient approach and move towards the Allowable Earned Yield method are required to specify and disclose an explicit transition date, and only apply the Allowable Earned Yield method to residuals acquired after that date. Residuals held prior to the disclosed accounting method transition date shall continue to follow the practical expedient until those residuals mature/terminate or are unwound.

36. Residuals shall be assessed for other-than-temporary impairment (OTTI) on an ongoing basis, with required assessment anytime that fair value is less than the reported value.

a. For residuals measured using the Allowable Earned Yield method, as detailed in paragraphs 33-34, an OTTI shall be considered to have occurred if the present value of expected cash flows discounted by the Allowable Earned Yield, is less than amortized cost. Upon identification of an OTTI, the reporting entity shall recognize a realized loss equal to the difference between the amortized cost and the present value of expected cash flows, with the present value of expected cash flows becoming the new amortized cost to which the Allowable Earned Yield is applied. After the OTTI is recognized, distributions received from the residual shall continue to be recorded in accordance with paragraphs 33-34. Subsequent recoveries in cash flows shall not result in increases to the amortized cost.

b. For residuals measured under the practical expedient, as detailed in paragraph 35, an OTTI shall be considered to have occurred if the fair value of the residual is less than the BACV. The reporting entity shall recognize a realized loss equal to the difference between the fair value and the BACV, with the fair value becoming the new BACV. After the OTTI is recognized, distributions received from the residual shall continue to be recorded in accordance with paragraph 35. Subsequent recoveries in cash flows shall not result in increases to the BACV.

37. Residuals recognized on Schedule BA as of December 31, 2024, and accounted for under a different SSAP, shall follow the following measurement transition guidance as of January 1, 2025:

a. Reporting entity shall determine whether they will follow the Allowable Earned Yield method detailed in paragraphs 33-34, or the practical expedient detailed in paragraph 35, for all residuals.

b. Residuals previously accounted for under SSAP No. 26R or SSAP No. 43R shall prospectively apply the Allowable Earned Yield measurement method elected under this Statement using the amortized cost as of December 31, 2024 as the starting point in the calculation. Residuals that will follow the practical expedient shall be recognized on January 1, 2025 at the lower of amortized cost or fair value as of December 31, 2024, realizing any unrealized loss existing at that date.

c. Residuals reported under the equity method or fair value as of December 31, 2024 (as they were previously captured in scope of SSAP No. 30R, 32R or 48) with unrealized gains or losses recognized, shall recognize any unrealized position as realized, with the reported value as of December 31, 2024 becoming the January 1, 2025 cost basis for subsequent measurement under this statement.

Effective Date and Transition

40. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.* The guidance for structured settlements when the reporting entity acquires the legal right to receive payments is effective December 31, 2018.

41. Revisions adopted March 16, 2024, to add guidance for “Debt Securities That Do Not Qualify as Bonds” and for “Residual Tranches or Interests/Loss Positions” are initially effective Jan. 1, 2025, to correspond with

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the effective date of the principles-based bond definition. The guidance for residual tranches is permitted for early application. Reporting entities that apply this guidance in 2024 shall continue to follow the transition guidance in paragraph 37 using the modified dates that correspond to the reporting entity's application date.

- ***SSAP No. 26R—Bonds (Effective 2025)***

4. This statement excludes:

a. Mortgage loans and other real estate lending activities made in the ordinary course of business. These investments are addressed in *SSAP No. 37—Mortgage Loans* and *SSAP No. 39—Reverse Mortgages*.

b. Investments that qualify within the principles-based definition as an ABS. These investments shall follow the guidance in *SSAP No. 43R—Asset-Backed Securities*.

c. Securities that provide varying principal or interest based on underlying equity appreciation or depreciation, an equity-based derivative, real estate or other non-debt variable, as described in paragraph 6.d.

d. Securities that do not qualify as bonds pursuant to the principles-based bond definition, including first loss positions that lack contractual payments or substantive credit enhancement. These investments shall follow the appropriate guidance in *SSAP No. 21R— Other Admitted Assets*.

e. Replication (synthetic asset) transactions addressed in *SSAP No. 86—Derivatives*. The admissibility, classification and measurement of a replication (synthetic asset) transactions are not preemptively determined by the principles-based bond definition and should be evaluated in accordance with the guidance on replication (synthetic asset) transactions within SSAP No. 86.

f. Investments that are captured specifically within other SSAPs. For example, reporting entity acquired structured settlements are captured in scope of *SSAP No. 21R—Other Admitted Assets*, held surplus notes are captured in scope of *SSAP No. 41R—Surplus Notes* and working capital finance investments are captured in scope of *SSAP No. 105—Working Capital Finance Investments*. Investments captured in scope of other SSAPs are subject to the measurement and admittance provisions of those SSAPs. Furthermore, investments that have specific reporting lines on dedicated schedules (such as with both surplus notes and WCFI) shall be reported on their dedicated lines.

10. The holder of a debt instrument issued by an ABS Issuer is in a different economic position than if the holder owned the ABS Issuer's assets directly. The holder of the debt instrument is in a different economic position if such debt instrument benefits from substantive credit enhancement through guarantees (or other similar forms of recourse), subordination and/or overcollateralization.

a. Substantive Credit Enhancement: The intent of the criteria requiring the holder to be in a different economic position is to distinguish qualifying bonds from instruments with equity-like characteristics or where the substance of the transaction is more closely aligned with that of the underlying collateral. To qualify as an ABS under this standard, there is a requirement that there are substantive credit enhancements within the structure that absorb losses before the debt instrument being evaluated would be expected to absorb losses. This is inherent in the context of an issuer credit obligation in scope of SSAP No. 26R as the owners of the equity in the operating entity are the first to absorb any variability in performance of the operating entity. The same concept applies to asset-backed securities. If substantive credit enhancement did not exist, the substance of the debt instrument being evaluated would be more closely aligned with that of the underlying collateral than that of a bond. Credit enhancement that is merely nominal or lacks economic substance does not put a holder in a different economic position. The substantive credit enhancement required to be in a different economic position is specific to each transaction; determined at origination; and

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refers to the level of credit enhancement a market participant (i.e., knowledgeable investor transacting at arm's length) would conclude is substantive.

b. The first loss position may be issued as part of a securitization in the form of a debt or equity interest, or it may be retained by the sponsor and not issued as part of the securitization. If the first loss position (or a more senior position(s), if the first loss position(s) lacks contractual payments along with a substantive credit enhancement) is issued as part of the securitization, and does not have contractual principal and interest payments along with substantive credit enhancement and is held by a reporting entity, the investment(s) does not qualify for reporting as a bond and shall be reported on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value consistent with the treatment for residuals. (These items are further addressed in *SSAP No. 21R—Other Admitted Assets*.)

- ***SSAP No. 30R—Unaffiliated Common Stock***

1. This statement establishes statutory accounting principles for common stocks.

2. Investments in common stock of subsidiaries, controlled or affiliated entities (investments in affiliates) are not within the scope of this statement. They are addressed in SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities.

3. Investments in the form of common stock that are in substance residual interests or a residual security tranche, as defined in SSAP No. 43R or SSAP No. 48, shall be reported on Schedule BA: Other Long-Term Assets in the dedicated reporting lines for residuals.

- ***SSAP No. 32R—Preferred Stock***

1. This statement establishes statutory accounting principles for preferred stock.

2. Investments in preferred stock of entities captured in *SSAP No. 97—Investments in Subsidiaries, Controlled or Affiliated Entities* or *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* as well as preferred stock interests of certified capital companies per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company* (CAPCO) are included within the scope of this statement. The requirement to file investments in preferred stock of certain subsidiaries, controlled or affiliated entities with the NAIC pursuant to SSAP No. 97 does not affect the application of the accounting, valuation or admissibility under this statement. In addition to the provisions of this statement, preferred stock investments in SCAs are also subject to the provisions of *SSAP No. 25—Affiliates and Other Related Parties* and *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

3. Investments in the form of preferred stock that are in substance residual interests or a residual security tranche, as defined in SSAP No. 43R or SSAP No. No. 48, shall be reported on Schedule BA: Other Long-Term Assets in the dedicated reporting lines for residuals.

- ***SSAP No. 43R—Asset-Backed Securities (Effective 2025)***

4. This statement excludes:

a. Securities captured in scope of *SSAP No. 26R—Bonds*.

b. Mortgage loans in scope of *SSAP No. 37—Mortgage Loans* that qualify under an SVO structural assessment as SVO-Identified Credit Tenant Loans. These investments are excluded as these are captured as issuer credit obligations under SSAP No. 26R.

***c.* Securities that do not qualify as Asset-Backed Securities per the bond definition in *SSAP No. 26R—Bonds*. This exclusion includes residual or interests, as well as first loss positions, that do not have contractual payments or substantive credit enhancement. Debt**

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securities that do not qualify and residual interests shall follow guidance in *SSAP No. 21R—Other Admitted Assets.*

11. After initial recognition, the carrying value shall be determined in accordance with the reported NAIC designation. The determination of NAIC designations shall be in accordance with the requirements detailed in the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual):

a. For reporting entities that maintain an Asset Valuation Reserve (AVR), asset-backed securities, **excluding residual tranches or interests**, shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value. 3

b. For reporting entities that do not maintain an AVR, asset-backed securities designated highest-quality and high-quality (NAIC designations 1 and 2, respectively), **excluding residual tranches or interests**, shall be reported at amortized cost; loan-backed and structured securities that are designated medium quality, low quality, lowest quality and in or near default (NAIC designations 3 to 6, respectively) shall be reported at the lower of amortized cost or fair value.

c. For residual tranches or interests[4], all reporting entities shall report the item on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value. Changes in the reported value from the prior period shall be recorded as unrealized gains or losses. For reporting entities that maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. These items are captured in *SSAP No. 21R—Other Admitted Assets* and subject to admittance restrictions detailed in that statement.

Footnote 4: Reference to "residual tranches or interests" intends to capture securitization tranches and beneficial interests as well as other structures that reflect loss layers without any contractual payments, whether principal or interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment's duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

Residual Tranches or Interests

27. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.

28. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive

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in determination. Classification as a residual should be based on the substance of the investment and how cash flows to the holder are determined.

a. Residuals often do not have contractual principal or interest.

b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance, and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.

c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.

d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.

e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.

- ***SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies***

Residual Interests and Reporting

18. Investments in scope of this statement are reported on *Schedule BA: Other Long-Term Assets*. Schedule BA includes dedicated reporting categories for joint ventures, partnerships, and limited liability company investments as well as for residual interests, both with reporting lines in accordance with underlying asset characteristics. Investments within scope of this standard shall be divided within these reporting categories, with investments that reflect residual interests, or that predominantly hold residual interests captured in the residual interest reporting category.

19. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.

20. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a residual should be based on the substance of the investment and how cash flows to the holder are determined.

a. Residuals often do not have contractual principal or interest.

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b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.

c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.

d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.

e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

- Agenda Item 2021-15 – SSAP No. 43R – Residual Tranches, was adopted November 10, 2021, to incorporate accounting guidance for residuals and clarify that residuals shall be reported on Schedule BA.

- Agenda item 2023-12 – Residuals in SSAP No. 48 Investments, was adopted September 21, 2023 to define residuals consistently between *SSAP No. 43R—Asset-Backed Securities* and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* and to add Annual Statement Instructions for the Schedule BA residual reporting category.

- Agenda Item 2023-23 – Residuals in Preferred Stock and Common Stock Structures was adopted during the 2023 Fall National Meeting to exclude residual interests from *SSAP No. 30R—Unaffiliated Common Stock* and *SSAP No. 32R—Preferred Stock*.

- Principles-Based Bond Definition – During the 2023 Summer National Meeting, the Working Group adopted the principles-based bond definition in a revised *SSAP No. 26R—Bonds* and *SSAP No. 43R—Asset-Backed Securities*. Subsequent to this adoption, revisions to *SSAP No. 21R—Other Admitted Asset*s were exposed to capture accounting and reporting guidance for non-bond debt securities as well as residual interests. The revisions to SSAP No. 21R for debt securities that do not qualify as bonds to prescribe the measurement method and accounting provisions for residual interests was adopted March 16, 2024 during the 2024 Spring National Meeting.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommend that the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP clarification and expose revisions to incorporate consistency revisions for residuals so that all SSAPs refer to SSAP No. 21R for the formal definition and accounting and reporting guidance. This recommendation involves revisions to *SSAP No. 26R—Bonds* (Effective 2025), *SSAP No. 30R—Unaffiliated Common Stock*, *SSAP No. 32R—Preferred Stock*, *SSAP No. 43R—Asset-Backed Securities* (Effective 2025), and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*.

Staff Review Completed by: Julie Gann, NAIC Staff—February 2024

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Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed consistency revisions for residuals so that *SSAP No. 26R—Bonds* (Effective 2025), *SSAP No. 30R—Unaffiliated Common Stock*, *SSAP No. 32R—Preferred Stock*, *SSAP No. 43R—Asset-Backed Securities* (Effective January 1, 2025), and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* refer directly to *SSAP No. 21R—Other Admitted Assets* for the formal definition and accounting and reporting guidance.

Proposed Revisions:

SSAP No. 26R—Bonds (Effective Jan. 1, 2025)

4. This statement excludes:

   a. Mortgage loans and other real estate lending activities made in the ordinary course of business. These investments are addressed in *SSAP No. 37—Mortgage Loans* and *SSAP No. 39—Reverse Mortgages.*

   b. Investments that qualify within the principles-based definition as an ABS. These investments shall follow the guidance in *SSAP No. 43R—Asset-Backed Securities*.

   c. Securities that provide varying principal or interest based on underlying equity appreciation or depreciation, an equity-based derivative, real estate or other non-debt variable, as described in paragraph 6.d.

   d. Securities that do not qualify as bonds pursuant to the principles-based bond definition, including first loss positions that lack ~~contractual payments or~~ substantive credit enhancement as described in paragraph 10.b., as those items are residual interests. All investments that are in substance residual interests or that is a residual security tranche, as defined in *SSAP No. 21R—Other Admitted Assets*, ~~. These investments~~ shall follow the appropriate guidance in SSAP No. 21R ~~*Other Admitted Assets*~~.

   e. Replication (synthetic asset) transactions addressed in *SSAP No. 86—Derivatives*. The admissibility, classification and measurement of a replication (synthetic asset) transactions are not preemptively determined by the principles-based bond definition and should be evaluated in accordance with the guidance on replication (synthetic asset) transactions within SSAP No. 86.

   f. Investments that are captured specifically within other SSAPs. For example, reporting entity acquired structured settlements are captured in scope of *SSAP No. 21R—Other Admitted Assets*, held surplus notes are captured in scope of *SSAP No. 41R—Surplus Notes* and working capital finance investments are captured in scope of *SSAP No. 105—Working Capital Finance Investments*. Investments captured in scope of other SSAPs are subject to the measurement and admittance provisions of those SSAPs. Furthermore, investments that have specific reporting lines on dedicated schedules (such as with both surplus notes and WCFI) shall be reported on their dedicated lines.

10. The holder of a debt instrument issued by an ABS Issuer is in a different economic position than if the holder owned the ABS Issuer's assets directly. The holder of the debt instrument is in a different economic position if such debt instrument benefits from substantive credit enhancement through guarantees (or other similar forms of recourse), subordination and/or overcollateralization.

   a. Substantive Credit Enhancement: The intent of the criteria requiring the holder to be in a different economic position is to distinguish qualifying bonds from instruments with equity-like

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characteristics or where the substance of the transaction is more closely aligned with that of the underlying collateral. To qualify as an ABS under this standard, there is a requirement that there are substantive credit enhancements within the structure that absorb losses before the debt instrument being evaluated would be expected to absorb losses. This is inherent in the context of an issuer credit obligation in scope of SSAP No. 26R as the owners of the equity in the operating entity are the first to absorb any variability in performance of the operating entity. The same concept applies to asset-backed securities. If substantive credit enhancement did not exist, the substance of the debt instrument being evaluated would be more closely aligned with that of the underlying collateral than that of a bond. Credit enhancement that is merely nominal or lacks economic substance does not put a holder in a different economic position. The substantive credit enhancement required to be in a different economic position is specific to each transaction; determined at origination; and refers to the level of credit enhancement a market participant (i.e., knowledgeable investor transacting at arm's length) would conclude is substantive.

b. The first loss position may be issued as part of an ~~securitization~~ ABS structure in the form of a debt or equity interest, or it may be retained by the sponsor and not issued as part of the ~~securitization~~ structure. If the first loss position (or a more senior position(s), if the first loss position(s) lacks ~~contractual payments along with a~~ substantive credit enhancement) is issued as part of the ~~securitization~~structure, and does not have ~~contractual principal and interest payments along with~~ substantive credit enhancement and is held by a reporting entity, the investment(s) does not qualify for reporting as a bond as it is a residual interest. All residual interests shall follow the accounting and reporting guidance in *SSAP No. 21R—Other Admitted Assets*. ~~and shall be reported on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value consistent with the treatment for residuals. (These items are further addressed in SSAP No. 21R—Other Admitted Assets.)~~

- ***SSAP No. 30R—Unaffiliated Common Stock***

1. This statement establishes statutory accounting principles for common stocks.

2. Investments in common stock of subsidiaries, controlled or affiliated entities (investments in affiliates) are not within the scope of this statement. They are addressed in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

3. Investments in the form of common stock that are in substance residual interests or a residual security tranche, as defined in *SSAP No. 21R—Other Admitted Assets*~~SSAP No. 43R or SSAP No. 48~~, shall follow the accounting and reporting guidance in SSAP No. 21R with reporting ~~be reported~~ on *Schedule BA: Other Long-Term Assets* in the dedicated reporting lines for residuals.

- ***SSAP No. 32R—Preferred Stock***

1. This statement establishes statutory accounting principles for preferred stock.

2. Investments in preferred stock of entities captured in *SSAP No. 97—Investments in Subsidiaries, Controlled or Affiliated Entities* or *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* as well as preferred stock interests of certified capital companies per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company* (CAPCO) are included within the scope of this statement. The requirement to file investments in preferred stock of certain subsidiaries, controlled or affiliated entities with the NAIC pursuant to SSAP No. 97 does not affect the application of the accounting, valuation or admissibility under this statement. In addition to the provisions of this statement, preferred stock investments in SCAs are also subject to the provisions of *SSAP No. 25—Affiliates and Other Related Parties* and *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

3. Investments in the form of preferred stock that are in substance residual interests or a residual security tranche, as defined in ~~SSAP No. 43R or SSAP No. No. 48~~*SSAP No. 21R—Other Admitted Assets*, shall follow the accounting and reporting guidance in SSAP No. 21R with reporting ~~be reported~~ on *Schedule BA: Other Long-Term Assets* in the dedicated reporting lines for residuals.

- ***SSAP No. 43R—Asset-Backed Securities (Effective 2025)***

4. This statement excludes:

a. Securities captured in scope of *SSAP No. 26R—Bonds*.

b. Mortgage loans in scope of *SSAP No. 37—Mortgage Loans* that qualify under an SVO structural assessment as SVO-Identified Credit Tenant Loans. These investments are excluded as these are captured as issuer credit obligations under SSAP No. 26R.

c. Securities that do not qualify as Asset-Backed Securities per the bond definition in *SSAP No. 26R—Bonds* and residual interests as defined in *SSAP No. 21R—Other Admitted Assets*. ~~This exclusion includes residual or interests, as well as first loss positions, that do not have contractual payments or substantive credit enhancement.~~ These securities ~~Debt securities that do not qualify~~ and residual interests shall follow the accounting and reporting guidance in SSAP No. 21R. ~~—Other Admitted Assets~~

11. After initial recognition, the carrying value shall be determined in accordance with the reported NAIC designation. The determination of NAIC designations shall be in accordance with the requirements detailed in the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual):

a. For reporting entities that maintain an Asset Valuation Reserve (AVR), asset-backed securities~~, excluding residual tranches or interests,~~ shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value. 3

b. For reporting entities that do not maintain an AVR, asset-backed securities designated highest-quality and high-quality (NAIC designations 1 and 2, respectively~~), excluding residual tranches or interests,~~ shall be reported at amortized cost; loan-backed and structured securities that are designated medium quality, low quality, lowest quality and in or near default (NAIC designations 3 to 6, respectively) shall be reported at the lower of amortized cost or fair value.

~~c. For residual tranches or interests[4], all reporting entities shall report the item on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value. Changes in the reported value from the prior period shall be recorded as unrealized gains or losses. For reporting entities that maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve. These items are captured in SSAP No. 21R—Other Admitted Assets and subject to admittance restrictions detailed in that statement.~~

~~Footnote 4: Reference to "residual tranches or interests" intends to capture securitization tranches and beneficial interests as well as other structures that reflect loss layers without any contractual payments, whether principal or interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment's duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.~~

~~Residual Tranches or Interests~~

~~27. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.~~

~~28. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a residual should be based on the substance of the investment and how cash flows to the holder are determined.~~

~~a. Residuals often do not have contractual principal or interest.~~

~~b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance, and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.~~

~~c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.~~

~~d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.~~

~~e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.~~

- ***SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies***

1. This statement establishes statutory accounting principles for investments in any joint ventures, partnerships, and limited liability companies, including investments in certified capital companies (CAPCO) per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company* (CAPCO), whether or not it is considered to be controlled by or affiliated with the reporting entity.

2. This statement excludes:

a. Single real estate property investments that are wholly-owned by an LLC that is directly and wholly-owned by the reporting entity, and that meet the criteria established in SSAP No. 40R—Real Estate Investments~~, are excluded from this statement~~.

b. ~~This statement does not address the accounting for i~~Investments in joint ventures, partnerships and limited liability companies that invest in tax credit programs and are in scope of ~~Low-Income Housing Tax Credit Properties as discussed in~~ *SSAP No. 93—Investments in Tax Credit Programs*~~Low-Income Housing Tax Credit Property Investments. However, investments in certain state Low-Income Housing~~

~~Tax Credit Property Investments that do not fall within the scope of SSAP No. 93 are covered by the requirements of this statement~~. ***(Staff Note: This text reflects edits proposed to reflect the revised tax credit guidance in SSAP No. 93 exposed under agenda item 2022-14.)***

c. Investments that are in substance residual interests or a residual security tranche, as defined in *SSAP No. 21R—Other Admitted Assets*, shall follow the accounting and reporting guidance in SSAP No. 21R with reporting on Schedule BA: Other Long-Term Assets in the dedicated reporting lines for residuals.

~~**Residual Interests and Reporting**~~

~~18. Investments in scope of this statement are reported on *Schedule BA: Other Long-Term Assets*. Schedule BA includes dedicated reporting categories for joint ventures, partnerships, and limited liability company investments as well as for residual interests, both with reporting lines in accordance with underlying asset characteristics. Investments within scope of this standard shall be divided within these reporting categories, with investments that reflect residual interests, or that predominantly hold residual interests captured in the residual interest reporting category.~~

~~19. A residual interest or a residual security tranche (collectively referred to as residuals) exists in investment structures that issue one or more classes of debt securities created for the primary purpose of raising debt capital backed by collateral assets. The primary source of debt repayment is derived through rights to the cash flows of a discrete pool of collateral assets. These designs could be backed directly or indirectly through a feeder fund. The collateral assets generate cash flows that provide interest and principal payments to debt holders through a contractually prescribed distribution methodology (e.g., waterfall dictating the order and application of all collateral cash flows). Once those contractual requirements are met, the remaining cash flows generated by (or with the sale of) the collateral assets are provided to the holder of the residual security/residual interest holder. When an asset within the discrete pool of assets does not perform as expected, it impacts the extent to which cash flows will be generated and distributed. The residual holders in the structure continue to receive payments from the collateral so long as there are cash flows in excess of the debt obligations. The payments to the residual holder may vary significantly, both in timing and amount, based on the underlying collateral performance.~~

~~20. The structural design of a residual interest or residual security tranche can vary, but the overall concept is that they receive the remaining cash flows after all debt holders receive contractual interest and principal payments. Determining whether an investment in a structure reflects a residual interest or tranche shall be based on the substance of the investment held rather than its legal form. Common characteristics of residual interests/residual security tranches include the items noted below, but the presence or absence of any of these factors should not be definitive in determination. Classification as a residual should be based on the substance of the investment and how cash flows to the holder are determined.~~

~~a. Residuals often do not have contractual principal or interest.~~

~~b. Residuals may be structured with terms that appear to be stated principal or interest but that lack substance and result in receiving the residual cash flows of the underlying collateral. The terms allow for significant variation in the timing and amount of cash flows without triggering a default of the structure.~~

~~c. Residuals do not have credit ratings or NAIC assigned designations. Rather, they are first loss positions that provide subordination to support the credit quality of the typically rated debt tranches.~~

~~d. Residuals may provide payment throughout the investment duration (and not just at maturity), but the payments received continue to reflect the residual amount permitted after debt tranche holders receive contractual principal and interest payments.~~

~~e. Frequently, there are contractual triggers that divert cash flows from the residual holders to the debt tranches if the structure becomes stressed.~~

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed consistency revisions for residuals with an effective date of January 1, 2025. These revisions result with all noted SSAPs referring to *SSAP No. 21R—Other Admitted Assets* for the formal definition and accounting and reporting guidance.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/06 - 24-08 - Residual Consistency Revisions.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
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Issue: SSAP No. 2R – Clarification

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to update the guidance in *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments* to remove a lingering reference to items that have been removed from scope pursuant to the principles-based bond definition project (asset-backed securities) or from agenda item 2023-17 (mortgage loans and Schedule BA assets). The edits are focused on the guidance that addresses 'rolling' cash equivalents and short-term investments in which there is a continued reference for SSAP No. 43R investments and 'other Invested assets.' This guidance has been revised to only reflect items in scope of SSAP No. 2R.

Existing Authoritative Literature:

- ***SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments***

7. Regardless of maturity date, related party or affiliated investments that would be in scope of *SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities,* or that would be reported as "Other Invested Assets" shall be reported as long-term investments if any of the following conditions apply,[1] unless the reporting entity has re-underwritten the investment, maintained appropriate re-underwriting documentation, and each participating party had the ability to independently review the terms and can terminate the transaction prior to renewal.

    a. The reporting entity does not reasonably expect the investment to terminate on the maturity date. This provision includes investments that are expected to be renewed (or rolled) with a maturity date that ends subsequent to the initial 90-day timeframe.

    b. The investment was previously reported as a cash equivalent investment and the initial maturity timeframe has passed. If an investment is reported as a cash equivalent and it is unexpectedly renewed/rolled, the reporting entity is not permitted to continue to report the held security as a cash equivalent, regardless of the updated maturity date, and shall report the security as a long-term investment. An investment is only permitted to be reported as a cash equivalent for one quarter reporting period. Meaning, if an investment was reported as a cash equivalent in the first quarter, it is not permitted to be reported as a cash equivalent in the second quarter.

    c. The reporting entity reacquired the investment (or a substantially similar investment) within one year after the original security matured or was terminated. These reacquired securities shall be reported as long-term investments. (These securities are also not permitted to be reported as short-term investments, regardless of the maturity date of the reacquired investment.)

15. Regardless of maturity date, related party or affiliated investments in scope of *SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities,* or that would be reported as "Other Invested

[1] Cash equivalents subject to the provisions of paragraph 7 are not permitted to be subsequently reported as short-term investments, even if the updated/reacquired maturity date is within one year. These investments shall be reported as long-term investments. To avoid changes in reporting schedules, reporting entities are permitted to report securities as long-term investments at initial acquisition, regardless of the initial maturity date.

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Assets" shall be reported as long-term investments if any of the following conditions apply,[2, 3] unless the reporting entity has re-underwritten the investment, maintained appropriate re-underwriting documentation, and each participating party had the ability to independently review the terms and can terminate the transaction prior to renewal.

a. The reporting entity does not reasonably expect the investment to terminate on the maturity date. This provision includes investments that are expected to be renewed (or rolled) with a maturity date that ends subsequent to the initial "less than one year" timeframe.

b. The investment was previously reported as a short-term investment and the initial maturity timeframe has passed. If an investment is reported as a short-term investment and it is unexpectedly renewed/rolled, the reporting entity is not permitted to continue to report the held security as a short-term investment (or as a cash equivalent) regardless of the updated maturity date and shall report the security as a long-term investment. An investment is only permitted to be reported as a short-term investment for one annual reporting period. Meaning, if an investment was reported as a short-term investment as of December 31, 2018, it is not permitted to be reported as short-term investment as of December 31, 2019.

c. The reporting entity reacquired the investment (or a substantially similar investment) within one year after the original security matured or was terminated. These reacquired securities shall be reported as long-term investments. (These securities are also not permitted to be reported as cash equivalent investments regardless of the maturity date of the reacquired investment.)

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

- *SSAP No. 26R—Bonds* and *SSAP No. 43R—Asset-Backed Securities*, reflecting new guidance to incorporate a principles-based bond definition were adopted during the 2023 Summer National Meeting. This guidance is effective Jan. 1, 2025. Pursuant to the revisions adopted, all ABS are required to be reported as long-term investments on Schedule D-1-2 and are not permitted for cash equivalent or short-term reporting.

- Agenda item 2023-17 – Short-Term Investments, was adopted during the 2023 Fall National Meeting and removes mortgage loans and all Schedule BA investments from being reported as cash equivalents or short-term investments.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommend that the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP Clarification and expose revisions to *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments* to eliminate lingering references that imply that asset-backed securities, mortgage loans, or other Schedule BA items are permitted to be reported as cash equivalents or short-term investments.

[2] Reverse repurchase transactions are excluded from these provisions if admitted in accordance with collateral requirements pursuant *to SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.*

[3] Short-term investments subject to the provisions of paragraph 15 are not permitted to be subsequently reported as cash equivalents, even if the updated/reacquired maturity date is within 90 days. These investments shall be reported as long-term investments. To avoid changes in reporting schedules, reporting entities are permitted to report securities as long-term investments at initial acquisition, regardless of the initial maturity date.

Staff Review Completed by: Julie Gann, NAIC Staff—February 2024

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments* to eliminate lingering references that imply that asset-backed securities, mortgage loans, or other Schedule BA items are permitted to be reported as cash equivalents or short-term investments.

Proposed Revisions to SSAP No. 2R—Bonds (Effective Jan. 1, 2025)

7. Regardless of maturity date, related party or affiliated investments that would be in scope of this statement pursuant to paragraph 6 ~~*SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities, or that would be reported as "Other Invested Assets"*~~ shall be reported as long-term investments if any of the following conditions apply,[4] unless the reporting entity has re-underwritten the investment, maintained appropriate re-underwriting documentation, and each participating party had the ability to independently review the terms and can terminate the transaction prior to renewal.

    a. The reporting entity does not reasonably expect the investment to terminate on the maturity date. This provision includes investments that are expected to be renewed (or rolled) with a maturity date that ends subsequent to the initial 90-day timeframe.

    b. The investment was previously reported as a cash equivalent investment and the initial maturity timeframe has passed. If an investment is reported as a cash equivalent and it is unexpectedly renewed/rolled, the reporting entity is not permitted to continue to report the held security as a cash equivalent, regardless of the updated maturity date, and shall report the security as a long-term investment. An investment is only permitted to be reported as a cash equivalent for one quarter reporting period. Meaning, if an investment was reported as a cash equivalent in the first quarter, it is not permitted to be reported as a cash equivalent in the second quarter.

    c. The reporting entity reacquired the investment (or a substantially similar investment) within one year after the original security matured or was terminated. These reacquired securities shall be reported as long-term investments. (These securities are also not permitted to be reported as short-term investments, regardless of the maturity date of the reacquired investment.)

15. Regardless of maturity date, related party or affiliated investments in scope of this statement pursuant to paragraph 14 ~~*SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities, or that would be reported as "Other Invested Assets"*~~ shall be reported as long-term investments if any of the following conditions apply,[5, 6] unless the reporting entity has re-underwritten the investment, maintained appropriate re-underwriting documentation, and each participating party had the ability to independently review the terms and can terminate the transaction prior to renewal.

[4] Cash equivalents subject to the provisions of paragraph 7 are not permitted to be subsequently reported as short-term investments, even if the updated/reacquired maturity date is within one year. These investments shall be reported as long-term investments. To avoid changes in reporting schedules, reporting entities are permitted to report securities as long-term investments at initial acquisition, regardless of the initial maturity date.

[5] Reverse repurchase transactions are excluded from these provisions if admitted in accordance with collateral requirements pursuant *to SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.*

[6] Short-term investments subject to the provisions of paragraph 15 are not permitted to be subsequently reported as cash equivalents, even if the updated/reacquired maturity date is within 90 days. These investments shall be reported as long-term investments. To avoid changes in reporting schedules, reporting entities are permitted to report securities as long-term investments at initial acquisition, regardless of the initial maturity date.

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a. The reporting entity does not reasonably expect the investment to terminate on the maturity date. This provision includes investments that are expected to be renewed (or rolled) with a maturity date that ends subsequent to the initial “less than one year” timeframe.

b. The investment was previously reported as a short-term investment and the initial maturity timeframe has passed. If an investment is reported as a short-term investment and it is unexpectedly renewed/rolled, the reporting entity is not permitted to continue to report the held security as a short-term investment (or as a cash equivalent) regardless of the updated maturity date and shall report the security as a long-term investment. An investment is only permitted to be reported as a short-term investment for one annual reporting period. Meaning, if an investment was reported as a short-term investment as of December 31, 2018, it is not permitted to be reported as short-term investment as of December 31, 2019.

c. The reporting entity reacquired the investment (or a substantially similar investment) within one year after the original security matured or was terminated. These reacquired securities shall be reported as long-term investments. (These securities are also not permitted to be reported as cash equivalent investments regardless of the maturity date of the reacquired investment.)

On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed revisions to *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments* with an effective date of January 1, 2025. These revisions eliminate lingering references that imply that asset-backed securities, mortgage loans, or other Schedule BA items are permitted to be reported as cash equivalents or short-term investments.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/24-09 - SSAP No. 2R Clarification.docx

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NAIC Accounting Practices and Procedures Manual
Editorial and Maintenance Update
March 16, 2024

Maintenance updates provide revisions to the *Accounting Practices and Procedures Manual* (Manual) such as editorial corrections, reference changes and formatting.

SSAP/Appendix	Description/Revision
Removal of "Revised" and "R" identifiers from SSAP titles and references within the Manual.	Remove "Revised" and "R," previously intended to identify a SSAP that has been substantively revised, from SSAP titles and SSAP references within the Manual. NAIC staff consider the "Revised" and "R" identifiers to no longer be useful as several SSAPs have now had multiple substantive revisions after their initial adoption.

Staff Recommendation:
NAIC staff recommend that the Statutory Accounting Principles (E) Working Group move this agenda item to the active listing, categorize as a SAP Clarification, and expose editorial revisions as illustrated within.

Removal of "R" identifier from SSAP titles and references within the AP&P Manual
Remove the "Revised" and "R" identifiers from SSAP titles and SSAP references throughout the Manual. NAIC staff consider the "Revised" and "R" identifier to no longer be useful. The following SSAPs currently have an "Revised" and "R" identifier in the title.

2R—Cash, Cash Equivalents, Drafts and Short-Term Investments
5R—Liabilities, Contingencies and Impairments of Assets
16R—Electronic Data Processing Equipment and Software
21R—Other Admitted Assets
22R—Leases
26R—Bonds
30R—Unaffiliated Common Stock
32R—Preferred Stock
35R—Guaranty Fund and Other Assessments
40R—Real Estate Investments
41R—Surplus Notes
43R—Loan-Backed and Structured Securities
51R—Life Contracts
54R—Individual and Group Accident and Health Contracts
61R—Life, Deposit-Type and Accident and Health Reinsurance
62R—Property and Casualty Reinsurance
94R—Transferable and Non-Transferable State Tax Credits
100R—Fair Value
103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
104R—Share-Based Payments
105R—Working Capital Finance Investments

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed editorial revisions to the Accounting Practices and Procedures Manual to remove the "Revised" and "R" identifiers from SSAP titles and SSAP references throughout the Manual.

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On August 13, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, the proposed editorial revisions to the Accounting Practices and Procedures Manual to remove the “Revised” and “R” identifiers from SSAP titles and SSAP references throughout the Manual.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Adoptions/24-14EP Spring 2024.docx

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Revisions to the
As of March 2024, Accounting Practices and Procedures Manual

On **September 12, 2024**, the Statutory Accounting Principles (E) Working Group adopted via e-vote the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2024-01	SSAP No. 26 IP No. 169	Bond Definition – Debt Securities Issued by Funds *SAP Concept* Effective January 1, 2025	With the adopted revisions, debt securities issued by non-SEC registered funds that reflect operating entities can qualify as issuer credit obligations. The guidance requires assessment as to the purpose of the issued debt security and is explicit that debt securities issued for the raising of debt capital are required to be assessed as asset-backed securities.

https://naiconline.sharepoint.com/teams/frsstatutoryaccounting/national meetings/a. national meeting materials/2024/09-12-24 - evote adoption/e-vote adoption 9.12.2024 toc.docx

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Bond Definition – Debt Securities Issued by Funds

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to clarify guidance in the principles-based bond definition on the treatment on debt securities issued by funds, particularly to eliminate inconsistent application between similar funds and to better align with the recently adopted definition of residual tranches. In the adopted bond definition, bonds issued by business development corporations (BDCs), closed-end funds (CEFs), or similar operating entities are provided as examples of issuer credit obligations (ICOs) when they are registered under the Investment Company Act of 1940 (1940 Act). It has been noted that this guidance is inconsistent with the stated intent of having the bond definition be principles-based as the registration of the fund appears to be the basis of classification as an ICO vs ABS, rather than based on principles. It has been noted that with the current guidance, two funds with issued debt that are virtually identical can have separate SSAP classification of the debt securities (resulting with different accounting/reporting) simply based on whether the fund is registered. Additionally, it would lead to debt securities being classified inconsistently with their equity counterparts. In concept, there should be consistency between the classification of a debt security as an asset-backed security, and the equity of that structure being classified as a residual interest. Using SEC-registration as currently adopted would result in misalignment of these concepts.

The changes captured within this agenda item propose to revise the principles-based bond definition guidance to clarify that debt securities issued by funds representing operating entities qualify as ICOs. This would allow consistent treatment of similar funds regardless of SEC registration status. Guidance is also proposed to assist with distinguishing whether a fund represents an operating entity or a securitization vehicle.

The original guidance, and the reference to the SEC registration, was an easy approach to determine whether a debt security from a fund qualified as an ICO. This is because SEC registered funds have leverage limits on how much debt can be issued. Although debt securities issued from SEC registered CEFs and BDCs are still permitted as ICOs, the proposed edits permit debt securities from non-registered funds to qualify as ICO if the funds are functioning as operating entities and are not issuing securities for the primary purpose of raising debt capital.

Existing Authoritative Literature:

- ***SSAP No. 26R—Bonds*** **(Effective Jan. 1, 2025)**

  7. An issuer credit obligation is a bond, for which the general creditworthiness of an operating entity or entities through direct or indirect recourse, is the primary source of repayment. Operating entity or entities includes holding companies with operating entity subsidiaries where the holding company has the ability to access the operating subsidiaries' cash flows through its ownership rights. An operating entity may be any sort of business entity, not-for-profit organization, governmental unit, or other provider of goods or services, but not a natural person or "ABS Issuer" (as defined in paragraph 8). Examples of issuer credit obligations include, but are not limited to:

  a. U.S. Treasury securities, including U.S. Treasury Inflation-Indexed Securities; (INT 01-25).

  b. U.S. government agency securities.

c. Municipal securities issued by the municipality or supported by cash flows generated by a municipally-owned asset or entity that provides goods or services (e.g., airport, toll roads, etc.).

d. Corporate bonds issued by operating entities, including Yankee bonds and zero-coupon bonds.

e. Corporate bonds issued by holding companies that own operating entities.

f. Project finance bonds issued by operating entities.

g. Investments in the form of securities for which repayment is fully supported by an underlying contractual obligation of a single operating entity (e.g., Credit Tenant Loans (CTLs), Equipment trust certificates (ETCs), other lease backed securities, Funding Agreement Backed Notes (FABNs), etc.). For purposes of applying this principal concept, repayment is fully-supported by the underlying operating entity obligation if it provides cash flows for the repayment of all interest and at least 95% of the principal of the security.

h. Bonds issued by real estate investment trusts (REITs) or similar property trusts.

i. Bonds issued by business development corporations, closed-end funds, or similar operating entities, in each case registered under the 1940 Act.

j. Convertible bonds issued by operating entities, including mandatory convertible bonds as defined in paragraph 20.b.

Issue Paper – Exposure Draft As of 2023 Summer National Meeting

32. Whether an issuer of debt represents an operating entity or ABS Issuer is expected to be clear in most instances, but certain instances may be less clear. Ultimately, for an issuer credit obligation, it comes down to whether support for repayment consists of direct or indirect recourse to an operating entity or entities. In addition to "traditional bond" structures previously included in SSAP No. 26R, examples of issuer credit obligations include:

a. Investments in the form of securities for which repayment is fully supported by an underlying contractual obligation of a single operating entity. (e.g., CTLs, ETCs, other lease backed securities, Funding Agreement Backed Notes (FABNs), etc.). For purposes of applying this principle concept, repayment is fully-supported by the underlying operating entity obligation if it provides cash flows for the repayment of all interest and at least 95% of the principal of the security.

b. Bonds issued by real estate investment trusts (REITS) or similar property trusts.

c. Bonds issued by business development corporations, closed-end funds or similar operating entities, in each case registered under the 1940 Act. With this inclusion, it is important to highlight that the intent is specific to bonds issued from SEC-registered entities. The reference to "similar entities" is not intended to capture items issued from collateralized fund obligations (CFOs) or other such structures. Although some may consider CFOs to be similar to closed-end funds, that assessment is not supported for classification as an issuer credit obligation. Instruments considered to reflect CFOs (and other like structures) are required to be assessed as asset-backed securities for inclusion on Schedule D-1.

d. Project finance debt issued by operating entities. These investments reflect financing of a single asset or "operation" (such as a toll road or power generation facility) that collateralizes a debt issuance and the cash flows produced by the asset/operation service the debt, where the issuer may also represent an operating entity. These designs have characteristics of both issuer credit operations, as the operation constitutes a stand-alone business, as well as characteristics of ABS, as they are formed for the purpose of raising debt capital backed by the cash flows from collateral held by a bankruptcy-remote entity. When viewed holistically, these issuing entities are typically used to facilitate the financing of an operating component of a project sponsor or municipality.

Although the use of a bankruptcy-remote entity (e.g., SPV) facilitates the efficient raising of debt as a source of financing, the primary purpose is to finance an operating project. Therefore, when the issuing entity represents a stand-alone business producing its own operating revenues and expenses, where the primary purpose is to finance an operating project, the issuing entity shall be considered an operating entity despite certain characteristics that resemble ABS issuances.

i. It is important to highlight that the guidance for project finance is strictly for instruments issued by operating entities, similar to other instruments that qualify as issuer credit obligations under the principles-based bond definition. Consistent with other concepts, the naming convention (e.g., referring to an instrument as project finance) or the presence or absence of an SPV/trust structure are not definitive components in determining whether an investment qualifies for reporting on Schedule D-1, or is classified as an issuer credit obligation or ABS. Instruments (even if identified as "project finance") that do not qualify as issuer credit obligations as they not issued by operating entities, shall be assessed for qualification for reporting on Schedule D-1 as ABS. If the instruments do not qualify for reporting as ABS, they shall not be reported on Schedule D-1.

e. U.S. Treasury Inflation-Protected Securities (TIPs): The inclusion of U.S. TIPs specifically as an issuer credit obligation intends to highlight a specific exception to the determination as a creditor relationship as the variation is due to plain-vanilla inflation adjustment mechanisms. Although U.S. TIPs are specific as issuer credit obligations, Under the bond definition encompassing both issuer credit obligations and asset-backed securities, in order for a debt instrument to represent a creditor relationship, it must have pre-determined principal and interest payments (whether fixed interest or variable interest) with contractual amounts that do not vary based on the appreciation or depreciation (e.g., performance) of any underlying collateral value or other non-debt variable . For example, an issued security that has varying principal and interest payments based on the appreciation of referenced equity, real estate or other non-debt variables are precluded from bond treatment as they do not reflect creditor relationships. Although US TIPS are indexed to the consumer price index and grows with inflation, these securities shall be captured as issuer credit obligations on Schedule D-1.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

- *SSAP No. 26R—Bonds* and *SSAP No. 43R—Asset-Backed Securities*, reflecting new guidance to incorporate a principles-based bond definition were adopted during the 2023 Summer National Meeting. This guidance is effective Jan. 1, 2025. The corresponding Issue Paper has been updated as discussions occurred and has not yet been finalized as discussions involving SSAP No. 21R for the debt securities that do not qualify as bonds is not yet adopted.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Recommendation:
NAIC staff recommend that the Working Group include this agenda item on their maintenance agenda as a SAP clarification and expose revisions to *SSAP No. 26R—Bonds* incorporating the principles-based bond definition to clarify that debt securities issued by funds that represent operating entities are permitted as issuer credit obligations. These revisions would be in effect pursuant to the effective date of the revised SSAP No. 26R guidance, which is Jan. 1, 2025. The edits revise paragraph 7.i and incorporate a new paragraph 12 to the SSAP No. 26R guidance.

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This agenda item also proposes revisions to the draft Issue Paper (paragraph 32c) to update the guidance previously included addressing 1940 Act registered BDCs and CEFs as issuer credit obligations.

Proposed Revisions to *SSAP No. 26R—Bonds* (Effective Jan. 1, 2025)

7. An issuer credit obligation is a bond, for which the general creditworthiness of an operating entity or entities through direct or indirect recourse, is the primary source of repayment. Operating entity or entities includes holding companies with operating entity subsidiaries where the holding company has the ability to access the operating subsidiaries' cash flows through its ownership rights. An operating entity may be any sort of business entity, not-for-profit organization, governmental unit, or other provider of goods or services, but not a natural person or "ABS Issuer" (as defined in paragraph 8). Examples of issuer credit obligations include, but are not limited to:

   a. U.S. Treasury securities, including U.S. Treasury Inflation-Indexed Securities;(INT 01-25).

   b. U.S. government agency securities.

   c. Municipal securities issued by the municipality or supported by cash flows generated by a municipally-owned asset or entity that provides goods or services (e.g., airport, toll roads, etc.).

   d. Corporate bonds issued by operating entities, including Yankee bonds and zero-coupon bonds.

   e. Corporate bonds, issued by holding companies that own operating entities.

   f. Project finance bonds issued by operating entities.

   g. Investments in the form of securities for which repayment is fully supported by an underlying contractual obligation of a single operating entity (e.g., Credit Tenant Loans (CTLs), Equipment trust certificates (ETCs), other lease backed securities, Funding Agreement Backed Notes (FABNs), etc.). For purposes of applying this principal concept, repayment is fully-supported by the underlying operating entity obligation if it provides cash flows for the repayment of all interest and at least 95% of the principal of the security.

   h. Bonds issued by real estate investment trusts (REITs) or similar property trusts.

   i. Bonds issued by funds representing operating entities as described in paragraph 12.~~Bonds issued by business development corporations, closed-end funds, or similar operating entities, in each case registered under the 1940 Act.~~

   j. Convertible bonds issued by operating entities, including mandatory convertible bonds as defined in paragraph 20.b.

8. An asset[1]-backed security is a bond issued by an entity (an "ABS Issuer") created for the primary purpose of raising debt capital backed by financial assets[2] or cash generating non-financial assets owned by the

[1] The underlying collateral supporting an asset-backed security shall meet the definition of an asset by the ABS Issuer. Certain forms of collateral, such as rights to future cash flows, may not be recognized as assets by the selling entity but may be recognized as assets when sold to an ABS Issuer. These assets are permitted as the collateral supporting an asset-backed security, although they may not represent an asset that can be liquidated to provide payment toward the issued debt obligations (i.e., if the future cash flows do not materialize). The limited ability to liquidate the underlying collateral supporting an asset-backed security does not impact the structural determination of whether an issued security meets the definition of an asset-backed security but may impact the recoverability of the investment, as well as the consideration of whether there is sufficient credit enhancement.

[2] *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* defines a financial asset as cash, evidence of an ownership interest in an entity, or a contract that conveys to one entity a right (a) to receive cash or another financial instrument from a second entity or (b) to exchange other financial instruments on potentially favorable terms with the second entity. As a point of clarity, for the purposes of this standard, financial assets do not include assets for which the realization of the benefits conveyed by the above rights

ABS Issuer, for which the primary source of repayment is derived from the cash flows associated with the underlying defined collateral rather than the cash flows of an operating entity[3]. In most instances, the ABS Issuer is not expected to continue functioning beyond the final maturity of the debt initially raised by the ABS Issuer. Also, many ABS Issuers are in the form of a trust or special purpose vehicle ("SPV"), although the presence or lack of a trust or SPV is not a definitive criterion for determining that a security meets the definition of an asset-backed security. The provisions in paragraphs 9-10 detail the two defining characteristics that must be present for a security to meet the definition of an asset-backed security.

9. The assets owned by the ABS Issuer are either financial assets or cash-generating non-financial assets. Cash-generating non-financial assets are defined as assets that are expected to generate a meaningful level of cash flows toward repayment of the bond through use, licensing, leasing, servicing or management fees, or other similar cash flow generation. For the avoidance of doubt, there must be a meaningful level of cash flows to service the debt, other than through the sale or refinancing of the underlying assets held by the ABS Issuer. Reliance on cash flows from the sale or refinancing of cash generating non-financial assets does not preclude a security from being classified as an asset-backed security so long as the conditions in this paragraph are met.

a. *Meaningful Level of Cash Flows*: Determining what constitutes a "meaningful" level of cash flows generated to service the debt from sources other than the sale or refinancing of the underlying collateral pursuant to paragraph 9 is specific to each transaction, determined at origination, and shall consider the following factors:

i. The price volatility in the principal market for the underlying collateral;
ii. The liquidity in the principal market for the underlying collateral;
iii. The diversification characteristics of the underlying collateral (i.e., types of collateral, geographic location(s), source(s) of cash flows within the structure, etc.);
iv. The overcollateralization of the underlying collateral relative to the debt obligation; and
v. The variability of cash flows, from sources other than sale or refinancing, expected to be generated from the underlying collateral.

The factors for price variability and the variability of cash flows are directly related to the "meaningful" requirement. That is, as price volatility or variability of cash flows increase, the required percentage of cash flows generated to service the debt from sources other than the sale or refinancing of the underlying collateral must also increase. The factors for liquidity, diversification and overcollateralization are inversely related to the "meaningful" concept. That is, as liquidity, diversification or overcollateralization increase, the required percentage of cash flows generated to service the debt from sources other than the sale or refinancing of the underlying collateral may decrease.

b. As a practical expedient to determining whether a cash generating non-financial asset is expected to produce meaningful cash flows, a reporting entity may consider an asset for which less than 50% of the original principal relies on sale or refinancing to meet the meaningful criteria. In applying this practical expedient, only contractual cash flows of the non-financial

depends on the completion of a performance obligation (e.g., leases, mortgage servicing rights, royalty rights, etc.). These assets represent non-financial assets, or a means through which non-financial assets produce cash flows, until the performance obligation has been satisfied.

[3] Dedicated cash flows from an operating entity can form the underlying defined collateral in an asset-backed security. This dynamic, perhaps noted in a whole-business securitization, still reflects an asset-backed security and is not an issuer credit obligation.

assets may be considered. This practical expedient should not be construed to mean that assets cannot meet the meaningful criteria if they rely on sale or refinancing to service greater than 50% of the original principal or if they rely on cash flows that are not contracted at origination. Rather, such instances would require a complete analysis of the considerations described within the meaningful level of cash flows definition in paragraph 9.

10. The holder of a debt instrument issued by an ABS Issuer is in a different economic position than if the holder owned the ABS Issuer's assets directly. The holder of the debt instrument is in a different economic position if such debt instrument benefits from substantive credit enhancement through guarantees (or other similar forms of recourse), subordination and/or overcollateralization.

    a. *Substantive Credit Enhancement*: The intent of the criteria requiring the holder to be in a different economic position is to distinguish qualifying bonds from instruments with equity-like characteristics or where the substance of the transaction is more closely aligned with that of the underlying collateral. To qualify as an ABS under this standard, there is a requirement that there are substantive credit enhancements within the structure that absorb losses before the debt instrument being evaluated would be expected to absorb losses. This is inherent in the context of an issuer credit obligation in scope of SSAP No. 26R as the owners of the equity in the operating entity are the first to absorb any variability in performance of the operating entity. The same concept applies to asset-backed securities. If substantive credit enhancement did not exist, the substance of the debt instrument being evaluated would be more closely aligned with that of the underlying collateral than that of a bond. Credit enhancement that is merely nominal or lacks economic substance does not put a holder in a different economic position. The substantive credit enhancement required to be in a different economic position is specific to each transaction; determined at origination; and refers to the level of credit enhancement a market participant (i.e., knowledgeable investor transacting at arm's length) would conclude is substantive.

    b. The first loss position may be issued as part of a securitization in the form of a debt or equity interest, or it may be retained by the sponsor and not issued as part of the securitization. If the first loss position (or a more senior position(s), if the first loss position(s) lacks contractual payments along with a substantive credit enhancement) is issued as part of the securitization, and does not have contractual principal and interest payments along with substantive credit enhancement and is held by a reporting entity, the investment(s) does not qualify for reporting as a bond and shall be reported on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value consistent with the treatment for residuals. (These items are further addressed in *SSAP No. 21R—Other Admitted Assets*.)

11. Whether an issuer of debt represents an operating entity or ABS Issuer is unambiguous in most instances, but certain instances may be less clear. For example, an entity may operate a single asset such as a toll road or power generation facility (e.g., project finance) which serves to collateralize a debt issuance, and the cash flows produced by the operation of the assets are pledged to service the debt. In many such instances, the entity is structured as a bankruptcy-remote entity that is separate from the municipality or project sponsor. Such entities have characteristics of operating entities as the operation of the asset constitutes a stand-alone business. They also have many common characteristics of ABS Issuers as they are formed for the purpose of raising debt capital backed by the cash flows from collateral held by a bankruptcy-remote entity. When viewed more holistically, these issuing entities are typically being used to facilitate the financing of an operating component of a project sponsor or municipality. The use of a bankruptcy-remote entity facilitates the efficient raising of debt to finance the operating project, but the primary purpose is to finance an operating project. Therefore, structures in which the issuing entity represents a stand-alone business producing its own operating revenues and expenses, where the primary purpose is to finance an operating project, shall be considered operating entities despite certain characteristics they may share with ABS Issuers.

12. Likewise, distinguishing between a fund that represents an operating entity and a securitization vehicle that represents an ABS Issuer can involve similar ambiguity. Both types of entities may hold only passive investments and issue debt securities for which ultimate recourse upon default is to those investments. However, a clear distinction can generally be made by evaluating the substance of the entity and its primary purpose:

a. A fund representing an operating entity has a primary purpose of raising equity capital and generating returns to its equity investors. Marginal amounts of debt may be issued to fund operations or produce levered returns to equity holders. However, this is in service to meeting the fund's primary equity-investor objective. For 1940-Act registered closed-end funds (CEFs) and business development corporations (BDCs), debt securities issued from the fund in accordance with permitted leverage ratios represent debt issued by operating entities and qualify as issuer credit obligations.

b. In contrast, an ABS Issuer has a primary purpose of raising debt capital and its structural terms and features serve to support this purpose. Perhaps most distinctively, in addition to the characteristics detailed in Paragraph 8, the contractual terms of the structure generally define how each cash flow generated by the collateral is to be applied. There is generally little discretion afforded to the manager/servicer of the vehicle and any discretion that is allowed is narrowly defined in the contractual agreements. This hardwiring of debtholder protections allows for the issuance of higher amounts of leverage than would be possible for a fund representing an operating entity, further supporting the entity's primary purpose of raising debt capital.

~~12.~~13. The definition of a creditor relationship, per paragraph 6, does not include equity/fund investments (such as mutual funds or exchanged-traded funds), or securities that possess equity-like characteristics or that represent an ownership interests in the issuer. However, as identified in paragraph 2, exchange traded funds (ETFs), which qualify for bond treatment, as identified in Part Three of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and included in the 'SVO-Identified Bond ETF List' published on the SVO's webpage are provided special statutory accounting treatment and are included within the scope of this statement. These investments shall follow the guidance within this statement, as if they were issuer credit obligations, unless different treatment is specifically identified in paragraphs 32-38.

~~13.~~14. Investments within the scope of this statement issued by a related party, or acquired through a related party transaction, are also subject to the provisions, admittance assessments and disclosure requirements of *SSAP No. 25—Affiliates and Other Related Parties.*

~~14.~~15. Investments within the scope of this statement meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement and SSAP No. 25.

Proposed Revisions to Draft Issue Paper:

32. Whether an issuer of debt represents an operating entity or ABS Issuer is expected to be clear in most instances, but certain instances may be less clear. Ultimately, for an issuer credit obligation, it comes down to whether support for repayment consists of direct or indirect recourse to an operating entity or entities. In addition to "traditional bond" structures previously included in SSAP No. 26R, examples of issuer credit obligations include:

a. Investments in the form of securities for which repayment is fully supported by an underlying contractual obligation of a single operating entity. (e.g., CTLs, ETCs, other lease backed securities, Funding Agreement Backed Notes (FABNs), etc.). For purposes of applying this principle concept,

repayment is fully-supported by the underlying operating entity obligation if it provides cash flows for the repayment of all interest and at least 95% of the principal of the security.

b. Bonds issued by real estate investment trusts (REITS) or similar property trusts.

c. Bonds issued by funds representing operating entities. Determining whether a fund represents an operating entity can generally be made by evaluating the substance of the entity and its primary purpose. A fund representing an operating entity has the primary purpose of raising equity capital and generating returns to its equity investors. Marginal amounts of debt may be issued to fund operations or produce levered returns to equity holders. These debt issuances occur in accordance with the fund's primary equity-investor objective. Debt securities issued by closed-end funds and business development corps registered under the 1940 Act are permitted automatic qualification as issuer credit obligations as those funds are subject to strict limits or reporting components on the leverage (debt issuance) within the fund. ~~Bonds issued by business development corporations, closed-end funds or similar operating entities, in each case registered under the 1940 Act. With this inclusion, it is important to highlight that the intent is specific to bonds issued from SEC-registered entities. The reference to "similar entities" is not intended to capture items issued from collateralized fund obligations (CFOs) or other such structures.~~ In contrast, an ABS Issuer has a primary purpose of raising debt capital and its structural terms and features serve to support this purpose. More distinctively, the contractual terms of the structure generally define how each cash flow generated by the collateral is to be applied. For these structures, there is little or no discretion afforded to the manager/servicer of the vehicle and any discretion that is allowed is narrowly defined in the contractual agreements. The hardwiring of debtholder protections allows for the issuance of higher amounts of debt securities to be issued than what would be possible for a fund representing an operating entity. These features support the entity's primary purpose of raising debt capital. Although some may consider CFOs to be similar to closed-end funds, that assessment is not supported for classification as an issuer credit obligation. Instruments considered to reflect CFOs (and other like structures) are required to be assessed as asset-backed securities for inclusion on Schedule D-1.

d. Project finance debt issued by operating entities. These investments reflect financing of a single asset or "operation" (such as a toll road or power generation facility) that collateralizes a debt issuance and the cash flows produced by the asset/operation service the debt, where the issuer may also represent an operating entity. These designs have characteristics of both issuer credit operations, as the operation constitutes a stand-alone business, as well as characteristics of ABS, as they are formed for the purpose of raising debt capital backed by the cash flows from collateral held by a bankruptcy-remote entity. When viewed holistically, these issuing entities are typically used to facilitate the financing of an operating component of a project sponsor or municipality. Although the use of a bankruptcy-remote entity (e.g., SPV) facilitates the efficient raising of debt as a source of financing, the primary purpose is to finance an operating project. Therefore, when the issuing entity represents a stand-alone business producing its own operating revenues and expenses, where the primary purpose is to finance an operating project, the issuing entity shall be considered an operating entity despite certain characteristics that resemble ABS issuances.

i. It is important to highlight that the guidance for project finance is strictly for instruments issued by operating entities, similar to other instruments that qualify as issuer credit obligations under the principles-based bond definition. Consistent with other concepts, the naming convention (e.g., referring to an instrument as project finance) or the presence or absence of an SPV/trust structure are not definitive components in determining whether an investment qualifies for reporting on Schedule D-1, or is classified as an issuer credit obligation or ABS. Instruments (even if identified as "project finance") that do not qualify as issuer credit obligations as they not issued by operating entities, shall be assessed for

qualification for reporting on Schedule D-1 as ABS. If the instruments do not qualify for reporting as ABS, they shall not be reported on Schedule D-1.

e. U.S. Treasury Inflation-Protected Securities (TIPs): The inclusion of U.S. TIPs specifically as an issuer credit obligation intends to highlight a specific exception to the determination as a creditor relationship as the variation is due to plain-vanilla inflation adjustment mechanisms. Although U.S. TIPs are specific as issuer credit obligations, Under the bond definition encompassing both issuer credit obligations and asset-backed securities, in order for a debt instrument to represent a creditor relationship, it must have pre-determined principal and interest payments (whether fixed interest or variable interest) with contractual amounts that do not vary based on the appreciation or depreciation (e.g., performance) of any underlying collateral value or other non-debt variable . For example, an issued security that has varying principal and interest payments based on the appreciation of referenced equity, real estate or other non-debt variables are precluded from bond treatment as they do not reflect creditor relationships. Although US TIPS are indexed to the consumer price index and grows with inflation, these securities shall be captured as issuer credit obligations on Schedule D-1.

Status:
On January 10, 2024, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and exposed this agenda item with the proposed revisions, as illustrated above, to clarify the guidance for debt securities issued by funds. These revisions permit debt securities issued by funds to be classified as issuer credit obligations if the fund represents an operating entity regardless of SEC-registration status. This item was exposed with a comment deadline of February 9, 2024.

On March 16, 2024, the Statutory Accounting Principles (E) Working Group re-exposed this item with a request for regulators and industry to provide comment on the proposed language that assists with clarifying the scope of guidance and to the types of debt securities issued by funds that should be considered as operating entities, and the proposed language to better define the extent of debt that may be issued to fund operations. This re-exposure and request for clarification intends to address interpretations from the original exposure that the revised guidance would permit feeder funds (and other structures that raise debt capital) to be classified as issuer credit obligations.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group exposed revised language to SSAP No. 26 and the adopted issue paper for a shortened comment period ending September 6, 2024, as shown below. These revisions permit debt securities issued by funds that reflect operating entities to qualify as issuer credit obligations. These revisions clarify that SEC registration is a practical safe harbor intended only for SEC registered funds and should not be utilized as a proxy for other debt securities issued by funds. Other debt securities issued by funds should be assessed as to the issuer's primary purpose. Debt securities issued to raise debt capital must be assessed as an asset-backed security regardless of the amount of debt being issued. If no comments are received, or if only supportive comments are received, the Working Group may consider adoption via an evote.

Proposed Revisions to *SSAP No. 26—Bonds*

(Note: Non-revised subparagraphs have not been included for brevity.)

7. An issuer credit obligation is a bond, for which the general creditworthiness of an operating entity or entities through direct or indirect recourse, is the primary source of repayment. Operating entity or entities includes holding companies with operating entity subsidiaries where the holding company has the ability to access the operating subsidiaries' cash flows through its ownership rights. An operating entity may be any sort of business entity, not-for-profit organization, governmental unit, or other provider of goods or services, but not a natural person or "ABS Issuer" (as defined in paragraph 8). Examples of issuer credit obligations include, but are not limited to:

i. Bonds issued by funds representing operating entities as described in paragraph 12.~~Bonds issued by business development corporations, closed-end funds, or similar operating entities, in each case registered under the 1940 Act.~~

12. Likewise, distinguishing between a fund that represents an operating entity and a securitization vehicle that represents an ABS Issuer can involve similar ambiguity. Both types of entities may hold only passive investments and issue debt securities for which ultimate recourse upon default is to those investments. However, a clear distinction can generally be made by evaluating the substance of the entity and its primary purpose:

a. A fund representing an operating entity has a primary purpose of raising equity capital and generating returns to its equity investors. ~~Marginal amounts of~~Ancillary debt may be issued to fund operations or produce levered returns to equity holders. However, this is in service to meeting the fund's primary equity-investor objective. As a practical safe harbor,~~For~~ 1940-Act registered closed-end funds (CEFs) and business development corporations (BDCs), debt securities issued from the fund in accordance with permitted leverage ratios represent debt issued by operating entities and qualify as issuer credit obligations. This safe harbor for SEC-registered funds should not be viewed to extend to funds that are not SEC-registered by analogy, through comparison of leverage levels for example. All other funds should be classified in accordance with the determination of the issuer's primary purpose.

b. In contrast, an ABS Issuer has a primary purpose of raising debt capital and its structural terms and features serve to support this purpose. Perhaps most distinctively, in addition to the characteristics detailed in paragraph 8, the contractual terms of the structure generally define how each cash flow generated by the collateral is to be applied. There is generally little discretion afforded to the manager/servicer of the vehicle and any discretion that is allowed is narrowly defined in the contractual agreements. This hardwiring of debtholder protections allows for the issuance of higher amounts of leverage than would be possible for a fund representing an operating entity, further supporting the entity's primary purpose of raising debt capital.

Proposed Revisions to Issue Paper No. 169:

32. Whether an issuer of debt represents an operating entity or ABS Issuer is expected to be clear in most instances, but certain instances may be less clear. Ultimately, for an issuer credit obligation, it comes down to whether support for repayment consists of direct or indirect recourse to an operating entity or entities. In addition to "traditional bond" structures previously included in SSAP No. 26R, examples of issuer credit obligations include:

c. Bonds issued by funds representing operating entities. Determining whether a fund represents an operating entity can generally be made by evaluating the substance of the entity and its primary purpose. A fund representing an operating entity has the primary purpose of raising equity capital and generating returns to its equity investors. ~~Marginal amounts of~~Ancillary debt may be issued to fund operations or produce levered returns to equity holders. These debt issuances occur in accordance with the fund's primary equity-investor objective. Debt securities issued by closed-end funds and business development corps registered under the 1940 Act are permitted automatic qualification as issuer credit obligations as those funds are subject to strict limits or reporting components on the leverage (debt issuance) within the fund. This safe harbor for SEC-registered funds should not be viewed to extend to funds that are not SEC-registered by analogy, through comparison of leverage levels for example. All other funds should be classified in accordance with the determination of the issuer's primary purpose. (For example, although some registered funds allow a large percentage of debt, non-registered funds with comparable amounts of issued debt may reflect debt securities from feeder funds or equity-backed ABS, and those debt securities are required to be assessed as ABS. As such the percentage of debt permitted for a registered funds should not be utilized as a proxy in determining whether debt issued from a fund is permitted to be

captured within the guidance.) ~~Bonds issued by business development corporations, closed-end funds or similar operating entities, in each case registered under the 1940 Act. With this inclusion, it is important to highlight that the intent is specific to bonds issued from SEC-registered entities. The reference to "similar entities" is not intended to capture items issued from collateralized fund obligations (CFOs) or other such structures.~~ In contrast, an ABS Issuer has a primary purpose of raising debt capital and its structural terms and features serve to support this purpose. More distinctively, the contractual terms of the structure generally define how each cash flow generated by the collateral is to be applied. For these structures, there is little or no discretion afforded to the manager/servicer of the vehicle and any discretion that is allowed is narrowly defined in the contractual agreements. The hardwiring of debtholder protections allows for the issuance of higher amounts of debt securities to be issued than what would be possible for a fund representing an operating entity. These features support the entity's primary purpose of raising debt capital. Although some may consider CFOs or feeder funds to be similar to closed-end funds, that assessment is not supported for classification as an ICO. Instruments considered to reflect CFOs (and other like structures) are required to be assessed as ABS for inclusion as a bond reported on Schedule D-1. Paragraphs 27-28 also detail the assessment expected in classifying feeder funds, and the requirement to determine the source of the underlying cash flows in determining classification and if the structure qualifies for reporting as a bond on Schedule D-1.

On September 12, 2024, the Statutory Accounting Principles (E) Working Group concluded an e-vote to adopt the August 2024 exposed revised language to SSAP No. 26 (effective Jan. 1, 2025) and related bond project issue paper. This e-vote noted a single comment letter received from interested parties indicating support for the exposed revisions. As the edits revise the guidance adopted for the bond definition, which is effective Jan. 1, 2025, the edits will follow the same effective date.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/09-12-24 - Evote Adoption/B - 24-01 - PBBD - SEC Funds.docx

Revisions to the
As of March 2024, Accounting Practices and Procedures Manual

On **November 17, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2019-21	**INT 24-01**	Principles-Based Bond Definition Implementation Questions and Answers *SAP Clarification* Effective January 1, 2025	Adopted INT 24-01 addresses specific questions related to the implementation of the Principles-Based Bond Project that had been brought to the Bond/AICPA small group.
2024-11	SSAP No. 101	*ASU 2023-09, Improvements to Income Tax Disclosures* *SAP Clarification* Effective Immediately (November 17, 2024)	Adopted revisions to SSAP No. 101 reject ASU 2023-09 for statutory accounting purposes and deletes the disclosure detailed in SSAP No. 101, paragraph 23.b., as it was determined to be no longer relevant due to changes made to federal tax codes.
2024-17	SSAP No. 108	*Clearly Defined Hedging Strategy* *SAP Clarification* Effective Immediately (November 17, 2024)	Adopted *SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees* revisions update the definition of a clearly defined hedging strategy (CDHS) to reflect the revised guidance pursuant to VM-01.
2024-18	SSAP No. 48 SSAP No. 93 SSAP No. 94	*Clarification of Accounting Guidance for Recognition of Tax Credits* *SAP Clarification* Effective January 1, 2025	Adopted revisions in *SSAP No. 93—Investments in Tax Credit Structures* clarify the accounting guidance for recognizing allocated and purchased tax credits in relation to the journal entry example. Adopted revisions in *SSAP No. 94—State and Federal Tax Credits* fix an inconsistency between the accounting guidance and journal entry examples. Adopted revisions to *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* revise a sentence which was inadvertently not updated as part of the project.

Ref #	SSAP/ Appendix	Title	Summary
2024-19	Appendix D	*ASU 2024-02, Codification Improvements—Amendments to Remove References to the Concepts Statements* *SAP Clarification* Effective Immediately (November 17, 2024)	Adopted revisions to *Appendix D—Nonapplicable GAAP Pronouncements* rejects ASU 2024-02 as not applicable to statutory accounting.

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Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers

INT 24-01 Dates Discussed

August 13, 2024, October 4, 2024, November 17, 2024

INT 24-01 References

Current:
SSAP No. 21—Other Admitted Assets
SSAP No. 26—Bonds

INT 24-014 Issue

1. The principles-based bond definition was adopted in August 2023 with an effective date of January 1, 2025. In response to questions presented, question-and-answer implementation guidance was developed to assist with consistent assessment and application under the principles-based bond definition.

INT 24-01 Discussion

2. The Working Group reached consensus that Exhibit A provides question-and-answer guidance consistent with the intent of the principles-based bond definition, including application of debt securities that qualify for bonds under SSAP No. 26 and guidance for debt securities that do not qualify as bonds under SSAP No. 21.

INT 24-01 Status

3. This interpretation, and the question-and-answer guidance in Exhibit A is effective January 1, 2025. Consideration of further components may occur if future questions are received on the application of the principles-based bond guidance.

4. No further discussion is planned.

Exhibit A – Principles-Based Bond Definition Implementation Questions and Answers

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Exhibit A – Principles-Based Bond Definition Implementation Questions and Answers

1. Q – When assessing whether a security has substantive credit enhancement, how should future cash flows be considered? Should future expected cash flows be incorporated into the overcollateralization disclosure? [SSAP No. 26, paragraph 6.a. and 10.a.]

1.1 A – There are two components to this question: 1) how to consider future cash flows in assessing substantive credit enhancement; and 2) how to disclose the overcollateralization percentage. For the first component, the purpose of the substantive credit enhancement concept is to determine whether the creditor is in a different economic position than owning the underlying collateral directly. This includes evaluating all forms of economic value that the creditor has recourse to, including "hard," saleable assets, contractual or expected future cash flows, operating entity guarantees or other sources, and determining whether there is another party that absorbs substantive losses in economic value before the creditor experiences any losses. Note however, **if** a reporting entity performs a quantitative assessment to support its conclusion, it should not double-count economic value. For example, in a lease-backed ABS, if the reporting entity incorporates future lease payments into its analysis, it should also consider the future, depreciated value of the "hard assets" rather than the current saleable value.

1.2 The second component of the question is how to complete the overcollateralization percentage disclosure on Schedule D, which is required for Non-Financial ABS that do not meet the practical expedient criteria and Financial ABS that are not self-liquidating. It was noted that including a quantification of all forms of economic value discussed in 1.1, which may include not only "hard," saleable assets but also future cash flows or operating entity guarantees, would be cumbersome to complete for each applicable investment, both at origination and an ongoing basis. It would also make the disclosure difficult to interpret, as it would not be apparent whether the overcollateralization is in the form of assets that could be liquidated upon default, or future cash flows which may be less readily able to be liquidated. Based on the discussion, it was determined that it would be most expedient, as well as most useful to annual statement users, for the overcollateralization percentage to only include "hard," saleable assets. For example, if a structure involved the leasing of railcars, and the structure had railcars and the associated lease cashflows pledged to the ABS Issuer as collateral, only the value of those railcars to the outstanding debt would be included in the disclosure. (This calculation is based on the value of the railcars, and not their future leasing potential.) Overcollateralization determined by the discounting of future cash flows is not permitted to be included in the disclosure.

1.3 Reporting entities shall report 'zero' when there is no "hard asset" overcollateralization in a structure on Schedule D. The column should not be left blank. A zero response is not standalone evidence that a structure does not qualify for bond reporting. A debt security can qualify for bond reporting without "hard asset" overcollateralization.

2. Q – Are securities issued by foreign governments or foreign government agencies considered Issuer Credit Obligations? [SSAP No. 26, paragraph 7.a.]

2.1 A – The examples of issuer credit obligations (ICO) in paragraph 7 are not all inclusive. Governmental entities are operating entities based on their substance, which does not change based on country. Securities issued as obligations of foreign governments or foreign government agencies are expected to be considered ICOs, unless the substance is more aligned with ABS. Schedule D-1-1 includes a reporting line for "Non-U.S. Sovereign Jurisdiction Securities." Foreign securities that reflect ABS, similar to US agency backed RMBS for example, are also expected to be considered ABS. Such ABS are anticipated to be reported on D-1-2 on the most appropriate reporting line that does not reflect a guarantee by the U.S. government.

3. Q – Are "Municipals" always Issuer Credit Obligations? [SSAP No. 26, paragraph 7.c. and 11]

3.1 A – The question received inquired on the classification of "municipals" noting the various structures and designs, and the explicit reporting lines on Schedule D-1-1 for general obligation and special revenue municipal structures. The answer to this question is that the naming convention of investment structures does not determine whether the investment qualifies for reporting as a bond or whether the investment is an issuer credit obligation (ICO) or asset-backed security (ABS). The first step in determining if an investment qualifies as a bond is whether it reflects a creditor-relationship in substance. The second step is determining whether the structure is an ICO or ABS, and that determination focuses on the primary source of cash flows that provides payment of interest and principal to the debtholder. Municipal securities are subject to the same assessment as other structures as to whether the cash flows are generated by the operations of an operating entity (the municipality) or whether the cash flows are generated from collateral outside of the operations of the municipality in determining whether the security shall be classified as ICO or ABS. However, this distinction is not always clear for several types of common municipal securities which warrants some additional interpretive guidance to promote consistency and streamline implementation efforts. The following summarizes preliminary assessments based on common designs of these structures. These assessments are contingent on the actual substance of the investment and shall not be inferred based on naming convention if the investment being reviewed does not conform to the traditional design.

a. General Obligation Municipal Bonds – These bonds are backed by the full faith and credit of the government issuer (municipality), which is an operating entity with the power to tax residents to pay bondholders. These securities, as general obligations of an operating entity (the municipality), would qualify as ICOs as explicitly stated in paragraph 7.c. of SSAP No. 26, and shall be reported in the "Municipal Bonds – General Obligation" reporting line.

b. Special Revenue Municipal Bonds – These bonds are not backed by the government's general taxing power but by revenues from a specific municipality-owned project or source, such as highway tolls, water and sewer, electric utility, lease fees or usage charges. Payment of interest and principal depends on the adequacy of the revenues derived from the project. Although the operating asset and/or its associated cash flows are often walled off in a bankruptcy remote SPV in order to facilitate more efficient financing of such projects, the primary purpose is still to raise debt capital to fund a component of a municipality's operations. Both paragraph 7.c. and 11 of SSAP No. 26 explicitly contemplate securities of this type qualifying as ICO, and shall be reported in the "Municipal Bonds – Special Revenue" reporting line.

c. Tax Revenue Bonds – These bonds are backed from certain dedicated tax revenues overseen by the municipality, such as sales taxes, gasoline or tobacco taxes, hotel or tourist taxes, special tax assessments or incremental property taxes. Payment of interest and principal depends on the adequacy of tax revenue. Although the obligation is secured only by a single revenue source, rather than the full faith and credit of the municipality, it is still backed by the municipality's taxing authority and is ultimately used to facilitate the raising of financing to be used in funding the needs and responsibilities of the municipality. Tax revenue bonds are determined to have the substance of an ICO and should be reported in the "Municipal Bonds – Special Revenue" reporting line.

d. Housing Bonds – These securities may be issued by a state or local government housing authority to facilitate construction or rehabilitation of multi-family apartments for low to moderate income residents. The bonds are secured by a pledge of rental or lease revenues and/or mortgage payments. These bonds generally only have recourse to the assets or mortgages pledged. These securities are

not backed by the operations of the municipality, the financing is not being used to fund any operations of the municipality and the primary source of repayment are non-municipal collateral assets. Based on these observations, their substance appears to more closely reflect that of an ABS and shall be assessed for bond qualification under the ABS requirements. If qualifying as ABS, these structures shall be reported on Schedule D-1-2, likely as a non-guaranteed, non-agency, mortgage-backed security.

e. Conduit Bonds – These debt securities are issued by a government entity as a conduit for the benefit of a business or non-governmental enterprise, such as a manufacturing company, developer, college, hospital or non-profit organization. Revenues pledged by the business or enterprise are used to pay interest and principal on the investments. The government issuer is not responsible for making payments on the bonds if the business or enterprise defaults. These debt securities will need to be assessed to determine whether the structure qualifies as an ICO or ABS. If the structure is backed by the creditworthiness of a single operating entity (such as a college), then the structure is expected to be an ICO. If qualifying as an ICO, the specific reporting line used should be the one that most closely reflects the nature of the investment. If historical reporting and/or market conventions would consider the ICO investment to be a municipal security, then it would be reasonable for the investment to be reported as a special-revenue municipal bond. However, this reporting is contingent on the ICO classification. If the structure represents an ABS (such as a conduit bond secured by housing assets or mortgages pledged), it should not be reported as a municipal on Schedule D-1-1 simply due to historical reporting or market convention as a municipal bond.

4. Q – Should common types of "Sports Deals" be classified as ICO or ABS? [SSAP No. 26, paragraphs 7-8]

4.1 A – There are two main types of leaguewide sports financing vehicles, with the key difference being whether or not noteholders have recourse to the individual sports teams.

4.2 Leaguewide Deals **with** Recourse to Teams - The League sets up an SPV or Trust that serves to aggregate debt issued by multiple teams within the League. The SPV (Trust) issues a Note, representing the aggregation of each underlying team's debt obligation. Through the SPV, Noteholders have recourse back to each individual team for its respective debt on a several (but not joint) basis. The Notes are also secured by Franchise rights for each team that participates in the financing and all revenues from current and future League media contracts and typically other ancillary revenue streams (e.g. online/streaming revenues, royalty fees from sports gear sold to fans, etc.). No cross-collateralization among teams or their respective revenue streams, but Noteholders have some protection from the League (which exercises considerable control over individual teams) and a pledge of team ownership rights as collateral. Should any individual team default, the League could (and in all practicality, would) step in to orchestrate a sale of the team, otherwise Noteholders could take ownership of the team.

4.3 The question raised was whether this type of deal would fall under the ICO or ABS criteria. Each team represents an operating entity, and each are individual obligors for their pro rata portion of the financing. Though the direct issuer is an SPV, it is being used to facilitate the efficient raising of debt capital by the individual teams/operating entities, as opposed to redistributing or transforming the underlying risk. In addition, the league itself is an operating entity, and though it is not a direct obligor on the financing, it has a significant role in the facilitation of the financing, its actions can significantly impact the paying ability of the individual teams and it has levers it can and would pull to ensure debtholders receive payment. Through discussion of this example, it was determined that the substance was more aligned with that of an ICO than an ABS. Under one perspective, the league could be viewed as a single-operating entity with all

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of its affiliated teams being part of that operating entity. This would allow the debt to be considered a "single operating entity backed obligation" under paragraph 7.g. of SSAP No. 26. Under another perspective, debtholders effectively hold debt obligations of each of the individual teams. If each team were to individually issue their debt to the noteholders, rather than through a coordinated offering, the noteholders would be in no different economic situation and each individual security would qualify as an ICO. As a result, this investment is effectively a series of "single operating entity backed obligations" under paragraph 7.g. Based on these observations, it was determined that this type of deal is an ICO in substance.

4.4 Leaguewide Deals **without** Recourse to Teams - Each participating team sells its share of all current and future contracted media revenues (and other ancillary revenues) to a newly created, bankruptcy remote subsidiary of the team in a true sale. The subsidiary then pledges the purchased assets to an SPV/Trust set up by the League. The SPV/Trust then issues Notes to investors. The structure has many features associated with ABS securities, including a bankruptcy-remote legal opinion, a true sale legal opinion, debt service reserves, and a payment waterfall (with Noteholders receiving priority of payment). The Notes are secured by revenues generated from the media contracts and other ancillary revenues (e.g. online/streaming revenues, royalty fees from sports gear sold to fans, etc.).

4.5 Unlike the previous example, these securities do not have recourse to an operating entity. They have all of the characteristics of a securitization of a revenue stream. Therefore, they must be evaluated under the ABS criteria. Also, there is a performance obligation for the cash flows to become collectible, as the product must be provided in order for the revenue to be generated (i.e. games must be played). As a result, the collateral are deemed to be non-financial assets, requiring the security to be assessed under the non-financial ABS criteria.

5. Q – Do cashflows produced by non-financial assets backing an ABS have to actually be used to make interest and principal payments throughout the life of the debt security for an investment to qualify as a non-financial backed ABS under the meaningful cash flow test? [SSAP No. 26, paragraph 8]

5.1 A – The principles-based bond definition is clear that the collateral supporting non-financial ABS must have a means of producing meaningful cash flows through other than sale or refinancing. However, it does not specify whether those cash flows must actually be used to pay the principal and interest in all scenarios. For example, it is not uncommon for an ABS to allow cash flows to be paid to equity holders prior to the debt tranches being repaid, so long as no covenants or triggering events have been breached. The example given was a continuation of the leaguewide sports deal **without** recourse to the individual teams as discussed in Question #4 in which the ABS was backed by current and future contracted media revenues (non-financial assets). The notes were issued as non-amortizing bullet maturities (e.g., 100% balloon payments). Therefore, the base case expectation is that the bonds will be refinanced at maturity. However, after full analysis, it was identified that the non-financial assets backing the structure generated substantially more cash flows over the life of the debt security than what would be needed to provide all interest and principal payments and would produce enough cash flows to "turbo" amortize and pay 100% of principal and interest in a short time frame if refinancing were not to occur. Additionally, there exist covenants (e.g. upon a significant decrease in media revenue) which, if triggered, would cause all cash flows to be diverted away from the equity holders and used to "turbo" amortize the debt. The question is, does the fact that the base case expectation is that the cash flows will not be used to pay down the debt result in the ABS lacking meaningful cash flows? Based on these discussions, it was determined that this situation would not preclude a conclusion that meaningful cash flows exist. Despite the meaningful cash flows not being used to pay the debt in the base case, the creditor still has rights to them and would collect them prior to experiencing any loss upon default. Therefore, all such cash flows available to creditors may be included in the assessment of meaningful cash flows.

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6. Q – How should CMBS Interest Only (IO) strips be assessed under the PBBD? [SSAP No. 26, paragraphs 8-10]

6.1 A – The question pertains to the classification of CMBS IO strips that are paid from the excess spread of a CMBS structure. Excess spread is the excess of the interest collected on the underlying commercial mortgages over the contractual interest to be paid on the issued securitized tranches. In these instances, the IO strip is "linked" to either a specific tranche (such as a specific B-rated or AAA-rated tranche), or the IO strip could be linked to a combination of the issued tranches (from the residual tranche through the top AAA tranche). The tranche or tranches to which an IO is linked refers to the notional amount of principal from which the IO interest is calculated. Regardless of which tranche an IO is linked to, it is paid pari-passu with AAA rated tranche. The calculation of the IO strip interest to be paid is the product of the remaining principal of the linked debt tranche and the contractual rate of the IO strip and the contractual rate is equal to the difference between the weighted average coupon of the underlying loans, and the weighted average coupon of the issued securitization tranches. The contractual rate of the IO strip is recalculated each period based on the loan and debt tranche balances that remain outstanding. For example, if weighted average coupon on the underlying loans is 9.2% and the weighted average coupon on the securitization tranches is 8%, the contractual rate on the CMBS IO is 1.2%. If the IO strip is linked to the BBB tranche and the BBB tranche has a principal value of $1,000, there would be a monthly coupon payment of $1.00 [(1.2% / 12 months) * 1,000]. The CMBS IO holder would receive their contractual interest pari-passu with the AAA tranche, meaning they would receive all contractual interest prior to any of the subordinated securitization tranches being entitled to receive interest. When losses or principal payments are applied to the linked securitization tranche, the notional amount on which the CMBS IO interest is calculated is reduced until fully paid or written off.

6.2 In assessing these structures under the bond definition, IO strips should be considered in the same manner as a debt security that reflect both principal and interest components. That is, for a CMBS security (a financial asset-backed security), the structure would be required to have substantive credit enhancement to qualify for bond classification. For these CMBS structures, even if the IO tranches may always be paid pari-passu with the AAA tranche, an assessment must still occur on whether there is substantive credit enhancement. If the IO tranche is linked to a debt tranche, or a combination of debt tranches, that have substantive credit enhancement, then the IO is also considered to have substantive credit enhancement resulting in an ABS bond classification. If the IO tranche is linked to a tranche that does not have substantive credit enhancement, or a combination of debt tranches that includes a tranche that does not have substantive credit enhancement (such as the residual tranche), the IO strip would also not be considered to have substantive credit enhancement and shall be classified as a non-bond debt security. This is because it would lack substantive credit enhancement to absorb losses before the notional balance from which the IO interest is calculated is reduced. As a result, principal losses on the underlying loans would result in an economic loss to the IO if there is no credit enhancement to absorb them.

7. Q – How should debt securities that reflect Single Asset Single Borrower (SASB) Commercial Mortgage Loan (CML) securitizations be assessed under the PBBD? [SSAP No. 26, paragraphs 8-10]

7.1 A – The question pertains to SASB commercial mortgage-backed security (CMBS) structures which involve securitizing a single mortgage loan collateralized by one property owned by a single borrower. Although structures can vary, SASBs are usually associated with high-value properties with many long-term tenants where the mortgage loan is too large for a single lender to hold. By securitizing the loan into rated, tradeable securities, it facilitates access to a broader lender base than would exist for commercial mortgage loans. SASB CMBS structures can issue multiple tranches with different priorities of payment, or they can issue one single tranche (i.e., uni-tranche) that simply passes through the cash flows of the

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underlying mortgage. In either scenario, the principal and interest payments on the underlying loan provide the cash flows to service the principal and interest on the issued debt securities. Usually, the principal and interest on the commercial mortgage loan and the issued securities are equal except for fees and expenses for servicing and structuring paid by the ABS Issuer.

7.2 Under the PBBD concepts, SASBs should be assessed as asset-backed securities (ABS), as the repayment of principal and interest is derived from the cash flows of the underlying collateral and not the general creditworthiness of an operating entity. SASB CMBS structures are not expected to qualify for reporting as issuer credit obligations reflecting a debt security fully supported by an underlying contractual obligation of a single operating entity pursuant to SSAP No. 26, paragraph 7.g. Although the ultimate cash flows for repayment are expected to be derived from the leasing of the property, the lease cash flows are typically not pledged and there are typically multiple lessees, thus not qualifying under paragraph 7.g. Under the ABS criteria, a SASB CMBS reflects a financial asset-backed structure (as a mortgage loan is a financial asset), therefore the debt security must qualify under the substantive credit enhancement concept to qualify for bond reporting. Determination of whether the debt issuance has substantive credit enhancement is contingent on the actual structure (multi-tranche or uni-tranche) and position of the security within the structure.

7.3. The senior tranches (those above the most junior tranche) in a multi-tranche SASB are expected to qualify under the substantive credit enhancement criteria, as the subordinated tranches will absorb losses first. Assuming the subordination is significant enough to be considered substantive, the subordination of the lowest tranche puts the reporting entity that holds a more senior tranche in a different economic position than if the mortgage loan was held directly.

7.4 The lowest tranche of a multi-tranche SASB, any tranche in which the subordinated tranches below it do not provide substantive credit enhancement, and uni-tranche SASBs are not expected to qualify for reporting as a bond as they do not meet the requirement for substantive credit enhancement. For these situations, the reporting entity is not in a different economic position than if they held the underlying mortgage loan directly. This is true regardless of the LTV or overcollateralization of the property compared to the underlying mortgage loan as the bond definition does not contemplate a broad look-through of the underlying collateral to indirect subordination. This is most clearly illustrated in Example 1 of Exhibit A of SSAP No. 26 which does not contemplate looking through the mortgage loan collateral to overcollateralization of the mortgage loans themselves through recourse to the underlying properties. While this is a legitimate source of overcollateralization, it represents overcollateralization of the mortgage loans in relation to the underlying properties, not overcollateralization of the debt securities in relation to the mortgage loans. The investor is in the same economic position as holding the mortgage loans directly. Therefore, these structures fail the substantive credit enhancement requirement and do not qualify for reporting as a bond.

7.5 SASB structures that do not qualify for reporting as a bond shall be captured as non-bond debt securities on Schedule BA within the reporting line specific for "Debt Securities That Lack Substantive Credit Enhancement." Life reporting entities can file these debt securities within the NAIC SVO to obtain an NAIC designation that can be used for RBC.

8. Q – Do synthetic or referenced pool structures within an ABS disqualify the ABS for reporting on Schedule D-1-2? [SSAP No. 26, paragraph 9]

8.1 A – The principles-based bond definition refers to ABS as being repaid with cash flows produced by collateral "owned" by the issuer. The term "owned" as used for this purpose is not necessarily intended to align with a legal view of ownership, but rather, all economic value to which the creditor has recourse. This may include rights to assets or payments derived through assignment, or other provisions. An example that has become common due to evolving banking regulations was discussed whereby a bank has a portfolio

of auto loans but wants to transfer their credit risk without transferring or selling their loans. The bank creates a special purpose trust (or vehicle) to which the bank issues a "credit linked note" (effectively equivalent to a "credit risk transfer") which references the performance of the bank's portfolio of auto loans. The securities issued by the special purpose trust (e.g., debt tranche(s) and an equity tranche) are exposed to the reference pool of collateral and the payments received are linked to the credit and principal payment risk of the underlying borrowers captured in the reference pool. The specific underlying collateral, and whether it resides within the ABS, or if the ABS references a collateral item/pool that generates cash flows is not a determining factor as long as the ABS Issuer has contractual rights to the cash flows produced to repay the debt. An ABS Issuer that owns derivatives in the structures (such as a credit default swap or total return swap) that solely transfers the performance of the referenced pool into the ABS structure does not automatically disqualify ABS classification, but the assessment of derivatives within a structure must be closely considered. Structures with derivatives that influence payments based on variables unrelated to the ultimate collateral would not qualify as a creditor relationship in substance. Further, consideration should be given to *SSAP No. 86—Derivatives* in determining whether structures with derivatives are subject to specific guidance, such as that for structured notes.

9. Q – Can expected but non-contractual cash flows (e.g., from future leases) be considered in determining the meaningful cash flow practical expedient for non-financial ABS? [SSAP No. 26, paragraph 9.b.]

9.1 A – The example given was a single-family rental where the lease duration is shorter than the duration of the debt security, subjecting the investor to re-leasing risk. The insurer has a high degree of confidence based on its understanding of the market that the property will be able to be re-leased and that the leases (including consideration of unleased time) will produce sufficient cash flows to satisfy all of the interest and at least 50% of the original principal. The question is whether this example qualifies under the practical expedient. Paragraph 9.b. explicitly states that only contractual cash flows are to be considered in assessing qualification under the practical expedient. As such, evaluating qualification under the practical expedient should not include any future leases that are not yet in place and this example would therefore not qualify. However, this does not necessarily mean that the full analysis will require significantly more effort than using the practical expedient in this case. In fact, the analysis the insurer performed to determine that all of the interest and at least 50% of the principal would be satisfied through expected lease payments is likely sufficient to conclude that there are meaningful cashflows, even though the practical expedient is not met.

9.2 This question was brought forward because, although paragraph 9.b. is explicit that only contractual cash flows are included, a paragraph in a prior draft of the issuer paper addressing this topic omitted the word "contractual". This has since been corrected. This question highlights an important point. Issue papers intend to provide key context regarding the discussions leading to the development of new accounting standards. However, any unintended language that conflicts with statements in the SSAP should be disregarded.

9.3 As one more element of clarity coming from the discussions on this topic, the meaningful cash flow practical expedient is that less than 50% of the original principal relies on sale or refinancing risk. In some cases, this has been phrased in the inverse, that all interest and more than 50% of the original principal must be satisfied by the contractual cash flows at investment acquisition for the investment to qualify under the practical expedient. These two phrasings would be expected to have the same meaning, but for the avoidance of doubt, the standard should be interpreted that any outstanding amounts that rely on sale or refinancing at maturity, whether characterized as principal or accrued interest, must be less than 50% of the original principal in order to qualify under the practical expedient.

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10. Q – How should hybrid securities be accounted and reported? [SSAP No. 26, paragraph 13]

10.1 A – SSAP No. 26 prior to the principles-based bond definition explicitly scoped in a class of assets referred to as "hybrid securities" which are defined as "securities whose proceeds are accorded some degree of equity treatment by one or more of the nationally recognized statistical rating organizations (NRSRO) and/or which are recognized as regulatory capital by the issuer's primary regulatory authority. Hybrid securities are designed with characteristics of debt and equity and are intended to provide protection to the issuer's senior note holders. Hybrid securities are sometimes referred to as capital securities." During the development of the principles-based bond definition, it was decided to remove the explicit scope-in and instead rely on the new principles to determine whether bond classification is appropriate. As these securities come in several forms, additional clarity on where to report such securities is warranted.

10.2 Equity Securities: Investments that represent shares, units, or an ownership interest in a company or other entity but do not reflect common stock that were previously considered hybrids under SSAP No. 26 are equity investments and shall be captured as preferred stock in scope of *SSAP No. 32—Preferred Stock*. Investments in debt securities are not permitted to be reported in scope of *SSAP No. 30—Unaffiliated Common Stock* or SSAP No. 32.

10.3 Debt Securities: Investments in debt securities previously considered hybrids under SSAP No. 26 (including those debt securities with cumulative interest features) **that qualify** under the principles-based bond definition shall be reported as bonds on Schedule D. An example may include certain debt securities which NRSROs allow to be treated as equity but for which all the principles-based bond definition requirements are present. To be clear, a set maturity date for a debt security is not a requirement for bond classification if the bond otherwise qualifies under the definition. (Perpetual bonds that qualify under the bond definition are permitted as bonds.)

10.4 Investments in debt securities treated as regulatory capital by the issuer's primary regulatory authority, and **that do not qualify** under the principles-based bond definition solely because interest can be cancelled in the event of financial stress in a non-resolution scenario without triggering an act of default are capital notes and shall be captured in *SSAP No. 41—Surplus Notes*. These capital notes are often issued by domestic or foreign banks, and the domestic or foreign bank regulator or the Issuer has the ability to cancel interest or dividends, without future interest accumulation or payment.

10.5 Debt securities other than capital notes (as defined in 10.4 above) that permit the issuing entity to cancel interest without future interest accumulation or payment and without triggering an act of default, or that incorporate other equity components that do not permit bond classification under the principles-based bond definition are non-bond debt securities and shall be captured in scope of *SSAP No. 21—Other Admitted Assets*.

10.6 Debt securities issued by regulated institutions where only the issuer's primary regulator may have regulatory power to cancel or convert to equity all or a portion of the debt and/or its related interest payments, solely **in a resolution scenario** were not previously considered hybrid securities and should continue to be reported as Schedule D bonds, as Issuer Credit Obligations under SSAP No. 26, so long as all principles-based bond definition requirements are met.

10.7 Exhibit A to this Q&A provides a summary of common types of securities and how they are to be treated under this Q&A.

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11. Q – When do non-bond debt securities need to be assessed for admittance based on underlying collateral? [SSAP No. 21, paragraph 22]

11.1 A – All debt securities that do not qualify as bonds, regardless of the reason for which they do not qualify, shall be assessed as to the primary source of repayment. If the primary source of repayment is derived through underlying collateral, then the collateral must qualify as an admitted asset in order for the non-bond debt security to be admitted. For example, if the source of repayment is derived from mortgage loans, and the structure failed because it did not reflect a creditor relationship, have substantive credit enhancement or meaningful cash flows, the debt security is permitted to be admitted if the mortgage loans would have qualified as admitted assets if held directly. If the source of repayment is derived from railcar leases, and the structure failed because it did not reflect a creditor relationship, have substantive credit enhancement or meaningful cash flows, the debt security shall be nonadmitted as directly held railcars would not qualify as admitted assets.

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Exhibit A – Principles-Based Bond Definition Implementation Questions and Answers

Appendix A – Summary of Securities for Application under Question 10

	Bank Issuers					All Issuers	
				Additional Tier 1 Capital			
Bank Debt/Capital & Hybrid Securities Matrix	**Sr. Unsecured OpCo Debt**	**Sr. Unsecured HoldCo Debt**	**Tier 2 Capital (Subordinated Debt)**	**Debt Form**	**Perpetual Preferred Form**	**Debt Issued for Partial Equity Treatment from NRSROs**	**Debt Issued for Partial Equity Treatment from NRSROs**
In scope of "hybrid securities" definition in Q&A?	No	**Yes***	**Yes***	**Yes***	**Yes***	**Yes**	**Yes**
Issuer Can Cancel Interest (or Dividend) Non-Cumulatively w/out Default**	No	No	No	**Yes**	**Yes**	**Yes**	**No**
Regulator Can Force Cancellation of Interest (or Dividends) Non-Cumulatively w/out Default	No	No***	No***	**Yes**	**Yes**	No	No
Regulator Can Force Write-down or Equity Conversion of Debt	No	**Yes**	**Yes**	**Yes**	**Yes**	No	No
Proposed Accounting Treatment	SSAP 26 Bond Schedule D, Part 1	SSAP 26 Bond Schedule D, Part 1	SSAP 26 Bond Schedule D, Part 1	SSAP 41 Capital Notes Section of Schedule BA	SSAP 32 Preferred Stock Schedule D, Part 2	SSAP 21 Non-Bond Section of Schedule BA	SSAP 26 Bond Schedule D, Part 1

*Bank regulators require a specific amount of debt that is subject to "bail-in" during a resolution. Additional Tier 1 Captial, Tier 2 Capital and Total Loss Absorbing Capacity (the latter of which includes Sr. Unsecured HoldCo Debt) are all subject to bail-in requirements and count towards various solvency ratio tests.

**Older verions of bank capital exist where the Issuer can defer interest on a cumulative basis without triggering a default. These securities would be treated as SSAP 26 Schedule D, Bonds, as would any security with cumulative interest features.

***Interest amount can be cancelled or reduced following a write-down of debt in resolution scenario only.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: ASU 2023-09, Improvements to Income Tax Disclosures

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In December 2023, the Financial Accounting Standards Board (FASB) issued *Accounting Standards Update (ASU) 2023-09, Improvements to Income Tax Disclosures* (the ASU) to enhance the transparency and decision usefulness of income tax disclosures. The ASU amends and expands the disclosures for rate reconciliation between income tax expense and statutory expectations for both public and private entities. Per the ASU, "The objective of these disclosure requirements is for an entity, particularly an entity operating in multiple jurisdictions, to disclose sufficient information to enable users of financial statements to understand the nature and magnitude of factors contributing to the difference between the effective tax rate and the statutory tax rate." Public entities are required to provide detailed quantitative and qualitative disclosures, while private are only required to provide qualitative rate reconciliation disclosures on certain specified categories. Additionally, the ASU also requires all entities to provide additional disclosures on income tax expense and income taxes paid, and removes the disclosure requirement for positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease within 12 months of the reporting date (ASC 740-10-50-15d), and the cumulative amount of each type of temporary difference related to unrecognized deferred tax liabilities (ASC 740-30-50-2b).

Existing Authoritative Literature:
SSAP No. 101—Income Taxes:

Disclosures

21. Statutory financial statement disclosures shall be made in a manner consistent with the provisions of paragraphs 43-45 and 48 of FAS 109. However, required disclosures with regard to a reporting entity's GAAP valuation allowance shall be replaced with disclosures relating to the statutory valuation allowance adjustment and the nonadmittance of some portion or all of a reporting entity's DTAs. The financial statements shall include the disclosures required by paragraph 47 of FAS 109 for non-public companies. Paragraphs 22-28 describe the disclosure requirements as modified for the difference between the requirements of FAS 109 and those prescribed by this statement.

22. The components of the net DTA or DTL recognized in a reporting entity's financial statements shall be disclosed as follows:

a. The total of all DTAs (gross, adjusted gross, admitted and nonadmitted) by tax character;

b. The total of all DTLs by tax character;

c. The total DTAs nonadmitted as the result of the application of paragraph 11;

d. The net change during the year in the total DTAs nonadmitted;

e. The amount of each result or component of the calculation, by tax character of paragraphs 11.a., 11.b.i., 11.b.ii., and 11.c., and the ExDTA ACL RBC Ratio, the ExDTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital Ratio, or the Adjusted Gross DTA/Adjusted Capital and Surplus Ratio used in the applicable *Realization Threshold*

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Limitation Table (the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) in paragraph 11.b., as applicable; and

f. The impact of tax-planning strategies on the determination of adjusted gross DTAs and the determination of net admitted DTAs, by percentage and by tax character, and whether the tax-planning strategies include the use of reinsurance-related tax planning strategies.

23. To the extent that DTLs are not recognized for amounts described in paragraph 31 of FAS 109, the following shall be disclosed:

a. A description of the types of temporary differences for which a DTL has not been recognized and the types of events that would cause those temporary differences to become taxable;

b. The cumulative amount of each type of temporary difference;

c. The amount of the unrecognized DTL for temporary differences related to investments in foreign subsidiaries and foreign corporate joint ventures that are essentially permanent in duration if determination of that liability is practicable or a statement that determination is not practicable; and

d. The amount of the DTL for temporary differences other than those in paragraph 23.c. that is not recognized in accordance with the provisions of paragraphs 31 of FAS 109.

24. The significant components of income taxes incurred (i.e., current income tax expense) and the changes in DTAs and DTLs shall be disclosed. Those components would include, for example:

a. Current tax expense or benefit;

b. The change in DTAs and DTLs (exclusive of the effects of other components listed below);

c. Investment tax credits;

d. The benefits of operating loss carryforwards;

e. Adjustments of a DTA or DTL for enacted changes in tax laws or rates or a change in the tax status of the reporting entity; and

f. Adjustments to gross deferred tax assets because of a change in circumstances that causes a change in judgment about the realizability of the related deferred tax asset, and the reason for the adjustment and change in judgment.

25. Additionally, to the extent that the sum of a reporting entity's income taxes incurred and the change in its DTAs and DTLs is different from the result obtained by applying the federal statutory rate to its pretax net income, a reporting entity shall disclose the nature of the significant reconciling items.

26. A reporting entity shall also disclose the following:

a. The amounts, origination dates and expiration dates of operating loss and tax credit carryforwards available for tax purposes;

b. The amount of federal income taxes incurred in the current year and each preceding year, which are available for recoupment in the event of future net losses; and

c. The aggregate amount of deposits admitted under Section 6603 of the Internal Revenue Service Code.

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27. For any federal or foreign income tax loss contingencies as determined in accordance with paragraph 3.a. for which it is reasonably possible that the total liability will significantly increase within 12 months of the reporting date, the reporting entity shall disclose an estimate of the range of the reasonably possible increase or a statement that an estimate of the range cannot be made.

28. If a reporting entity's federal income tax return is consolidated with those of any other entity or entities, the following shall be disclosed:

a. A list of names of the entities with whom the reporting entity's federal income tax return is consolidated for the current year; and

b. The substance of the written agreement, approved by the reporting entity's Board of Directors, which sets forth the manner in which the total combined federal income tax for all entities is allocated to each entity which is a party to the consolidation. (If no written agreement has been executed, explain why such an agreement has not been executed.) Additionally, the disclosure shall include the manner in which the entity has an enforceable right to recoup federal income taxes in the event of future net losses which it may incur or to recoup its net losses carried forward as an offset to future net income subject to federal income taxes.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
None.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None.

Convergence with International Financial Reporting Standards (IFRS):
None.

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP clarification and expose revisions, as detailed below, to reject *ASU 2023-09 Improvements to Income Tax Disclosures* in *SSAP No. 101—Income Taxes*. NAIC staff does recommend that the Working Group remove the disclosure detailed in paragraph 23b as it is no longer considered relevant due to changes in federal tax law.

The disclosure detailed in ASC 740-30-50-2(b) (SSAP No. 101, paragraph 23b) was removed by ASU 2023-09 as it requires disclosure of the cumulative amount of each type of temporary tax difference when a deferred tax liability is not recognized for undistributed foreign earnings. Based on discussion within the ASU, Stakeholders indicated that the changes as a result of the Tax Cuts and Jobs Act reduces the relevance of the existing disclosure of the cumulative temporary differences related to foreign subsidiaries when a deferred tax liability is not recognized. As the rationales detailed within the ASU would also be relevant under statutory accounting, we have recommended that paragraph 23b disclosures be removed.

The disclosure detailed in ASC 740-10-50-15(d) (SSAP No. 101, paragraph 27) was removed by ASU 2023-09 due to a conflict with Chapter 8 of the FASB Concepts Statement 8, however the FASB Concepts Statements have not been adopted within the statutory accounting framework. As this conflict does not exist within statutory accounting, we do not recommend removal of the disclosure detailed in SSAP 101 paragraph 27.

Staff Review Completed by:
NAIC Staff – William Oden, February 2024

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Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to adopt, with modification, *ASU 2023-09 Improvements to Income Tax Disclosures* in *SSAP No. 101—Income Taxes*, as illustrated below.

Spring National Meeting - Proposed Revisions to SSAP No. 101:

Disclosures

23. To the extent that DTLs are not recognized for amounts described in paragraph 31 of FAS 109, the following shall be disclosed:

a. A description of the types of temporary differences for which a DTL has not been recognized and the types of events that would cause those temporary differences to become taxable;

b. ~~The cumulative amount of each type of temporary difference;~~

26. A reporting entity shall also disclose the following:

a. The amounts, origination dates and expiration dates of operating loss and tax credit carryforwards available for tax purposes;

b. The amount of federal income taxes incurred in the current year and each preceding year, which are available for recoupment in the event of future net losses; and

c. The aggregate amount of deposits admitted under Section 6603 of the Internal Revenue Service Code.

d. Income (or loss) from continuing operations before income tax expense (or benefit) disaggregated between domestic and foreign shall.

~~d.~~e. Income tax expense (or benefit) from continuing operations disaggregated by federal (national), state, and foreign. Income taxes on foreign earnings that are imposed by the jurisdiction of domicile shall be included in the amount for that jurisdiction of domicile (that is, the jurisdiction imposing the tax).

f. The amount of income taxes paid (net of refunds received) disaggregated by federal (national), state, and foreign.

~~e.~~g. The amount of income taxes paid (net of refunds received) to each individual jurisdiction in which income taxes paid (net of refunds received) is equal to or greater than 5% of total income taxes paid (net of refunds received)

29. Nothing in this statement is intended to discourage an entity from reporting additional information specific to the disclosures detailed below to further an understanding of the entity and the related disclosures. If not already disclosed in paragraph 24, the reporting entity shall disclose the following:

a. The nature and effect of specific categories of reconciling items, as listed below, and individual jurisdictions that result in a significant difference between the tax rate and the effective tax rate. The objective of this disclosure requirement is for an entity, particularly an entity operating in multiple jurisdictions, to disclose sufficient information to enable users of financial statements to understand the nature and magnitude of factors contributing to the difference between the effective tax rate and the tax rate.

i. State and local income tax, net of federal (national) income tax effect

ii. Foreign tax effects

iii. Effect of changes in tax laws or rates enacted in the current period

iv. Effect of cross-border tax laws

v. Tax credits

vi. Changes in valuation allowances

vii. Nontaxable or nondeductible items

viii. Changes in unrecognized tax benefits.

Relevant Literature

30. This statement adopts, with modification, *ASU 2023-09 Improvements to Income Tax Disclosures*. The statutory modifications include:

a. Did not include public entity only disclosures as statutory accounting does not a the private/public company concept. Additionally, the public entity rate reconciliation was determined to be too onerous to apply to all insurance companies.

~~a.~~b. Did not delete the disclosure detailed in paragraph 27 from this statement as the conceptual conflict between the disclosure and FASB Concepts Statement 8, Chapter 8, does not exist within statutory accounting.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions, as detailed below, to reject ASU 2023-09 Improvements to Income Tax Disclosures in *SSAP No. 101—Income Taxes* and delete the disclosure in SSAP No. 101, paragraph 23.b., as it is no longer considered relevant due to changes in federal tax law.

Summer National Meeting - Proposed Revisions to SSAP No. 101:

Disclosures

23. To the extent that DTLs are not recognized for amounts described in paragraph 31 of FAS 109, the following shall be disclosed:

a. A description of the types of temporary differences for which a DTL has not been recognized and the types of events that would cause those temporary differences to become taxable;

~~b. The cumulative amount of each type of temporary difference;~~

~~c.~~b. The amount of the unrecognized DTL for temporary differences related to investments in foreign subsidiaries and foreign corporate joint ventures that are essentially permanent in duration if determination of that liability is practicable or a statement that determination is not practicable; and

~~d.~~c. The amount of the DTL for temporary differences other than those in paragraph 23.c. that is not recognized in accordance with the provisions of paragraphs 31 of FAS 109.

Relevant Literature

38. This statement rejects *ASU 2023-09, Improvements to Income Tax Disclosures*. The disclosure detailed in paragraph 23.b. was deleted from statutory accounting guidance as the Tax Cuts and Jobs Act made this disclosure effectively irrelevant.

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On November 17, 2024, the Statutory Accounting Principles (E) Working Group adopted the revisions exposed at the Summer National meeting, as shown above, to reject *ASU 2023-09 Improvements to Income Tax Disclosures* in *SSAP No. 101—Income Taxes* and delete the disclosure detailed in SSAP No. 101, paragraph 23.b

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Adoptions/24-11 - ASU 2023-09 Improvements to Income Tax Disclosures.docx

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Clearly Defined Hedging Strategy

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been prepared to update the guidance in *SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees* for a clearly defined hedging strategy (CDHS) to mirror guidance adopted by the Life Actuarial (A) Task Force in 2022, and in effect starting with the 2023 version of the Valuation Manual. The guidance previously included in SSAP No. 108 referred to the CDHS defined in VM-21, and the actuarial guidance has been modified to ensure consistent definitions of a CDHS in both VM-20 and VM-21 and is now captured within VM-01.

The proposed revisions are limited to the definition of a CDHS in paragraph 7 of SSAP No. 108 as well as references in SSAP No. 108 that refer to VM-21 as the location of the definition of a CDHS.

Existing Authoritative Literature:

- ***SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees***

7. As identified in paragraph 2, eligibility for the special accounting provision within this standard is strictly limited to variable annuity contracts and other contracts involving certain guaranteed benefits similar to those offered with variable annuities that are reserved for in accordance with VM-21. This special accounting provision requires the reporting entity to engage in highly effective fair value hedges that follow a Clearly Defined Hedging Strategy, as defined in VM-21, meeting all required provisions of VM-21 allowing the reporting entity to reduce the amount of the Conditional Tail Expectation (CTE) Amount. In order to qualify as a Clearly Defined Hedging Strategy (which may be dynamic, static, or a combination thereof), the strategy must meet the principles outlined in VM-21, be in place (implemented) for at least three months[1], and shall at a minimum, identify:

    a. Specific risks being hedged[2],

    b. Hedge objectives,

    c. Risks not being hedged,

    d. Financial instruments that will be used to hedge the risks,

    e. Hedge trading rules, including permitted tolerances from hedging objectives,

[1] As detailed in VM-21, before a new or revised hedging strategy can be used to reduce the amount of the Conditional Tail Expectation (CTE) otherwise calculated, the hedging strategy should be in place (effectively implemented) for at least three months. As detailed in VM-21, the reporting entity may meet the time requirement by having evaluated the effective implementation of the hedging strategy for at least three months without actually having executed the trades indicated by the hedging strategy (e.g., mock testing or by having effectively implemented the strategy with similar annuity products for at least three months.)

[2] The specific risk being hedged shall include a measure of the hedge coverage (e.g., percentage of interest rate sensitivity being hedged).

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f. Metric(s) used for measuring hedging effectiveness,

g. Criteria that will be used to measure effectiveness,

h. Frequency of measuring hedging effectiveness,

i. Conditions under which hedging will not take place, and

j. The individuals responsible for implementing the hedging strategy.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing and expose revisions to SSAP No. 108 to update the definition of a clearly defined hedging strategy (CDHS) to reflect the revised guidance pursuant to VM-01. (Only references to the CDHS are being revised to VM-01. Other references to VM-21 are product specific to variable annuity contracts and shall be retained in SSAP No. 108.)

Proposed revisions to SSAP No. 108:

6.b.ii Certification by a financial officer of the company (CFO, treasurer, CIO, or designated person with authority over the actual trading of assets and derivatives) that the hedging strategy meets the definition of a Clearly Defined Hedging Strategy within ~~VM-21~~VM-01 and that the Clearly Defined Hedging Strategy is the hedging strategy being used by the company in its actual day-to-day risk mitigation efforts. This provision does not require reporting entities to use a hedging strategy in determining VM-21 reserves, nor does it require entities to use the special accounting provision within this standard. However, it does require reporting entities that use the special accounting provisions within this standard to certify that the hedging strategy within scope of this standard is a Clearly Defined Hedging Strategy and is reflected in the establishment of VM-21 reserves.

7. As identified in paragraph 2, eligibility for the special accounting provision within this standard is strictly limited to variable annuity contracts and other contracts involving certain guaranteed benefits similar to those offered with variable annuities that are reserved for in accordance with VM-21. This special accounting provision requires the reporting entity to engage in highly effective fair value hedges that follow a Clearly Defined Hedging Strategy, as defined in ~~VM-21~~VM-01, meeting all required provisions of VM-21 allowing the reporting entity to reduce the amount of the Conditional Tail Expectation (CTE) Amount. In order to qualify as a Clearly Defined Hedging Strategy (which may be dynamic, static, or a combination thereof), the strategy must meet the principles outlined in VM-21, be in place (implemented) for at least three months[3], and shall at a minimum, identify:

[3] As detailed in VM-21, before a new or revised hedging strategy can be used to reduce the amount of the Conditional Tail Expectation (CTE) otherwise calculated, the hedging strategy should be in place (effectively implemented) for at least three months. As detailed in VM-21, the reporting entity may meet the time requirement by having evaluated the effective implementation of the hedging strategy for at least three months without actually having executed the trades indicated by the hedging strategy (e.g., mock testing or by having effectively implemented the strategy with similar annuity products for at least three months.)

a. The ~~S~~specific risks being hedged[4],

b. The hedging~~Hedge~~ objectives,

c. The material ~~R~~risks that are not ~~being~~ hedged,

d. The f~~F~~inancial instruments ~~that will be~~ used to hedge the risks,

e. The hedging strategy's ~~Hedge~~ trading rules, including permitted tolerances from hedging objectives,

f. The metrics, criteria, and frequency for measuring effectiveness, ~~Metric(s) used for measuring hedging effectiveness,~~

~~g. Criteria that will be used to measure effectiveness,~~

~~Frequency of measuring hedging effectiveness,~~

~~h.~~g. The ~~C~~conditions under which hedging will not take place, and for how long the lack of hedging can persist,

h. The group or area, including whether internal or external, ~~The individuals~~ responsible for implementing the hedging strategy.~~,~~

i. Areas where basis, gap, or assumption risk related to the hedging strategy have been identified, and

~~i.~~j. The circumstances under which hedging strategy will not be effective in hedging the risks.

23.a. Discussion of hedged item, including information on the guarantees sensitive to interest rate risk, along with information on the designated hedging instruments being used to hedge the risk. Discussion of the hedging instruments shall identify whether a hedging instrument is a single instrument or portfolio, as well as information on the hedging strategy (including whether there have been changes in strategy from the prior reporting period, along with detailed information on the changes), and assessment of hedging effectiveness and compliance with the "Clearly Defined Hedging Strategy" of ~~VM-21~~VM-01. Identification shall occur on whether the hedged item is intended to be fully hedged under the hedging strategy, or if the strategy is only focused on a portion of the liability characteristics or a portion of the interest rate sensitivity. Hedging strategies shall be identified as highly effective or not highly effective. If the strategy for a particular hedging relationship excludes a specific component of the gain or loss, or related cash flows, from the assessment of hedge effectiveness, details on the excluded components shall be disclosed.

Staff Review Completed by: Julie Gann, NAIC Staff—May 2024

On August 13, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing as a SAP clarification, and exposed revisions to SSAP No. 108, as shown above, to update the definition of a clearly defined hedging strategy to mirror guidance previously adopted by the Life Actuarial (A) Task Force. This item was exposed until September 27, 2024, to allow for consideration at the 2024 Fall National Meeting.

[4] The specific risk being hedged shall include a measure of the hedge coverage (e.g., percentage of interest rate sensitivity being hedged).

On November 17, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed revisions to SSAP No. 108, as shown above, to update the definition of a clearly defined hedging strategy to mirror guidance previously adopted in 2022 by the Life Actuarial (A) Task Force.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Adoptions/24-17 - SSAP No. 108 - VM-01.docx

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: *Clarification of Accounting Guidance for Recognition of Tax Credits*

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group adopted, as final, agenda item 2022-14 which exposed revisions to *SSAP No. 34—Investment Income Due and Accrued*, *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, *SSAP No. 93—Low-Income Housing Tax Credit Property Investments*, and *SSAP No. 94R—Transferable and Non-Transferable State Tax Credits* to expand and amend statutory guidance to include all tax credit investments regardless of structure and type of state or federal tax credit program, and all state and federal purchased tax credits.

After adoption of agenda item 2022-14, NAIC staff received questions from public accounting firms on the accounting guidance and example journal entries provided in the new guidance. It was noted that the SSAP No. 94R accounting guidance appeared inconsistent with the journal entry examples and the guidance in SSAP No. 93 for recognizing allocated tax credits was confusing when compared to the journal entry examples. Both interested parties and NAIC staff agreed that the journal entries reflect the proper accounting for both the recognition and utilization of tax credits, as such revisions have been drafted to revise the accounting guidance to match the journal entry examples more accurately.

It was also noted that a sentence in SSAP No. 48 was accidentally not updated as part of the New Market Tax Credit project. Updates to this sentence are proposed below.

Existing Authoritative Literature:
SSAP No. 93—Low-Income Housing Tax Credit Property Investments (Superseded 1/1/2025)
SSAP No. 94R—Transferable and Non-Transferable State Tax Credits (Superseded 1/1/2025)

SSAP No. 93—Investments in Tax Credit Structures (Effective 1/1/2025)
SSAP No. 94—State and Federal Tax Credits (Effective 1/1/2025)

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *SSAP No. 93—Investments in Tax Credit Structures, SSAP No. 94—State and Federal Tax Credit*, and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*, to be effective as of January 1, 2025.

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Staff Review Completed by: William Oden – June 2024

Status:
On August 13, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *SSAP No. 93—Investments in Tax Credit Structures*, *SSAP No. 94—State and Federal Tax Credit*, and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*.

Drafting Note: The SSAP guidance shown below includes the revisions adopted in agenda item 2022-14, which are effective 1/1/2025.

Proposed Revisions to SSAP No. 93:

14. Tax credits and other tax benefits, not to include amortization of the investment, shall be reflected as follows:

a. Tax credits shall be recognized in the period that they are allocated to the reporting entity for tax purposes:

i. ~~Federal tax credits that can be utilized in the year allocated shall be reported in the income statement as an offset to federal taxes in accordance with *SSAP No. 101—Income Taxes*. Federal tax credits that cannot be utilized in the year allocated and are carried forward to a future tax year shall be reported as a deferred tax asset (DTA) in accordance with SSAP No. 101.~~If utilized in the same year allocated, federal tax credits shall be recognized and reported as a reduction to federal income tax liabilities and federal income tax expense. If the allocated tax credits are not utilized in the year allocated, they shall be reported as a deferred tax asset (DTA) and change in DTA in accordance with *SSAP No. 101—Income Taxes*.

ii. ~~State tax credits that can be utilized in the year allocated shall be reported in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax reporting year in which the credit is utilized. State tax credits that cannot be utilized in the year allocated and are carried forward to a future tax year shall be reported gross of any related state tax liabilities and reported in the category of other-than-invested assets (not to be reported net).~~If utilized in the same year allocated, state tax credits shall be recognized and reported as a reduction to the related state tax liability and state premium tax or state income tax, whichever is applicable. If the allocated tax credits are not utilized in the year allocated, they shall be reported gross of the related state tax liability in the category of other-than-invested assets (not to be reported net).

iii. ~~Use~~ Utilization of tax credits in settlement of tax liabilities ~~carried forward in a future period~~ shall be reflected ~~as an offset to~~net of the corresponding income or premium tax liability in the ~~tax~~ reporting ~~year~~ period in which the tax credit is utilized.

iv. Tax credits allocated from tax credit investments, as defined within this SSAP, and held by reporting entities meet the definition of assets as specified in SSAP No. 4 and are admitted assets to the extent that they comply with the requirements of this statement. The admissibility of tax credits is subject to SSAP No. 101.

b. Federal tax benefits other than tax credits (e.g., tax benefits from investment depreciation) shall be recognized in the year allocated pursuant to SSAP No. 101. When utilized, the federal tax benefits are recognized as a component of income tax expense.

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c. State tax benefits other than tax credits shall be recognized in the year allocated gross of any related state tax liabilities pursuant to SSAP No. 101. When utilized, the state tax benefits are recognized as a component of taxes, licenses, and fees.

Proposed Revisions to SSAP No. 94R:

9. Tax credits shall be recognized in the period that they are purchased or allocated to the reporting entity for tax purposes:

a. ~~Federal tax credits that can be utilized in the year allocated or purchased shall be reported in the income statement as an offset to federal taxes in accordance with *SSAP No. 101—Income Taxes*.~~ Federal tax credits ~~that cannot be utilized in the year allocated or purchased and are carried forward to a future tax year shall~~are to be recognized and reported as a deferred tax asset (DTA) in accordance with *SSAP No. 101—Income Taxes*~~SSAP No. 101~~.

b. ~~State tax credits that can be utilized in the year allocated or purchased shall be reported in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized.~~ State tax credits ~~that cannot be utilized in the year allocated or purchased and are carried forward to a future tax year shall~~ are to be recognized reported gross of any related state tax liabilities ~~and reported~~ in the category of other-than-invested-assets (not to be reported net).

10. ~~Use~~ Utilization of ~~carried forward~~ tax credits in settlement tax liabilities ~~in a future period~~ shall be reflected ~~as an offset to~~ net of the corresponding income or premium tax liability in the ~~tax~~ reporting ~~year~~ period in which the tax credit is utilized.

Proposed Revisions to SSAP No. 48:

1. This statement establishes statutory accounting principles for investments in any joint ventures, partnerships, and limited liability companies, including investments in certified capital companies (CAPCO) per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)*, whether or not it is considered to be controlled by or affiliated with the reporting entity. Single real estate property investments that are wholly-owned by an LLC that is directly and wholly-owned by the reporting entity, and that meet the criteria established in *SSAP No. 40R—Real Estate Investments*, are excluded from this statement. This statement does not address the accounting for investments in joint ventures, partnerships, and limited liability companies that invest in tax credit programs and are in the scope of *SSAP No. 93—Investments in Tax Credit Structures.* However, investments in joint ventures, partnerships, and limited liability companies which allocate tax credits but ~~certain state Low-Income Housing Tax Credit Property Investments that~~ do not fall within the scope of SSAP No. 93 are covered by the requirements of this statement.

On November 17, 2024, the Statutory Accounting Principles (E) Working Group adopted the exposed revisions to *SSAP No. 93—Investments in Tax Credit Structures*, *SSAP No. 94—State and Federal Tax Credit*, and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* as shown above, as clarifying edits to the previously-adopted tax credit guidance.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: *ASU 2024-02, Codification Improvements—Amendments to Remove References to the Concepts Statements*

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
FASB issued *ASU 2024-02, Codification Improvements—Amendments to Remove References to the Concepts Statements*, which removes references to FASB Concept Statements from the Codification. The main rationale for this amendment is to simplify the Codification by removing Concepts Statements in the guidance and draw a clear distinction between authoritative and nonauthoritative literature. The Board was concerned that references to Concept Statements would result in users incorrectly inferring that the referenced Concept Statements were authoritative.

The FASB Concept Statements are referenced in the *Accounting Policies and Procedures Manual* within the Statutory Hierarchy which notes that FASB Concept Statements as either Level 4 or 5. However, the revisions in ASU 2024-02 are not relevant to this and other references to FASB Concept Statements in the AP&P Manual.

Existing Authoritative Literature:
None

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2024-02, Codification Improvements—Amendments to Remove References to the Concepts Statements* as not applicable to statutory accounting. This guidance is not considered relevant to the existing statutory accounting references to FASB Concept statements.

Staff Review Completed by: William Oden – May 2024

Status:
On August 13, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2024-02, Codification Improvements—Amendments to Remove References to the Concepts Statements* as not applicable to statutory accounting.

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On November 17, 2024, the Statutory Accounting Principles (E) Working Group adopted revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2024-02, Codification Improvements—Amendments to Remove References to the Concepts Statements* as not applicable to statutory accounting.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Adoptions/24-19 - ASU 2024-02, Codification Improvements.docx

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Revisions to the
As of March 2024, Accounting Practices and Procedures Manual

On **December 17, 2024**, the Statutory Accounting Principles (E) Working Group adopted the following revisions to the *As of March 2024 Accounting Practices and Procedures Manual*. Documents associated with these revisions are linked to the reference items in bold text.

Ref #	SSAP/ Appendix	Title	Summary
2024-26EP	SSAP No. 26	*Editorial Update* *SAP Clarification* Effective January 1, 2025	Adopted revisions to the annual audited disclosure for bonds in paragraph 39.e. of *SSAP No. 26—Bonds* to prescribe that the information presented should be by category and subcategory as reported in annual statement schedule D – Part 1, Section 1 (Issuer Credit Obligations) and Section 2 (Asset-Backed Securities). This disclosure is effective in accordance with the Jan. 1, 2025, effective date of the revised bond definition detailed in SSAP No. 26.

https://naiconline.sharepoint.com/teams/frsstatutoryaccounting/national meetings/a. national meeting materials/2024/12-17-2024/adoptions/00 - adoptions 11.17.2024 toc.docx

NAIC Accounting Practices and Procedures Manual
Editorial and Maintenance Update
November 17, 2024

Maintenance updates provide revisions to the *Accounting Practices and Procedures Manual* (Manual) such as editorial corrections, reference changes, and formatting.

SSAP/Appendix	Description/Revision
SSAP No. 26—Bonds	Editorial change to reinstate disclosure language and reporting category provision.

***SSAP No. 26—Bonds*:**

Overview: The disclosure in paragraph 39.e. is an existing disclosure (pre-bond-definition revisions) in SSAP No. 26. However, the pre-bond-definition version of the disclosure included direction for disclosure by Schedule D broad reporting categories, with categories listed in the SSAP. These reporting categories were removed from the adopted revised SSAP No. 26 disclosure effective Jan. 1, 2025. Although this disclosure is satisfied by the completion of Schedule D-1-1 and D-1-2 for statutory accounting purposes, comments have been made that the adopted revised language could require a listing of all bonds in the audited financial statements. As such, editorial revisions have been proposed to reinstate the prior language for "receiving bond treatment" (as adopted, revised *SSAP No. 43—Asset-Backed Securities*, paragraph 44.m., points to this SSAP No. 26 disclosure for ABS items), and to include reference to reporting categories. A listing of the reporting categories is not deemed necessary within the SSAP.

Proposed Edits to SSAP No. 26 (effective Jan. 1, 2025):

> 39.e. For each annual balance sheet presented, the book/adjusted carrying values, fair values, excess of book/carrying value over fair value or fair value over book/adjusted carrying values for each pertinent bond or assets ~~in scope of this statement~~receiving bond treatment, by category and subcategory as reported in annual statement Schedule D – Part 1, Section 1 (Issuer Credit Obligations) and Section 2 (Asset-Backed Securities).

Staff Recommendation:
NAIC staff recommend that the Statutory Accounting Principles (E) Working Group move this agenda item to the active listing, categorized as a SAP clarification, and expose editorial revisions as illustrated within.

On November 17, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing and exposed the above editorial revisions to *SSAP No. 26—Bonds* for a shortened comment period ending December 9, 2024.

On December 17, 2024, the Statutory Accounting Principles (E) Working Group adopted the above exposed revisions effective Jan. 1, 2025, as part of the revised SSAP No. 26 reflecting the bond definition.

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