Statutory Accounting Principles (E) Working Group
Hearing Agenda
February 25, 2025

ROLL CALL

Dale Bruggeman, Chair	Ohio	Steve Mayhew/Kristin Hynes	Michigan
Kevin Clark, Vice Chair	Iowa	Doug Bartlett	New Hampshire
Sheila Travis/Richard Russell	Alabama	Bob Kasinow	New York
Kim Hudson	California	Diana Sherman	Pennsylvania
William Arfanis/Michael Estabrook	Connecticut	Jamie Walker	Texas
Rylynn Brown	Delaware	Doug Stolte/Jennifer Blizzard	Virginia
Cindy Andersen	Illinois	Amy Malm/Levi Olson	Wisconsin
Melissa Gibson/Shantell Taylor	Louisiana		

NAIC Support Staff: Julie Gann, Robin Marcotte, Jake Stultz, Jason Farr, Wil Oden

Note: This meeting will be recorded for subsequent use.

The Statutory Accounting Principles (E) Working Group met in regulator-to-regulator session on February 18, 2025. This regulator-only session was pursuant to the NAIC Open Meetings Policy paragraph 3 (discussion of specific companies, entities or individuals). No actions were taken at this meeting as the discussion related to reinsurance transactions at certain companies.

NOTICE OF EXTENDED EXPOSURE

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2023-23 (Wil)	**Current Expected Credit Losses (CECL)**	**Not Attached**	**Exposure Extension**	**IP – 2**

Summary:
On August 13, 2024, the Working Group exposed a draft issue paper to document pre-CECL GAAP impairment guidance to be maintained for historical purposes. The original comment deadline was November 8, 2024, but was extended to December 16, 2025.

Interested Parties' Comments:
Interested parties agree with the concepts noted in the draft Issue Paper but would like additional time to address some of the descriptions of current GAAP practice versus statutory accounting to ensure that the descriptions are technically correct.

Recommendation:
Upon receipt of the comment letter, on Dec. 19, 2024, the Working Group chair agreed to extend the comment period for this issue paper until May 2, 2025. This comment deadline extension was provided to allow industry more review time subsequent to the 2024 year-end statutory filing timeframe and the Spring National Meeting. No further action is needed at this time.

REVIEW of NON-CONTESTED POSITIONS

The Working Group may individually discuss the following items, or may consider action in a single motion:

1. Ref #2024-16: Repacks and Derivative Instruments
2. Ref #2024-22: ASU 2024-01, Scope Application of Profits Interest and Similar Awards
3. Ref #2024-25: SSAP No. 16 Clarifications

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-16 (Julie)	**Repacks and Derivative Instruments**	**1 – Agenda Item**	**No Comments**	**IP - 19**

Summary:
On December 17, 2024, the Working Group exposed proposed annual statement instructions, to clarify that held debt securities that are sold to an SPV and then reacquired reflecting the addition of derivative or other components shall be reported as a disposal and reacquisition in the investment schedules. With this exposure, the Blanks (E) Working Group will also proceed with exposing a blanks proposal sponsored by the Statutory Accounting Principles (E) Working Group.

Interested Parties' Comments:
Interested parties have no comments on this item.

Recommendation:
NAIC staff recommends that the Working Group adopt the agenda item, which is currently limited to proposed Annual Statement Instructions, and communicate support for the adoption of the related proposal (2024-21BWG) exposed by the Blanks (E) Working Group.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-22 (Wil)	**ASU 2024-01, Scope Application of Profit Interest and Similar Awards**	**2 – Agenda Item**	**No Comments**	**IP - 25**

Summary:
On November 17, 2024, the Working Group moved this item to the active listing and exposed revisions to adopt with modification *ASU 2024-01, Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards* within *SSAP No. 104—Share-Based Payments*.

Interested Parties' Comments:
Interested parties have no comments on this item.

Recommendation:
NAIC staff recommends that the Working Group adopt the revisions, as exposed, which adopt with modification *ASU 2024-01, Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards* within *SSAP No. 104—Share-Based Payments*.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-25 (Jake)	**SSAP No. 16 Clarifications**	**3 – Agenda Item**	**Agree**	**IP - 25**

Summary:
On November 17, 2024, the Working Group moved this item to the active listing, categorized as a SAP clarification, and exposed revisions to *SSAP No. 16—Electronic Data Processing Equipment and Software* to clarify the references to the U.S. GAAP Accounting Standards Codification (ASC).

Interested Parties' Comments:
Interested parties agree with the updated references in this item.

Recommendation:
NAIC staff recommends that the Working Group adopt the revisions, as exposed, to clarify the references to the U.S. GAAP Accounting Standards Codification (ASC).

REVIEW of COMMENTS on EXPOSED ITEMS

The following items are open for discussion and will be considered separately.

1. Ref #2022-14: Tax Credits Project
2. Ref #2024-10: SSAP No. 56 – Book Value and Separate Account
3. Ref #2024-23: Derivative Premium Clarifications
4. Ref #2024-24: Medicare Part D – Prescription Payment Plan
5. Ref #2024-27: Issue Papers in the Statutory Hierarchy
6. Ref #2024-28: Holders of Capital Notes

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2022-14 (Wil)	**Tax Credits Project**	**4 – Issue Paper**	**No Comments**	**IP – 1**

Summary:
On August 13, 2024, the Working Group exposed a draft issue paper to detail the revisions and discussion for the adopted revisions to *SSAP No. 93—Investments in Tax Credit Structures* and *SSAP No. 94—State and Federal Tax Credits*. The original comment deadline was November 8, 2024, but on November 12 was extended to December 16, 2024.

Interested Parties' Comments:
Interested parties have no comments on this item.

(Staff Note: Although no comments were received on the exposure, NAIC staff is proposing minor edits to be considered as part of the adoption.)

Recommendation:
NAIC staff recommends that the Working Group adopt the exposed draft of Issue Paper 170 – Tax Credits Project along with minor edits proposed (shown as tracked changes in the attachment) that reflect the following:

- Revised the title from New Market Tax Credits Project to Tax Credits Project.
- Minor changes to the wording in the first paragraph and added a drafting note regarding the "R" references.
- Paragraphs 31 & 32: Added reference to address the historical actions of the Blanks (E) Working Group to adopt the corresponding blanks change (2024-11BWG), as well as referrals provided to the Capital Adequacy (E) Task Force and the Life-Risk Based Capital (E) Working Group.
- Paragraph 34: Added a response to inquiries received on CAPCOs and yield guaranties in October.
- Paragraph 35-36: Added to reference the adoption date of agenda item 2024-18 and to document the receipt of interested parties' comment letter on the issue paper.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-10 (Julie)	**SSAP No. 56 – Book Value Separate Accounts**	**5 – Agenda item**	**Comments Received**	**IP – 17**

Summary:
On December 17, 2024, the Working Group exposed updated revisions to *SSAP No. 56—Separate Accounts*, for a comment period ending January 31, 2025. The revisions from the prior exposure are summarized as follows:

- Paragraph 18b: Revisions to incorporate some ACLI comments to clarify that separate account contracts similar to contracts found in the general account, but do not directly pass all investment experience of the underlying assets to the policyholder, may be recorded as if the assets were held in the general account. The revisions delete the reference to the general account providing contract benefits not directly tied to performance of the underlying assets, with updated language that the general account may serve as an overall backstop or provide an implied guarantee. The revisions do not reflect the ACLI comments to remove the example contracts, and the examples have been expanded to include BOLI contracts as that was identified by the ACLI as another common contract reported at book value in the separate account.

- Paragraph 22: Revisions add guidance that other types of asset transfers shall be recorded at fair value. Although the ACLI did not agree with codifying the measurement approach guidance for these transfers and referred to existing separate account memorandums of understanding filed with the domestic regulator, this was supported in accordance with the statutory accounting consistency concept. By codifying a set measurement method, then deviations utilized and approved by the domiciliary regulator shall be detailed in Note 1. With this addition, comments are requested on whether additional guidance, particularly with the treatment of IMR for these transfers, shall be incorporated. The impact to IMR for these items was also noted to be included as a discussion topic at the IMR ad hoc group.

Interested Parties' Comments:
Interested parties continue to support clarification of statutory accounting guidance for Book Value Guaranteed Separate Accounts. ACLI is very appreciative of the on-going dialogue with SAPWG and the IMR Ad Hoc Working Group and stands ready to continue working with the NAIC on this initiative.

ACLI would like to provide specific comments regarding existing SSAP 56 guidance and proposed changes to SSAP 56

The ACLI is in support of much of the exposed guidance updates. Particularly, we continue support for the proposed guidance for transfers between General Account and Separate Account (paragraphs 19 – 22). The ACLI previously provided a detailed presentation entitled "ACLI Derivative IMR Solution Proposal" ("ACLI Solution," included as Appendix I) to the IMR Ad Hoc Working Group. Discussions of the ACLI solution at the NAIC Ad Hoc IMR WG were the impetus for this exposure. The exposed guidance updates to SSAP 56 largely reflect the findings from the ACLI Solution presentation and, should it be beneficial to regulators, the ACLI would appreciate the opportunity to present to the full SAPWG membership and any additional interested regulators.

While in support of much of the exposed guidance updates, the ACLI would like to further discuss some of the proposed guidance for Book Value Guaranteed Separate Accounts:

Paragraph 22 requires that all other transfers of assets between Separate Account and General Account, excluding those assets sales for cash transfers already described in Paragraphs 19 through 21, be recorded at fair value. In order to avoid any potential for diversity in practice, we believe guidance should be added clarify that IMR should be utilized for these transactions in a similar way to how IMR is utilized in the transfer for cash transactions. The ACLI recommends at minimum the addition of the following phrase (changes shaded): "Asset transfers that do not reflect sales for cash between the general account and separate account are subject to domiciliary state approval and shall be recorded at fair value with gains and losses offset to IMR similar to asset sales for cash guidelines as detailed in Paragraphs 20 & 21…". Should it be decided that more detailed instruction be required, the ACLI would like to request some additional time to build out a more detailed proposal.

Paragraph 24 identifies the in-scope Separate Account population as "…separate accounts that would qualify for separate account classification under U.S. GAAP…". We do not believe the direct reference to US GAAP regulation within the SSAP to be appropriate, especially as not all insurers perform U.S. GAAP filings and would not be sufficiently expert in U.S. GAAP Separate Account guidance. Language surrounding guaranteed separate accounts is already included in Paragraph 18. Rather than creating separate language to identify non-guaranteed separate accounts which do not require AVR, direct reference to a "population excluding that population identified in Paragraph 18 would both provide clarity without reference to U.S. GAAP guidance and provides inclusive language ensuring the entire population of separate accounts to fall in either bucket rather than risk any population that may not fall in either the U.S. GAAP standard or the Paragraph 18 standard.

Paragraphs 34.C.iii. and 39.F. appear to be seeking additional disclosure (within General Account and Separate Account filings, respectively) of the assets supporting book value separate accounts, as specific reference is made to product types identified as book value in Paragraph 18 (PRT and RILA), We believe this additional disclosure to be redundant to the Book Value column reporting in the Separate Account Asset Page, providing no additional detail or value to what has already been reported. While the ACLI recognizes that there is no prohibition of domicile approval of non-guaranteed book value separate account with Statutory guidance surrounding Plan/Memorandum of Operations process, we feel that proposed guidance within SSAP 56 Paragraph 25 eliminates that probability: "*Assets supporting separate account contracts where the insurer bears the risk of investment performance, which shall include all book value separate accounts…"*. Due to the Paragraph 25 requirement that all book value separate accounts shall be in support of guaranteed separate accounts where the insurer bears the risk of investment performance, it is not probable that the Book Value column breakout within the Separate Account Assets page filing will include any population other than the Guaranteed population and thus cannot not diverge from the disclosures proposed in Paragraphs 34.C.iii. and 39.F. The ACLI requests that these disclosure requirements be removed from SSAP 56.

<u>*Recommendation:*</u>
NAIC staff recommends that the Working Group adopt the exposed revisions to *SSAP No. 56—Separate Accounts*, with additional revisions as described below. If preferred, the Working Group could elect to expose the item for an additional comment period. The new revisions from the exposure reflect the proposed edits from interested parties for paragraph 22 and paragraph 24. The new edits also propose the inclusion of a January 1, 2026 effective date to allow reporting entities to update separate account "plans of operation" with their domiciliary state as necessary before the revisions are effective.

The revisions do not include the deletion of paragraph 34.c.iii. and 39.f as requested by interested parties. These disclosures require identification of the separate account contracts where there is an inherent or ultimate guarantee to the general account, the identification of any risk charges that have been provided to the general account for this non-specific risk, and to affirm the inclusion of these separate account products within asset adequacy testing. This disclosure goes beyond the existing book-value measurement disclosure and intends to provide regulators with needed information as to the obligations of the general account for separate account products and to confirm inclusion in asset adequacy testing. (These paragraphs are included within the hearing agenda below – shown clean – for quick review. The reference in paragraph 34.c.iii for "asset-liability testing" was replaced to reflect "asset adequacy testing".)

Edits proposed for adoption:

1) **<u>Paragraph 22 – Incorporate revisions as recommended by interested parties</u>.** These revisions direct IMR determination in accordance with paragraphs 20-21. (New guidance tracked.)

    22. Asset transfers that do not reflect sales for cash between the general account and separate account are subject to domiciliary state approval and shall be recorded at fair value <u>with gains and losses offset to IMR similar to asset sales for cash guidelines as detailed in paragraphs 20 & 21</u>. Any transfer that does not represent an asset sale for cash shall be specifically disclosed in both the general account and separate account as detailed in paragraph 34.e. This shall include, but not be limited to, the following transfers:

        a. Asset to asset swaps

        b. Contributions of general account assets to support separate account deficiencies

        c. Dividends of assets from the separate account to the general account.

2) **<u>Paragraph 24 – Incorporate revisions as recommended by interested parties</u>.** These revisions revise the scope of paragraph 24 to be all separate account contracts except those captured in paragraph 18.

    Although interested parties provided comments opposing guidance based on a comparison to US GAAP, and NAIC staff has incorporated edits to refer to paragraph 18 as suggested, it should be noted that SSAP No. 56 already requires all entities to assess whether their separate account product would have qualified as a separate account product under U.S. GAAP even if they do not file U.S. GAAP financials. This is a requirement in paragraph 39 of the current SSAP No. 56 (paragraph 43 of the proposed revised SSAP No. 56). Although industry raised similar comments when it was considered, the Working Group supported this disclosure in 2009 as part of the initiative to better identify products that are approved for statutory accounting separate account classification that are outside the parameters from what has historically been considered a separate account product in line with U.S. GAAP.

    The additional new edits are limited to paragraph 24 and are shown shaded. However, the full section with the exposed tracked changes has been included. The section is also shown clean for ease of review.

Separate Account AVR and IMR Reporting

23. An AVR is ~~generally~~ required for separate accounts when the ~~insurer~~reporting entity, rather than the policyholder/contractholder, suffers the loss in the event of asset default or fair value loss. ~~An AVR is required unless:~~

~~a. The asset default or fair value risk is borne directly by the policyholders; or~~

~~b. The regulatory authority for such separate accounts already explicitly provides for a reserve for asset default risk, where such reserves are essentially equivalent to the AVR.~~

24. Assets supporting ~~traditional variable annuities and variable life insurance~~separate accounts, excluding products captured in paragraph 18, ~~that would qualify for separate account classification under U.S. GAAP~~ ~~generally~~ do not require an AVR because the policyholders/contractholders bear the risk of change in the value of the assets. However, for those contracts an AVR is required for that portion of the assets representing seed money (including accumulated earnings on seed money) from the general account. ~~the insurer's equity interest in the investments of the separate account (e.g., seed money).~~

25. Assets supporting separate account contracts where the insurer bears the risk of investment performance, which shall include all book value separate accounts, ~~typical modified guaranteed contracts, market value adjusted contracts, and contracts with book value guarantees similar to contracts generally found in the general account do~~ require an AVR because the insurer is responsible for credit related asset or fair value loss.

26. "Book Value" separate accounts, pursuant to paragraph 18, ~~Certain separate accounts are also~~are required to maintain an Interest Maintenance Reserve (IMR). Separate accounts with assets reported at fair value are not required to maintain an IMR. ~~The IMR requirements for investments held in separate accounts are applied on an account by account basis.~~ Once~~If~~ an IMR is required for a separate account, all of the investments in that separate account are subject to the requirement. If an IMR is not required for a separate account, none of the investments in that separate account are subject to the requirement.

~~27.~~ As detailed in the Annual Statement Instructions, ~~An IMR is required for separate accounts with assets recorded at book value, but is not required for separate accounts with assets recorded at fair value. For example, separate accounts for traditional variable annuities or variable life insurance do not require an IMR because assets and liabilities are valued at fair value.~~

~~28.~~27. ~~If an~~ Separate account IMR ~~is required for investments held by separate accounts, it~~ is kept separate from the general account IMR and accounted for in the separate accounts statement.

~~29.~~28. The AVR and IMR shall be calculated and reported in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve* and the ~~NAIC~~ Annual Statement Instructions ~~for Life, Accident and Health Insurance Companies~~.

Shown Clean. The new edits to paragraph 24 are shaded. (The disclosures with proposed edits from the exposure are also included.)

Separate Account AVR and IMR Reporting

23. An AVR is required for separate accounts when the reporting entity, rather than the policyholder/contractholder, suffers the loss in the event of asset default or fair value loss.

24. Assets supporting separate accounts, excluding products captured in paragraph 18, do not require an AVR because the policyholders/contractholders bear the risk of change in the value of the assets. However, for those contracts an AVR is required for that portion of the assets representing seed money (including accumulated earnings on seed money) from the general account.

25. Assets supporting separate account contracts where the insurer bears the risk of investment performance, which shall include all book value separate accounts, require an AVR because the insurer is responsible for credit related asset or fair value loss.

26. "Book Value" separate accounts, pursuant to paragraph 18, are required to maintain an Interest Maintenance Reserve (IMR). Separate accounts with assets reported at fair value are not required to maintain an IMR. Once an IMR is required for a separate account, all of the investments in that separate account are subject to the requirement. If an IMR is not required for a separate account, none of the investments in that separate account are subject to the requirement.

27. As detailed in the Annual Statement Instructions, Separate account IMR is kept separate from the general account IMR and accounted for in the separate accounts statement.

28. The AVR and IMR shall be calculated and reported in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve* and the Annual Statement Instructions.

Disclosures (Paragraphs 29-33 not duplicated.) Paragraph 34ciii was new in the exposure. The staff recommendation does not propose changes although industry commented to delete.

34. The general account financial statement shall include detailed information on the reporting entity's separate account activity. These disclosures shall include:

   a. A narrative of the general nature of the reporting entity's separate account business.

   b. Identification of the separate account assets that are legally insulated from the general account claims.

   c. Identification of the separate account products that have guarantees backed by the general account. This shall include:

      i. Amount of risk charges paid by the separate account to the general account for the past five (5) years1 as compensation for the risk taken by the general account; and

      ii. Amount paid by the general account due to separate account guarantees during the past five (5) years.

      iii. Separate account contracts where the general account provides an inherent or ultimate guarantee, such as with pension risk transfer (PRT) or registered index-linked annuity (RILA) products. These products often do not have stated yield or death benefit guarantees, but rather the general account serves as a final backstop if the separate account assets are insufficient to support the product obligations. This disclosure shall identify whether risk charges have been provided to the general account and affirm the inclusion of these separate account products within asset adequacy testing.

(Paragraphs 35-38 not duplicated.) Paragraph 39f was new in the exposure. The staff recommendation does not propose changes although industry commented to delete.

39. The Separate Account Annual Statement Blank shall include detailed information on the characteristics of the separate account assets, specifically categorizing separate account assets in accordance with the following characteristics:

[1] Reporting entities are permitted to prospectively 'build' the five-year disclosure. Thus, upon the first year of application of the disclosure requirements, reporting entities should illustrate one year of the disclosure requirement. In the second year, the reporting entity would disclose two years, and so forth until the disclosure includes five years of disclosures.

a. Identification of separate account assets that are legally insulated from the general account and those which are not legally insulated.

b. Aggregation of separate account assets from products registered with the SEC and separate account assets from products excluded from registration. In addition to the overall aggregation, this disclosure shall specifically identify separate account assets from private placement variable annuities (PPVA) and private placement life insurance (PPLI). The disclosures in this paragraph (36.b.) were effective December 31, 2018.

c. Amount of separate account assets that represent seed money, other fees and expenses due to the general account, and additional required surplus amounts.2 This disclosure shall include the amount of seed money and other fees and expenses currently included in the separate account, as well as the amount of seed money received and repaid to the general account during the current year. This disclosure shall also include information on insulation (if applicable)3, the time duration for which seed money and other fees and expenses due the general account are retained in the separate account, and information on how whether seed money is invested pursuant to general account directives or in accordance with stated policies and procedures.

d. Identification of the separate account assets in which the investment directive is not determined by a contractholder. (In most instances, having multiple investment choices at the option of a contractholder would be considered a situation in which the investment directive is determined by a contractholder. This is not true for situations in which the asset is invested in a manner that mirrors the investment directives of the general account.) Situations in which the investment directive is not determined by the contractholder (and situations in which the reporting entity is the contractholder) shall include disclosure regarding whether the investments of the respective separate account assets, if included within the general account investments, would have resulted with the reporting entity exceeding any investment limitations imposed on the general account.

e. Identification of the separate account assets in which less than 100% of investment proceeds are attributed to a contractholder. This shall include identification of the separate account investment income attributed to the reporting entity during the reporting period and whether such income was transferred to the general account or reinvested within the separate account. Instances in which such income is reinvested within the separate account shall include disclosure on whether the subsequent investments, if categorized with investments in the general account, would have exceeded investment limitations imposed on the general account.

f. Identification of the assets supporting separate account contracts where the general account provides an inherent or ultimate guarantee, such as with pension risk transfer (PRT) or registered index-linked annuity (RILA) products. These products often do not have stated yield or death benefit guarantees, but the general account serves as a final backstop if the separate account assets are insufficient to support the product obligations or by the general account providing an inherent guarantee, although a distinct performance guarantee is not specified (such as a minimum crediting rate, death benefit, etc.).

<u>Effective Date and Transition</u>

47. This statement is effective for years beginning January 1, 2001. Contracts with assets held in a Separate Account that were issued in accordance with applicable state laws and regulations and issued prior

[2] Additional Required Surplus Amounts is defined as additional or permanent surplus that is required to be retained in the separate account in accordance with state law or regulations. These amounts should not include reinvested separate account investment proceeds that have not been allocated to separate account contract holders.

[3] As seed money is considered a temporary transfer of funds, it is generally not considered insulated.

to that effective date, for which assets and liabilities have been recorded using a consistent basis since issue, i.e., both assets and liabilities are recorded either as if in the general account ("book value") or as at fair value (current interest rates based on market rates shall be used for liabilities when assets are recorded at fair value), shall continue to be recorded using such basis until such time as the applicable contract terms or provisions are substantially changed, such as by a contract amendment modifying interest rate or withdrawal provisions. State laws and regulations shall be understood to include anything considered authoritative by the domiciliary state under the individual state's statutory authority and due process procedures. Changes that do not require change in the basis of recording would include: address changes, continued deposits, and other non-substantive changes such as these. For example, additional funds received after January 1, 2001 under contracts issued prior to January 1, 2001 may continue to be recorded using the basis in effect prior to January 1, 2001 until such time as a triggering change is made. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors.*

48. Disclosure revisions adopted in September 2009 to paragraphs 30-39 shall initially be reported within the 2010 annual financial statements, with annual reporting thereafter.

49. Revisions adopted (add month) 2025 in agenda item 2024-10, that clarifies the measurement of separate account assets, particularly for "book-value separate accounts" and that prescribes the treatment for transfers between the general account and separate account with IMR and AVR recognition are effective January 1, 2026, with early adoption permitted. The January 1, 2026, effective date intends to allow reporting entities to modify their separate account product "plans/memorandums of operation" with the state of domicile as necessary to comply with this revised statement. After January 1, 2026, reporting entities are required to have an approved permitted or prescribed practice to utilize a book-value measurement method or a different approach for transfers and recognition of IMR/AVR outside of what is detailed within this statement.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-23 (Wil)	**Derivative Premium Clarification**	**6 – Agenda item**	**Comments Received**	**IP – 25**

<u>*Summary:*</u>

On August 13, 2024, the Working Group exposed revisions *SSAP No. 86—Derivatives* to provide clarifications on two issues: the language surrounding financing premiums and the calculation of realized losses in relation to derivative premium. Issue 1, NAIC staff noted during internal reviews of SSAP No. 86 and the Annual Statement Instructions that the terminology used for derivative financing premiums was inconsistent and that the guidance for derivative financing premiums could be clarified. Issue 2, as part of the ongoing Interest Maintenance Reserve (IMR) Ad Hoc Group meetings NAIC staff learned that there is some confusion within industry regarding whether statutory accounting guidance allows derivative premium costs to be captured in the calculation of realized losses for the derivative transaction. NAIC staff noted that within SSAP No. 86 there are several sections which provide derivative specific accounting guidance, and within these sections the guidance is clear that companies are to amortize derivative premiums over the life of the derivative contract. With amortization of the derivative premium, the derivative premium costs would not be a component in determining realized losses at expiration. As noted within the Definitions section of SSAP No. 86, derivative premiums represent the cost to acquire or write a derivative contract and is not an "underlying" in a derivative contract. As SSAP No. 86 only allows for the change in value attributable to the derivative underlying to be capitalized to IMR as a realized loss and as derivative premium costs are NOT a component of the derivative underlying, the guidance is clear that derivative premium costs should not be included in losses capitalized into IMR. To ensure this is abundantly clear, revisions have been recommended to both the "Definitions" and "Derivative Premium" sections to add language which specifically states that derivative premium costs cannot be capitalized into IMR.

Interested Parties' Comments:
After discussion with NAIC staff, interested parties suggest that the Ref #2024-23: Derivative Premium clarification be captured in the discussion of Ref #2024-15: ALM Derivatives.

Recommendation:
NAIC staff recommends that the Working Group adopt the exposed revisions to SSAP No. 86 related to financing premium (Issue 1). NAIC staff also recommend that the previously exposed revisions regarding clarifications on the calculation and recognition of realized losses from derivative premium be combined with agenda item 2024-15. Based on discussions with interested parties, there are several complicating factors when trying to clarify this calculation and it was also noted that the main concern on the inclusion of derivative premium costs in the calculation of realized losses was that it could be capitalized into IMR and deferred.

Updated Proposed Edits to SSAP No. 86 – The following edits proposed for adoption are unchanged from the 2024 Fall National Meeting exposure, however edits from the 2024 Fall National Meeting exposure concerning the calculation of realized losses in relation to derivative premium have been removed:

6. "Derivative Premium" is the cost to acquire or write a derivative contract. Derivative premium is not an "underlying" in a derivative contract and is not impacted by changes in an underlying interest of the derivative agreement. A derivative with contract terms that finance the derivative premium (financing premium), so that the ~~cost is~~premiums are paid or received throughout the derivative term or at derivative maturity, does not result with an "embedded derivative" which is addressed in paragraph 17. For the purposes of this statement, unpaid or deferred premiums are considered synonymous with financing premium.

Derivative Premium

19. Derivative premium is the amount paid (acquired derivative) or received (written derivative) to enter into a derivative contract. At inception, the premium generally represents the fair value of the derivative but does not represent an underlying in the derivative contract. Derivative premium that is not paid or received at inception of the derivative contract represents financing premium and shall be recorded as a liability or receivable for the reporting entity. Derivatives with premiums not remitted at acquisition are considered "financed derivatives." Financed derivatives shall be reported in accordance with the following provisions:

a. At acquisition and subsequently, the gross reported fair value of the derivative shall exclude the impact of financing premiums. Only market changes in the actual fair value of the derivative shall be reflected as unrealized gains or losses. Even if the derivative premium is fully financed, a derivative contract asset/liability must be recorded.

b. At acquisition and subsequently, financing premiums payable (acquired derivative) and financing premiums receivable (written derivatives) shall be separately reported as "payable for securities" and "receivables for securities."

24. For those derivatives which qualify for hedge accounting, the change in the carrying value or cash flow of the derivative shall be recorded consistently with how the changes in the carrying value or cash flow of the hedged asset, liability, firm commitment or forecasted transaction are recorded. Upon termination of a derivative that qualified for hedge accounting, the gain or loss shall adjust the basis of the hedged item and be recognized in income in a manner that is consistent with the hedged item (alternatively, if the item being hedged is subject to Interest Maintenance Reserve (IMR), the gain or loss on the hedging derivative may be realized and shall be subject to IMR upon termination.) Entities who choose the alternative method shall apply it consistently thereafter.

63.a.v. Identification of whether the reporting entity has derivative contracts with financing premiums. (For purposes of this term, this includes scenarios in which the premium cost is paid/received at the end of the derivative contract or throughout the derivative contract.);

63.h.i. Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums excluding the impact of ~~the deferred or~~ financing premiums.

63.h.ii. For each derivative contract with financing premiums:

(a) *Whether premium cost is paid/received throughout the contract, or at derivative maturity;*
(b) *Next premium cost payment date;*
(c) *Total premium cost;*
(d) *Premium cost paid/received in prior years;*
(e) *Current year premium cost paid/received;*
(f) *Future unpaid/unreceived premium cost;*

Footnote [3] Pursuant to paragraph 19, the gross reported value of a derivative and the determination of unrealized gains or losses shall exclude the impact of financing premiums. Financing ~~P~~premiums payable or receivable from the acquisition or writing of a derivative shall not be reflected in the gross reporting of derivatives or in determining the fair value change in a derivative.

Proposed Edits to Annual Statement Instructions:

NOTE 8.A.(8) Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums, excluding the impact of ~~the deferred or~~ financing premiums.

Illustration:

THIS EXACT FORMAT MUST BE USED IN THE PREPARATION OF THIS NOTE FOR THE TABLES BELOW. REPORTING ENTITIES ARE NOT PRECLUDED FROM PROVIDING CLARIFYING DISCLOSURE BEFORE OR AFTER THIS ILLUSTRATION.

A. Derivatives under *SSAP No. 86—Derivatives*

(8) a.

	Fiscal Year	Derivative Premium Payments Due
1.	2025	$ ....
2.	2026	....
3.	2027	....
4.	2028	....
5.	Thereafter	
6.	Total ~~Future Settled~~Financing Premiums (Sum of 1 through 5)	$

b.

	Undiscounted Future Premium Commitments	Derivative Fair Value with Premium	Derivative Fair Value Excluding Impact of ~~Future~~

			Commitments (Reported on DB)	~~Settled~~ Financing Premiums
1.	Prior Year	$	$	$ ....
2.	Current Year	$	$	$ ....

SCHEDULE DB – PART A – SECTION 1

Column 30 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~ financing premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 30 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 31 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~ financing premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premiums owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

SCHEDULE DB – PART A – SECTION 2

Column 29 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~financing premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 29 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 30 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~financing premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premiums owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

SCHEDULE DB – PART B – SECTION 1

Column 28 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~financing premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 28 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 29 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~financing premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premiums owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

SCHEDULE DB – PART B – SECTION 2

Column 24 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~financing premiums. For example, if the fair value of the derivative reported in column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in column 30 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 25 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~ financing premiums. For example, if the valuation increase/valuation decrease reported in column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premium owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-24 (Robin)	**Medicare Part D – Prescription Payment Plan**	**7- Agenda Item 8 – INT 24-02**	**Comments Received**	**IP – 25 AHIP/BCBSA – 29-49**

Summary:
On November 17, 2024, the Statutory Accounting Principles (E) Working Group exposed tentative *Interpretation (INT) 24-02: Medicare Part D Prescription Payment Plans* as well as minor edits to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*. The Working Group directed notice of the exposures to the Health Insurance (B) Committee and Health Risk-Based Capital (E) Working Group. In addition, NAIC staff were directed to coordinate on the annual statement blanks proposals and to develop disclosures for future discussion.

The Inflation Reduction Act of 2022 introduced changes to Medicare Part D, which is the voluntary outpatient prescription drug program (Part D), including a new program to offer Part D enrollees the option to their out-of-pocket Part D prescription drug costs through monthly payments over the course of the plan year instead of at the pharmacy counter. This program, known as the Medicare Prescription Payment Plan (MPPP), is effective on January 1, 2025. INT 24-02 was developed with input from health industry representatives and provides statutory accounting and reporting guidance for aspects of MPPP. Key components of the MPPP guidance include the following:

- Allows admitted asset treatment for receivables from MPPP participants which are less than 90 days overdue. with reporting on the on the Health care receivables asset line.
- MPPP recoverables from participants which are more than 90 days overdue based on program billing requirements are nonadmitted.
- MPPP recoverables are also subject to impairment analysis.
- Uncollectible receivables from MPPP participants which are written off as are reported as a Medicare prescription claims expense.

Interested Parties Comments:
Interested parties support the comment letter submitted by AHIP and BCBSA.

Blue Cross Blue Shield Association and AHIP Comments:
AHIP and the Blue Cross and Blue Shield Association (BCBSA) (jointly, the Trades) are pleased to respond to the Statutory Accounting Principles (E) Working Group's (SAPWG) proposed exposure 2024-24 regarding the Medicare Prescription Payment Plan (MPPP) ("the exposure").

The Trades (1) appreciate SAPWG's on-going engagement on the exposure, (2) support the proposed conclusions in INT 24-02, and (3) believe that INT 24-02, if adopted by SAPWG, will be useful in enhancing consistency and providing meaningful interpretive guidance to Medicare prescription drug plan sponsors (Part D plan sponsors) and state insurance regulators alike.

In an earlier issue paper, the Trades brought forward certain statutory accounting-related issues about MPPP to SAPWG's attention:

- Since MPPP is new, it is not currently mentioned in the NAIC's Accounting Practices and Procedures Manual ("Manual"); thus, there is no current statutory accounting guidance to indicate whether recoverables from Part D plan enrollees who elect to participate in MPPP (MPPP participants) are admitted assets in the statutory financial statements of Part D plan sponsors.

- As described in the Trade's issue paper, recoverables from MPPP participants are distinctly different in their nature from other health care receivables for which guidance currently exists in the Manual; additional guidance should be developed for the Manual to clarify how impairments of recoverables from MPPP participants should be reported, i.e., to what expense category.

The above-referenced exposure includes a proposed new Interpretation (INT 24-02) of SAPWG, which, if adopted, would address the above issues by providing the following guidance:

- Current MPPP recoverables, meaning those that are less than and up to 90 days overdue, are admitted assets to the extent that they comply with the guidance in this interpretation. Repayment by MPPP participants represents a probable future economic benefit to the Part D plan sponsor resulting from past transactions or events (i.e., paying the MPPP participants' out-of-pocket costs to the pharmacy). MPPP recoverables are also subject to impairment analysis.

- Uncollected MPPP recoverables more than 90 days overdue are nonadmitted. The due date for aging of the MPPP recoverables shall follow the program billing guidelines.

- Uncollected MPPP recoverables from MPPP participants are subject to impairment analysis which shall be assessed using the evaluation guidelines in SSAP No. 5— *Liabilities, Contingencies, and Impairment of Assets*. However, when impairments for uncollectible MPPP recoverables are recorded, the expense for the impairment shall be reflected in as incurred Medicare Part D prescription drug claims in the statutory income statement.

The Trades concur with those conclusions expressed in proposed INT 24-02. The Trades have some suggestions to clarify wording in the document.

- Many of the Trades' proposed revisions to the text are self-explanatory or intended to enhance the consistency of terminology throughout the document. Please refer to the Trades' suggested mark-ups in the attached document.

- Where the Trades believe suggested text revisions may not be self-explanatory or warrant more attention, the Trades have flagged that language via text that is highlighted in yellow in the attached document and provided a brief explanation below.

Finally, the Trades note that SAPWG also exposed changes to INT 05-05, for which the Trades have no comments.

INT 24-02T: Medicare Prescription Payment Plan

As a general comment, the Trades have suggested changes to some of the terminology in the proposed INT 24-02 to more closely track usage in CMS rules. That is not because CMS rules are authoritative as regards statutory accounting used by state insurance regulators, rather it simply recognizes that Part D plan sponsors and regulators alike may refer to CMS published materials to understand the context of MPPP, and to the extent the terminology in INT 24-02 tracks CMS terminology, it would facilitate that process. For example, in the issue paper that the Trades submitted to SAPWG last Fall, the term "MP3" was used; in this letter and in our comments on the proposed INT 24-02, we have changed that to MPPP to more clearly track the context as described in CMS' rules and published materials.

- ***Use of "program" or "plan" terminology:*** In a sense, either term could apply to Medicare as a whole, to Part D as a part of Medicare, or to MPPP as a part of Part D. The Trades believe it would be helpful to adhere to specific terms that are unique to each to make the proposed guidance as clear as possible. In the attached mark-up of INT 24-02, the Trades have suggested to use "Medicare" when referring to Medicare as a whole; to use "Part D" when referring to the Prescription Drug component within Medicare; and to use "MPPP" when referring to the new feature of Part D that is the subject of INT 24-02, i.e., the Medicare Prescription Payment Plan. Where the word "plan" applies to "Medicare prescription drug plans," or to "Medicare Advantage plans", "Part D plan sponsors," or "plan year," those terms are spelled out without use of a shortened reference such as "plan." Note that only a few instances where such revisions were made in the mark-up document are highlighted in yellow (to provide examples), but the Trades suggest that corresponding changes be made throughout the document where the respective terms appear whether highlighted or not.

- ***Use of "member" or "enrollee" terminology:*** Likewise, the use of terms such as "member" or "enrollee" can be interpreted to be someone who has coverage with a Part D plan sponsor, or more specifically be interpreted to be those with such coverage and who also have elected to take advantage of MPPP within Part D. In the attached mark-up of INT 24-02, the Trades suggest using "Part D Enrollee" to refer to an individual who has coverage with a Part D plan sponsor, and "MPPP participant" to apply more specifically to those Part D plan members who have elected to participate in the MPPP program in order to have their out-of-pocket payments apportioned over the remaining months of the plan year as per the pertinent provisions of MPPP. Note that only a few instances where such revisions were made in the mark-up document are highlighted in yellow (to provide examples), but the Trades suggest that corresponding changes be made throughout the document where the respective terms appear whether highlighted or not.

- ***Clarifying Paragraph:*** In paragraph 10 of the mark-up of INT 24-02, the Trades have added a paragraph to provide a conclusion to the section that refers to various CMS rules that prohibit or limit many of the common methods Part D plan sponsors might otherwise use to mitigate losses from uncollectible MPPP balances. That conclusion statement is necessary to clarify that MPPP presents an underwriting risk to Part D plan sponsors which cannot be addressed through administrative means, rather through underwriting activities. This is an important point in considering where MPPP-related impairment losses should be reported for statutory accounting – to bad debt (administrative expense) or to claims expense.

- ***Medical Loss Ratio.*** In the section on "Medical Loss Ratio", clarification is provided to recognize that CMS guidance does not dictate statutory accounting guidance promulgated by the NAIC and its member state insurance regulators. The mark-up also clarifies that it is losses (not outstanding balances) related to impairments of MPPP-related balances that are considered by CMS as administrative expenses and excluded from the MLR. The mark-up also clarifies that it is the additional premium revenue that is attributable to the estimates of impairments of recoverables from MPPP participants (not the recoverable balance) included in premium bids by Part D plan sponsors that is included in the MLR denominator.

<u>SAPWG Maintenance Agenda Submission Form, Form A</u>

The Trades understanding is that the Form A serves to facilitate discussion at SAPWG, but it is the proposed INT 24-02 that, if adopted by SAPWG, will be the authoritative interpretive guidance on statutory accounting for MPPP. Therefore, the Trades do not have formal comments on the Form A to submit to SAPWG. That said, the Trades note the following with respect to the Form A.

- The Form A describes CMS' requirements as to how Part D plan sponsors should address MPPP-related losses in their MLR filings with CMS but does not mention the proposed statutory accounting treatment which is the purpose of INT 24-02 – to provide guidance as to the admissibility of MPPP-related balances and the expense category to which MPPP-related impairments should be reported. Presumably, this discussion of MLR requirements is provided for context, but as SAPWG discussions continue, we expect that the focus of the Form A will appropriately shift from context (MLR) to the area of focus (statutory accounting). While the MLR discussion might provide some context, it also may cause confusion when referenced in a discussion about statutory accounting. That is because MLR is a separate subject with separate considerations from statutory accounting used by state-regulated health plans.

<u>*Recommendation:*</u>
NAIC staff recommends re-exposure of the revised *INT 24-02: Medicare Part D Prescription Payment Plans* and the previously exposed minor edits to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* <u>for a shortened comment period ending on March 5, 2025</u> to allow for discussion at the Spring National Meeting. In addition, NAIC should be directed to continue with the blanks proposals on this topic with the goal of incorporation into the 2025 annual statement instructions.

NAIC staff has incorporated most of the revisions suggested by Blue Cross Blue Sheild Association and AHIP. NAIC has also included a few additional clarifications, however, the three entirely new proposed paragraphs were not incorporated and an existing paragraph was deleted as redundant. Although the majority of the revisions are terminology revisions, in aggregate the revisions are extensive. NAIC staff also did not incorporate the optional guidance wording that was proposed for the initial paragraph on recording of out-of-pocket MPPP pharmacy payments as it proposed that the methodology be optional, which would be inconsistent with the illustration. However, more comments are requested on other possible methodologies that do not record a contra claim expense which is not recognized until the receivable is determined to be uncollectible and is written-off as an incurred claims expense. If additional language is recommended, modifications to the illustration are also requested.

The revised INT 24-02 retains the key points noted in the summary section above. Key terminology revisions include the following:

a. MP3 to MPPP
b. Member to enrollee (in Part D Plan)
c. Part D plan to Part D plan sponsor
d. MP3 enrollee to MPPP participant
e. Enrollee balance to recoverable from MPPP participant.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-27 (Julie)	**Issue Papers in the Statutory Hierarchy**	**9 – Agenda item**	**Comments Received**	**IP – 25**

<u>*Summary:*</u>
On December 17, 2024, the Working Group moved this item to the active listing as a SAP clarification and exposed revisions to classify issue papers in Level 5 of the statutory hierarchy.

<u>*Interested Parties' Comments:*</u>
Interested parties raised the issue of the placement of Issue Papers in the statutory hierarchy in our previous comment letter of September 27, 2024, where we suggested that Issue Papers be recognized as authoritative guidance and included in either Level 2, or alternatively Level 4, in the statutory hierarchy of authoritative guidance. Because Issues Papers frequently have more accounting guidance rather than reporting guidance, we suggested first Level 2 as this would place issue papers higher in the hierarchy than the annual statement instructions (Level 3) which is arguably more appropriate.

Level 4 specifically includes the preamble as authoritative guidance and paragraph 45 of the preamble states, "While it is not intended that there be any significant differences between an underlying issue paper and the resultant SSAP, if differences exist, the SSAP prevails and shall be considered definitive." This part of the preamble puts the guidance in an SSAP above the guidance in an Issue Paper if a difference exists between the two, which we agree is appropriate. However, there are instances where there is no guidance in an SSAP and the underlying Issue Paper has either a detailed discussion or specific guidance that is on point for an accounting issue that a preparer or auditor is researching. As mentioned in our prior comment letter, examples include feeder funds related to the new principles-based bond definition (PBBD) and superseded US GAAP OTTI impairment guidance that is still applicable for statutory accounting but is not codified within the SSAPs).

The current exposure draft recommends that Issue Papers be included in Level 5 of the statutory hierarchy as "nonauthoritative guidance" which includes "Accounting textbooks, handbooks and articles." We believe this is inappropriate as the guidance in Issue Papers is the result of the deliberative process used by the Working Group and the Accounting Practices and Procedures Task Force to identify appropriate statutory accounting guidance and practices, expose draft guidance for comment, receive public comment, and deliberate a final Issue Paper that is and should be maintained as part of the process for developing authoritative statutory accounting practices and procedures. In short, the Issue Papers are the product of an iterative, open process that become part of the documented discussion of statutory accounting guidance by the Working Group, industry, and others. We believe this should result in Issue Papers being placed in Level 4.

Recommendation:

NAIC staff recommends that the Working Group adopt the exposed revisions to capture issue papers in Level 5 of the statutory hierarchy. As shown in the agenda item, these revisions will be to the *Accounting Practices and Procedures Manual* (AP&P) within the Preamble, the introduction to Appendix E – Issue Papers, the guidance for "How to Use this Manual" and the NAIC Policy Statement on Maintenance of Statutory Accounting Principles.

Although industry is currently proposing a Level 4 classification, consistent with the rationale documented in the agenda item, a Level 5 classification is supported for the following reasons:

- A Level 5 classification would better prevent unintended conflicts between issue papers and other sources of statutory guidance. Issue papers are not always updated after adoption of an SSAP, especially a clarification adoption, and should not be considered more applicable than any other statutory-specific guidance, whether that guidance is in SSAP, interpretation, reporting instructions or information from the *Purposes and Procedures Manual of the Investment Analysis Office*.

- By classifying issue papers as Level 5, issue papers will be on the same level as non-authoritative U.S. GAAP guidance/literature and will be behind all other sources of statutory guidance. Although this inclusion clarifies that issue papers are a source of statutory guidance that can be applied and utilized, the Level 5 classification would only allow application if they do not conflict with other statutory guidance. This classification confirms that an issue paper cannot be used or cited above any other source of established statutory guidance captured in the statutory hierarchy. It has been noted that some users have attempted to cite issue paper guidance as authoritative, particularly once they were publicly posted on the website, although the guidance had been replaced by a more current SSAP. It has also been noted that some citations in issue papers discuss proposed guidance that is evaluated and rejected. Although inclusion in Level 5 confirms that issue papers are a source of statutory accounting, the guidance shall be applied only to the extent that they do not conflict with a higher level of guidance.

- By adding issue papers to Level 5 of the statutory hierarchy, the reference would clarify the intent to use issue papers, and the use of information detailed within, eliminating questions on the use of the guidance that is consistent with currently adopted SSAPs. However, the Level 5 Classification is necessary in comparison to the industry request for Level 2 or Level 4 for the following specific reasons:

  - By classifying issue papers as Level 5, instead of Level 2, if there is a subsequent reporting revision that is not captured in statutory accounting but only reflected in the annual statement instructions, the updated instructions, which are Level 3, shall be followed. If issue papers were classified as Level 2, there could be inherent reporting conflict if the issue paper detailed reporting requirements at the time of adoption as that issue paper guidance would not be subsequently updated.

- By classifying issue papers as Level 5, instead of Level 4, issue papers will continue to be below the Level 4 SAP Preamble and Statement of Concepts. As such, if there are revisions to the Preamble, those revisions will continue to override any potential conflicts with a previously adopted issue paper.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-28 (Julie)	**Holders of Capital Notes**	**10 – Agenda item**	**Comments Received**	**IP – 26**

Summary:
On December 17, 2024, the Working Group moved this item to the active listing as a SAP clarification and exposed revisions to *SSAP No. 41—Surplus Notes* to incorporate changes to clarify capital notes references and guidance. With exposure, the Working Group agreed to sponsor a blanks proposal to update the definitions in the Schedule BA annual statement instructions as proposed in the agenda item.

Interested Parties' Comments:
Interested parties appreciate the attempted clarification in the exposure regarding paragraph 9a as this paragraph was a point of confusion during interested parties' pre-exposure review of SSAP No. 41. Even with the proposed changes, there is still confusion surrounding this paragraph. More specifically, do the state law admission limits discussed pertain to ownership related to an individual company, affiliates, an aggregate equity limit or something else? As noted in the NAIC Staff Note, it is not generally characteristic of the SSAPs to detail provisions used in state limitations. As a result, absent further clarification and/or a compelling rationale from regulators as to the purpose of having such guidance in SSAP No. 41, interested parties would support the deletion of this paragraph if determined appropriate by regulators in response to the question asked of them in the NAIC Staff Note.

Interested parties are also supportive of the proposed changes to paragraph 21 as not only is this language likely not purposeful or used but it also not readily obtainable for issuers if at all. Relatedly, the disclosure in paragraph 18c includes the following to be disclosed for as long as the surplus notes are outstanding:

> *Holder of the note, or if public, the names of the underwriter and trustee, with the identification on whether the holder of the surplus note is a related party per SSAP No. 25 – Affiliates and Other related Parties.*

Interested parties believe this disclosure can also be deleted as: 1) the holder of the note, is duplicative of the proposed deletion in paragraph 21, is likely not purposeful or used and not readily obtainable 2) the names of the underwriter and trustee are likely not purposeful or used, and 3) any surplus note for which the holder is a related party would appear to be captured in paragraph 21 which is not being deleted. If a distinction is being made between related party and affiliate, maybe that could be clarified within paragraph 21 and thus allow the deletion of paragraph 18c.

Interested parties do not believe it is appropriate for capital notes to be nonadmitted in the event the regulatory authority halts principal or interest payments as suggested in paragraph 9b. Mechanisms already exist to appropriately reduce capital such as the carrying value of NAIC designations of 3 through 6 capital notes are reported as the lesser of amortized cost or fair value in paragraph 11 and proposed impairment guidance in paragraph 16 recording an impairment down to fair value.

A wide range of scenarios may exist in regard to regulator authority cancelling coupons and/or writing off par value. Typically, a cancellation of a coupon would cause a downgrade and likely an impairment decision. Carrying the capital note at fair value (which is generally readily available in the market) is more suitable than non-admitting the remaining fair value of a capital note. During 2009, several bank issuers agreed with their EU regulators on cancelling coupons for 24 months. If held, many of these hybrid securities recovered and ultimately were called by the issuer at par value. Further, nonadmitting an asset that may have a significant fair value would work to incentivize companies to sell at depressed prices, ultimately hurting policyholders, rather than holding the capital note for a potential recovery.

Recommendation:

NAIC staff recommends that the Working Group adopt the exposed *SSAP No. 41—Surplus Notes*, with revisions as described below.

- **Paragraph 9a:** There is a question as to the application of paragraph 9a, as well as regulator questions as to whether the added exposed language reflects the intent of the original guidance and/or results in proper clarification. **It is recommended that the Working Group either 1) direct deletion of the entire paragraph 9a or 2) not incorporate the proposed revisions to paragraph 9a (clarifying application under state investment law/limits) at this time - (no changes to existing guidance)**. As the existing guidance is unclear as to application, if the Working Group chooses not to delete the paragraph, a subsequent agenda item will be drafted to assess the guidance and how to clarify applicability under statutory accounting principles. (Interested party comments support deletion of the paragraph.)

- **Paragraphs 18c/21:** Edits to paragraph 18c and paragraph 21 as recommended by interested parties.

- **Paragraph 9b:** NAIC staff does not recommend revisions to paragraph 9b as recommended by interested parties and recommends that the guidance be retained to require nonadmittance in any event in which the regulatory authority halts principal or interest payments.

Illustrated changes to the noted paragraphs:

1) **Paragraph 9a.** As detailed in the agenda item, NAIC staff originally questioned the inclusion of this paragraph, as SSAPs do not have equity limits for admitted assets. As such, if applying the guidance in accordance with the SSAPs, there would never be a situation in which a surplus/capital note would be nonadmitted under the guidance. With the exposure, the proposed edits attempted to clarify that it would only apply in the absence of specific instruction under state investment limits but provided an option that the Working Group could elect to delete the paragraph entirely.

With comments on whether the proposed language properly reflects how items are captured in state investment limits (as items can be admitted under basket clauses even if exceeding set equity limits), it is proposed that either the paragraph be deleted fully, or that changes to this paragraph be deferred (no changes to existing language) and addressed under a separate agenda item. (If deleted, formatting/renumbering edits will be incorporated as existing paragraph 9b will become paragraph 9a.)

Original Language:

9. Investments in capital or surplus notes meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement. Additionally, the amount admitted is specifically limited to the following two provisions:

   a. The admitted asset value of a capital or surplus note shall not exceed the amount that would be admitted if the instrument was considered an equity instrument and added to any other equity instruments in the issuer held directly or indirectly by the holder of the capital or surplus note.

Exposed Language:

9. Investments in capital or surplus notes meet the definition of assets as defined in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement. Additionally, the amount admitted is specifically limited to the following ~~two~~ provisions~~s~~:

    b. In the absence of specific instruction pursuant to state law or direction of the domiciliary regulator, ~~T~~the admitted asset value of a capital or surplus note shall not exceed the amount that would be admitted under state investment limits if the instrument was considered an equity instrument and added to any other equity instruments in the issuer held directly or indirectly by the holder of the capital or surplus note.

    NAIC Staff Note: The SSAPs do not have equity limits for admitted assets. The above paragraph would pertain to state investment limits. This guidance requires capital and surplus notes to be combined with other equity items to determine whether the state investment limit for equity instruments has been surpassed. It is not characteristic of the SSAPs to detail provisions used in state investment limitations, but this paragraph has been part of SSAP No. 41 since codification. If preferred by Working Group members, this paragraph could be deleted.

2) **Propose to delete paragraph 18 and reference related parties in paragraph 21.** NAIC staff agrees that a disclosure of all holders of surplus notes, as well as other components of paragraph 18 (names of the underwriter and trustee) are likely unnecessary and not beneficial to the regulator. Further, with the disclosure of affiliates in paragraph 21, components of this disclosure would be duplicative. NAIC staff proposes to delete paragraph 18 and add reference to related parties in paragraph 21. (With deletion of paragraph 18c, the remaining subparagraphs will be renumbered. Only the words "related parties and" (shaded) in paragraph 21 are new from this change. The proposed deletions to this paragraph were part of the last exposure.)

18. The notes to the financial statements of a reporting entity that issues surplus notes shall disclose the following as long as the surplus notes are outstanding:

    a. Date issued;

    b. Description and fair value of the assets received;

    ~~c. Holder of the note or, if public, the names of the underwriter and trustee, with identification on whether the holder of the surplus note is a related party per *SSAP No. 25—Affiliates and Other Related Parties*;~~

21. ~~In addition to the above, a~~A reporting entity shall identify all related parties and affiliates that hold any portion of a surplus debenture or similar obligation (including an offering registered under the Securities Act of 1933 or distributed pursuant to rule 144A under the Securities Act of 1933)., ~~and any holder of 10% or more of the outstanding amount of any surplus note registered under the Securities Act of 1933 or distributed pursuant to Rule 144A under the Securities Act of 1933~~.

3) **Paragraph 9b to Clarify Nonadmittance.** There is no proposed change to the exposed guidance. NAIC staff supports retaining the language that requires nonadmittance in any event in which the regulatory authority halt principal or interest payments. As detailed in the paragraph, the guidance already allows for admittance to occur once those conditions cease to exist.

b. The surplus note shall be nonadmitted if issued by an entity that is subject to any order of liquidation, conservation, rehabilitation or any company action level event based on its risk-based capital. Capital notes shall be nonadmitted in any event in which the regulatory authority halts principal or interest payments. Subsequent to this nonadmittance, if any of the conditions described ceased to exist, the holder may admit the capital or surplus note at the value determined under paragraph 11. If a capital or surplus note was nonadmitted pursuant to this paragraph, and the capital or surplus note was ultimately determined to be other-than-temporarily impaired, the reporting entity shall recognize a realized loss for the portion of the surplus note determined to be other-than-temporarily impaired, with elimination of a corresponding amount of the previously nonadmitted assets.

The comment letters are included in Attachment 11 (50 pages).
(Note – Not all items captured in the comment letters are planned for discussion on Feb. 25, 2025.)

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