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.

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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*.

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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.)

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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.

Recommendation:

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) **Paragraph 22 – Incorporate revisions as recommended by interested parties.** 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 with gains and losses offset to IMR similar to asset sales for cash guidelines as detailed in paragraphs 20 & 21. 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) **Paragraph 24 – Incorporate revisions as recommended by interested parties.** 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

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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.

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- 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.

<u>INT 24-02T: Medicare Prescription Payment Plan</u>

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.

SAPWG Maintenance Agenda Submission Form, Form A

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.

Recommendation:
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* for a shortened comment period ending on March 5, 2025 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**

Summary:
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.

Interested Parties' Comments:
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~~ provision~~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.)

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/00 - 02-25-25 - SAPWG Hearing Agenda.docx

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Repack and Derivative Investments

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☐	☐	☐
New Issue or SSAP	☒	☒	☒
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to address debt security investments with derivative components that do not qualify as structured notes. Although the original focus was on specific "credit repack" investments, the agenda item has been expanded to ensure that all debt security investments with derivative wrappers / components are captured.

As an overview of a special purpose vehicle (SPV) "repacking," the structure consists of an SPV acquiring a debt security and reprofiling the cash flows by entering a derivative transaction with a derivative counterparty (known as "credit repacks"). The redesigned debt instrument (reflecting the combined debt security and derivative) is then sold to an investor. NAIC staff has recently received calls on the classification of repacks under the bond definition, but the discussions of these transactions have identified that additional guidance may be warranted to ensure consistent reporting of these transactions within the statutory financial statements. From the discussions, there are initiatives for these combined investments to become more prevalent with U.S. insurance entities, but investment makers have noted that these investments are already common in other countries.

As a key element, repacking (and potentially other derivative wrapped debt structures) takes two separate items (debt security and derivative) and combines them into one instrument that resembles a debt security. This is done at an SPV, with the SPV issuing a new debt security to the reporting entity. From discussions, there are several variations of the derivative components that can be combined with the debt security. Some of them are very simple (such as a cross-currency swap), but others are complex, altering both the amount and timing of cash flows. The structures can be customized allowing for ongoing innovation, benefiting insurers with the ability of entering derivative transactions to appropriately reduce risk, but creating difficulty in the ability to group repacks structures into limited exception guidance.

For all of these structures, the derivative arrangements could be entered into separately and do not need to be entered into as a combined transaction, however, the noted benefits for entering into a combined structure include:

1) **Derivative Margin / Collateral Requirement:** There is no daily settling of a margin requirement at the derivative counterparty based on fair value changes in the derivative. **This is because the debt security in the structure serves as constant collateral, and any amount owed to the derivative counterparty would be taken first from debt instrument cash flows before payment is made to the investor. (The derivative counterparty is senior in priority.)** The repack structure limits the collateral obligation to the debt security in the structure, so there is no potential for the reporting entity to be obligated for more collateral beyond the linked debt security. This is a benefit of a repack in comparison to normal derivatives that do not have a collateral limit.

    - Although perceived as a benefit from the entity / investment maker as it reduces liquidity risk associated with margin calls, from a statutory accounting perspective, if the transactions were reported separately and the debt investment was pledged as collateral, the debt instrument would be identified as a restricted asset. If the repack is collectively reported as a debt instrument, there would be no identification that the debt instrument is restricted or encumbered as collateral to the derivative counterparty. This is

because the restriction is at the SPV and not the reporting entity. Also, if separately engaging in derivative transactions, the derivative counterparty is known and reported. If a repack is collectively reported as a debt instrument, it is uncertain if the affiliation between the derivative counterparty and reporting entity would be known.

2) **Bond Reporting:** If these structures are accounted for as bonds, **reporting entities would determine measurement method and RBC impact based on the NAIC designation. Ultimately, this structure provides the reporting entity with a derivative arrangement, with no separate reporting or acknowledgement of the derivative instrument within the financial statements.**

   - From a statutory accounting perspective, if reporting is combined in a repack, derivatives would not be captured on Schedule DB and reporting entities would not be required to assess whether the derivative is effective under *SSAP No. 86—Derivatives*. (There is also a question on whether these arrangements would be captured in a reporting entity's derivative use plan filed with the domiciliary state.) Any obligation based on the performance of the derivative would not be reported in the investor's financials.

3) **RBC Impact:** By reporting as a bond investment, the reporting entity would incur a single RBC factor charge based on the NAIC designation on the debt security issued by the SPV.

   - From a statutory perspective, if the investment had been reported separately as a bond and a derivative, there would be RBC impacts for both components. The collateral pledged to the derivative counterparty (bond) would also be coded as a restricted asset. Whether the combined reporting results in a benefit to RBC depends on how the derivative would have been reported separately (at amortized cost or fair value) and whether the derivative is in a loss position. However, if reported separately, these components are captured in the RBC formula to reflect those dynamics.

The following identifies specific elements for discussion:

1) **Sale / Reacquisition:** A "credit repack" can be originated with a reporting entity's currently held debt security. In those situations, the insurer would sell the debt security to an SPV, that security would be combined with a derivative at the SPV, and the SPV would sell the restructured combined instrument back to the insurer.

   From the discussions held, inconsistent interpretations may exist on whether the initial debt security should be reflected as disposed, with the reporting entity acquiring a new investment for the "repack." The discussions have referred to "substantially similar" U.S. GAAP guidance and have noted that the base investment (original debt security) has not changed, therefore the action did not warrant disposal / new acquisition reporting. If this interpretation was applied, the original debt security would still be shown on the financial statements, but with the repack the issuer, yield and NAIC designation have been impacted. If it is concluded that the revised instrument is substantially similar to what was originally held and did not require a disposal / reacquisition, it is likely that there would be no indication in the financial statements that the entity has entered into a new arrangement that combines a debt security and derivative instrument. NAIC staff does not agree with interpretations that the repack is substantially similar based on existing guidance in SSAP No. 103, paragraph 52, but this has been noted as part of the discussions. Under SSAP No. 103, to be considered substantially the same, an investment needs to have the same primary obligor, identical contractual interest rates and identical form and type to provide the same risks and rights. Under a repack, the issuer, yield and designation are impacted as follows, disallowing consideration that the instrument is substantially the same:

   - The revised issuer is the SPV and the new instrument is a combined instrument of the debt instrument and the derivative.

   - The fees for engaging in this instrument are built into the investment yield, resulting in a lower yield than what would have been received if the original debt instrument was still held.

- The NAIC designation (CRP rating) could also be impacted, as the revised instrument reflects the credit quality of both the original issuer and the derivative counterparty. From discussions, this is often a 1-level decrease in rating.

Not all repacks involve a previously held debt instrument. An entity may acquire a repack directly from the SPV rather than sell a currently owned debt security to the SPV. From the discussions, if this was to occur, it is believed that entities would report the acquired investment as a bond (under existing SSAP guidance), unless the structure is considered to be a structured note under paragraph 5.g. of *SSAP No. 86—Derivatives:*

> 5.g. "Structured Notes" in scope of this statement are instruments defined in *SSAP No. 26R—Bonds* (often in the form of debt instruments), in which the amount of principal repayment or return of original investment is contingent on an underlying variable/interest[1]. Structured notes that are "mortgage-referenced securities" are captured in *SSAP No. 43R—Loan-Backed and Structured Securities.*

There is also a question on whether all repacks should be considered structured notes. In a repack structure, if the debt security is liquidated early and there is an amount owed from the derivative performance, the SPV must first satisfy that amount to the derivative counterparty. This could result in a payment less than the principal amount being remitted to the insurer holder. Although the repack designs differ based on the derivative instrument and intent, in some situations this is only driven by the early liquidation of the structure and not a component that comes into play if the structure is held to maturity. In those structures, the design would not be considered a structured note. However, in other designs, the repack may reflect a structured note regardless, and the structured note guidance should be followed.

2) **<u>Derivative Obligation</u>**: A credit repack investment ultimately could allow an insurer to enter into derivative arrangements that are not separately reported or assessed within the scope of SSAP No. 86, which is currently explicit that embedded derivatives shall not be separated from the host contract. If the derivative was to be separately reported, it would only qualify for amortized cost treatment if determined to be highly effective pursuant to SSAP No. 86, otherwise it would be reported at fair value.

   From discussions of these investment / derivative designs, NAIC staff has the impression that these derivative arrangements would be reported at fair value if held separately from the debt instrument. (Discussions have indicated that they would be separately reported at fair value under U.S. GAAP.) By combining with the debt security, and if permitted to follow bond accounting, reporting entities would utilize an amortized cost measurement for the combined credit repack based on the NAIC designation pursuant to current guidance within SSAP No. 26 / SSAP No. 43.

   Although it has been communicated that the derivative is designed to match the maturity duration of the debt instrument, if the investment was to be liquidated in advance of the maturity date, the obligation with the derivative counterparty must still be satisfied. If the derivative was in a liability position, upon liquidation of the debt instrument, the SPV would collect the proceeds from the debt instrument and first remit any amount owed to the derivative counterparty before providing the remaining balance to the reporting entity. Although it depends on the derivative arrangement, in some designs, the reporting entity could receive less than the stated

[1] The "structured notes" captured within scope of this statement is specific to instruments in which the terms of the agreement make it possible that the reporting entity could lose all or a portion of its original investment amount (for other than failure of the issuer to pay the contractual amounts due). These instruments incorporate both the credit risk of the issuer, as well as the risk of an underlying variable/interest (such as the performance of an equity index or the performance of an unrelated security). Securities that are labeled "principal-protected notes" are captured within scope of this statement if the "principal protection" involves only a portion of the principal and/or if the principal protection requires the reporting entity to meet qualifying conditions in order to be safeguarded from the risk of loss from the underlying linked variable. Securities that may have changing positive interest rates in response to a linked underlying variable or the passage of time, or that have the potential for increased principal repayments in response to a linked variable (such as U.S. Treasury Inflation-Indexed Securities) that do not incorporate risk of original investment/principal loss (outside of default risk) are not captured as structured notes in scope of this statement.

principal amount of the bond. For these designs, unless the derivative was reported separately (or the repack was reported at fair value), the amount to be received at any point in time for the repack investment may be overstated due to the derivative impact. *(The inverse is also true, whereas if the derivative was in an asset position, the SPV would collect funds from the derivative counterparty and the reporting entity would receive an amount that exceeds the principal amount of the bond.)*

3) **Principles-Based Bond Definition Application**: The discussion with NAIC staff on credit repacks initially occurred due to questions on whether the repack is an issuer credit obligation (ICO) or an asset-backed security (ABS) under the principles-based bond definition. Initially, it was noted that a repack with a derivative that simply converted cash flows (fixed to floating or foreign currency), but which did not impact the timing or extent of cash flows could still potentially reflect an ICO obligation under the single-entity payer provision, assuming that the investment did not reflect a structured note. However, any design that was to alter the timing or amount of cash flows would result in an ABS classification. For example, if the repack altered the timing of cash flows so instead of periodic interest in line with the debt security terms, all interest payments were accumulated at the SPV and provided at maturity, this would require an ABS classification. If classified as an ABS, it was noted that there would be no substantive credit enhancement (as the structure simply passes through cash flows) and the structure would fail to qualify as a bond. However, after further assessment of these structures, NAIC staff recommends explicit guidance for the accounting of these combined debt / derivative structures. From discussions on these investments, a key driver is getting the combined structure classified as a Schedule D investment. From information shared, a vast array of different derivative structures could be combined with the debt security to form a combined item, with many different cashflow desired outcomes.

Ultimately, NAIC staff believes the issue goes further than bond classification as ICO or ABS. As such, this agenda item proposes SSAP guidance / interpretation to address all situations in which a debt security may be wrapped or combined with a derivative structure to ensure consistent and transparent reporting as well as information to the regulators on these investment transactions. NAIC staff believes the potential for these structures originates from the existing SSAP No. 86 guidance that indicates that embedded derivatives shall not be separated from the host contract and accounted for separately as a derivative instrument. NAIC staff notes that this SSAP No. 86 guidance allows these investment structures to be reported in ways that were perhaps not intended when that embedded derivative guidance was originally established.

Existing Authoritative Literature:

- ***SSAP No. 26R—Bonds (Effective Jan. 1, 2025)***

SSAP No. 26R includes the adopted principles-based bond definition and the provisions for detailing an ICO or ABS. Key provisions from this SSAP are provided below. These excerpts focus on the definition of a bond, the creditor relationship review involving pre-determined interest and principal payments, and relevant provisions of the ICO and ABS terms.

Specific Excerpts:

5. A bond shall be defined as any security representing a creditor relationship, whereby there is a fixed schedule for one or more future payments, and which qualifies as either an issuer credit obligation or an asset-backed security as described in this statement.

6. Determining whether a security represents a creditor relationship should consider its substance, rather than solely the legal form of the instrument. The analysis of whether a security represents a creditor relationship should consider all other investments the reporting entity owns in the investee as well as any other contractual arrangements. A security that in substance possesses equity-like characteristics or represents an ownership interest in the issuer does not represent a creditor relationship.

6.d. In order for a debt instrument to represent a creditor relationship in accordance with Paragraph 6, it must have pre-determined principal and interest payments (whether fixed interest

or variable interest) with contractual amounts that do not vary based on the appreciation or depreciation (i.e., performance) of any underlying collateral value or other non-debt variable. For example, an issued security that has varying principal and interest payments based on the appreciation of referenced equity, real estate or other non-debt variable is precluded from bond treatment. This exclusion is not intended to restrict variables that are commonly related to debt instruments such as, but not limited to, plain-vanilla inflation or benchmark interest rate adjustments (such as with U.S. TIPs or SOFR-linked coupons, respectively), scheduled interest rate step-ups, or credit-quality related interest rate adjustments. This exclusion is also not intended to encompass nominal interest rate adjustments[2]. For clarification purposes, all returns from a debt instrument in excess of principal are required to be considered as interest. Therefore, investments with "stated" interest and then "additional returns" to which the holder of the debt instrument is entitled are collectively considered as interest and shall be assessed together in determining whether the investment has variable principal or interest due to underlying referenced non-debt variables. Examples of securities excluded from the bond definition under this guidance:

i. Structured Notes, which are securities that otherwise meet the definition of a bond, but for which the contractual amount of the instrument to be paid at maturity (or the original investment) is at risk for other than the failure of the borrower to pay the principal amount due, are excluded from the bond definition. These investments, although in the form of a debt instrument, incorporate the risk of an underlying variable in the terms of the agreement, and the issuer obligation to return the full principal is contingent on the performance of the underlying variable. These investments are addressed in *SSAP No. 86—Derivatives*. Mortgage-referenced securities issued by a government sponsored enterprise are explicit inclusions in scope of SSAP No. 43. Foreign-denominated bonds subject to variation as a result of foreign currency fluctuations are not structured notes.

ii. Principal-protected securities, as defined in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* are excluded from the bond definition as they have a performance component whose payments originate from, or are determined by, non-fixed income securities. These investments shall follow the guidance for non-bond securities in *SSAP No. 21—Other Admitted Assets.*

7. An issuer credit obligation is a bond, for which the general creditworthiness of an operating entity or entities through direct or indirect recourse, is the primary source of repayment. Operating entity or entities includes holding companies with operating entity subsidiaries where the holding company has the ability to access the operating subsidiaries' cash flows through its ownership rights. An operating entity may be any sort of business entity, not-for-profit organization, governmental unit, or other provider of goods or services, but not a natural person or "ABS Issuer" (as defined in paragraph 8). Examples of issuer credit obligations include, but are not limited to:

7.g. Investments in the form of securities for which repayment is fully supported by an underlying contractual obligation of a single operating entity (e.g., Credit Tenant Loans (CTLs), Equipment trust certificates (ETCs), other lease backed securities, Funding Agreement Backed Notes (FABNs), etc.). For purposes of applying this principal concept, repayment is fully-supported by the underlying operating entity obligation if it provides cash flows for the repayment of all interest and at least 95% of the principal of the security.

8. An asset-backed security is a bond issued by an entity (an "ABS Issuer") created for the primary

[2] Nominal interest rate adjustments are those that are too small to be taken into consideration when assessing the investment's substance as a bond. Nominal adjustments are not typically influential factors in an investors' evaluation of investment return and are often included to incentivize certain behavior of the issuer. An example would include sustainability-linked bonds where failure to achieve performance metrics could cause interest rate adjustments. In general, interest rate adjustments that adjust the total return from interest by more than 10% (e.g., >0.4% for a 4% yielding bond), would not be considered nominal. Further, any such adjustments that cause an investment to meet the definition of a structured note would not be considered nominal.

purpose of raising debt capital backed by financial assets or cash generating non-financial assets owned by the ABS Issuer, for which the primary source of repayment is derived from the cash flows associated with the underlying defined collateral rather than the cash flows of an operating entity. In most instances, the ABS Issuer is not expected to continue functioning beyond the final maturity of the debt initially raised by the ABS Issuer. Also, many ABS Issuers are in the form of a trust or special purpose vehicle ("SPV"), although the presence or lack of a trust or SPV is not a definitive criterion for determining that a security meets the definition of an asset-backed security. The provisions in paragraphs 9-10 detail the two defining characteristics that must be present for a security to meet the definition of an asset-backed security.

10. The holder of a debt instrument issued by an ABS Issuer is in a different economic position than if the holder owned the ABS Issuer's assets directly. The holder of the debt instrument is in a different economic position if such debt instrument benefits from substantive credit enhancement through guarantees (or other similar forms of recourse), subordination and/or overcollateralization.

> 10a. *Substantive Credit Enhancement*: The intent of the criteria requiring the holder to be in a different economic position is to distinguish qualifying bonds from instruments with equity-like characteristics or where the substance of the transaction is more closely aligned with that of the underlying collateral. To qualify as an ABS under this standard, there is a requirement that there are substantive credit enhancements within the structure that absorb losses before the debt instrument being evaluated would be expected to absorb losses. This is inherent in the context of an issuer credit obligation in scope of SSAP No. 26R as the owners of the equity in the operating entity are the first to absorb any variability in performance of the operating entity. The same concept applies to asset-backed securities. If substantive credit enhancement did not exist, the substance of the debt instrument being evaluated would be more closely aligned with that of the underlying collateral than that of a bond. Credit enhancement that is merely nominal or lacks economic substance does not put a holder in a different economic position. The substantive credit enhancement

- ***SSAP No. 86—Derivatives***

SSAP No. 86 provides guidance for derivatives. Paragraph 5.g. addresses structured notes, paragraph 16 addresses variation margin, paragraph 17 addresses embedded derivative investments, with paragraphs 20-21 providing recognition guidance.

5. Derivative instruments include, but are not limited to; options, warrants used in a hedging transaction and not attached to another financial instrument, caps, floors, collars, swaps, forwards, futures, structured notes with risk of principal/original investment loss based on the terms of the agreement (in addition to default risk), and any other agreements or instruments substantially similar thereto or any series or combination thereof.

> 5g. "Structured Notes" in scope of this statement are instruments defined in *SSAP No. 26R—Bonds* (often in the form of debt instruments), in which the amount of principal repayment or return of original investment is contingent on an underlying variable/interest3. Structured notes that are "mortgage-referenced securities" are captured in *SSAP No. 43R—Loan-Backed and Structured Securities.*

[3] The "structured notes" captured within scope of this statement is specific to instruments in which the terms of the agreement make it possible that the reporting entity could lose all or a portion of its original investment amount (for other than failure of the issuer to pay the contractual amounts due). These instruments incorporate both the credit risk of the issuer, as well as the risk of an underlying variable/interest (such as the performance of an equity index or the performance of an unrelated security). Securities that are labeled "principal-protected notes" are captured within scope of this statement if the "principal protection" involves only a portion of the principal and/or if the principal protection requires the reporting entity to meet qualifying conditions in order to be safeguarded from the risk of loss from the underlying linked variable. Securities that may have changing positive interest rates in response to a linked underlying variable or the passage of time, or that have the potential for increased principal repayments in response to a linked variable (such as U.S. Treasury Inflation-Indexed Securities) that do not incorporate risk of original investment/principal loss (outside of default risk) are not captured as structured notes in scope of this statement.

16. “Variation Margin” reflects the daily change in market value of derivative contracts (e.g., daily gain/loss on a derivative contract due to market movements). Amounts received/paid to adjust variation margin on derivative contracts that are both cleared and settled on an exchange shall be recognized as an adjustment to the carrying value of the derivative contract (e.g., futures). Amounts received/paid to adjust variation margin on all other derivative contracts shall be recognized on the balance sheet as an asset or liability separate from the carrying value of the derivative instrument. This treatment shall occur under statutory accounting regardless if the counterparty/exchange considers amounts exchanged for variation margin to be legal settlement or collateral. Changes in variation margin shall not be treated as realized gains or adjustments to the basis of the hedged item until the derivative contract has been sold, matured or expired.

Embedded Derivative Instruments

17. Contracts that do not in their entirety meet the definition of a derivative instrument, such as bonds, insurance policies, and leases, may contain “embedded” derivative instruments—implicit or explicit terms that affect some or all of the cash flows or the value of other exchanges required by the contract in a manner similar to a derivative instrument. The effect of embedding a derivative instrument in another type of contract (“the host contract”) is that some or all of the cash flows or other exchanges that otherwise would be required by the contract, whether unconditional or contingent upon the occurrence of a specified event, will be modified based on one or more underlyings. An embedded derivative instrument shall not be separated from the host contract and accounted for separately as a derivative instrument.

Recognition of Derivatives

20. Derivative instruments represent rights or obligations that meet the definitions of assets (SSAP No. 4—Assets and Nonadmitted Assets) or liabilities (SSAP No. 5R) and shall be reported in financial statements. In addition, derivative instruments also meet the definition of financial instruments as defined in *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures*. Should the cost basis of the derivative instrument be undefined (i.e., no premium is paid), the instrument shall be disclosed in accordance with paragraphs 46-50 of *SSAP No. 100R—Fair Value*. Derivative instruments used in hedging, income generation or replication (synthetic asset) transactions shall be recognized and measured in accordance with the specific provisions within this statement and are admitted assets to the extent they conform to the requirements of this statement.

21. Derivative instruments that are not used in hedging, income generation or replication (synthetic asset) transactions shall be considered “Other” derivatives. These derivatives shall be accounted for at fair value and the changes in fair value shall be recorded as unrealized gains or losses. These derivatives do not qualify as admitted assets.

- ***SSAP No. 103—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities***

SSAP No. 103 provides guidance for the transfers of assets and liabilities, including guidance for when a sale shall be considered to have occurred. Guidance is captured for when securities are sold/reacquired are considered to be substantially the same and how those transactions should be reflected. As detailed in paragraph 52, credit repack notes would not qualify as substantially the same as the credit repack generally has a different issuer, different yield and modified NAIC designation/CRP rating from the original underlying investment.

12. Repurchase agreements, reverse repurchase agreements, repurchase financing, collateral requirements and dollar repurchase agreements are described in paragraphs 102-118. When an asset is sold and the proceeds are reinvested within 30 days in the same or substantially the same security, such transfers shall be considered to be wash sales and shall be accounted for as sales as discussed in paragraphs 96-101 and disclosed as required by paragraph 28[4]. Unless there is a concurrent contract

[4] Paragraph 28.l. also details the items that are excluded from the wash sale disclosure.

to repurchase or redeem the transferred financial assets from the transferee, the transferor does not maintain effective control over the transferred financial assets.

Agreement to Repurchase or Redeem Transferred Financial Assets

51. An agreement that both entitles and obligates the transferor to repurchase or redeem transferred financial assets from the transferee maintains the transferor's effective control over those assets as described in paragraph 8.c.(1) when all of the following conditions are met:

a. The financial assets to be repurchased or redeemed are the same or substantially the same as those transferred (paragraph 52).

b. The agreement is to repurchase or redeem them before maturity, at a fixed or determinable price.

c. The agreement is entered into contemporaneously with, or in contemplation of, the transfer.

52. To be substantially the same, the financial asset that was transferred and the financial asset that is to be repurchased or redeemed need to have all of the following characteristics:

a. The same primary obligor (except for debt guaranteed by a sovereign government, central bank, government-sponsored enterprise or agency thereof, in which case the guarantor and the terms of the guarantee must be the same);

b. Identical form and type so as to provide the same risks and rights;

c. The same maturity (or in the case of mortgage-backed pass-through and pay-through securities similar remaining weighted-average maturities that result in approximately the same market yield);

d. Identical contractual interest rates;

e. Similar assets as collateral; and

f. The same aggregate unpaid principal amount or principal amounts within accepted "good delivery" standards for the type of security involved.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

In 2023, the Working Group adopted the principles-based bond definition, which resulted in key revisions to *SSAP No. 26R—Bonds* and *SSAP No. 43R—Asset-Backed Securities*, and *SSAP No. 21R—Other Admitted Assets* for the review and classification of debt securities pursuant to the bond definition. This guidance is effective Jan. 1, 2025.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing as a new SAP concept and expose proposed edits to *SSAP No. 86—Derivatives*, to establish guidance that requires separate accounting and reporting of derivatives that are captured in debt security structures. This is a change from existing guidance that explicitly precludes the separation of embedded derivatives. In addition to these changes, minor revisions are also proposed to *SSAP No. 26—Bonds* and to the annual statement instructions to clarify application guidance. NAIC staff will also draft an issue paper to document these revisions.

From initial discussions with banks / investment makers, guidance to separate the derivative from the debt security is believed to be preferred over a conclusion that would preclude bond treatment for the combined structure. With the proposal, debt security repack structures will be treated similarly to investments where the bond and derivative are not combined. (Ultimately, there would be no capital benefit or detriment due to the structure.) Additionally, this proposal will allow transparency as to the derivatives being used and ensure compliance with the reporting entity's derivative use plan. (If this proposed guidance is not supported, the combined repack, which represents a debt structure, would need to be assessed under the bond definition. This may require more detailed guidance to assess different types of derivative structures to determine whether the repack should qualify as a bond or as a non-bond debt security.)

NAIC staff has not proposed revisions to SSAP No. 103 as the existing guidance is clear that a sale of a debt security which is subsequently or simultaneously reacquired as a credit repack would not meet the criteria of substantially the same. This is because a credit repack generally has a revised issuer, yield and NAIC designation to reflect the additional derivative risk. As noted, minor revisions have been proposed to the annual statement instructions to clarify that the sale of a security that is reacquired with different terms shall be reported as a sale on Schedule D-Part 4 and a new acquisition on Schedule D-Part 3.

Proposed Revisions to *SSAP No. 86—Derivatives*:

Embedded Derivative Instruments

17. Contracts that do not in their entirety meet the definition of a derivative instrument, such as ~~bonds,~~ insurance policies, and leases, may contain "embedded" derivative instruments—implicit or explicit terms that affect some or all of the cash flows or the value of other exchanges required by the contract in a manner similar to a derivative instrument. The effect of embedding a derivative instrument in another type of contract ("the host contract") is that some or all of the cash flows or other exchanges that otherwise would be required by the contract, whether unconditional or contingent upon the occurrence of a specified event, will be modified based on one or more underlyings. For these contracts, excluding debt securities with derivative components/wrappers pursuant to paragraph 18, ~~A~~ an embedded derivative instrument shall not be separated from the host contract and accounted for separately as a derivative instrument.

18. Debt securities that have derivative components or wrappers shall initially be assessed to determine if they are a structured note pursuant to paragraph 5.g. Structured notes shall not be bifurcated and shall be collectively reported as a derivative investment and shall be measured and reported pursuant to the guidance within this statement. Debt securities that are not structured notes, but have been combined with a derivative instrument[FN1] shall be bifurcated with separate reporting as a debt security and a derivative instrument. Once the investment is bifurcated, the debt security shall be reviewed in accordance with the bond definition within *SSAP No. 26—Bonds* and captured as an issuer credit obligation, asset-backed security, or non-bond debt security, based on the characteristics of the debt security[FN2]. If the debt security serves as collateral to the derivative counterparty, the reported debt security shall be coded as a restricted asset under *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures*. The derivative shall be captured in scope of this statement, measured and classified pursuant to the guidance within and reported on Schedule DB.

New Footnote 1: This guidance applies to all debt securities with derivative components or wrappers but was incorporated in response to credit repack notes. With a credit repack, a debt security is combined with a derivative instrument at an SPV, with the reporting entity acquiring a new debt security ("repack") from the SPV reflecting the combined components. This structure can be viewed as advantageous over the separate acquisition of a derivative instrument as the debt security held in the structure serves as the sole source of collateral to the derivative counterparty, reducing potential liquidity concerns based on future market fluctuations. However, if this repack structure was collectively reported as a debt security, information on the use of derivatives would not be identifiable within the statutory financial statements. A repack note often has a reduced interest yield from the stated yield of

the underlying debt security held in the structure to cover the fees of issuing the repack, as well as a revised NAIC designation/CRP rating that reflects the added risk of the SPV and derivative counterparty.

New Footnote 2: Assessment under the bond definition shall be based on the characteristics of the underlying debt security, but the issuer, investment yield, NAIC designation/CRP rating, as well as any other reported investment components, shall reflect the terms of the held (combined) investment and not the terms of the underlying security.

Proposed Revisions to SSAP No. 26—Bonds

4. This statement excludes:

e. Replication (synthetic asset) transactions and debt security structures that have been combined with derivative components or wrappers addressed in *SSAP No. 86—Derivatives*. The admissibility, classification and measurement of a replication (synthetic asset) transactions are not preemptively determined by the principles-based bond definition and should be evaluated in accordance with the guidance on replication (synthetic asset) transactions within SSAP No. 86. Debt security structures combined with a derivative, such as a credit repack note that does not reflect a structured note, shall follow the guidance in SSAP No. 86 for bifurcation. After bifurcation, the underlying debt security is subject to the guidance in this statement in determining whether it qualifies for bond reporting.

Proposed Revisions to Annual Statement Instructions:

Schedule D – Part 4 – Long Term Bonds and Stocks Sold, Redeemed or Otherwise Disposed Of During Current Year

This schedule should include a detailed listing of all securities that were sold/disposed of during the current reporting year that were owned as of the beginning of the current reporting year (amounts purchased and sold during the current reporting year are reported in detail on Schedule D, Part 5 and only in subtotal in Schedule D, Part 4). This should include all transactions that adjust the cost basis of the securities (except other-than-temporary impairments that are not part of a disposal transaction). ~~Thus, it~~This schedule should not be used for allocations of TBAs to specific pools subsequent to initial recording in Schedule D, Part 3 or ~~other~~ situations ~~such as~~that only involve CUSIP number changes. The following list of items provides examples (not all inclusive) of the items that should be included:

Pay downs of securities still owned (including CMO prepayments);

Subsequent partial sales of investment issues still owned;

Sales of securities to an SPV or other entity for which a new instrument is reacquired from the SPV/entity reflecting a combined instrument containing the original security and derivative instruments or other components (such as a credit repack note). The sale shall be captured on this schedule (or Schedule D, Part 5 if the debt security was acquired in the current year), and the new security shall be reported on Schedule D, Part 3.

Reallocation of the cost basis of an already owned stock to the cost basis of a new stock received as a dividend (e.g., spin off); and

Any decreases in the investments in SCA companies that adjust the cost basis, not including other-than-temporary impairments alone (e.g., subsequent return of capital from investments in SCA companies valued using the equity method).

Schedule D – Part 5 – Long-Term Bonds and Stocks Acquired During the Year and Fully Disposed Of During Current Year

As with Schedule D, Parts 3 and 4, this schedule should ~~not~~ be used for ~~a~~ transactions ~~unless it~~that affect~~s~~ the cost basis of the securities. ~~Thus, it~~This schedule should not be used for allocations of TBAs to specific pools subsequent to initial recording in Schedule D, Part 3 or ~~other~~ situations ~~such as~~ that only involve CUSIP number changes. Refer to the examples on Schedule D, Part 4 of transactions that should be captured.

Existing Guidance in SSAP No. 103, paragraph 52 – No Revisions Proposed:

With this existing guidance, debt securities sold and reacquired as a credit repack should not be considered to be substantially the same. This is because the credit repack is acquired from a new issuer, with a revised yield and with revised risks and rights (including revised NAIC designation/CRP rating) to reflect the derivative components / counterparty. Comments are requested on different interpretations and if edits are needed to ensure proper application of this guidance.

52. To be substantially the same, the financial asset that was transferred and the financial asset that is to be repurchased or redeemed need to have all of the following characteristics:

    a. The same primary obligor (except for debt guaranteed by a sovereign government, central bank, government-sponsored enterprise or agency thereof, in which case the guarantor and the terms of the guarantee must be the same);

    b. Identical form and type so as to provide the same risks and rights;

    c. The same maturity (or in the case of mortgage-backed pass-through and pay-through securities similar remaining weighted-average maturities that result in approximately the same market yield);

    d. Identical contractual interest rates;

    e. Similar assets as collateral; and

    f. The same aggregate unpaid principal amount or principal amounts within accepted "good delivery" standards for the type of security involved.

Staff Review Completed by: Julie Gann, NAIC Staff—June 2024

On August 13, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing, classified as a new SAP concept, and exposed revisions to *SSAP No. 86--Derivatives,* as shown above, to require bifurcation of debt securities with derivative wrappers or components if the item does not reflect a structured note. The guidance details the accounting and reporting guidance for the bifurcated debt and derivative components. This item was exposed until September 27, 2024 to allow for discussion at the 2024 Fall National Meeting.

On November 17, 2024, the Statutory Accounting Principles (E) Working Group elected to not proceed with the proposed edits to SSAP No. 86 to require bifurcation of debt securities with derivative wrappers or components. With this action, debt securities with derivative components that reflect structured notes will be retained in *SSAP No. 86—Derivatives*, and all other debt securities with derivative components and wrappers shall be assessed in accordance with the principles-based bond definition. Debt securities that do not qualify as bonds under the principles-based bond definition and shall be reported as non-bond debt securities in scope of *SSAP No. 21—Other Admitted Assets* and on Schedule BA. The Working Group did agree with proceeding with the clarifications in the investment disposal schedules, and the sponsoring of a blanks proposal, to ensure that a debt security sold to an

SPV and reacquired with derivative components is shown as a disposal and an acquisition in the investment schedules. With the action that occurred on November 17, 2024, this agenda item is limited to the investment schedule revisions as shown below:

December 2024 Proposed Revisions to Annual Statement Instructions:

Schedule D – Part 4 – Long Term Bonds and Stocks Sold, Redeemed or Otherwise Disposed Of During Current Year

This schedule should include a detailed listing of all securities that were sold/disposed of during the current reporting year that were owned as of the beginning of the current reporting year (amounts purchased and sold during the current reporting year are reported in detail on Schedule D, Part 5 and only in subtotal in Schedule D, Part 4). This should include all transactions that adjust the cost basis of the securities (except other-than-temporary impairments that are not part of a disposal transaction). ~~Thus, it~~This schedule should not be used for allocations of TBAs to specific pools subsequent to initial recording in Schedule D, Part 3 or ~~other~~ situations ~~such as~~that only involve CUSIP number changes. The following list of items provides examples (not all inclusive) of the items that should be included:

Pay downs of securities still owned (including CMO prepayments);

Subsequent partial sales of investment issues still owned;

Sales of securities to an SPV or other entity for which a new instrument is reacquired from the SPV/entity reflecting a combined instrument containing the original security and derivative instruments or other components (such as a credit repack note). The sale shall be captured on this schedule (or Schedule D, Part 5 if the debt security was acquired in the current year), and the new security shall be reported on Schedule D, Part 3.

Reallocation of the cost basis of an already owned stock to the cost basis of a new stock received as a dividend (e.g., spin off); and

Any decreases in the investments in SCA companies that adjust the cost basis, not including other-than-temporary impairments alone (e.g., subsequent return of capital from investments in SCA companies valued using the equity method).

Schedule D – Part 5 – Long-Term Bonds and Stocks Acquired During the Year and Fully Disposed Of During Current Year

As with Schedule D, Parts 3 and 4, this schedule should ~~not~~ be used for ~~a~~ transactions ~~unless it~~that affect~~s~~ the cost basis of the securities. ~~Thus, it~~This schedule should not be used for allocations of TBAs to specific pools subsequent to initial recording in Schedule D, Part 3 or ~~other~~ situations ~~such as~~ that only involve CUSIP number changes. Refer to the examples on Schedule D, Part 4 of transactions that should be captured.

On December 17, 2024, the Statutory Accounting Principles (E) Working Group exposed proposed annual statement instructions, as shown above under “December 2024 Proposed Revisions to 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 at the 2024 Fall National Meeting.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: ASU 2024-01, Scope Application of Profits Interest and Similar Awards

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In March 2024, FASB issued *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards,* which includes amendments to Topics 718 to provide clarifications on the application of guidance on stock compensation in the form of profits interest. The primary changes made were the creation of application examples and amendments to certain language in the Scope and Scope Exceptions Section of Topic 718 to improve clarity and operability without changing the guidance.

Because profits interest holders only participate in future profits and/or equity appreciation and have no rights to the existing net assets of the partnership, it can be complex to determine whether a profits interest award should be accounted for as a share-based payment arrangement (Topic 718) or similar to a cash bonus or profit-sharing arrangement (Topic 710, Compensation—General, or other Topics).

For statutory accounting assessments, prior U.S. GAAP guidance related to share-based payments has been predominantly adopted with modification in *SSAP No. 104—Share-Based Payments*. Statutory accounting modifications to the U.S. GAAP guidance have mostly pertained to statutory terms and concepts. (For example, statutory reporting lines, nonadmittance of prepaid assets, etc.)

Existing Authoritative Literature:
Stock compensation is addressed by *SSAP No. 104—Share-Based Payments* and *SSAP No. 95—Nonmonetary Transactions*.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
Agenda item 2018-35 adopted with modification *ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting* and incorporated the U.S. GAAP amendments from that ASU into SAP.

Agenda items 2016-19 and 2017-37 address the main ASUs related to *ASC Topic 606 Contracts with Customers* and there have been several other agenda items for minor updates to revenue recognition guidance, which have been rejected *in SSAP No. 47—Uninsured Plans*.

Agenda item 2023-07 addressed *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*, which was adopted with modification in 2023 to SSAP Nos. 47, 95, and 104.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None.

Convergence with International Financial Reporting Standards (IFRS):
None.

Staff Recommendation:
NAIC Staff recommends that the Working Group move this item to the active listing of the maintenance agenda, categorized as a SAP clarification, and expose 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*. The proposed revisions to SSAP No. 104 are illustrated below.

Proposed Revisions* to *SSAP No. 104—Share-Based Payments

Scope and Scope Exceptions

4. This statement applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in the grantor's own operations or provides consideration payable to a customer by either of the following:

a. Iissuing (or offering to issue) its shares, share options, or other equity instruments to an employee or nonemployee.or by

a.b. Iincurring liabilities to an employee or nonemployee that meet either of the following conditions:

i. The amounts are based, at least in part[1], on the price of the entity's shares or other equity instruments.

ii. The awards require or may require settlement by issuing the entity's equity shares or other equity instruments.

5. Share-based payments awarded to a grantee by a related party or other holder of an economic interest in the entity as compensation for goods or services provided to the reporting entity are share-based payment transactions to be accounted for under this statement unless the transfer is clearly for a purpose other than compensation for goods or services to the reporting entity. The substance of such a transaction is that the economic interest holder makes a capital contribution to the reporting entity, and that entity makes a share-based payment to the grantee in exchange for services rendered or goods received. An example of a situation in which such a transfer is not compensation is a transfer to settle an obligation of the economic interest holder to the grantee that is unrelated to goods or services to be used or consumed in a grantor's own operations. Reporting entities which issue profits interest or similar awards as compensation to either employees and nonemployees in exchange for goods or services shall apply the guidance in paragraph 4 in determining whether the award is a share-based payment transaction and in scope of this statement.

NAIC Drafting Note: Some of the relevant guidance added by ASU 2024-01 is included in illustrative examples. As SSAP No. 104 does not have illustrative examples, NAIC Staff drafted language (see tracked changes immediately above) using the guidance provided in the ASU illustrative examples and commentary.

Relevant Literature

127. This statement adopts with modification the U.S. GAAP guidance for share-based payment transactions reflected in FASB *Accounting Standards Codification (ASC) Topic 718, Compensation – Stock Compensation*, as modified by the ASUs listed in paragraphs 127.a. through 127.e., excluding the guidance in *ASC Subtopic 718-40, Employee Stock Ownership Plans* (ESOPs). Statutory accounting guidance for ESOPs is addressed in *SSAP No.*

[1] The phrase "at least in part" is used as an award of share-based compensation may be indexed to both the price of an entity's shares and something else that is neither the price of the entity's shares nor a market, performance, or service condition.

12—Employee Stock Ownership Plans. This adoption with modification includes the related implementation guidance reflected within the FASB Codification Topic 718 not reflected within this standard. The U.S. GAAP guidance adopted with modification reflects the adoption with modification of the following ASUs:

a. *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards*. The statutory modification did not incorporate the application examples and added additional language to clarify that profits interest and similar awards need to be considered under this statement.

~~a.~~b. *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer.*

~~b.~~c. *ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting*. The revisions from ASU 2018-07 expand the scope of ASC 718 to include share-based payment transactions for acquiring goods and services from nonemployees. With ASU 2018-17, *ASC 505-50, Equity – Equity Payments to Nonemployees* was superseded.

~~c.~~d. *ASU 2017-09, Scope of Modification Accounting*

~~d.~~e. *ASU 2016-09, Improvements to Employee Share-Based Payment Accounting*

~~e.~~f. *ASU 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*

~~f.~~g. *ASU 2010-13, Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Current of the Market in Which the Underlying Equity Security Trades*

Effective Date and Transition

132. Since the initial adoption of SSAP No. 104, subsequent revisions were effective as follows:

a. *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards* was adopted with modifications. This SAP clarification is effective December 31, 2025.

~~a.~~b. *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*. The SAP clarification is effective August 10, 2022.

Staff Review Completed by:
NAIC Staff – William Oden, September 2024

On November 17, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing and exposed revisions, as shown above, 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*.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: SSAP No. 16 Clarifications

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: NAIC staff were contacted about a question related to *SSAP No. 16—Electronic Data Processing Equipment and Software*. While working on the issue, staff noted several instances in the SSAP where the FASB ASC Topic has been referenced directly instead of the ASU. When guidance is adopted by FASB, it is issued through an accounting standards update which formally adopts the guidance into the FASB Accounting Codification. The Working Group will then address the guidance in the ASU, which is the guidance at a moment in time instead of the actual ASC, which represents guidance that will change over time as other ASUs are adopted. As the guidance stands now, a new ASU could be issues that impacts the ASC sections that are referenced in the SSAP, thereby changing statutory accounting guidance without the Working Group addressing and considering the issue.

Existing Authoritative Literature: There are multiple instances that need to be addressed in SSAP No. 16, which are detailed below in the Staff Recommendation.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Recommendation: NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose revisions to *SSAP No. 16—Electronic Data Processing Equipment and Software*, to include proper references to the specific FASB ASU or SOP when not specifically referenced in the SSAP, as illustrated below.

8. This statement adopts with modification FASB Codification 985-20, Software - Costs of Software to be Sold, Leased or Marketed (ASC 985-20), as revised by *ASU 2009-14, Certain Revenue Arrangements That Include Software Elements*, to preclude the capitalization of software development costs and to reject guidance regarding the treatment of capitalized costs. Additionally, this statement rejects FASB Codification 985-330, Software - Inventory (ASC 985-330). Statutory modifications to ASC 985-20 and rejection of ASC 985-330 precludes capitalization of costs, and requires such costs to be expensed, for:

10. This statement adopts with modification *FASB Accounting Standards Codification (ASC) 350-40, Internal Use Software* (ASC 350-40), as originally adopted as part of SOP 98-1, as described in this statement. (This adoption reflects adjustments to ASC 350-40 from *ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*.) This statement also adopts *FASB Accounting Standards Codification 350-50, Website Development Costs* (ASC 350-50) in its entirety.

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

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

b. The implementation costs shall be amortized over the lesser of the term of the hosting arrangement, or five years. (This statement adopts the provisions in ASC 350-40-35-13 through ASC 350-40-35-17, as originally adopted with modification as part of SOP 98-1, for determining the term of the hosting arrangement and for when amortization shall begin.) The amortization cost shall be recognized as depreciation of the nonoperating system software. (This is a modification from U.S. GAAP as the amortization is not recognized in the same expense line as the service contract lease.)

Staff Review Completed by: Jake Stultz—NAIC Staff

On November 17, 2024, the Statutory Accounting Principles (E) 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).

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/03 - 24-25 - SSAP 16 Clarifications.docx

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Statistical Issue Paper No. ~~xxx~~170

~~New Market~~ Tax Credits Project

STATUS
Exposure Draft – August 13, 2024

Original SSAP: SSAP No. 93 and SSAP No. 94R
Current Authoritative Guidance: SSAP No. 93 and SSAP No. 94

Type of Issue:
Common Area

SUMMARY OF ISSUE

1. The purpose of this issue paper is to document for the historical record the ~~substantive~~ conceptual changes to statutory accounting guidance detailed in *SSAP No. 93—Investments in Tax Credit Structures* and *SSAP No. 94—State and Federal Tax Credits*, respectively.

2. This issue paper illustrates tracked changes in SSAP No. 93 and SSAP No. 94R, effective January 1, 2025. The ~~substantive~~ conceptual revisions to SSAP No. 93 and SSAP No. 94R include revised accounting guidance on tax ~~equity and bond~~credit investments~~,~~ and purchased tax credits ~~earned or purchased~~. The adopted revisions to SSAP No. 93, SSAP No. 94R, *SSAP No. 34—Investment Income Due and Accrued*, and *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* are illustrated as tracked changes in Exhibits A, B, and C, respectively. Exhibit D is a flowchart which details the order of operations for applying the revised SSAP No. 93.

Drafting Note: On August 13, 2024, the Working Group adopted revisions to remove the "R" identifier from SSAP titles and references within the AP&P Manual. As 2022-14 was adopted prior to this change, the "R" identifiers have been maintained throughout the issue paper for the sake of clarity and consistency to the original discussions.

DISCUSSION

3. This issue paper provides a historical reference that includes tracked changes adopted within SSAP No. 34, SSAP No. 48, SSAP No. 93 and SSAP No. 94R. The conceptual changes were a result of the passage of the Inflation Reduction Act (IRA) and the Financial Accounting Standards Board (FASB) adopting *ASU 2023-02, Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method* (ASU 2023-02) which amends ASC Topic 323 to allow reporting entities to consistently account for equity investments made primarily for the purpose of receiving income tax credits and other income tax benefits.

4. The IRA was signed into law by President Biden effective August 16, 2022. The tax law was expansive but had a significant effect on the tax laws underlying several significant federal tax credit programs. The changes to the wind and solar tax credit programs, which were effectively extended for 12 years (10 years plus a 2-year phase out), were particularly significant as the programs had previously been extended for brief periods of time at each renewal. Additionally, while the overall base tax credit rate was lowered for most tax credit programs, the total potential tax credits generated from these tax credit programs was increased (potentially as much as 5x to 6x the base rate) through the provision of bonus tax credits. To qualify for these bonus tax credits the project must meet specific wage, labor, material, or project location requirements. Other significant changes included expansion of the ability to transfer/sell certain types of tax credits to for-profit entities and the creation of a 2025 statutory transition for the technology specific Production Tax Credits (PTCs) and Investment Tax Credits (ITCs). Subsequent to

2025, PTCs and ITCs will be superseded by technology neutral tax credits known as Clean Electricity Production Tax Credits (CEPTC).

5. From a statutory accounting perspective, a tax credit investment is an asset representing a future stream of tax credits and benefits, which can be used to pay policyholder obligations by either offsetting tax liabilities, selling the allocated tax credits on a secondary market, or through receipt of a tax refund for the tax credits. This definition is one of the main foundational concepts used while formulating the SSAP No. 93R draft. While most tax credit investments may be sold, the primary purpose of acquiring a tax credit investment is to generate tax credits which benefit reporting entities, most commonly through a reduction in tax liability~~ or, when permitted by IRS or state tax provisions, through the sale of certificated/transferable tax credits~~. As the primary purpose of these investments is the generation of tax credits, impairment guidance focuses on the investment's ability to generate tax credits and admittance guidance focuses on the ability of the company to utilize the tax credits to be received (clean initial tax opinion and unqualified annual audits) and the reporting entity's ability to utilize these tax credits (prospective utilization assessment).

6. While ASU 2023-02 was adopted with modification, it should be noted that the revisions to SSAP No. 93 were ultimately more expansive than those adopted to U.S. GAAP by ASU 2023-02. These departures are discussed in detail in SSAP No. 93R, paragraph 36.

Actions of the Statutory Accounting Principles (E) Working Group

7. In August 2022, FASB issued *Proposed Accounting Standards Update Investments—Equity Method and Joint Ventures (Topic 323)—Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method*. On December 13, 2022, the Working Group moved agenda item *2022-14: New Market Tax Credits* to the active listing, categorized as a new SAP concept, and exposed a discussion document to expand current statutory accounting guidance for low-income housing tax credits to capture all tax equity investments that provide general federal business tax credit and state premium tax credits if they meet specified criteria. The initial discussion document utilized the August 2022 Proposed ASU as the basis for the changes to SSAP No. 93 and included 12 specific discussion items.

8. On February 10, 2023, the Working Group received a comment letter from interested parties which provided responses to the discussion items detailed in document 2022-14b. Interested parties' comments and the Working Group's responses are detailed below:

a. **Comment:** Interested parties agreed that all investments, no matter what legal form, which primarily earn tax credits should utilize the proportional amortization method. It is noted that the discussion document appeared to only scope in tax equity investments and that interested parties would suggest the inclusion of language to either include tax credit bonds or clarify their exclusion from SSAP No. 93. As part of this clarification, interested parties asked if the Working Group intends to change CAPCO guidance or continue to allow CAPCOs to be reported on Schedule D. Interested parties noted that tax credit bonds are currently being reported on Schedule D and if the intent is to move these investments to Schedule BA, then interested parties would request that they be allowed to report with an NAIC designation, which reflects the low-risk nature and high-credit quality implicit in tax credit bonds.

i. **Response:** As a result of interested parties' comments, the Working Group directed NAIC staff to expand its draft of SSAP No. 93R to include tax credit bonds but directed that the CAPCO guidance remain in place and not be extended to other tax credit bonds as this is a legacy one-off exception. Additionally, it is the intent of both the bond project and the draft of SSAP No.

93R that investments in which the primary returns are tax credits are to be reported on Schedule BA.

b. **Comment:** Interested parties noted no issues with requiring the proportional amortization method under statutory accounting, which is a departure from U.S. GAAP which makes the proportional amortization method an election. Interested parties would also like to confirm that the 'Substantially All Projected Benefits" criterion along with the rest of the criteria are assessed at the time of purchase of the investment and not at every reporting period. Interested parties also noted that if NAIC staff intend to include tax credit bonds in the scope of SSAP No. 93, then the scoping criteria will need to be amended. Additionally, interested parties included an appendix of tax credit investments issued in debt/bond form to aid NAIC staff.

i. **Response:** NAIC staff noted that the paragraph which precedes the scope criterions notes that investments must meet these criteria at the point of initial investment. The Working Group reviewed interested parties' list of tax credit bond investments and noted the following:

(a) *Certified Capital Companies (CAPCOs):* As noted above, the Working Group does not intend to amend the existing carveout guidance for CAPCO investments as part of the SSAP No. 93R draft.

(b) *Other State Tax Credits issued in Bond Form and Federal New Market Tax Credit (NMTC) Programs:* As the described investment vehicles issue securities to investors through the issuance of equity, these tax credit investment examples would firmly fall within the tax equity investment category rather than as true tax credit bonds. Further revisions will be made within the SSAP No. 93R draft guidance that any tax investment which includes an equity component, however nominal, would be considered a tax equity investment rather than a tax credit bond.

(c) *State or Municipal Tax Credit Bond Strips*: At the Working Group's direction, NAIC staff have included Tax Credit Bond Strips within the SSAP No. 93R draft guidance as an example of a tax credit bond (Note: This was later clarified to only include tax credit strips which had stripped the future stream of tax credits from a debt security). NAIC staff also included a footnote noting that BABs and QTCBs are examples of tax credit bonds.

c. **Comment:** Interested parties noted that guidance needs clarification on the inclusion of tax credit investments structured as bonds. Additionally, interested parties noted that there are other exceptions to the "at-risk" requirement for tax credit investments as well as the guaranteed returns exclusion.

i. **Response:** At the Working Group's direction, NAIC staff removed references to yield/return guarantees and at-risk requirements for certain tax credit programs from the SSAP No. 93R draft. As these requirements and exclusions can change program to program and state to state, trying to detail specific guidance on these issues would be cumbersome and easily made out-of-date. Additionally, the current version of the SSAP No. 93R draft requires a fund level tax opinion for tax credit investments which would be required to provide a high confidence

level on the efficacy of any yield/return guarantees and whether the investment vehicle is subject to 'at-risk' rules.

d. **Comment:** Interested parties noted that existing statutory accounting guidance requires the amortization of LIHTC tax equity investments be recorded in net investment income, whereas U.S. GAAP has proportional amortization recorded to the income tax line along with the earned and utilized tax credits.

i. **Response:** The initial draft proposed revisions to make the statutory accounting treatment for PAM expense substantially consistent with U.S. GAAP. The original intent for segregating proportional amortization activity from the income tax line was out of concern for any non-tax income or gains recognized from the investment. Current U.S. GAAP guidance stipulates that any non-tax income or gains are to be recognized as investment income which addresses this concern. However, upon further discussion with the Working Group it was determined that inclusion of the proportional amortization in income taxes would result in errors on the Schedule BA Verification between Years and on the Exhibit of Net Investment Income. The cost basis of Tax Credit Investments would be recorded to Schedule BA, but if the amortization were to be excluded from net investment income, then the change in the book value of investments would not roll. Upon review of the initial draft proposal, the Working Group determined that while changes could be made to the Schedule BA Verification between Years and the Exhibit of Net Investment Income, these updates would represent significant changes to these forms. The Working Group decided that the best path forward was to map out the changes that this would require to both schedules and then present it to the state insurance regulators for input (Note: Discussions with state insurance regulators and interested parties later determined that convergence with U.S. GAAP on this issue was not feasible due to the significance of the changes needed to the annual statement).

e. **Comment:** Interested parties noted that one additional difference between statutory and U.S. GAAP accounting treatment of proportional amortization is that under U.S. GAAP, there are no DTAs set up for tax credit carryovers since the amortization and the tax credits are reported in the same line.

i. **Response:** As of the NAIC 2023 Spring National Meeting, the Working Group directed NAIC Staff to expand the ~~New Market~~ Tax Credits Project to also include SSAP No. 94R, which addresses the recognition of purchased tax credits. Based on current revisions, federal tax credits which cannot be utilized are subject to DTA guidance as detailed in *SSAP No. 101—Income Taxes*.

f. **Comment:** Interested parties believe that the non-admittance criteria detailed in the discussion document are too punitive as it would require the reporting entity to non-admit the entire investment if it does not have taxable income in a given year. Interested parties also questioned whether there is overlap between the non-admittance criteria and the impairment criteria. Additionally, interested parties requested clarification that the tax opinion requirement was only for the initial year of investment.

i. **Response:** At the Working Group's direction, the non-admittance criteria was modified to ensure that it was clearly separate for impairment guidance and relax the non-admittance criteria so that the investment is not fully non-admitted if the entity has a short period of no taxable income. As part of these changes, a 3-year

window in which the tax investment is fully admitted less any tax credit amounts not anticipated to be used. The updated guidance is intended to non-admit tax credit investments only to the extent a portion of the credits earned during that period cannot be used. In the event the reporting entity cannot substantially utilize those 3 years of tax credits an assessment must be performed to determine how much of the total investment cost basis can be admitted. (Note: The admittance test described here was substantially revised in 2024. See the prospective utilization assessment.)

Revisions were also made to clarify that the tax opinion requirement is required at the point of initial investment by the reporting entity, as well as to add additional guidance on the scope and required confidence level expressed by the tax opinion.

g. **Comment:** Interested parties agreed that loss contingency guidance is appropriate for determining if future contributions give rise to a liability.

   i. **Response:** None.

h. **Comment:** Interested parties did not have an objection to incorporating fair value in the assessment of impairment.

   i. **Response:** None.

i. **Comment:** Interested parties noted that under question 8.f, non-admitting the entire investment appears too punitive for companies that expect to utilize the credits in a later year. Interested parties agreed that impairment would occur when the credits will not emerge at all. Question #6 needs to be clarified to explain these concepts since the way it is currently written, it seems to scope in the impairment criteria into the non-admission review.

   i. **Response:** See the response detailed in paragraph 8.f.

j. **Comment:** Interested parties did not have an objection to disclosing information about the nature of investments for which tax credits are earned. Paragraph 27(b) seems repetitive with the other information that is being required under paragraph 28 regarding the amount of tax credits and other tax benefits during the years presented.

   i. **Response:** The Working Group aims to conform to U.S. GAAP where feasible and these disclosures were pulled from the proposed ASU. Regarding the concerns of duplication, the guidance in paragraph 27 requires qualitative disclosures on tax credit investments (method of accounting used, nature of the investment, etc.) whereas paragraph 28 requires primarily quantitative disclosures of tax investment financial data.

k. **Comment:** Interested parties noted that while most disclosures are substantively the same as was previously required under SSAP No. 93, except the 15-year future realization of tax credit disclosure which is more detailed than most other investments and would require additional work to prepare.

   i. **Response:** The Working Group agreed with Industry that the 15-year future realization disclosure was more detailed than is required for other investments,

and directed NAIC Staff to remove these disclosures, and reduce the future realization disclosure to 5 years and thereafter.

l. **Comment:** Interested parties noted that the additional disclosure requirements for tax credit investments in excess of 10% of admitted assets should be removed as they believe the detail does not provide relevant information and it would be quite rare for an insurer to have tax credit investments of such significance.

i. **Response:** The Working Group agreed that such a situation would be rare, and that it does not make sense to codify a separate set of disclosure requirements for such an unusual situation. NAIC staff were directed to remove these additional disclosures in their entirety.

m. **Comment:** Interested parties provided several other general comments on the discussion document which were: 1) Clarification on the difference between SSAP No. 93 and SSAP No. 94R on the matter of certificated tax credits. 2) SSAP No. 94R currently requires purchased tax credits to be recorded under "Aggregate Write-Ins for Other Than Invested Assets". 3) Gains and Losses on certificated tax credits are required to be reported in other income per SSAP No. 94R whereas SSAP No. 93 requires inclusion of gains and losses from tax equity investments to be reported in net investment income.

i. **Response:** The Working Group direct NAIC Staff to draft revisions to SSAP No. 93R and SSAP No. 94R to clarify the usage and inter-relationship of these SSAPs. As part of the revisions to SSAP No. 94R directed by the Working Group, NAIC staff will propose moving the reporting of federal tax credits from within the "Aggregate Write-ins for Other Than Invested Assets" line to inclusion within the reporting line for DTAs. The SSAP No. 93R draft will also be revised to provide guidance on tax credit investments whereas SSAP No. 94R would provide guidance on both allocated and purchased tax credits. (Note: The guidance discussed in this paragraph was substantially revised later on during 2023. As in, tax credits allocated from SSAP No. 93R investment are NOT within the scope of SSAP No. 94R.)

9. In March 2023, FASB issued and adopted ASU 2023-02. A comparison of the final ASU to the proposed ASU and noted during that most of the changes made to the final ASU would have no effect on the revisions proposed for SSAP No. 93 as the use of the proportional amortization would be a requirement under statutory accounting rather than an election. As a result of its review of the final ASU, new language to replace existing SSAP No. 93 language in SSAP No. 48 was drafted for Working Group review.

10. At the NAIC 2023 Spring National Meeting, the Working Group directed NAIC staff to draft statutory accounting guidance in the form of a new or revised SSAP that expands the current LIHTC guidance for equity investments that general federal business tax credit and state premium tax credits.

11. During April 2023, the Working Group discussed further proposed changes to the SSAP No. 93R draft. Significant changes resulting from this discussion were as follows:

a. References to equity and bond style tax credit investments were further simplified to generically refer to 'tax credit investments' with the intent to capture any investment vehicle that generates returns primarily in the form of tax credits and tax benefits. Additionally, there were concerns expressed that the inclusion of bond terminology within the SSAP No. 93R draft could cause confusion or conflict once the Principles

Based Bond Definition (PBBD) project was completed and adopted for statutory accounting purposes. Tax credit debt instruments would certainly not qualify as bonds under the new bond guidance and the decision was made to remove references to "tax credit bonds" or "tax equity investments" except where strictly necessary for clarification purposes.

b. Admittance of tax credit investments were discussed in detail and the determination was made to separate the requirements into three parts: 1) Require companies to obtain an initial year tax opinion thus defined to include the fund and the projects and, as part of this definition, guidance was added regarding the confidence level required for the tax opinion to support admittance. 2) Require annual audits of tax credit investments. Based on discussion with industry experts, an audited financial statement requirement should not result in additional costs incurred by insurers as audits are typically performed as a matter of course on tax equity investment entities. To ensure that valid tax investments aren't nonadmitted due to a delay in audit completion, an allowance for insurers to use the prior year's audit as an alternative as well as a carve out from the annual audit requirement for any tax credit investments which, by virtue of their structure, could not be audited. It should be noted that the intent of the carve out was to prevent the annual audit requirement effectively non-admitting tax credit investments structured as debt securities. However, it was also the intent that any component of equity ownership involved in the investment, no matter how nominal, would exclude it from this carve out.

c. Additional changes were made to the sections detailing accounting guidance on future equity contributions and additional tax credits. It was noted that the version presented in the discussion document could result in a situation where the reporting entity would be required to recognize a liability and expense on future contributions as the SSAP No. 93R draft requires any equity contributions not resulting in additional tax credits to be expensed. The Working Group determined that not only did this miss the mark on proper application of the matching principle, but it was also unnecessarily punitive. Based on this discussion, the proposal was amended to require the accrual of a liability for future equity contributions which result in additional tax credits, but only disclosures are required if the future equity contributions do NOT result in additional tax credits. Furthermore, the Working Group discussed what potential benefit would be gained by requiring companies to segregate additional tax credits allocated from future equity contributions and determined that no value was gained from this requirement. As such, the revisions to the SSAP No. 93R draft were changed to allow for the existing amortization schedule for the investment to be adjusted on a prospective basis for additional tax credits allocated.

d. NAIC staff noted that one of the more significant departures from existing U.S. GAAP and statutory accounting guidance was the exclusion of proportional amortization from income taxes. Under current statutory accounting guidance, proportional amortization from LIHTC investments is recorded to net investment income which (above the line or as component of net income) on the annual statement, whereas U.S. GAAP accounting guidance has proportional amortization recorded as a component of income taxes (below the line or after net income). At the direction of the Working Group, NAIC began to explore converging with U.S. GAAP on this issue. Initially, NAIC staff believed that guidance it would be fairly simple to converge statutory accounting with existing U.S. GAAP guidance on this issue but upon further review and discussion of the annual statement NAIC staff became unsure whether this was feasible. One of the main concerns identified was that if proportional amortization from tax credit investments was not run through net investment income, then a reconciling item would be required to ensure the

Exhibit of Net Investment Income and Schedule BA Verification between Years rolls properly. Otherwise, net investment income per Schedule BA would not be recalculable to the exhibit of net investment income and the Schedule BA verification would fail its cross-checks. NAIC staff mapped out the changes that would be required to the blanks to conform statutory recognition of proportional amortization to U.S. GAAP. NAIC staff's initial draft Blanks proposal included a reconciling item to the Exhibit of Net Investment income to back-out proportional amortization from tax credit investment recognized in income taxes, and bi-furcation of row 8, 'Deduct amortization of premium and depreciation' between amounts recognized from SSAP No. 93R investments and other types of investments. Based on this initial draft, the Working Group determined that convergence with U.S. GAAP was not practical as it would require a number of changes to the blanks, verifications, and instructions. While it would be possible, tax credit investments do not currently represent a significant position on insurer portfolios, and it would not be reasonable to substantially change reporting lines and schedules simply to convergence with U.S. GAAP on what amounts to a minor reporting variance. At the direction of the Working Group, the changes to the SSAP No. 93R draft to converge statutory reporting of proportional amortization expense with U.S. GAAP were scrapped.

12. On May 16, 2023, the Working Group exposed revisions to SSAP No. 93 and SSAP No. 94R. The revisions to SSAP No. 93 propose adoption with modification of ASU 2023-02, which would include modifications to scope in all qualifying state and federal tax credit investments regardless of structure or the underlying tax credit program. The revisions to SSAP No. 94R expanded its scope to include all state and federal tax credits whether purchased or allocated, and that tax credits received should be recorded at face value with losses realized immediately and gains deferred on the balance sheet.

13. On June 30, 2023, the Working Group received a comment letter from interested parties on the exposed revisions to SSAP No. 93 and SSAP No. 94R. Interested parties provided several comments on both SSAPs which are summarized below along with the Working Group's responses. The interested party comments provided on the SSAP No. 93R draft were:

a. **Comment:** Interested parties noted that paragraph 3 does not provide specific direction for which SSAPs would be applicable for tax credit investment which do not fall within SSAP No. 93.

i. **Response:** The Working Group agreed with the recommendation and directed NAIC Staff to update SSAP No. 93R, paragraph 3 to provide readers with specific SSAPs which could apply to non-qualifying equity or debt structure tax credit investments.

b. **Comment:** Interested parties noted that the current draft directed readers to refer to SSAP No. 94R for how to account for tax credits allocated from tax credit investments. They felt that this cross-reference was confusing and could potentially lead to conflicting interpretations.

i. **Response:** To reduce confusion, the Working Group directed NAIC staff to remove the paragraph directing readers to SSAP No. 94R and instead pulled in the specific paragraphs from SSAP No. 94R which would be applicable to tax credits allocated from tax credit investments.

c. **Comment:** Interest Parties noted that they were unclear on whether the tax credits earned, or the tax credit investments were subject to the admittance criteria detailed in SSAP No. 93R paragraphs 18.a.-18.c. Interested parties felt that admissibility concerns

are adequately addressed by the tax opinion and audit requirements. Additionally, if NAIC staff's concern is the admittance of tax credits carried forward to a future period, then this should be adequately addressed by the admittance rules detailed in SSAP No. 101 for deferred tax assets. Interested parties suggested that paragraphs 18.a.-18.c. be deleted in full.

i. **Response:** NAIC staff noted that the admittance rules detailed in SSAP No. 93R paragraphs 18.a.-18.c. do NOT provide guidance on the admittance of allocated tax credits. For tax credit investment structures to fall within the scope of the SSAP No. 93R draft, substantially all benefits must be from tax credits or other tax benefits which essentially means that balance of a tax credit investment represents a future stream of tax credits and tax benefit. As such, the admittance rules in paragraph 18.a.-18.c. would require a company to assess its ability to utilize that future stream of tax credits to what amount of the tax credit investment would be non-admitted. If the company's projections determine it will be unable to substantially utilize the future stream of tax credits (i.e., the tax credit investment balance) then potentially all or a portion of the tax credit investment would be considered non-admitted as the company is unable to utilize the future stream of tax credits to offset tax liabilities. (Note: The admittance test discussed in this paragraph was substantially revised in 2024. See the prospective utilization assessment.)

ii. In response to these comments, the Working Group directed NAIC staff to revise SSAP No. 93R paragraphs 18 through 18.c. to further clarify the intent and purpose of the guidance, as well as the order of operations to be followed when assessing the reporting entity's ability to utilize unallocated tax credits from the investment were incorporated.

iii. Tax credit investments are essentially an asset representing a future stream of tax credits and benefits, which could be used to pay policyholder obligations by either offsetting tax liabilities, sale on a secondary market, or through receipt of a refund. However, if a reporting entity is unable to utilize the tax credits and benefits received from these investments due to the reporting entity's financial performance then the benefits received from the tax credit investment would no longer represent an asset that can be used to pay policyholder obligations. SSAP No. 93R paragraphs 18 and 18.a. would require the reporting entity to nonadmit the investment, either partially or fully, due to its inability to utilize the future stream of tax credits and benefits. This differs from impairment as the intent is not to assess the investment's viability, but rather to assess the company's ability to utilize the future stream of tax credits and benefits. Without these paragraphs, there would exist no mechanism in statutory accounting guidance, which would require a poorly performing company (for example, one which has fallen below the RBC control threshold) to nonadmit tax credit investments, even though they cannot be used to pay policyholder benefits since the tax credits cannot be utilized. Paragraphs 18.b. and 18.c. provide a carve out for the admittance of tax credit investments which provide transferable/certificated or refundable tax credits. (Note: The admittance test discussed in this paragraph was substantially revised in 2024. See the prospective utilization assessment.)

d. **Comment:** Interested parties noted that U.S. GAAP requires retrospective adoption of ASU 2023-02 and that this would result in U.S. GAAP vs. statutory accounting differences.

i. **Response:** In response to industry's concerns on differences between U.S. GAAP vs. Statutory implementation, the Working Group directed NAIC Staff to update the draft of SSAP No. 93R to be adopted retrospectively to conform with industry's request. (Note: It was later clarified by interested parties that this comment was a question rather than a request. Upon adoption in 2024, the revisions in the SSAP No. 93R draft are to be applied prospectively.)

14. The interested party comments provided on SSAP No. 94R were:

a. **Comment:** Interested parties requested that paragraph 1 of the Scope of Statement section be amended to clarify which types of tax credits are within scope of SSAP No. 94R. Interested parties felt that the key difference between SSAP No. 94R and SSAP No. 93 is that the former is for purchased tax credits and the ladder is for tax credits earned from investments.

i. **Response:** The Working Group generally agreed with the comments provided but directed NAIC staff to remove the term "certificate" from the requested changes. The intent of SSAP No. 94R is to provide guidance on all purchased state and federal tax credits, not just certificated tax credits. Additional language was also added to clarify the scope of SSAP No. 94R for allocated tax credits, as detailed in the next Response paragraph.

b. **Comment:** Interested parties noted that they do not believe allocated tax credits from SSAP No. 93 investments should be within the scope of SSAP No. 94R as the guidance was confusing and could potentially lead to conflicting interpretations. Additionally, Interested Parties believe that tax credits from investments vs. purchased tax credits are distinctly different assets. The only similarity in accounting for the tax credits relates to instances when the credits earned under a SSAP No. 93 investment cannot be utilized in the current year. Under that scenario, a DTA would be recorded, which would be subject to the admissibility rules under SSAP No. 101.

i. **Response:** In response to the interested parties' comments, the Working Group elected to remove tax credits allocated from SSAP No. 93R investments from the scope of SSAP No. 94R to avoid confusion when application the statutory accounting guidance. As a general note from the Working Group, irrespective of whether the tax credits are allocated from an investment or purchased outright, the tax credits received represent the same type of financial instruments which can be utilized as an offset to tax liabilities, sold, or redeemed for cash as a tax refund. Additionally, irrespective of how the tax credits are received they are recorded at face value upon acquisition. The only significant difference is that tax credits purchased at a premium or discount may result in a recognized loss or deferred gain, respectively, whereas any premium or discount on an allocated tax credit is implicit in the recognition of the proportional amortization.

ii. At the direction of the Working Group, additional language was also added noting that allocated tax credits earned from tax credit investments NOT within the scope of SSAP No. 93R should refer to SSAP No. 94R for guidance on how to record allocated tax credits. It was noted that without this language there would be no guidance within Accounting Practices and Procedures Manual for how to account for tax credits allocated from Non-SSAP No. 93R investments (see issue paper paragraph 15 below for further discussion on this guidance).

c. **Comment:** Interested parties noted that most tax certificates reduce a reporting entity's tax liability and do not directly impact the income statement at the time they are used. In addition, interested parties believe that upon purchase, the tax credits should be reported as an other-than-invested asset since the asset represents a right to receive future benefits. As the tax credits become available for use, a reduction to the insurer's income tax payable or premium/state taxes payable should take place.

i. **Response:** The Working Group disagrees with this proposed change as purchased federal tax credits would be reported as other-than-invested assets, versus allocated federal tax credits which would be reported as a deferred tax asset. This would result in the same type of asset being reported on two separate lines based on the manner in which it was acquired. As noted above, the Working Group position is that allocated and purchased tax credits are substantially the same assets irrespective of the way in which they are acquired. Additionally, interested parties also propose that if a tax credit cannot be utilized in the same period in which it was purchased it should be transferred to Deferred Tax Assets. This would not resolve the short-term reporting discrepancy noted previously and adds further complications to the accounting process by requiring a reporting line transfer if the asset is held for longer than a year. As such, at the direction of the Working Group, these changes were not incorporated into the proposed revisions.

d. **Comment:** Interested parties noted that the accounting for purchased tax credits in the SSAP No. 94R exposure is different from the current guidance in that the credits will be recorded at face value instead of at cost. This is not an issue perse, but interested parties did want to point out this discrepancy as compared to the accounting treatment for other assets like bonds and mortgage loans.

i. **Response:** The Working Group's position is that tax credits, whether received via purchase or allocation, do not represent investments, and has opted to propose accounting guidance that differs from bonds or mortgage loans. The position that tax credits do not represent investments was the main reason for the original SSAP No. 94R guidance which required state tax credits be recorded to Other Than Invested Assets and effectively required tax credits purchased at a discount to defer the gain off the balance sheet by recording the acquired tax credit at cost. The revised guidance currently proposed should be less confusing and provide a more accurate financial picture to record acquired tax credits at face value and defer any gains from discount purchases on the balance sheet.

e. **Comment:** Interested parties proposed changes to Exhibit B to reflect a pro-rata utilization of purchased tax credits in relation to the quarterly accrual of income tax liabilities. The main purpose of these changes was to reflect interested parties' proposed changes in item #2.

i. **Response:** Exhibit B was updated to incorporate revisions proposed by interested parties and recognizing tax credit utilization is also applicable to exposed draft of SSAP No. 94R.

15. Outside of the changes made in response to the interested parties' comment letter, both exhibits in the SSAP No. 93R draft were revised based on discussions with the Working Group to provide example journal entries of the Proportional Amortization method. As part of this revision, the assumptions in Exhibit B were revised so that a journal entry example could be provided for a residual sale at the end of the proportional amortization period. Additionally, a new footnote was also added to SSAP No. 94R

based on informal comments the Working Group received from the public. The new footnote provides clarification on what constitutes a purchased tax credit vs. an allocated tax credit. Purchased tax credits are typically acquired through receipt of a tax credit certificate (certificated) or execution of a transfer form (transferable).

a. The distinction made between a purchased vs. allocated tax credits is intended to address concerns that companies could improperly recognize tax credit investment transactions as tax credit purchases (e.g. expensing equity contributions). Insurers should first consider whether their tax credits are purchases, as defined by footnote 1 in SSAP No. 94R. If the tax credits are received through other means, for example a Form K-1, are indicative of an allocation from an investment. Any investment which allocates tax credits must be assessed to determine if it is within the scope of SSAP No. 93R.

b. Assuming this assessment has already been performed, the insurer may still look to SSAP No. 94R for accounting guidance on how to recognize and utilize tax credits allocated from investments NOT within the scope of SSAP No. 93R. The Working Group's intent with the revised guidance was to clearly disallow tax credit investments from being accounted for under SSAP No. 94R, while still providing some measure of accounting guidance for how to recognize and utilize tax credits allocated from investments NOT within the scope of SSAP No. 93R.

16. In June of 2023, the Working Group received a comment letter from interested parties on the Bond Definition Project which addressed the Schedule BA reporting lines. Included in this comment letter were notes on changes to the Blanks for tax credit investments. Based on NAIC staff's review, the following Blanks Instruction pages identified as potentially needing updates to conform with the proposed revisions to SSAP No. 93 and SSAP No. 94R (the following page numbers are from the Life blank instructions):

a. *Other Invested Assets - Pg. 29:* Line 8 to be updated for new title of SSAP No. 93R.

b. *Disclosures - Pgs. 165, 241, 268, 273:* Page 165 to be replaced with disclosures detailed in SSAP No. 93R, and update page 241 for new language. Page 268 & 273 to be replaced with disclosures detailed in SSAP No. 94R.

c. *Reserve Calculation Instructions - Pg. 372:* Update instructions for changes.

d. *Schedule BA Instructions - Pgs. 522, 523, 527:* Replacement of all existing Low Income Housing Tax Credit categories, Line Numbers 3599999-4499999, and replacement of instructions for these lines on page 527.

e. *Schedule BA Examples - Pg 526:* Update for new language and examples in updated SSAP No. 93R.

17. The following Blanks forms require update for the current proposal (the following page numbers are from the Life Blanks):

a. *Exhibit of Net Investment Income (Pg. 8):* No changes required.

b. *Schedule BA (Pgs. E07-09):* No changes required.

c. *Schedule BA Verification (Pg. SI03):* Add proportional amortization to the title of row 8.

d. *Asset Valuation Reserve (Pg. 35):* Update LIHTC language for updated line numbers, as noted in 13.3i. – 13.3iii above.

18. At the NAIC 2023 Summer National Meeting, the Working Group exposed additional revisions made to SSAP No. 93 and SSAP No. 94R, and directed NAIC staff to work with interested parties to draft revisions to the annual statement instructions and reporting updates.

19. Subsequent to the NAIC 2023 Summer National Meeting, the Working Group direct NAIC staff to make the following changes:

a. *Tax Credit Strips from Equity Investments:* The Working Group received an informal comment from the public on footnote 4 in the SSAP No. 93R draft and amended it accordingly to note that tax credit strips created from equity method investment tax credit streams would NOT qualify for the audit exception as the underlying source of the tax credits is, in fact, from an auditable entity. A tax credit strip is simply an instrument which separates the ownership of the tax credits earned from the ownership of the tax credit investment. Stripping the future stream of tax credits from a tax equity investment entity to be sold separately from the equity ownership does not negate the requirement to audit the investor entity and, in turn, the underlying assets generating the stripped tax credit benefits. This clarification was specifically intended to prevent a practice that could be used to circumvent the audit requirement; simply because the stream of tax credits have been stripped from the tax equity investment and placed into a structure resembling a debt instrument does not mean the company can forgo annual audits. In this situation, the company would still need to receive qualifying audits from the tax equity entity which originally held the stream of tax credits.

b. *Unused Allocated Tax Credit Disclosures:* NAIC staff noted that the SSAP No. 93R draft did not have disclosures for unused allocated tax credits. As there is no fundamental difference between a tax credits asset that was acquired via allocation vs. purchase, it made no sense to exclude tax credits received from SSAP No. 93R investments from the majority of the tax credit disclosures required in SSAP No. 94R. The Working Group directed NAIC staff to pull in most of the tax credit disclosures from SSAP No. 94R into the disclosure section of the SSAP No. 93R draft.

c. *Investments in Variable Tax Credit Programs:* The Working Group received an informal comment from industry asking for clarification on whether the normal variations in tax credit allocations in certain tax credit programs (for example, production tax credits) would trigger impairment concerns. NAIC staff were directed by the Working Group to add a new paragraph to the impairment section noting that situations in which actual allocated tax credits from variable programs are less than estimated tax credit by more than 10% in a single period or have consistently returned less than estimated tax credits over multiple allocation periods must either record for impairment or specifically address the issue in its impairment analysis if variable tax credits are less than. The intent of this guidance was to be simple and easy to follow, but more importantly to clarify that companies did not need to consider their investments impaired due to normal and reasonable variations in allocated variable tax credits.

i. On a practical note regarding the last sentence in SSAP No. 93R paragraph 29, if the tax credit allocation time frame has ended and the investment is in a net loss position when comparing actual tax credits allocated vs estimated tax credits then the remaining balance should be written off as an other-than-temporary-impairment loss in the same period the last tax credit is allocated.

d. *Awarded Tax Credits:* The Working Group received an informal comment from industry which noted that awarded tax credits would not be within the scope of SSAP No. 94R and asked if this was the intent. After discussing the matter, the Working Group felt that it did not make sense to extend the scope of SSAP No. 94R to include tax credits which were not acquired through a financial transaction and directed NAIC Staff to make edits to the Scope of Statement to define what an awarded tax credit is and that reporting entities should refer to SSAP No. 101.

e. *Commitments to Purchase Tax Credits:* NAIC staff noted that SSAP No. 94R provided no guidance on commitments to purchased tax credits. Based on this information, the Working Group directed NAIC staff to add a new paragraph to the end of the Accounting and Disclosure sections to address this issue.

20. On September 29, 2023, the Working Group received an interested party comment letter on the exposed revisions to SSAP No. 93 and SSAP No. 94R. Interested parties provided several comments on both SSAPs which are summarized below along with the Working Group's responses. Interested parties' comments on the SSAP No. 93R draft have been summarized for brevity and are shown below:

a. **Comment:** Interested parties noted that the SSAP No. 93R, paragraph 18, admittance test[1] requires reporting entities to annually assess the future utilization of the unallocated tax credits associated with an entity's ownership interest in a tax credit investment project to determine if the investment can be admitted. However, interested parties suggested that this admittance criteria only be applicable to investments which do not allocate transferable or refundable tax credit and if the reporting entity is contractually restricted from selling its ownership interest. Additionally, interested parties suggested deleting paragraphs 18.a. and 18.b. as admissibility is adequately addressed through the impairment analysis required in paragraph 25; mainly that since both the tax credits and investments are saleable there is not significant concern about the reporting entity's ability to utilize these investments and their tax credit returns for policyholder liabilities.

Response: The Working Group noted that interested parties' argument is twofold:

i. First, usage of the investment's fair value as a carve out in SSAP No. 93R paragraphs 18.a. and 18.b. is confusing due to the requirement to test for impairment based on fair value. At the direction of the Working Group, NAIC staff amended paragraph 18.a. to clarify that the carve out allows for admittance of the fair value of the unallocated transferable/certificated tax credits rather than the fair value of the tax credit investment. The tax credit investment balance would include other tax benefits which cannot be sold apart from the investment ownership. The intent of paragraph 18.a. is to allow a reporting entity to at least admit the fair value of the tax credits which can be readily liquidated to pay policyholder claims, which is potentially higher than the admitted amount calculated in paragraph 18.

ii. Second, since these investments may be sold, the admittance assessment of the reporting entity's ability to utilize the tax credits is not needed unless the reporting entity contractually restricted from the selling the investment. As part

[1]The "paragraph 18 admittance test" is specifically referenced in both the meeting minutes and historical versions of the Form A; however, in 2024 the paragraph 18 admittance test was renamed the "Prospective Utilization Assessment" as the paragraph numbering changed due to revisions made to the SSAP No. 93R draft.

of this comment, it was noted that these investments may be actively managed and are readily saleable. NAIC staff noted that acquiring tax credit investments with the intent of re-sale puts an insurance company in a similar position as a syndicator in which tax credit investments are developed or acquired for the purpose of sale. At the direction of the Working Group, the SSAP No. 93R draft was revised under the assumption that tax credit investments are acquired for the purpose of obtaining returns through the receipt of tax credits and other tax benefits rather than through the sale of the tax credit investment. Additionally, the Working Group does not believe the paragraph 18 admittance criteria should be amended to provide a carve out for actively managed tax credit investments as it is not feasible to delineate between tax credit investments purchased for sale vs. purchased for generation of tax benefits without introducing some kind of available-for-sale and held-to-maturity framework which is not compatible with statutory accounting concepts. NAIC staff noted that restrictions which prevent investors from selling their ownership represent a minority of tax credit programs. As such, limiting the scope of paragraph 18 to only tax credit investments which cannot be sold would effectively carve out the majority of tax credit investment structures from its scope. Additionally, the assertion that these investments are readily saleable does not change the fact that the balance sheet value of a tax credit investment is predicated on the assumption that the company can use the tax credits and benefits and if they company cannot use these tax credits then the investment returns have no value. Until the investment has been sold, its ability to satisfy future policyholder obligations is beholden to the company's ability to utilize the generated tax credits and benefits. Interested parties noted that there are other investments which do not have as stringent admittance criteria as have been proposed in paragraph 18. NAIC staff noted that other investments generate returns primarily through the receipt of fungible cash income or by providing a claim to the entity's earnings and assets (bonds, stocks, joint ventures, partnerships and LLCs). In comparison, the main purpose of a tax credit investment is to provide returns in the form of tax credits and other tax benefits, and this purpose is further borne out by the commonly used partnership flip structure for tax credit investments which typically retain zero, or occasionally nominal, residual value once the tax credits have been fully allocated.

iii. Additionally, the requirement to assess tax credit investments by looking at the company's ability to realize future tax credits is not a new concept. Under current SSAP No. 93 OTTI guidance, companies are required to record OTTI if the company determines it is probable that future tax benefits will not be received as expected. As stated in SSAP No. 93, paragraph 17, sentences 2 through 5, companies are required to assess whether the investment will continue to issue the tax credits as anticipated AND whether the company will be able to realize/utilize the future tax benefits to be received. As part of the SSAP No. 93R draft, the requirement to assess the company's ability to utilize future tax credits was moved out of impairment to admissibility. As currently revised, the impairment test specifically addresses the functionality of the investment whereas the paragraph 18 admittance test specifically addresses the ability of the company to realize/utilize the future tax benefits. This was done to simplify the impairment analysis by focusing on investment functionality, but also because that the company's ability to utilize future tax benefits is more accurately characterized as an admittance concern rather than impairment of the investment balance.

b. **Comment:** Interested parties suggested a number of editorial changes to effect clearer guidance in paragraphs 18 and 18.a. These included clarifying that the paragraph 18 assessment of unallocated tax credit utilization should be performed over the life of the tax credits rather than the life of the investments, including its carryforward periods. Interested parties also suggested clarifying in paragraph 18 that tax planning strategies are to be used when assessing the utilization of unallocated tax credits, similar to the valuation allowance requirements under SSAP No. 101. In paragraph 18.a. Interested parties suggested removing the sentence detailing what to do if fair value is not non-determinable.

i. **Response:** The Working Group agreed with substantially all the editorial clarifications suggested by Interested parties and directed NAIC Staff to update accordingly.

c. **Comment:** Interested parties suggested adding a definitions section to the guidance regarding the following terminology:

"Unallocated Tax Credits" – The portion of tax credits expected to be earned and allocated to the reporting entity through the investment structure.

"Current Portion" – The credits to be allocated within one year of the reporting period.

i. **Response:** The Working Group agreed with the suggestion by interested parties to add definitions and directed NAIC staff to update accordingly with some minor modifications. Some additional definitions were also added to provide clarifications on other terms used in the SSAP No. 93R draft. (Note: The definition of "current portion" was later removed as this term was eliminated from the paragraph 18 admittance test in 2024.)

d. **Comment:** Interested parties suggested that the new SSAP No. 93 be applied prospectively effective January 1, 2025, but no early adoption.

i. **Response:** The Working Group agreed with the changes suggested by interested parties and directed NAIC Staff to update accordingly.

21. The comments provided on SSAP No. 94R are below and have been summarized for brevity:

a. **Comment:** Interested parties suggested that the revised SSAP No. 94R should also be applied prospectively, effective January 1, 2025, with early adoption permitted. Additionally, interested parties suggested a clarification to the scope of SSAP No. 94R by adding the following language to paragraph 1:

"This statement establishes statutory accounting principles for state and federal tax credits that are purchased by the reporting entity without being a~~n~~ bond or equity investor in the entity from which the tax credit were purchased."

i. **Response:** The Working Group agrees with prospective application of SSAP No. 94R with an effective date of January 1, 2025, however elected to not direct NAIC Staff to make the requested changes to the scope of SSAP No. 94R. The reasoning was that this guidance intends to exclude tax credits allocated from SSAP No. 93R investments, which does not specifically identify which tax credit investment structures are within scope of the guidance. However, other adjustments were made to the SSAP No. 94R Scope paragraph to better clarify

that tax credits from SSAP No. 93R investments were not within the scope of SSAP No. 94R.

22. On December 1, 2023, the Working Group exposed revisions made to SSAP No. 34, SSAP No. 48, SSAP No. 93, and SSAP No. 94R as part of the ~~new market~~ Ttax cCredits Pproject. Revisions to the SSAP No. 93R and SSAP No. 94R drafts included miscellaneous editorial updates and the items discussed above in issue paper paragraphs 19 through 21. The exposure also included new revisions to SSAP No. 34 and SSAP No. 48 which clarified that tax credits are not within the scope of investment income guidance and updated for new SSAP No. 93R language, respectively. Additionally, the Working Group requested comments from state insurance regulators and industry on new RBC reporting categories.

23. Subsequent to the NAIC 2023 Fall National Meeting, interested parties reached out to the Working Group to continue discussions on the paragraph 18 admittance test. The two main concerns raised were that the test would nonadmit previously admitted LIHTC investments and that the test's current structure would significantly increase the administrative burden on insurers who hold tax credit investments. Regarding the first concern, it was pointed out that for all intents and purposes the paragraph 18 admittance test already existed in a simplified form within the impairment LIHTC guidance shown within SSAP No. 93 (see discussion in issue paper paragraph 20). Further discussion developed an initial idea which would allow companies to forgo the paragraph 18 test if the company had no valuation allowance recorded against its DTAs. Based on these discussions and at the direction of the Working Group, NAIC staff drafted new language which would revise the paragraph 18 admittance test. The revisions were as follows:

a. The paragraph 18 admittance test was renamed "Prospective Utilization Assessment" (a specific name was deemed necessary as a new paragraph was added which would have re-numbered the paragraphs).

b. Rather than a practical expedient, language was drafted which would direct companies to perform the Prospective Utilization Assessment if either of two criteria were present in the current or prior period. The first criteria is the existence of a valuation allowance, the second criteria is if the company is aware of any other facts and circumstances which indicate the company would, more likely than not, be unable to substantially utilize the unallocated tax credits. NAIC staff noted that since the valuation allowance, under statutory accounting, is specific to federal income tax it could not be the sole criteria for the Prospective Utilization Assessment as tax credit investments which allocate state income tax or premium tax credits are commonplace. Other changes made to SSAP No. 93R as part of revising admittance test were:

i. Included in the Glossary is a definition of the probability of "more likely than not," which is 50% or greater, as this probability concept already existed within SSAP No. 101. As these investments provide earnings primarily in the form of tax benefits it makes sense to utilize similar concepts as those used in SSAP No. 101.

ii. For the other facts and circumstances criteria, to avoid requiring companies to prove a negative (e.g., prove to auditors that other facts and circumstances did not exist) as such the language specifically notes that the company only need perform the Prospective Utilization Assessment if it is aware of other facts and circumstances. However, for this criterion is intentionally broad, and companies should not limit their consideration of other facts and circumstances to the confines of statutory accounting concepts. To this end, two examples of other

facts and circumstances were included within the guidance that would meet criteria 2.

iii. The Prospective Utilization Assessment test was also simplified by removing the requirement to perform an initial assessment of the utilization of the current portion of unallocated tax credits; the current portion definition was also removed from the glossary as this term was only used in what was previously referred to as the paragraph 18 admittance test.

24. On January 29, 2024, the Working Group exposed, through an evote, revisions made to SSAP No. 93 and SSAP No. 94R as part of the New Market Tax Credits Pproject (see items discussed in issue paper paragraph 23) as well additional editorial updates. The comment period was accelerated to allow the Working Group the opportunity to adopt the New Market Tax Credits Pproject at the 2024 Spring National Meeting.

25. On February 9, 2024, interested parties provided comments to the Working Group on the January 29th exposure. Interested parties noted that they agreed with the changes made to the Prospective Utilization Assessment (previously the paragraph 18 admittance test) and no further comments on this issue. Comments were provided on a consistency issue with Example 2 of the SSAP No. 93R draft and on the reporting categories that would be used to report tax credit investments for RBC purposes. The comments have been summarized below for brevity:

a. **Comment:** Interested parties noted that Schedule BA has reporting sections for Guaranteed, Non-Guaranteed, and All Other Low Income Housing Tax Credit (LIHTC) investments. The RBC charges are driven by these categories and are 0.14%, 2.6%, and 15%, respectively.

i. **Suggestion 1:** Keep the same categories but remove all references to LIHTC tax credit investments if the expectation is that the RBC charges will remain the same regardless of tax credit program type.

ii. **Suggestion 2:** Keep the same categories, but to have two separate sections in each category, for debt and equity investments.

iii. **Suggestion 3:** Assuming the reporting lines delineate between debt and equity, provide separate RBC treatment for debt structured investments with SVO designation.

b. **Comment:** Interested parties also noted that the current annual statement instructions for LIHTC investments may need some clarity as there is diversity in interpretation as to what the instructions require. For example:

i. Under the non-guaranteed section, there is a reference to “level of leverage below 50%”. It is not clear why this requirement is included and whether this requirement is for the insurer to determine whether debt in the structure is below 50% of the total capitalization of the entity or how to classify the investment for accounting and reporting if leverage is higher than 50%.

ii. The “all other” category refers to non-qualifying LIHTC investments. Interested parties are not clear on what non-qualifying means.

c. **Comment:** Interested parties noted that Example 2 was amended to include a residual value, but the computations for proportional amortization and journal entries were not updated for this fact.

26. At the NAIC 2024 Spring National Meeting, the Working Group voted to adopt the exposed revisions, updated for the corrections to Example 2 in the SSAP No. 93R draft, and the revisions, which are as exposed, to SSAP No. 34, SSAP No. 48, and SSAP No. 94R. The effective date of the revisions is January 1, 2025. The Working Group also directed NAIC staff to:

a. Sponsor a blanks proposal on the annual statement reporting categories for tax credit investment RBC by using the suggestion from the interested parties comment letter to maintain the same categories but without reference to LIHTC (suggestion 1) and to also update/clarify the instructions accordingly.

b. Send a referral to the Life Risk Based Capital (E) Working Group to inform them of the planned reporting line changes, which may indicate review of the RBC charges as different categories of tax credits will be reported in the form.

c. Draft an issue paper to document the discussions and revisions for agenda item 2022-14.

27. The Working Group sponsored a blanks proposal (#2024-11BWG) to update the annual statement instructions for changes made by the adoption of ~~the New Market~~ Tax Credits P~~p~~roject. This agenda item was exposed by the Blanks (E) Working Group on April 1, 2024, and included the following updates:

a. Updates to the annual statement instructions in accordance with the SSAP No. 93R and SSAP No. 94R drafts (terminology, disclosures, etc.).

b. AVR/Schedule BA reporting lines were amended to replace references to "Low-Income Housing Tax Credits" with the general term "Tax Credit Investments." While the reporting lines and RBC factors were generally kept the same, the Working did elect to remove the Federal Guaranteed Tax Credit programs from the draft proposal because these types of tax credit investment structures with "make whole" guarantees were substantially eliminated by the Historic Boardwalk Hall, LLC v. Comm of Internal Revenue court decision in 2012.

28. On April 2, 2024, the Working Group sent a referral to the Capital Adequacy (E) Task Force and Life Risk-Based Capital (E) Working Group informing them of the changes made to the annual statement instructions in response to the adoption of the ~~New Market~~ Tax Credits Project.

29. Per discussion with industry, agenda item #2024-11BWG was updated for the following:

a. **Comment:** Interested parties noted that it would increase consistency in reporting if an example disclosure were provided for Note K(5).

i. **Response:** The Working agreed and directed NAIC Staff to add an example of the disclosure format for aggregate disclosure schedule of tax credits expected to be generated each year for the subsequent five years and thereafter.

b. **Comment:** Interested parties noted that the reporting line titles in the AVR/RBC Instructions were confusing as the guaranteed reporting line is only for yield guaranteed tax credit investments and the criteria for the non-guaranteed reporting line requires compliance guarantees.

i. **Response:** The Working agreed and directed NAIC Staff to update the reporting line titles to increase clarity; the "non-guaranteed" reporting lines were renamed "qualifying" and the "guaranteed" reporting line was renamed "yield guaranteed."

c. **Comment:** Interested parties requested some clarifying edits to the criteria for the yield guaranteed and qualifying tax credit investment categories.

i. **Response:** The Working agreed and directed NAIC Staff to add language to be clear that only yield guaranteed federal tax credit investment previously reported under the federal guaranteed line would need to go to the Other Tax Credit Investments line (assuming it is within the scope of the revised SSAP No. 93).

ii. The criteria for Qualifying tax credit investments were also amended to be clear that investments must meet all of the stated criteria and that tax credit guarantee agreements from developers or an insurer are acceptable, assuming the transaction is executed at arm's length.

d. **Comment:** Interested parties requested that the duration of the tax credit guarantee agreement, "life of the investment structure" be deleted as often times the life of the investment structure exceeds that of the tax credit compliance period.

i. **Response:** The Working Group agreed that the life of the investment structure was too restrictive, but also noted that the preferential RBC factor for Qualifying Tax Credit Investments is because the guarantees help limit any potential losses from recapture. A tax credit guarantee agreement could have a compliance guarantee, but only during the construction phase. Without terminology setting the acceptable duration of the compliance guarantee, investments with compliance guarantees lasting only a fraction of the regulatory compliance period would receive the same RBC treatment as those with more robust compliance guarantees. When the LRBC Working Group originally set the RBC factors for the "Non-guaranteed" (now renamed "Qualifying") reporting lines, the presence of these guarantees over the course of the investment was one of the stated reasons for the preferential RBC factor. As a result of these discussion, the Working Group directed NAIC staff to retain a duration requirement but to replace the language "for the life of the investment structure" with "for the duration of the regulatory compliance period of the tax credit program."

30. During July 2024, NAIC Staff received informal questions from a public accounting firm on two topics, which are shown below:

Q1: *SSAP No. 93R paragraph 3 makes references to SSAP Nos. 26R and 48. Should this also include a reference to SSAP 94R for purchased credits?*

NAIC Staff noted that paragraph 3 is intended to be a redirect for investments which failed to meet the criteria in paragraph 2. Purchased tax credits wouldn't need to be considered under SSAP No. 93R as they aren't an investment structure. As stated in footnote 1 of SSAP No. 94R, a purchased tax credit typically refers to tax credits acquired via certification or transfer form. Whether purchased or allocated, tax credits are not an investment but rather a type of other than invested asset.

Q2: *SSAP No. 93R paragraph 14(iv) states, "The admissibility of tax credits are subject to SSAP No. 101." Is this meant to apply to federal credit carryovers only? If so, suggest clarifying this.*

NAIC Staff noted that SSAP No. 101 is applicable to both state and federal tax liabilities per the scope of statement in paragraph 1. While the majority of SSAP No. 101 pertains to federal taxes, paragraph 4 provides guidance on state taxes. Per SSAP No. 101 paragraph 4, the guidance is applicable to state taxes, including income and premium, and the last two sentences of the paragraph address the admissibility of state tax recoverables. The Working Group would consider an unused state tax credit to be synonymous with a state tax recoverable when applying this guidance.

31. On August 7, 2024, the Blanks (E) Working Group adopted, as final, 2024-11BWG with an effective date of 1/1/2025.

31.32. On August 13, 2024, the Working Group exposed a draft of the Tax Credits Project issue paper and agenda item 2024-18 which proposes clarifying revisions to the adopted changes detailed agenda item 2022-14. These revisions would be effective 1/1/2025 and include:

a. Revisions to SSAP No. 94R accounting guidance as comments noted it was inconsistent with the journal entry examples.

b. Revisions to SSAP No. 93R accounting guidance for recognizing allocated tax credits as comments noted it confusing when compared to the journal entry examples.

c. Revisions to the Scope paragraph in SSAP No. 48 as it was noted that one sentence accidentally wasn't updated as part of the New Market Tax Credits Pproject.

33. On October 7, 2024, the Working Group sent an updated referral to the Capital Adequacy (E) Task Force and Life Risk-Based Capital (E) Working Group recommending that the RBC instructions shown in LR008, PR008, and XR08 either be removed or updated as the current instructions are no longer relevant.

34. During October 2024, NAIC Staff received informal questions from industry professionals on two topics, which are shown below:

Q1: *Does the Certified Capital Companies (CAPCO) carve-out detailed in SSAP No. 93 extend to investments in entities with structures similar to CAPCOs?*

NAIC Staff noted that CAPCO carve-out is a historical item and the recently adopted 2022-14 does not intend to change its application. To be clear, the CAPCO carve-out is deliberately narrow in scope and applies exclusively to debt instrument investments in state-legislated "certified capital companies". Investments in entities that are "effectively" a CAPCO or are structured similarly to CAPCOs do not qualify for this carve-out.

Q2: *If a yield guaranty only covers certain components of the investment, can it still qualify for reporting as a "Yield Guaranteed State Tax Credit Investment"?*

The blanks instructions for Yield Guaranteed State Tax Credit Investments state, "There must be an all-inclusive guarantee from a CRP-rated entity that guarantees the yield on the investment. This reporting line is only allowed for tax credit investments which issue state tax credits." NAIC staff noted that the term "all-inclusive" would require the yield guarantee to encompass the entire investment structure, not just specific components. Furthermore, an investment cannot be deemed to "effectively" contain a yield guarantee based on various contract provisions. A yield guarantee must be explicitly stated in the contract, ensuring that the investor will receive a specified yield or internal rate of return on the tax credit investment structure.

35. On November 17, 2024, the Working Group adopted agenda item 2024-18, as final, with an effective date of 1/1/2025.

36. On December 16, 2024, the Working Group received a comment letter from interested parties stating no comments on the issue paper exposed at the 2024 Summer National Meeting.

Effective Date

32.37. The new concept revisions to SSAP No. 93 and SSAP No. 94R and clarifying revisions to SSAP No. 34 and SSAP No. 48 are contained in Exhibit A. Users of the *Accounting Practices and Procedures Manual* should note that issue papers are not represented in the Statutory Hierarchy (see Section IV of the Preamble) and therefore the conclusions reached in this issue paper should not be applied until the corresponding revisions to SSAP No. 93 and SSAP No. 94R have been adopted by the Plenary of the NAIC. SSAP No. 93R is effective on January 1. 2025, no early adoption permitted. SSAP No. 94R is effective on January 1. 2025, with early adoption permitted.

RELEVANT STATUTORY ACCOUNTING AND U.S. GAAP GUIDANCE

Statutory Accounting

- *SSAP No. 93R—Investments in Tax Credit Structures*
- *SSAP No. 94R—State and Federal Tax Credits*

Generally Accepted Accounting Principles

- *FASB Accounting Standards Update No. 2023-02*

33.38. FASB issued ASU 2023-02 to allow reporting entities to consistently account for equity investments made primarily for the purpose of receiving income tax credits and other income tax benefits. Prior to ASU 2023-02, U.S. GAAP allowed for the option to apply the proportional amortization method to tax equity investments, but the option was limited to investments in low-income-housing tax credit (LIHTC) structures. The amendments in ASU 2023-02 remove this limitation and permit reporting entities to elect to account for their tax equity investments, regardless of the tax credit program from which the income tax credits are received, using the proportional amortization method if certain conditions are met.

34.39. The proportional amortization method results in the cost of the investment being amortized in proportion to the income tax credits and other income tax benefits received, with the amortization of the investment and the income tax credits being presented net in the income statement as a component of income tax expense (benefit). Equity investments in other tax credit structures are typically accounted for using the equity method or Topic 321, Investments—Equity Securities, which results in investment income, gains and losses, and tax credits being presented gross on the income statement in their respective line items.

35.40. Stakeholders asserted that tax equity investors in economically similar investments that are made primarily for the purpose of receiving income tax credits and other income tax benefits should have the same election as LIHTC investors to account for those investments using the proportional amortization method. In their view, the proportional amortization method provides investors, lenders, creditors, and other allocators of capital (collectively, “investors”) with a better understanding of the returns from such investments than the equity method or Topic 321. Because of the current limitation on the application of the proportional amortization method to account only for eligible LIHTC investments, stakeholders asked

that the Board allow reporting entities to elect to apply the proportional amortization method to account for tax equity investments that generate income tax credits through other tax credit programs.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/04 - 22-14 - Issue Paper 170 - Tax Credits Project.docx

EXHIBIT A – TRACKED REVISIONS TO SSAP NO. 93

Statements of Statutory Accounting Principles No. 93R

Low-Income Housing Tax Credit Property Investments in Tax Credit Structures

STATUS

Type of Issue .... Common Area
Issued .... June 13, 2005; Conceptually revised March 16, 2024
Effective Date .... January 1, 2006 Conceptual revisions detailed in Issue Paper No. xxx170 effective January 1, 2025
Affects... No other pronouncements
Affected by... No other pronouncements
Interpreted by .... INT 06-07
Relevant Appendix A Guidance .... None

STATUS......1
SCOPE OF STATEMENT......1
SUMMARY CONCLUSION......2
Accounting......2
Impairment......3
Audited Financial Statements......4
Disclosures......4
Relevant Literature......5
Effective Date and Transition......7
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STATUS ERROR! BOOKMARK NOT DEFINED.
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EXHIBIT A – APPLICATION OF PROPORTIONAL AMORTIZATION METHOD 40

~~**SCOPE OF STATEMENT**~~

~~1. This statement establishes statutory accounting principles for investments in federal and certain state sponsored Low-Income Housing Tax Credit (LIHTC) properties owned through limited liability entities that are flow-through entities for tax purposes. State sponsored LIHTC programs that have the following characteristics are within the scope of and shall be accounted for in accordance with this statement:~~

~~a. The program is based upon Internal Revenue Code (IRC) section 42.~~

~~b. The investment requires an ongoing interest in a limited liability entity, which is a flow-through entity, and cannot be transferred apart from this interest.~~

~~c. Resale value of the investment is not based upon the fair value of the underlying real estate.~~

~~d. Fair value of the investment is directly tied to the remaining stream of tax credits and deductible losses available to investors.~~

~~e. The critical element of value is known with a high degree of certainty before being marketed to investors.~~

~~f. The proportional amortization method (as modified by this statement) is more indicative of liquidation value than the equity method.~~

~~State sponsored LIHTC programs requiring ownership in a partnership or limited liability entity that do not have the foregoing characteristics shall continue to be accounted for in accordance with the requirements of *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*.~~

~~2. Some states have enacted laws that create programs by which transferable and non-transferable state tax credits are granted to entities under certain specified conditions (e.g., an entity makes an investment in a particular industry). Investments in transferable and non-transferable state tax credits are~~

~~not within the scope of this statement. See *SSAP No. 94R—Transferable and Non-Transferable State Tax Credits*.~~

~~**SUMMARY CONCLUSION**~~

~~3. LIHTC investments held by reporting entities meet the definition of an asset as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement.~~

~~1. Resale valuation of these investments is based on the present value of the future stream of tax credits and deductible losses, and not the fair value of the underlying real estate.~~

~~2. Investors in entities that manage or invest in low-income housing projects receive tax benefits in the form of tax deductions from operating losses and tax credits. The tax credits are allowable on the tax return each year over a 10-year period as a result of renting a sufficient number of units to qualifying tenants and are subject to restrictions on gross rentals paid by those tenants. These credits are subject to recapture over a 15-year period starting with the first year tax credits are earned. Corporate investors generally purchase an interest in a limited liability entity that manages or invests in the low-income housing projects.~~

~~**Accounting**~~

~~6. LIHTC investments shall be initially recorded at cost and carried at proportional amortized cost as specified in this statement unless considered impaired as discussed in paragraphs 16-19. An illustration has been provided in Exhibit A of this statement.~~

~~7. A reporting entity investor using the proportional amortized cost method shall amortize any excess of the carrying amount of the investment over its estimated residual value during the periods in which tax benefits are allocated to the investor. The estimated residual value used in determining the amount to be amortized is the estimated residual value at the end of the last period in which tax benefits are allocated to the investor and should not reflect anticipated inflation. Annual amortization shall be based on the proportion of tax benefits received in the current year to total estimated tax benefits to be allocated to the investor. The amortization amount shall be calculated as follows:~~

~~a. The initial investment balance less any expected residual value of the investment, multiplied by,~~

~~b. The percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be received by the reporting entity over the life of the investment.~~

~~8. Under the proportional amortized cost method, the amortization of the investment in the limited liability entity is recognized in the income statement as a component of net investment income/expense. The current tax credit (or benefit) shall be accounted for as a component of income tax expense.~~

~~9. Federal tax credits shall be recognized in the income statement as an offset to federal taxes in the tax reporting year in which the tax credit is utilized in accordance with *SSAP No. 101—Income Taxes*. State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax reporting year in which the credit is utilized. Tax benefits received, other than tax credits, shall be accounted for pursuant to SSAP No. 101.~~

~~10. At the time of initial investment, immediate recognition of the entire benefit of the tax credits to be received during the term of an investment in a low-income housing project is not appropriate. (That is,~~

low-income housing tax credits shall not be recognized in the financial statements before their inclusion in the investor's tax return.)

11. Many LIHTC investments require future equity contributions by the investor (equity contributions), that may be contingent on a variety of conditions, such as receiving representations, contract performance, meeting occupancy requirements, etc. If the commitment by the investor to provide equity contributions meets the definition of a liability as defined in *SSAP No. 5R—Liabilities Contingencies and Impairments of Assets,* a liability shall be recorded.

12. If the commitment to provide equity contributions does not meet the definition of a liability, the contingent commitment shall be disclosed in the notes to the financial statements with other contingent commitments. A liability shall also be recognized for equity contributions that are contingent on a future event when that contingent event becomes probable.

13. Additional funding that does not result in additional tax credits for the reporting entity (investor) shall be expensed as a component of net investment income. In the event a reporting entity obtains additional tax credits for a LIHTC investment, the following shall be applied:

a. If additional tax credits are allocated without additional funding, the additional tax credits shall not be afforded any value; rather, the tax benefit is only recognized when realized.

b. If additional funding directly related to the additional tax credits is required, the provisions of this statement shall be followed as if the additional funding were a new investment in LIHTC property.

14. An investment amortized to residual value in accordance with paragraph 7 of this statement shall not be revalued under any other method during or subsequent to the amortization period, other than as discussed in this statement.

15. Changes in estimated losses shall be accounted for in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* as a change in estimate and included as a component of net investment income.

Impairment

16. Reporting entities with investments in LIHTC properties shall complete and document an impairment analysis at each reporting period. If it is determined that an impairment exists, the book value of the LIHTC investment shall be compared to the present value of future tax benefits discounted at a risk free rate of return, i.e., the rate on U.S. Treasury obligations of a similar duration, and the investment shall be written down if the book value is higher. This will result in a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries in fair value.

17. Among other things, an other-than-temporary impairment[(INT 06-07)] shall be considered to have occurred if it is probable that future tax benefits will not be received as expected. For example, for LIHTC properties based on state tax credits, if the reporting entity intends to decrease premium volume in that state, it may affect whether or not the tax credits in that state are realizable. The best available information about market share or premiums by state and premiums by line of business generally should be used to estimate the amount of future tax credits that are realizable. For purposes of determining impairment, future tax benefits consist of both estimated tax losses and anticipated tax credits. Loan default or a reasonable probability of credit recapture would signify that tax benefits would not be received as expected.

~~18. In a multi-tiered partnership, whereby one limited partnership exists only to hold interests in other limited partnerships that are each invested in different developments, the impairment should be determined at the lowest tier. The partnership that holds the assets in which the impairment is determined to exist will be adjusted to a new cost basis representing the lower of book value or the present value of future tax benefits discounted at a risk-free rate of interest. This new cost basis and related realized loss shall be recognized by the holder of a LIHTC investment.~~

~~19. It should be noted that a foreclosure of a single property within an LIHTC investment fund only affects the loss of tax credits on a proportional basis. For example, a foreclosure of one property in a six-property fund generating equal levels of credits would only eliminate 1/6 of the credits, thereby, only affecting 1/6 of the LIHTC investment fund value to the individual investors.~~

~~Audited Financial Statements~~

~~20. The reporting entity's return and book value of an LIHTC investment is reliant upon maintaining tax credit eligibility and not its share of the equity as reported on a financial statement. As such, a reporting entity shall monitor the tax credit eligibility of an LIHTC investment through requiring either audited GAAP or audited tax basis financial statements. In the event an audited GAAP or audited tax basis financial statement is not obtained, the asset shall be nonadmitted.~~

~~Disclosures~~

~~21. Disclose the number of remaining years of unexpired tax credits and the required holding period for the LIHTC investments.~~

~~22. Disclose the amount of low-income housing tax credits and other tax benefits recognized during the years presented.~~

~~23. Disclose the balance of the investment recognized in the statement of financial position for the reporting period(s) presented.~~

~~24. Disclose if the LIHTC property is currently subject to any regulatory reviews and the status of such review. (Example investigations by the housing authority.)~~

~~25. Any commitment or contingent commitment (e.g., guarantees or commitments to provide additional capital contributions) including the amount of equity contributions that are contingent commitments related to LIHTC properties investments and the year(s) that contingent commitments are expected to be paid shall be disclosed.~~

~~26. The significance of an investment to the reporting entity's financial position and results of operations shall be considered in evaluating the extent of disclosures of the financial position and results of operations of an investment in a LIHTC. If in the aggregate the LIHTC investments exceed 10% of the total admitted assets of the reporting entity the following disclosures shall be made:~~

~~a. (i) The name of each partnership or limited liability entity and percentage of ownership, (ii) the accounting policies of the reporting entity with respect to investments in partnerships and limited liability entities (iii) the difference, if any, between the amount at which the investment is carried and the amount of underlying equity in net assets (i.e., nonadmitted goodwill or other nonadmitted assets) and (iv) the accounting treatment of the difference;~~

b. For partnerships, and limited liability entities for which a quoted fair value is available, the aggregate value of each partnership, or limited liability entity investment based on the quoted fair value; and

c. Summarized information as to assets, liabilities and results of operations for partnerships, and limited liability entities, either individually or in groups.

27. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment and how fair value was determined.

28. Disclose the amount and nature of the write-downs or reclassifications made during the year resulting from the forfeiture or ineligibility of tax credits, etc. These write-downs may be based on actual property level foreclosure, loss of qualification due to occupancy levels, compliance issues with tax code provisions within an LIHTC investment, or other issues.

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

Relevant Literature

30. This statement adopts with modification *ASU 2014-01, Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects*. The modifications include:

a. ASU 2014-01 allows the election of using the proportional amortization method if an affordable housing project investment meets several criteria, including the lack of significant influence. This statement requires the proportional amortization method, with modifications as discussed in this statement, for all investments within its scope. Although the terminology is updated, the balance sheet amount and timing of amortization should be the same under this statement and the proportional amortization method in ASU 2014-01.

b. The proportional amortization method in ASU 2014-01 utilizes a net presentation in the income statement by including the amortized initial cost of the investment and the tax credits and benefits received within income tax expense. This statement requires a gross presentation on the income statement, with proportional amortization of the initial cost of the investment in investment income and the tax credits and benefits included in income tax expense.

c. Paragraphs 323-740-50-2c and 323-740-50-2d related to disclosures of the optionality of the method used and net reporting, are rejected as not applicable to statutory accounting.

d. Disclosures should be followed as indicated in the disclosures section in this statement.

31. This statement adopts with modification *EITF 94-1: Accounting for Tax Benefits from Investments in Affordable Housing Projects* as applicable to statutory accounting to the extent it is not modified by ASU 2014-01. In 2006, this statement modified *Issue Paper No. 99—Nonapplicable GAAP Pronouncements* to remove the reference to EITF 94-1.

32. ASU 2014-01 and EITF 94-1 are modified for the following statutory concepts:

a. The elective effective yield method and the net income statement reporting in EITF 94-1 are rejected. The elective proportional amortization method in ASU 2014-01, which replaced the effective yield method, is required for only the balance sheet calculation reflecting the timing and amount of amortization. The proportional amortization method net income statement reporting in ASU 2014-01 is rejected for statutory accounting.

b. Investments that meet the criteria of this statement are required to use a proportional amortization method as prescribed in this statement. This method requires the tax credits and benefits to be recognized in proportion to the percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be received by the reporting entity over the life of the investment. This statement requires a gross presentation on the financial statements, with amortization in investment income.

c. Federal tax credits shall be recognized in the income statement as an offset to federal income taxes in the tax reporting year in which the tax credit is utilized in accordance with *SSAP No. 101—Income Taxes*. State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax reporting year in which the credit is utilized.

d. Tax benefits received, other than tax credits, shall be accounted for pursuant to SSAP No. 101. Amortization shall be reported as a component of net investment income.

e. Reporting entities shall follow the guidance in paragraphs 11 and 12 regarding the application of the definition of a liability and contingent commitments from *SSAP No. 5R—Liabilities Contingencies and Impairments of Assets* to equity contributions.

f. *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* shall be utilized to account for investments that qualify as subsidiary, controlled or affiliated entities.

g. The impairment guidance contained in this statement shall be followed.

h. For statutory accounting purposes, deferred taxes are not reported as a component of income from continuing operations in the income statement; rather deferred taxes are recognized as a separate component of gains and losses in unassigned funds (surplus).

33. *AICPA Statement of Position 78-9, Accounting for Investments in Real Estate Ventures* (SOP 78-9) is rejected for purposes of statutory accounting in SSAP No. 48. This statement does not intend to establish SOP 78-9 as applicable to statutory accounting.

34. *FASB Interpretation No. 46, Consolidation of Variable Interest Entities* (FIN 46) is rejected for purposes of statutory accounting in SSAP No. 3. This statement does not intend to establish FIN 46 as applicable to statutory accounting.

35. *EITF 85-16: Leveraged Leases* (EITF 85-16) is adopted for purposes of statutory accounting in *SSAP No. 22R—Leases*. This statement does not intend to readdress the conclusions reached in SSAP No. 22R.

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for qualifying tax credit investments[2] in programs made primarily for the purpose of receiving allowable general business federal tax credits and/or state tax credits, including state premium tax credit programs. Although these investments are often in the form of equity, this statement shall be applied to all investments (regardless of the structure of the investment) that qualify pursuant to paragraph 2.

2. A reporting entity that invests in projects or programs that generate general business federal tax credits, corresponding state tax credits or state premium tax credits that meet the following conditions at the time of initial investment are required to capture the investment in scope of this statement:

a. It is probable that the tax credits allocable to the investor will be available.

b. Reporting entity investor does not have the ability to exercise significant influence over the operating and financial policies of the underlying projects.

c. Substantially all the projected benefits are from tax credits and other tax benefits, determined on a discounted basis using a discount rate that is consistent with the cash flow assumptions utilized by the reporting entity for the purpose of deciding to invest in the project.

d. The reporting entity's projected yield based solely on the cash flows from the tax credits and other tax benefits is positive.

3. Tax credit investments that do not meet the conditions in paragraph 2 shall be captured within the statutory accounting statement that addresses the underlying investment structure. Equity structured tax credit investments would generally fall within *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*. Debt structured tax credit investments should be assessed in accordance with *SSAP No. 26R—Bonds* to determine eligibility for reporting as a bond.

4. Investments in a CAPCO (Certified Capital Company), organized as a partnership or an LLC, which is a company, authorized by state statute that borrows from investors, to make venture capital investments in "qualified" businesses, are not within the scope of this statement. Although associated with tax credits, the reporting entity is paid principal and interest on its investment with the CAPCO. Depending upon the terms of the CAPCO offering, principal and interest payments to the reporting entity will come from the CAPCO and/or the state. The CAPCO will make cash payments directly to the investors while the state will make payments in the form of premium or income tax credits. Investments in a CAPCO shall be accounted for in accordance with *Interpretation (INT) 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)* and specific statutory accounting guidance addressing CAPCOs.

SUMMARY CONCLUSION

5. Investments in tax credit structures are generally acquired to obtain a positive yield through tax credits and other tax benefits. The value of the investment is primarily based on the value of the remaining stream of tax credits and deductible expenses available to the reporting entity investor. The

[2] The scope of *ASC 323-740–Investments—Equity Method and Joint Ventures—Income Taxes—Proportional Amortization Method* only extends to income tax equity investments, whereas this statement is intended to capture all tax credit investments which meet the criteria in paragraph 2, regardless of structure. This includes, but is not limited to, tax equity investments and tax credit debt investments.

primary purpose of investing in these tax credit structures is to generate tax credits which benefit reporting entities, most commonly through a reduction in tax liability or, when permitted by IRS or state tax provisions, through the sale of certificated/transferable tax credits.

6. Investments in tax credit structures held by reporting entities meet the definition of an asset as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement.

Accounting

7. This guidance addresses the methodology for measuring an investment that is accounted for using the proportional amortization method. At initial recognition, investments in scope of this statement shall be recorded at cost.

8. Subsequent to initial recognition, the investment shall be carried at proportional amortized cost. Under the proportional amortization method, the reporting entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits allocated to the investor. The amortization amount shall be calculated as follows:

a. The initial investment balance less any expected residual value of the investment, multiplied by;

b. The percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be received by the reporting entity over the amortization timeframe (life of the investment).

9. Reporting entities shall recognize tax credits in the period they are allocated to the investor for tax purposes. Unless all tax credits are allocated to the reporting entity at the date of initial investment, immediate recognition of the entire benefit of the tax credits to be received during the term of the investment project that generates tax credits and other tax benefits is not permitted. Tax credits shall not be recognized in the financial statements before the year in which the tax credits are allocated.

10. Any expected residual value of the investment shall be excluded from the proportional amortization calculation. Non-tax related benefits received from the investment shall be included as a component of net investment income when realized or realizable. Gains or losses on the sale of the investment, if any, shall be included as a capital gain or loss at the time of the sale. Determination of gain or loss will depend on the reported value (e.g., residual value at the end of the amortization timeframe) compared to the amount received in exchange for the investment. Liquidation of the investment commonly occurs at the end of the tax credit timeframe through a put or call agreement, often reflecting a nominal residual value that was established at the time of acquisition. The liquidation amount from such agreements shall reflect the expected residual value when available.

11. At the end of the amortization timeframe, if the reporting entity retains the investment, the investment shall be subsequently measured and assessed within the statutory accounting statement applicable to the investment held. Retained investments will remain on Schedule BA until disposal and cannot exceed the initial expected residual value.

12. Exhibit A illustrates the application of accounting guidance in two examples that generate tax credits and tax benefits using the proportional amortization method. The first example illustrates the application of a standard project. The second example illustrates the application of accounting guidance in a project that has expected residual value and generates non-tax related benefits in addition to tax credits and other tax benefits using the proportional amortization method.

Application of Proportional Amortization Method

13. Under the proportional amortized cost method, the amortization of the investment is to be recognized in the income statement as an expense component of the net investment income calculation. Non-tax related benefits received from operations, or sale of the investment should be accounted for in accordance with paragraph 10.

14. Tax credits and other tax benefits, not to include amortization of the investment, shall be reflected as follows:

Drafting Note: The revisions adopted in agenda item 2024-18 revise paragraphs 14.a.i. through 14.a.iii., and are also effective 1/1/2025.

a. Tax credits shall be recognized in the period that they are allocated to the reporting entity for tax purposes:

   i. Federal tax credits that can be utilized in the year allocated shall be reported in the income statement as an offset to federal taxes in accordance with *SSAP No. 101—Income Taxes*. Federal tax credits that cannot be utilized in the year allocated and are carried forward to a future tax year shall be reported as a deferred tax asset (DTA) in accordance with SSAP No. 101.

   ii. State tax credits that can be utilized in the year allocated shall be reported in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized. State tax credits that cannot be utilized in the year allocated and are carried forward to a future tax year shall be reported gross of any related state tax liabilities and reported in the category of other-than-invested assets (not to be reported net).

   iii. Use of tax credits carried forward in a future period shall be reflected as an offset to the corresponding income or premium tax in the tax reporting year in which the tax credit is utilized.

   iv. Tax credits allocated from tax credit investments, as defined within this SSAP, and held by reporting entities meet the definition of assets as specified in SSAP No. 4 and are admitted assets to the extent that they comply with the requirements of this statement. The admissibility of tax credits is subject to SSAP No. 101.

b. Federal tax benefits other than tax credits (e.g., tax benefits from investment depreciation) shall be recognized in the year allocated pursuant to SSAP No. 101. When utilized, the federal tax benefits are recognized as a component of income tax expense.

c. State tax benefits other than tax credits shall be recognized in the year allocated gross of any related state tax liabilities pursuant to SSAP No. 101. When utilized, the state tax benefits are recognized as a component of taxes, licenses, and fees.

Admittance of Tax Credit Investments

15. Although investments in tax credit programs do not represent investments that can be readily liquidated for policyholder claims, the reduction of tax liability or sale of allocated tax credits represents a benefit that supports admittance of these investments, but only if the tax credits will be received and can be utilized by the reporting entity. Investments in tax credit programs that will not result in any of the

anticipated tax credits or that will result in tax credits which cannot be utilized or sold by the reporting entity shall be considered impaired and should refer to paragraphs 27 and 28.

16. Reporting entities shall, at initial investment, obtain a clean[3] fund level tax opinion[4] on the validity of the credits and structure of the underlying program and investment fund. Investments not supported by an initial tax opinion shall be nonadmitted. If the program is a permitted syndicated program with a yield guarantee, the opinion must verify that the investment and guarantee have been properly structured under IRS or state tax provisions and the guarantee does not disqualify the reporting entity from obtaining the tax credits.

17. Reporting entities shall annually obtain U.S. GAAP or U.S. tax basis audited financial statements on the investment fund. In the event audited U.S. GAAP or U.S. tax basis financial statements are not obtained or the audit receives an opinion other than unqualified, the asset shall be nonadmitted. If the audited financial statements are in-process but not completed as of the annual statement filing deadline, the reporting entity may admit the investment based on the results of the immediately preceding prior year audited financial statements. A lag in reporting shall be consistent from period to period.

a. Other tax credit investments – If the reporting entity has a tax credit investment which by virtue of its structure cannot be audited, the investment is exempt from the annual audit requirement. One example of this type of investment would be tax credit debt investments[5] which do not involve any amount of equity ownership as a component of the investment. This type of tax credit debt investment is exempt from the annual audit requirement, but the reporting entity is still required to obtain a clean tax opinion, in accordance with paragraph 16, to support admittance at initial investment.

Prospective Utilization Assessment

18. The prospective utilization assessment, as detailed below in paragraphs 19-21, must be performed annually by the reporting entity if any of the following circumstances exist in either the current or prior reporting period:

a. Reporting entity records a valuation allowance against a deferred tax asset (DTA) balance.

b. Reporting entity becomes aware of other facts and circumstances which indicate that it will, more likely than not, be unable to substantially utilize the unallocated tax credits. Such instances include, but are not limited to:

i. If the reporting entity holds an investment which allocates state premium tax credits and intends to decrease premium volume in that state, it may affect whether or not the unallocated tax credits in that state can be utilized.

[3] While not quantified or defined in either the Internal Revenue Code or state regulations, common industry standards consider a "should" opinion to be the minimum degree of confidence associated with a clean tax opinion. For the purposes of this statement, a "should" opinion must represent a probability of success no less 70%. Any tax credit investment which receives a tax opinion with a degree of confidence less than "should" is to be nonadmitted.

[4] A fund level tax opinion for the purposes of this statement is defined as a full IRS Circular 230 tax opinion which covers from the fund level through to the underlying assets generating the tax credit benefits. The fund level is defined as the entity, or level, at which the investor comes directly into the investment without any intermediaries.

[5] Common examples of tax credit debt investments are Tax Credit Strips derived from tax credit bonds, Qualified Tax Credit Bonds, and Build America Tax Credit Bonds. Tax opinions received on these tax credit investments are also referred to as "bond counsels." Tax Credit Strips derived from tax equity investments would not qualify for the paragraph 17.a. carve out as the source of the stripped tax credits is auditable.

ii. If the reporting entity holds an investment allocating state income tax credits and records a valuation allowance in its U.S. GAAP financial statements against state DTA balances, including the same state as the tax credit investment, it cannot ignore the circumstances that led to the valuation allowance, even though statutory accounting does not permit state DTAs.

19. Prospective Utilization Assessment – If any of the circumstances detailed in paragraph 18 exist, the reporting entity is required to assess the future utilization of the investment's unallocated tax credits against estimated tax liabilities and determine the extent to which it will be able to utilize the investment's unallocated tax credits over the life of the tax credits. If assessment projections identify that the investment's unallocated tax credits will exceed what can be utilized under IRS or state tax provisions, the reporting entity shall nonadmit investments as necessary so that investments in scope of this statement (in aggregate) are only admitted to the extent tax credits are expected to be utilized within current, carryback, and carryforward periods. In making this assessment, the reporting entity is not permitted to assume increased operations (e.g., expanded product sales) beyond those allowed under prudent and feasible tax-planning strategies to conclude that additional federal or state tax liability will exist that would allow additional utilization of tax credits. A reporting entity may subsequently admit a previously nonadmitted tax credit investment, based on subsequent assessments in which the reporting entity determines that they will be able to utilize the unallocated tax credits.

20. Additional Admittance to Prospective Utilization Assessment – If the tax credit investment allocates tax credits with the following features, the reporting entity may perform a secondary assessment to determine if additional amounts of the tax credit investment nonadmitted under paragraph 19 can be admitted:

a. Tax credit investments which allocate tax credits which are certificated or transferable in accordance with permitted IRS or state tax provisions shall admit up to the lesser of the proportional amortized cost or fair value of the unallocated tax credits.

b. Tax credit investments which allocate tax credits eligible for direct payment shall admit up to the lesser of the proportional amortized cost or the estimated proceeds from unallocated tax credits.

21. For tax credit investments which have an amortization timeframe greater than the tax credit allocation timeframe (as demonstrated in Exhibit A), the reporting entity would still, if required, perform the prospective utilization assessment but on the reporting entity's ability to utilize the remaining stream of anticipated tax benefits.

Future Contributions and Additional Tax Credits

22. Many tax credit investments require future contributions by the investor, that may be contingent on a variety of conditions, such as receiving representations, contract performance, meeting occupancy requirements, etc. A liability shall be recognized for delayed contributions which result in additional tax credits that are unconditional and legally binding, and a liability shall also be recognized for contributions which result in additional tax credits that are contingent upon a future event when that contingent event becomes probable pursuant to the loss contingency guidance in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Liabilities or loss contingencies recognized for future contributions which result in additional tax credits shall be reported as 'Payable for Securities' until remitted or until the obligation is otherwise eliminated.

23. If a commitment to provide future contributions is not required to be recognized pursuant to paragraph 22, the commitment shall be disclosed in the notes to the financial statements with other commitments.

24. Additional contributions that do not result in additional tax credits for the reporting entity investor shall be immediately expensed as a component of net investment income.

25. If additional contributions result in additional tax credits for the reporting entity, the proportional amortization method for the tax credit investment shall be adjusted, on a prospective basis, to reflect the increased cost with the revised expected tax credits and other tax benefits.

26. In the event a reporting entity obtains additional tax credits without the reporting entity making additional contributions, the reporting entity shall not adjust the book/adjusted carrying value of the tax credit investment. (The proportional amortization method shall not be adjusted to reflect the expected additional tax credits.) Rather, the tax credit shall be recognized when allocated pursuant to paragraph 14.

Impairment of Tax Credit Investments

27. Reporting entities with investments in tax credit programs shall complete and document an impairment analysis at each reporting period. For this analysis, the reporting entity shall compare the current book/adjusted carrying value to the fair value of the investment. (If fair value is not determinable, an entity can compare book/adjusted carrying value to the present value of future tax credits and other tax benefits discounted at a risk-free rate of return.) If book/adjusted carrying value is higher, the difference between book/adjusted carrying value and fair value shall be recognized as an other-than-temporary impairment (INT 06-07) to the tax credit investment. This will result in a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries in fair value.

28. An other-than-temporary impairment shall also be considered to have occurred if a previously allocated tax credit has been recaptured or if it is probable that future tax credits will not be allocated as expected. If a project no longer qualifies for tax credits, the entire investment, less any residual established at initial recognition, shall be written off as other-than-temporarily impaired. If the reporting entity experiences a tax credit recapture, the reporting entity shall assess whether future tax credits and other benefits will qualify for use by the reporting entity. If future credits will not be generated or will be subject to future recapture, then the reporting entity shall write-off the investment as other-than-temporarily impaired so that the resulting investment value only reflects expected qualifying tax credits and other benefits expected to be allocated. This will result in a new cost basis and the amount of the write-down shall be accounted for as a realized loss. The new cost basis shall not be changed for subsequent recoveries or revision to tax credit expectations.

29. Certain tax credit programs allocate variable amounts of tax credits (for example, clean energy production tax credit programs) which will result in regular differences between actual allocated tax credits and estimated tax credit allocations as calculated upon acquisition of the investment. Variable tax credits allocated in excess of estimates should be accounted for in accordance with paragraph 26~~—~~. If the allocated variable tax credits are less than estimates by more than 10% or consistently allocate less than the estimated amounts over multiple allocation periods, then the reporting entity must either recognize an other-than-temporary impairment or specifically address within its impairment analysis the reason why consistently diminished tax credit returns do not represent an impairment event. Note that if the company determines it is probable that the total amount of anticipated variable tax credits will not be received, it would still be considered an other-than-temporary impairment in accordance with paragraph 28.

Disclosures

30. A reporting entity shall disclose information that enables users of its financial statements to understand the following information about its investments in projects that generate tax credits and other tax benefits from tax programs captured in scope of this statement:

a. The nature of its investments in projects that generate tax credits and other tax benefits.

b. The effect of the recognition and measurement of its investments in projects that generate tax credits and other tax benefits and the related tax credits on its financial position and results of operations.

31. To meet the objective of paragraph 30, a reporting entity shall disclose the following information about its investments in projects that generate tax credits and other tax benefits from a tax credit program in scope of this statement:

a. The amount of tax credits and other tax benefits recognized during the reporting period(s).

b. The balance of the investments recognized in the statement of financial position for the reporting period(s) presented.

c. The amount of investment amortization and non-income tax related activity recognized as a component of net investment income, and other returns allocated that were recognized outside of income tax expense.

d. An aggregate schedule of tax credits expected to be generated each year for the subsequent five years and thereafter, disaggregated by transferable/certificated and non-transferable.

e. Any commitment or contingent commitment (e.g., guarantees or commitments to provide additional capital contributions) including the amount of contributions that are contingent commitments related to tax credit investments and the year(s) that contingent commitments are expected to be paid shall be disclosed.

32. The following disclosures shall be included if applicable to tax credit investments:

a. If the underlying project is currently subject to any regulatory reviews and the status of such review. (Example: Investigations by the housing authority.)

b. Significant modifications or events that resulted in a change in the nature of the investment or a change in the relationship with the underlying project for investments in scope.

33. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:

a. A description of the impaired assets and the facts and circumstances leading to the impairment; and

b. The amount of the impairment and how fair value was determined.

34. The following disclosures pertain only to those tax credits allocated from tax credit investments and are unused as of the reporting period(s). For purposes of this disclosure, total unused tax credits represent the entire amount of tax credits available:

c. Carrying value of tax credits, disaggregated by transferable/certificated and non-transferable, gross of any related tax liabilities by jurisdiction and in total.

d. Total unused tax credits by jurisdiction, disaggregated by transferable/certificated and non-transferable.

e. Method of estimating utilization of remaining tax credits or other projected recovery of the current carrying value.

f. Impairment amount recognized in the reporting period(s), if any.

g. Identify tax credits by transferable/certificated and non-transferable classifications and identify the admitted and nonadmitted portions of each classification.

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

Relevant Literature

36. This statement adopts with modification *Accounting Standards Update (ASU) 2023-02, Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method*. The ASU is modified for the following statutory concepts:

a. This statement is applicable to all federal and state tax credit programs earned through any tax credit investment structure that meets the requirements in paragraph 2. Under the ASU, use of the proportional amortization method is an election and only pertains to income tax equity investment structures in which the reporting entity does not exercise significant influence. With this statement, the U.S. GAAP election to use the proportional amortization method is rejected and use of proportional amortization for investments within the scope of this statement is required. The guidance is expanded for state premium tax credits.

b. Investments that meet the criteria of this statement are required to use a proportional amortization method as prescribed in this statement. This method requires the tax credits and benefits to be recognized in proportion to the percentage of actual tax credits and other tax benefits allocated to the reporting entity in the current period divided by the total estimated tax credits and other tax benefits expected to be allocated by the reporting entity over the life of the investment. This statement requires a gross presentation on the financial statements. Under the ASU, a practical expedient is allowed for the calculation of proportional amortization but has been rejected with this statement.

c. Federal tax credits shall be recognized in the income statement as an offset to federal income taxes in the tax reporting year in which the tax credit is utilized in accordance with SSAP No. 101. State tax credits shall be recognized in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax reporting year in which the credit is utilized.

d. Tax benefits allocated, other than tax credits, shall be accounted for pursuant to SSAP No. 101. Amortization shall be reported as a component of net investment income.

e. Reporting entities shall follow the guidance in paragraphs 22 and 23 regarding the recognition of contingent commitments from SSAP No. 5R to equity contributions.

f. This statement has specific impairment and nonadmittance requirements.

g. For statutory accounting purposes, deferred taxes are not reported as a component of income from continuing operations in the income statement; rather deferred taxes are recognized as a separate component of gains and losses in unassigned funds (surplus).

h. Disclosures should be followed as indicated in the disclosures section in this statement.

i. The examples detailed in Exhibit A were modified to better illustrate the statutory accounting method for tax credit investments.

Effective Date and Transition

37. This statement is effective for reporting periods beginning on or after January 1, 2006. Early adoption is permitted. 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*. The guidance previously in paragraph 3 of this statement superseded paragraph 1 of SSAP No. 48. In 2011, this guidance was moved to SSAP No. 48*—Joint Ventures, Partnerships and Limited Liability Companies* and deleted from this statement. The original guidance included in this standard is retained for historical purposes in Issue Paper No. 125. The guidance from ASU 2014-01 is effective for reporting periods beginning on or after January 1, 2015, with early adoption permitted.

38. In March 2024, new SAP concept revisions, as detailed in Issue Paper No. XXX170, were adopted. These revisions, effective January 1, 2025, expanded the scope of SSAP No. 93R to include all federal and state tax credit investment structures and provide new guidance on the accounting, recognition, and reporting of tax credit investment structures. As of the effective date, reporting entities shall prospectively modify the recognition, accounting, and reporting of tax credit investment structures to reflect the guidance in the conceptual revisions. Additionally, all tax credit investment structures which fall within the scope of this statement not currently reported on Schedule BA are to be transferred to Schedule BA as of the effective date.

Glossary

39. The following definitions are provided for the purposes of this statement.

a. Unallocated tax credits – The portion of tax credits expected to be earned and allocated to the reporting entity through the tax credit investment structure.

b. Transferable/Certificated – The tax credits are certified for sale (certificated tax credits) or saleable through the execution of a state or federal transfer form (transferable tax credits).

i.c. More Likely Than Not – Refers to a likelihood of more than 50%.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 125—Accounting for Low-Income Housing Tax Credit Property Investments*
- *Issue Paper No. XX170—New Market Tax Credits Project*

EXHIBIT A – APPLICATION OF PROPORTIONAL AMORTIZATION METHOD

Example 1: Qualifying Tax Credit Investment Structure

On January 1, 20X1, ABC Insurance Company purchases a 5% equity stake in a tax credit investment structure for $100,000. The allocated tax credits are transferable, and ABC anticipates that all tax credits received will be fully utilized prior to expiration of the tax credit carryover period.

Assumptions:

1. All cash flows (except initial investment) occur at the end of each year.
2. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).
3. The investor made a $100,000 investment for a 5% limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.
4. The partnership finances the project cost of $4,000,000 with 50% equity and 50% debt.
5. The annual tax credit allocation (equal to 4% of the project's original cost) will be received for a period of 10 years.
6. The investor's tax rate is 40%.
7. For simplicity, the project will operate with break-even pretax cash flows including debt service during the first 15 years of operations.
8. The project's taxable loss will be equal to depreciation expense. The cumulative book loss (and thus the cumulative depreciation expense) recognized by the investor is limited to the $100,000 investment.
9. It is assumed that all requirements are met to retain allocable tax credits so there will be no recapture of tax credits.
10. The investor expects that the estimated residual value of the investment will be zero.

Proportional Amortization Method with Statutory Modifications

Year	Net Investment (1)	Amortization of Investment (2)	Tax Credits (3)	Net Losses/Tax Depreciation (4)	Other Tax Benefits from Tax Depreciation (5)	Tax Credits and Other Tax Benefits (6)
	100,000					
1	90,909	9,091	8,000	7,273	2,909	10,909
2	81,818	9,091	8,000	7,273	2,909	10,909
3	72,727	9,091	8,000	7,273	2,909	10,909
4	63,636	9,091	8,000	7,273	2,909	10,909
5	54,545	9,091	8,000	7,273	2,909	10,909
6	45,454	9,091	8,000	7,273	2,909	10,909
7	36,363	9,091	8,000	7,273	2,909	10,909
8	27,272	9,091	8,000	7,273	2,909	10,909
9	18,181	9,091	8,000	7,273	2,909	10,909
10	9,090	9,091	8,000	7,273	2,909	10,909
11	6,666	2,424		7,273	2,909	2,909
12	4,242	2,424		7,273	2,909	2,909
13	1,818	2,424		7,273	2,909	2,909
14	0	1,818		5,451	2,183	2,183
15	0					0
Total		100,000	80,000	100,000	40,000	120,000

(1) End-of-year investment for a 5% limited liability interest in the project net of amortization in Column (2).

(2) Initial investment of $100,000 x (total tax benefits allocated during the year in Column (6) / total anticipated tax benefits over the life of the investment of $120,000).

(3) Annual 4% tax credit on $200,000 tax basis of the underlying assets.

(4) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.5 years up to the amount of the initial investment of $100,000.

(5) Column (4) x 40% tax rate.

(6) Column (3) + Column (5).

Initial Year

	Debit	Credit
Tax credit investment	100,000	
Cash		100,000
To record the purchase of tax credit investment		

Years 1-10

	Debit	Credit
Amortization expense	9,091	
Tax credit investment		9,091
Federal tax credits	8,000	
Income tax expense		8,000

To record annual receipt of allocated tax credits and proportional amortization of investment.

		Debit	Credit
	Income taxes payable	8,000	
	Federal tax credits		8,000
	To record annual utilization of allocated tax credits.		
Year 11-13			
	Amortization expense	2,424	
	Tax credit investment		2,424
	To record annual proportional amortization of tax credit investment.		
Year 14			
	Amortization expense	1,818	
	Tax credit investment		1,818
	To record annual proportional amortization of tax credit investment.		

Example 2: Qualifying Tax Credit Investment Structure with Non-Income Tax Related Benefits

On January 1, 20X1, J&K Insurance Company purchased a 5% equity stake in a tax credit investment structure for $100,000. The allocated tax credits are non-transferable, and J&K anticipates that all tax credits received will be fully utilized prior to expiration of the tax credit carryover period.

Assumptions:

1. All cash flows (except initial investment) occur at the end of each year.

2. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).

3. The investor made a $100,000 investment for a 5% limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.

4. The partnership will receive production tax credits based on the energy the project produces. The credits will be allocated over a four-year period.

5. The tax equity investor will receive cash proceeds based on 2% of the project's cash generated during the life of the investment.

6. The investor's tax rate is 40%.

7. All requirements are met to retain allocable income tax credits such that there will be no recapture of income tax credits.

8. All of the conditions are met to require use of the proportional amortization method.

9. After 10 years, the tax equity investor has a right to require that the project sponsor purchase the tax equity investor's equity interest for a nominal amount. It is assumed that the Put option will be exercised and has a contractually agreed upon residual value of $1,000.

10. In Years 1-3 the investor is able to utilize all allocated tax credits in the same period they were received~~—~~. In Year 4, the investor is only able to utilize half of that year's allocated tax credit and defers the remainder for utilization in Year 5.

Proportional Amortization Method with Statutory Modifications

Year	Net Investment (1)	Amortization of Investment (2)	Tax Credits (3)	Net Losses/Tax Depreciation (4)	Other Tax Benefits from Tax Depreciation (5)	Tax Credits and Other Tax Benefits (6)	Non-Tax Related Cash Returns (7)
	100,000						
1	79,605	20,395	20,000	8,300	3,320	23,320	58
2	59,210	20,395	20,000	8,300	3,320	23,320	58
3	38,815	20,395	20,000	8,300	3,320	23,320	58
4	18,420	20,395	20,000	8,300	3,320	23,320	58
5	15,516	2,904		8,300	3,320	3,320	58
6	12,612	2,904		8,300	3,320	3,320	58
7	9,708	2,904		8,300	3,320	3,320	58
8	6,804	2,904		8,300	3,320	3,320	58
9	3,900	2,904		8,300	3,320	3,320	58
10	1,000	2,900		8,300	3,320	3,320	58
							580
Total	1,000	99,000	80,000	83,000	33,200	113,200	

(1) End-of-year investment for a 5% limited liability interest in the project net of amortization in Column (2).

(2) Initial investment, less residual value of $1,000, of $99,000 x (total tax benefits allocated during the year in Column (6) / total anticipated tax benefits over the life of the investment of $113,200).

(3) These tax credits have been generated through the production of electricity, which generates production tax credits. The tax equity investor is not receiving renewable energy credits or carbon offsets.

(4) Depreciation /other tax losses passed on to the investor.

(5) Column (4) x 40% tax rate.

(6) Column (3) + Column (5).

(7) Non-income-tax-related benefits recognized in current-period pre-tax earnings when allocated. This represents the cash proceeds allocated by the tax equity investor based on the cash generated from the project

Initial Year

Account	Debit	Credit
Tax credit investment	100,000	
Cash		100,000
To record the purchase of tax credit investment		

Years 1-3

Account	Debit	Credit
Amortization expense	20,395	
Tax credit investment		20,395
Federal tax credits	20,000	
Income tax expense		20,000

	Debit	Credit
Cash	58	
Investment Income		58

To record annual receipt of allocated tax credits, proportional amortization of investment, and receipt of non-tax cash returns.

	Debit	Credit
Income taxes payable	20,000	
Federal tax credits		20,000

To record annual utilization of allocated tax credits.

Year 4

	Debit	Credit
Amortization expense	20,395	
Tax credit investment		20,395
Federal tax credits	20,000	
Income tax expense		20,000
Cash	58	
Investment Income		58

To record annual receipt of allocated tax credits, proportional amortization of investment, and receipt of non-tax cash returns.

	Debit	Credit
Income taxes payable	10,000	
Federal tax credits		10,000
Income tax expense	10,000	
Deferred tax expense		10,000

To record the portion of allocated tax credits utilized in the current year and defer the remainder. (Federal tax credit account should be mapped to the DTA reporting line as any balance remaining at year-end would be a DTA)

Year 5

	Debit	Credit
Amortization expense	2,904	
Tax credit investment		2,904
Cash	58	
Investment Income		58

To record annual proportional amortization of tax credit investment and receipt of non-tax cash returns.

	Debit	Credit
Income taxes payable	10,000	
Federal tax credits		10,000
Deferred tax expense	10,000	
Income tax expense		10,000

To record utilization of deferred tax credit.

Years 6-9

	Debit	Credit
Amortization expense	2,904	
Tax credit investment		2,904
Cash	58	
Investment Income		58

To record annual proportional amortization of tax credit investment and receipt of non-tax cash returns.

Year 10

Amortization expense	2,900	
Tax credit investment		2,900
Cash	58	
Investment Income		58

To record annual proportional amortization of tax credit investment and receipt of non-tax cash returns.

Cash	1,000	
Tax credit investment		1,000

To record sale of interest in tax credit investment at stated residual value.

EXHIBIT A – LOW-INCOME HOUSING TAX CREDIT PROPERTY INVESTMENTS

A Limited Partnership Investment in an Affordable Housing Project Accounted for Using the Amortized Cost Method (modified to include tax benefits and record amortization as a component of net investment income):

This exhibit is based on ASU 2014-01, paragraph 323-740-55-7 of the Accounting Standards Codification. The amount and timing of amortization in the proportional amortization method is consistent with the statutory modifications; therefore, the table incorporated in this exhibit is based on the proportional amortization table. The statutory income statement requires a gross presentation on the income statement, with proportional amortization of the initial cost of the investment in investment income and the tax credits and benefits included in income tax expense.

Terms:
Date of Investment: January 1, 20X1
Purchase Price of Investment: $100,000

Assumptions:

1. All cash flows (except initial investment) occur at the end of each year.

2. Depreciation expense is computed, for book and tax purposes, using the straight-line method with a 27.5 year life (the same method is used for simplicity).

3. The investor made a $100,000 investment for a 5% limited partnership interest in the project at the beginning of the first year of eligibility for the tax credit.

4. The partnership finances the project cost of $4,000,000 with 50% equity and 50% debt.

5. The annual tax credit allocation (equal to 4% of the project's original cost) will be received for a period of 10 years.

6. The investor's tax rate is 40%.

7. For simplicity, the project will operate with break-even pretax cash flows including debt service during the first 15 years of operations.

8. The project's taxable loss will be equal to depreciation expense. The cumulative book loss (and thus the cumulative depreciation expense) recognized by the investor is limited to the $100,000 investment.

9. It is assumed that all requirements are met to retain allocable tax credits so there will be no recapture of tax credits.

10. The investor expects that the estimated residual value of the investment will be zero.

Proportional Amortization Method with Statutory Modifications

Year	Net Investment (1)	Amortization of Investment (2)	Tax Credits (3)	Net Losses/Tax Depreciation (4)	Other Tax Benefits from Tax Depreciation (5)	Tax Credits and Other Tax Benefits (6)
	100,000					
1	90,909	9,091	8,000	7,273	2,909	10,909
2	81,818	9,091	8,000	7,273	2,909	10,909
3	72,727	9,091	8,000	7,273	2,909	10,909
4	63,636	9,091	8,000	7,273	2,909	10,909
5	54,545	9,091	8,000	7,273	2,909	10,909
6	45,454	9,091	8,000	7,273	2,909	10,909
7	36,363	9,091	8,000	7,273	2,909	10,909
8	27,272	9,091	8,000	7,273	2,909	10,909
9	18,181	9,091	8,000	7,273	2,909	10,909
10	9,090	9,091	8,000	7,273	2,909	10,909
11	6,666	2,424		7,273	2,909	2,909
12	4,242	2,424		7,273	2,909	2,909
13	1,818	2,424		7,273	2,909	2,909
14	0	1,818		5,451	2,183	2,183
15	0					0
Total		100,000	80,000	100,000	40,000	120,000

(1) End-of-year investment for a 5% limited liability interest in the project net of amortization in Column (2).

(2) Initial investment of $100,000 x (total tax benefits received during the year in Column (6)/total anticipated tax benefits over the life of the investment of $120,000).

(3) A 4% tax credit on $200,000 tax basis of the underlying assets.

(4) Depreciation (on $200,000 tax basis of the underlying assets) using the straight-line method over 27.5 years up to the amount of the initial investment of $100,000.

(5) Column (4) x 40% tax rate.

(6) Column (3) + Column (5).

EXHIBIT B – TRACKED REVISIONS TO SSAP NO. 94R

Statements of Statutory Accounting Principles No. 94 – Revised

~~Transferable and Non-Transferable State~~ State and Federal Tax Credits

STATUS

Type of Issue	Common Area
Issued	June 12, 2006; Substantively revised December 7, 2011; Conceptually revised March 16, 2024.
Effective Date	December 31, 2006; Substantive revisions detailed in Issue Paper No. 145 effective December 31, 2011; Conceptual revisions detailed in Issue Paper No. 170 effective January 1, 2025.
Affects	No other pronouncements
Affected by	No other pronouncements
Interpreted by	No other pronouncements
Relevant Appendix A Guidance	None

STATUS ERROR! BOOKMARK NOT DEFINED.
SCOPE OF STATEMENT ERROR! BOOKMARK NOT DEFINED.
SUMMARY CONCLUSION ERROR! BOOKMARK NOT DEFINED.
Accounting 50
Admittance 52
Impairment **Error! Bookmark not defined.**
Disclosures **Error! Bookmark not defined.**
Effective Date and Transition **Error! Bookmark not defined.**
REFERENCES ERROR! BOOKMARK NOT DEFINED.
Relevant Issue Papers **Error! Bookmark not defined.**
EXHIBIT A – ACCOUNTING FOR TRANSFERABLE TAX CREDITS ERROR! BOOKMARK NOT DEFINED.
EXHIBIT B – ACCOUNTING FOR NON-TRANSFERABLE TAX CREDITS ERROR! BOOKMARK NOT DEFINED.
~~**STATUS** 1~~
~~**SCOPE OF STATEMENT** 1~~
~~**SUMMARY CONCLUSION** 2~~
~~Transferable State Tax Credits 2~~
~~Non-Transferable State Tax Credits 2~~
~~Acquisition 3~~
~~Balance Sheet Treatment 3~~
~~Income Statement Treatment 3~~
~~Impairment 3~~
~~Disclosures 3~~
~~Effective Date and Transition 4~~
~~**REFERENCES** 4~~

~~Relevant Issue Papers .... 4~~

~~**EXHIBIT A – ACCOUNTING FOR TRANSFERABLE STATE TAX CREDITS .... 5**~~

~~**EXHIBIT B – ACCOUNTING FOR NON-TRANSFERABLE STATE TAX CREDITS .... 6**~~

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for state and federal tax credits that are purchased[fn] by the reporting entity. Tax credits allocated from investments NOT within the scope of *SSAP 93R—Investments in Tax Credit Structures* should refer to this statement for tax credit accounting guidance. Tax credits which have been awarded[fn] to the reporting entity are not within the scope of this statement and should refer to *SSAP No. 101—Income Taxes*.~~transferable and non-transferable state tax credits that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).~~

2. Tax credits allocated from, and investments in, tax credit structures, as discussed in SSAP No. 93R which involve investments in projects or programs that generate general business federal tax credits or state tax credits~~Investments in Low-Income Housing Tax Credits as discussed in *SSAP No. 93—Low-Income Housing Tax Credit Property Investments*, which involve an investment by a reporting entity in a limited liability company or similar entity that earns tax credits as a consequence of its operating activities involving low-income housing developments and passes those tax credits to its investors~~, are not within the scope of this statement.

3. Investments in a CAPCO (Certified Capital Company), organized as a partnership or an LLC, which is a company, authorized by state statute that borrows from investors~~ (insurance companies)~~, in order to make venture capital investments in "qualified" businesses, are not within the scope of this statement. Although associated with tax credits, the ~~insurance company~~investors is paid principal and interest on its investment with the CAPCO. Depending upon the terms of the CAPCO offering, principal and interest payments to the ~~insurance company~~investors will come from the CAPCO and/or the state. The CAPCO will make cash payments directly to the ~~insurance company~~investors while the state will make payments in the form of premium or income tax credits. Investments in a CAPCO shall be accounted for in accordance with *Interpretation (INT) 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)* and specific statutory accounting guidance addressing CAPCOs.

SUMMARY CONCLUSION

4. Both state and federal governments have enacted laws that create programs by which tax credits are granted to entities under certain specified conditions. The terms of these tax credits vary based on the issuing jurisdiction and from program to program.~~The criteria in paragraphs 5 and 6 are for transferable state tax credits (i.e., credits which may be sold or assigned). The criteria in paragraphs 7 and 8 are for non-transferable state tax credits (i.e., those which cannot be sold or assigned to other parties).~~

5. For the purposes of this statement, "tax credits" must be issued by either a federal or state governmental entity and must be refundable[fn] or can be applied against income tax or premium tax in accordance with permitted IRS or state tax provisions. Tax credits which may be sold or otherwise transferred to another entity are referred to as "transferable tax credits" whereas all other tax credits are referred to as "non-transferable."

~~**4. Transferable State Tax Credits**~~

~~5. Some states have enacted laws that create programs by which transferable state tax credits are granted to entities under certain specified conditions (e.g., an entity makes an investment in a particular industry). The terms of these state tax credits vary from state to state and, within a state, from program to program. However, many of these transferable state tax credit programs share the following four characteristics:~~

~~6. The tax credit is nonrefundable;~~

~~7. The holder of the transferable state tax credit may sell or otherwise transfer the transferable state tax credit to another entity, which can likewise resell or transfer the credit;~~

~~8. The transferable state tax credit will expire if not used by a predetermined date; and~~

~~9. The transferable state tax credit can be applied against either state income tax or state premium tax.~~

6. ~~For purposes of this statement, such programs will be referred to as "transferable state tax credits." The criteria in paragraphs 5.b., 5.c. and 5.d. must be present in order for the transferable state tax credit to receive the accounting treatment described in this statement.~~ When a reporting entity purchases a transferable or certificated ~~state~~ tax credit from another entity, the transaction does not result in a continuing investment in a business entity (i.e. limited partnership). Direct payment elections are non-revocable and supersede the transferability of tax credits, as such, once the election has been made the tax credit would be considered a non-transferable tax credit.

Accounting

7. All tax credits within the scope of the statement must be recognized in the period they are allocated to or purchased by the reporting entity for tax purposes and must be recorded at face value upon receipt. Tax credits acquired at a premium or discount to their face value must record the gain/loss as follows:

   a. Tax credits acquired at a discount must defer the gain as a miscellaneous liability upon receipt of the tax credit.

   b. Tax credits acquired at a premium must realize the loss within the income statement upon receipt of the tax credit.

8. Deferred ~~G~~gains on ~~transferable and non-transferable state~~ tax credits are deferred until the value of the ~~state~~ tax credits utilized exceeds the initial acquisition cost of the ~~state~~ tax credits, or until the ~~state~~ tax credits are sold to other entities or the direct payment election is utilized and the payment(s) ~~received is greater than the book value~~exceed the initial acquisition cost.

9. Tax credits shall be recognized in the period that they are purchased or allocated to the reporting entity for tax purposes:

Drafting Note: The revisions adopted in agenda item 2024-18 revise paragraphs 9.a. through 10 and are also effective 1/1/2025.

   a. Federal tax credits that can be utilized in the year allocated or purchased shall be reported in the income statement as an offset to federal taxes in accordance with SSAP No. 101~~–~~ ~~*Income Taxes*~~. Federal tax credits that cannot be utilized in the year allocated or

purchased and are carried forward to a future tax year shall be reported as a deferred tax asset (DTA) in accordance with SSAP No. 101.

b. State tax credits that can be utilized in the year allocated or purchased shall be reported in the income statement as an offset to state premium tax or state income tax, whichever is applicable, in the tax-reporting year in which the credit is utilized. State tax credits that cannot be utilized in the year allocated or purchased and are carried forward to a future tax year shall be reported gross of any related state tax liabilities and reported in the category of other-than-invested-assets (not to be reported net).

~~10.~~ Use of carried forward tax credits in a future period shall be reflected as an offset to the corresponding income or premium tax in the tax reporting year in which the tax credit is utilized.~~Non-Transferable State Tax Credits~~

~~11. If the original or subsequent holder of the transferable tax credit is not able to transfer the tax credit, then the admissibility criteria in paragraph 8 for non-transferable tax credits apply. These non-transferable state tax credits share the following characteristics:~~

~~12. The tax credit is nonrefundable;~~

~~13. The successive holder of a state tax credit must redeem the credit by April 15 of the subsequent year to the entity's acquisition of the state tax credit and is not permitted to carry-over, carry-back, obtain a refund, sell or assign the credit;~~

~~14. The non-transferable state tax credit will expire if not used by the predetermined date; and~~

~~15. The non-transferable state tax credit can be applied against either state income tax or state premium tax.~~

~~16. The criteria in paragraphs 7.b., 7.c. and 7.d. must be present in order for the non-transferable state tax credit to receive the accounting treatment described in this statement.~~

~~17. Transferable and non-transferable state tax credits as defined within this SSAP held by reporting entities meet the definition of assets as specified in SSAP No. 4—Assets and Nonadmitted Assets and are admissible assets to the extent that they comply with the requirements of this statement. If the criteria in paragraphs 6 or 8 are not met, the tax credits are nonadmitted.~~

~~18. Acquisition~~

~~19. Transferable and non-transferable state tax credits are recorded at cost at the date of acquisition.~~

~~20. Balance Sheet Treatment~~

~~21. Transferable and non-transferable state tax credits expected to be realized are initially recorded at cost.~~

~~22. Transferable and non-transferable state tax credits shall be established gross of any related state tax liabilities and reported in the category of other-than-invested assets (not reported net).~~

~~23. As transferable and non-transferable state tax credits are redeemed, the carrying value of the tax credits is reduced dollar for dollar by the amount of state tax credits applied toward the reporting entity's applicable state tax liability.~~

~~24. Income Statement Treatment~~

25. Gains on transferable and non-transferable state tax credits are deferred until the value of the state tax credits utilized exceeds the cost of the state tax credits or until the state tax credits are sold to other entities and the payment received is greater than the book value.

26.10. Losses on transferable and non-transferable state tax credits are recognized when known.

11. Gains and losses on transferable and non-transferable state tax credits are reflected in other income when realized.

12. A tax credit asset is considered purchased or allocated once the tax credit is received and available for use. If the reporting entity determines a commitment to purchase tax credits has met the definition of a liability, then the asset would be reported in other-than-invested assets as tax credits receivable.

Admittance

13. Transferable and non-transferable tTax credits as defined within this SSAP held by reporting entities meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admissible assets to the extent that they comply with the requirements of this statement. The admissibility of tax credits is subject to SSAP No. 101.

Impairment

27.14. An impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to recover the book/carrying amount value of the transferable or non-transferable state tax credits. State tTax credits should be evaluated for impairment at each reporting date.

28.15. When there is a decline in the realizability of a transferable or non-transferable state tax credit owned by the reporting entity that is other--than--temporary(INT 06-07), the asset shall be written down to the expected realizable amount and the amount of the write down shall be accounted for as a realized loss. The expected realizable value is the new cost basis.

29.16. The new cost basis shall not be changed for subsequent recoveries in realizability.

Disclosures

30.17. The following disclosures shall be made in the financial statements. For purposes of this disclosure, total unused transferable and non-transferable state tax credits represent the entire transferable and non-transferable state amount of tax credits available:

a. Carrying value of transferable and non-transferable state tax credits, disaggregated by transferable/certificated and non-transferable, gross of any related state tax liabilities by state jurisdiction and in total.;

b. Total unused transferable and non-transferable state tax credits by statejurisdiction, disaggregated by transferable/certificated and non-transferable.;

c. Method of estimating utilization of remaining transferable and non-transferable state tax credits or other projected recovery of the current carrying value.

d. Impairment amount recognized in the reporting period, if any.

e. Identify state tax credits by transferable/certificated and non-transferable classifications, and identify the admitted and Nnonadmitted portions of each classification.

18. Any commitment or contingent commitment to purchase tax credits shall be disclosed.

Effective Date and Transition

19. This statement is effective for reporting periods ending on or after December 31, 2006. Early adoption is permitted. 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*. Substantive revisions to 1) revising the title; 2) incorporating the criteria for non-transferable state tax credits as described in paragraphs 7 and 8; 3) adding a disclosure; and 4) updating terminology throughout the document as appropriate, are effective for reporting periods ending on or after December 31, 2011.

20. In March 2024, new SAP concept revisions, as detailed in Issue Paper No. 170, were adopted. These revisions, effective January 1, 2025, with early adoption permitted, expanded the scope of SSAP No. 94R to include all purchased, and certain allocated, state and federal income or premium tax credits and provide new guidance on the accounting, recognition, and reporting for state and federal tax credits within the scope of this statement. As of the effective date, reporting entities shall prospectively modify the recognition, accounting, and reporting of tax credits within the scope of this statement to reflect the guidance in the conceptual revisions. For unutilized tax credits which were carried forward from prior to the effective date:

a. Federal tax credits in other-than-invested assets are to be transferred and reported as a DTA in accordance with SSAP No. 101.

b. Tax credits previously recorded at acquisition cost should be adjusted to reflect the face value of the acquired tax credits with the corresponding loss immediately recognized or the gain deferred.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 126—Accounting for Transferable State Tax Credits*
- *Issue Paper No. 145—Accounting for Transferable and Non-Transferable State Tax Credits*
- *Issue Paper No. 170—Tax Credits Project*

EXHIBIT A – ACCOUNTING FOR TRANSFERABLE STATE TAX CREDITS

On 1/1/X1 SAM Insurance Company purchased transferable state tax credits for a cost of $100,000. The transferable state tax credits are redeemable for $160,000 and expire at the end of 12/31/X4. SAM initially expects to utilize the tax credits before expiration in their state of domicile in the amount of $40,000 per year. In year X4, SAM sells the remaining $30,000 in transferable state tax credits for $20,000.

Date	Account	Debit	Credit
1/1/x1	Transferable state tax credits	160,000	
	Deferred gains on acquired tax credits		60,000
	Cash		100,000
	To record the purchase of the tax credits		
6/30/x1	Premium tax expense	40,000	
	Premium taxes payable to domiciliary state		40,000
	To record premium tax expense and accrue the liability in Year 1.		
10/1/x1	Premium tax payable	40,000	
	Transferable state tax credits		40,000
	To record the use of tax credits in Year 1. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x2	Premium tax expense	60,000	
	Premium taxes payable to domiciliary state		60,000
	To record premium tax expense and accrue the liability in Year 2.		
9/30/x2	Premium tax payable	60,000	
	Transferable state tax credits		60,000
	To record the use of taxes credits in Year 2. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x3	Premium tax expense	30,000	
	Premium taxes payable to domiciliary state		30,000
	To record premium tax expense and accrue the liability in Year 3.		
9/30/x3	Premium tax payable	30,000	
	Transferable state tax credits		30,000
	Deferred gains on acquired tax credits	30,000	
	Other income		30,000
	To record the use of premium tax credits in excess of cost and recognize a gain on premium tax credits in other income. The Company intends to sell the remaining tax credits in year 4.		
6/30/x4	Cash	20,000	
	Other income	10,000	
	Transferable state tax credits		30,000
	Deferred gains on acquired tax credits	30,000	
	Other income		30,000
	To record the sale of the remaining tax credits.		
1/1/x1	Transferable state tax credits	100,000	
	Cash		100,000
	To record the purchase of the tax credits		

6/30/x1	Premium tax expense	40,000	
	Premium taxes payable to domiciliary state		40,000
	To record premium tax expense and accrue the liability in Year 1.		
10/1/x1	Premium tax payable	40,000	
	Transferable state tax credits		40,000
	To record the use of tax credits in Year 1. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x2	Premium tax expense	60,000	
	Premium taxes payable to domiciliary state		60,000
	To record premium tax expense and accrue the liability in Year 2.		
9/30/x2	Premium tax payable	60,000	
	Transferable state tax credits		60,000
	To record the use of taxes credits in Year 2. The reporting entity expects to be able to utilize remaining tax credits before expiration.		
6/30/x3	Premium tax expense	30,000	
	Premium taxes payable to domiciliary state		30,000
	To record premium tax expense and accrue the liability in Year 3.		
9/30/x3	Premium tax payable	30,000	
	Other income		30,000
	To record the use of premium tax credits in excess of cost and recognize a gain on premium tax credits in other income. The Company intends to sell the remaining tax credits in year 4.		
6/30/x4	Cash	20,000	
	Other income		20,000
	To record the sale of the remaining tax credits.		

EXHIBIT B – ACCOUNTING FOR NON-TRANSFERABLE ~~STATE~~ TAX CREDITS

On 7/1/X1 LJW Insurance Company purchased non-transferable ~~state~~ federal tax credits for a cost of $100,000. The ~~state~~ federal tax credits are redeemable for $110,000~~, are not transferable~~ and expire on, April 15, 20x2. LJW expects to utilize the tax credits before expiration in their state of domicile in the amount of $110,000. Tax credits are utilized pro-rata, approximately $36,666 every quarter, from acquisition date to expiration date. The illustration below assumes that LJW Insurance Company's quarterly income tax liability equals the amount of credits that were purchased.

Date	Account	Debit	Credit
7/1/x1	Federal tax credits	110,000	
	Deferred gains on acquired tax credits		10,000
	Cash		100,000
	To record the purchase of the tax credits		
9/30/x1	Income tax expense	36,666	
	Income taxes payable		36,666
	To record quarterly income tax liability.		
10/1/x1	Income taxes payable	36,666	
	Federal tax credits		36,666
	To record the use of tax credits in the quarter.		
12/31/x1	Income tax expense	36,666	
	Income taxes payable		36,666
	To record quarterly income tax liability.		
1/1/x2	Income taxes payable	36,666	
	Federal tax credits		36,666
	To record the use of tax credits in the quarter.		
3/31/x2	Income tax expense	36,668	
	Income taxes payable		36,668
	To record quarterly income tax liability.		
4/1/x2	Income taxes payable	36,668	
	Deferred gains on acquired tax credits	10,000	
	Other Income		10,000
	Federal tax credits		36,668
	To record the use of tax credits in the quarter.		

Date	Account	Debit	Credit
~~7/1/x1~~	~~State tax credits~~	~~100,000~~	
	~~Cash~~		~~100,000~~
	~~*To record the purchase of the tax credits*~~		
~~9/30/x1~~	~~Premium tax expense~~	~~200,000~~	
	~~Premium taxes payable to domiciliary state~~		~~200,000~~
	~~*To record premium tax expense and accrue the liability.*~~		
~~3/15/x2~~	~~Premium tax payable~~	~~110,000~~	
	~~Other Income~~		~~10,000~~
	~~State tax credits~~		~~100,000~~

To record the use of premium tax credits in excess of cost and recognize a gain on premium tax credits in other income. (The additional $90,000 of premium taxes payable would still be due.)

EXHIBIT C – CONSISTENCY REVISIONS TO SSAP NO. 34 AND SSAP NO. 48

Revisions to ***SSAP No. 34—Investment Income Due and Accrued***

SCOPE OF STATEMENT

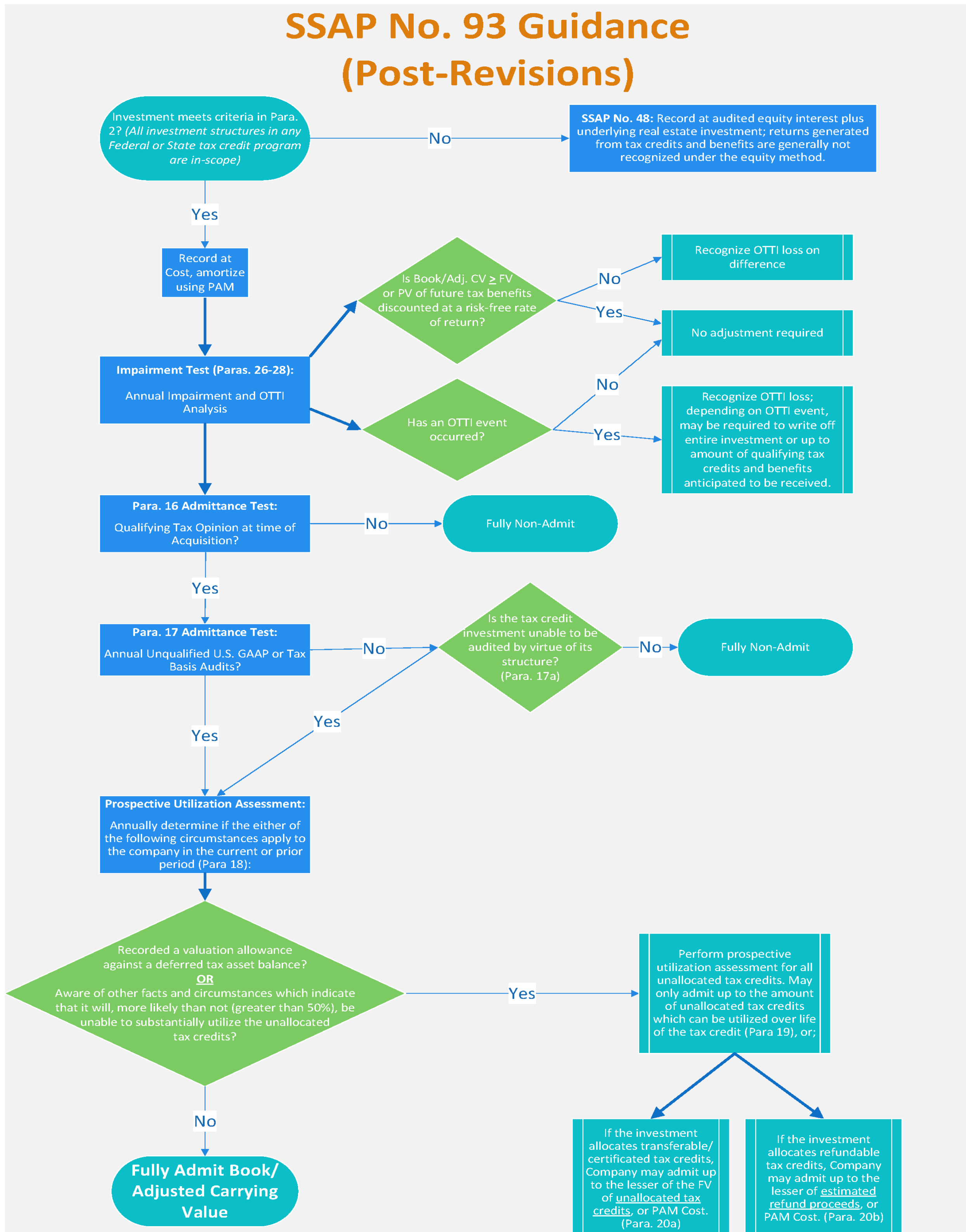
1. This statement establishes statutory accounting principles for investment income due and accrued. This statement does not address the accounting for tax credits allocated or purchased, which are discussed in *SSAP No. 93R—Investments in Tax Credit Structures* and *SSAP No. 94R—State and Federal Tax Credits*.

Revisions to ***SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies***

SCOPE OF STATEMENT

2. This statement establishes statutory accounting principles for investments in any joint ventures, partnerships, and limited liability companies, including investments in certified capital companies (CAPCO) per *INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)*, whether or not it is considered to be controlled by or affiliated with the reporting entity. Single real estate property investments that are wholly-owned by an LLC that is directly and wholly-owned by the reporting entity, and that meet the criteria established in *SSAP No. 40R—Real Estate Investments*, are excluded from this statement. This statement does not address the accounting for investments in joint ventures, partnerships, and and limited liability companies that invest in tax credit programs that and are in the scope ofhold an equity interest in either a tax syndication structure or tax equity fund invest in Low-Income Housing Tax Credit Properties as discussed in *SSAP No. 93R—Low-Income Housing Tax Credit Property InvestmentsInvestments in Tax Credit Structures*.

EXHIBIT D – FLOWCHART OF ORDER OF OPERATIONS FOR REVISED SSAP NO. 93



Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: SSAP No. 56 – Book Value Separate Accounts

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been developed to expand the guidance in *SSAP No. 56—Separate Accounts* to further address situations and provide consistent accounting guidelines for when assets are reported at a measurement method other than fair value. The guidance in SSAP No. 56 predominantly focuses on separate account products in which the policyholder bears the investment risk. In those situations, the assets in the separate account are reported at fair value. SSAP No. 56, paragraph 17 provides limited guidance for assets supporting fund accumulation contracts (GICs), and this measurement method is generally referred to as "book value":

> Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, will be recorded as if the assets were held in the general account. Assets supporting all other contractual benefits shall be recorded at fair value on the date of valuation, or if there is no readily available market, then in accordance with the valuation procedures in the applicable contract.

NAIC staff are aware that there has been an increase in assets reported at "book value" within the separate account. These have been approved under state prescribed practices and/or interpretations that the reference for fund accumulation contracts captures pension risk transfer (PRT) or registered indexed-linked annuities (RILA) and other similar general-account type products that have been approved by the state of domicile for reporting in the separate account.

The guidance in *SSAP No. 56—Separate Accounts* focuses on the accounting and reporting for both the separate account and general account, with specific focus on what is captured within each account as well as transfers between the two accounts. As the focus is on fair value separate account assets, there is not guidance that details how transfers should occur between the separate and general accounts when the assets will be retained and reported at "book value." Particularly, the guidance does not address whether assets should be disposed / recognized at fair value when transferring between accounts, with subsequent reporting at the general account measurement guidance or whether the assets should be transferred at the "book value" that is reported in the existing account. The process has the potential to impact recognition of gains / losses and IMR, so it should be clearly detailed to ensure consistent reporting.

Existing Authoritative Literature:

- ***SSAP No. 56—Separate Accounts***

Although the entirety of SSAP No. 56 may be relevant, key paragraphs have been identified.

General Account Reporting

5. For those separate account contracts classified as life contracts under *SSAP No. 50—Classification of Insurance or Managed Care Contracts,* premiums and annuity considerations shall be recorded as income in the Summary of Operations of the general account, and as transfers to premiums and considerations in the

separate account statement. Deposit-type contracts shall be recorded in the general account in accordance with *SSAP No. 52—Deposit-Type Contracts*.(INT 00-03) Charges (e.g., fees associated with investment management, administration, and contract guarantees) assessed on the separate accounts, as well as the net gain from operations of the separate account, shall be recorded as income in the Summary of Operations of the general account. Expenses relating to investment management, administration, and contract guarantees pertaining to separate account operations, as well as benefits and surrenders incurred on behalf of separate account contracts classified as life contracts, net transfers between separate accounts, commissions, and premium taxes (if any) shall be recorded as expenses in the Summary of Operations of the general account.

6. The general account shall include the total assets and liabilities, including transfers due or accrued, of any separate accounts business which it maintains and, therefore, the surplus, if any, of its separate accounts business. Transfers to the general account due or accrued shall be reported on a net basis so that the asset and the liability totals of the general account are not overstated. Changes in the surplus of the separate accounts business of an insurer, except for changes resulting from the net gain from operations of the separate account, shall be charged or credited directly to the unassigned funds (surplus) of the general account.

Separate Account Reporting

15. The separate accounts annual statement is concerned with the flow of funds related to investment activities and obligations of the separate accounts and with the transfer of funds between the separate account and the general account. As a result, the separate account statement shall report only the assets, liabilities, and operations of the separate account and shall not include general account expenses related to investment management, administration, or contract guarantees pertaining to separate account operations which are recorded in the general account.

16. The separate account records premiums, considerations (net of loading for sales charges such as commissions and premium taxes) and receipts (other than for net investment income and realized capital gains and losses) as income transfers from the general account. Net investment income and realized and unrealized capital gains and losses relating to the investment operations of the separate account are recorded as income in the Summary of Operations. When the contract provides for such, expenses and taxes associated with the separate account investment operations shall be deducted in the determination of net investment income. Deposits and withdrawals on deposit-type contracts shall be recorded in the Summary of Operations. Benefits and surrenders, reserve transfers, policy loans1, policyholder charges (e.g., fees associated with investment management, administration, and contract guarantees), and federal income taxes relating to the separate account are recorded as expense transfers to the general account in the Summary of Operations. The net change in aggregate reserves relating to separate account contracts is reported as an expense in the Summary of Operations.

17. Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, will be recorded as if the assets were held in the general account. Assets supporting all other contractual benefits shall be recorded at fair value on the date of valuation, or if there is no readily available market, then in accordance with the valuation procedures in the applicable contract.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):

1. Agenda Item 2022-19: Negative IMR introduced the discussion of interest maintenance reserve (IMR) within statutory accounting, specifically the guidance for nonadmittance of disallowed negative IMR. This agenda item resulted with *INT 23-01: Net Negative (Disallowed) Interest Maintenance Reserve*. This INT

[1] Policy loans related to separate account products shall follow the guidance in *SSAP No. 49—Policy Loans*. As detailed within SSAP No. 49, as part of the expense transfer, policy loans related to separate account products require a liquidation of the separate account assets to fund the loan issued by the general account. A transfer of assets from the separate account to the general account must have occurred to fund the policy loan issuance; otherwise the policy loan is nonadmitted in the general account.

permits admittance of disallowed negative IMR up to 10% of adjusted capital and surplus. The guidance permits admittance of the separate account negative IMR once the general account negative IMR has been admitted if the 10% limit has not been reached. The INT identifies that the concept of nonadmitted assets does not exist in the separate account, therefore the guidance includes application guidance for reversing prior actions that charged negative IMR to surplus before permitting the negative IMR to be recognized as an asset.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommend that the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP clarification with direction to work with industry in determining current application / differences in interpretations to present to the Working Group along with suggested revisions to codify the approach within SSAP No. 56.

Staff Review Completed by: Julie Gann, NAIC Staff—February 2024

Updated Recommendation – 2024 Summer National Meeting:

The IMR Ad Hoc Subgroup has discussed a number of elements generating IMR, including the transfer of assets for cash between the general account (GA) and book value separate accounts (BVSA). This discussion is about transfers of assets where one account is purchasing existing assets held by the other account. This discussion received information from the ACLI noting that reporting entities have taken different approaches in the recording of these transfers, with three broad methods. All methods have a net zero surplus impact.

1. Market Value Offsetting Method:
   - Selling Account transfers the asset at fair value, with a realized gain or loss and allocation to IMR.
   - Purchasing Account records the asset at book value, with an adjustment to IMR for the difference between the fair value and book value.
   - This method has offsetting IMR impacts between the GA and BVSA, with a zero net impact to surplus.

2. Market Value SSAP No. 25 Method:
   - Selling Account transfers the asset at fair value. If resulting in a gain, the gain is offset by a *SSAP No. 25—Affiliates and Other Related Parties* adjustment (deferral until gain is permanent). Losses are recognized and allocated to IMR.
   - Purchasing Account records the asset at market value and records applicable amortized cost valuation adjustments over the term to maturity.
   - This method results in different IMR treatment between the GA and BVSA based on whether the transaction resulted in a gain or loss. This method requires the reporting entity to track the asset and recognize the deferred gain once the asset is subsequently sold or matured in the BVSA.
   - The reporting results in a net zero impact to surplus.

3. Book Value Method:
   - Both accounts (selling / purchasing) record the asset at book value.
   - There is no IMR impact and no surplus impact.
   - This method has raised concerns on whether a transfer from the GA at book value to an insulated BVSA, provides appropriate treatment to the GA policyholders.

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The ACLI noted that although the above different approaches have been used, if the NAIC decides a standard accounting practice should be applied for transfers for cash between the GA and BVSA (and vice versa), the ACLI would support the market value offsetting IMR method. The rationale for supporting this method is as follows:

1. Market value transactions ensure the insurer is transacting to meet the fiduciary obligations of all policyholders (both GA and BVSA).
2. The method results in a net zero impact to surplus.
3. The method ensures a net zero impact to the combined GA and BVSA IMR in both gain and loss scenarios. (Although IMR is recognized in both accounts, the amounts recognized are offsetting.)
4. The method is more favorable operationally than the SSAP No. 25 method in which gains from the transfer must be deferred until a subsequent act that makes the transaction permanent (subsequent selling or maturity of asset).
5. The transfer at fair value combined with the offsetting IMR ensure that both the GA and BVSA retain the economic impact of the transaction without mingling the economics between the books.

The ACLI noted that this recommendation was only for transfers for cash between the GA and BVSA accounts and recommend additional research and discussion before creating a standard practice for less common transactions between the GA and BVSA, such as asset for asset swaps, contributions of assets to support deficiency in the SA and dividends of assets from the BVSA.

For the 2024 Summer National Meeting, NAIC staff recommend that the Working Group expose proposed revisions to SSAP No. 56 to clarify and expand guidance for book value separate accounts, and to incorporate accounting guidance for transfers of assets in exchange for cash between the general account and book value separate accounts. (Due to the design / order of SSAP No. 56, the entire SSAP has been reflected with the proposed edits shown as tracked changes.)

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed this agenda item and directed NAIC staff to work with industry in determining current application and differences in the treatment of book value assets within the separate account and to prepare suggested revisions to codify an approach within *SSAP No. 56—Separate Accounts*.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *SSAP No. 56—Separate Accounts,* as shown below as "2024 Summer National Meeting Exposed Revisions," to allow for initial review and consideration of potential changes to update measurement method guidance and specify the process to transfer assets for cash between the general and book-value separate accounts. The Working Group also requested comments from regulators and industry on the noted questions, which are shown shaded in grey. This item was exposed with a longer comment period ending November 8, 2024. This item is not planned for detailed discussion at the 2024 Fall National Meeting but is planned for discussion in the interim after that meeting, or at the 2025 Spring National Meeting.

2024 Summer National Meeting Exposed Revisions to SSAP No. 56:
(Paragraph references have been shaded for subsequent confirmation.)

SCOPE OF STATEMENT
1. This statement establishes statutory accounting principles for accounting and reporting for separate accounts in both the general account and separate account statements.

SUMMARY CONCLUSION

Introduction

2. Separate accounts are used to fund variable life insurance, variable annuities, modified guaranteed annuities and modified guaranteed life insurance, or various group contracts under pension or other employee benefit plans where funds are held in a separate account to support a liability. When separate accounts are established and filed accordingly, they may be used to fund guaranteed benefits. Separate account contracts may also be used to accumulate funds which are intended to be applied at some later time to provide life insurance or to accumulate proceeds applied under settlement or dividend options.

3. Assets held in separate accounts are owned by the insurer. All investment income and realized and unrealized capital gains and losses from assets allocated to a separate account, net of related investment expenses, are generally reflected in the separate account and, except for modified guaranteed annuities, modified guaranteed life insurance, and separate accounts established and filed to provide guaranteed benefits, investment performance is generally not guaranteed by the insurer. Charges relating to contract guarantees, administration, and investment management are deducted from separate accounts.

General Account Reporting

4. Insurance activities such as sales, underwriting and contract administration, premium collection and payment of premium taxes, claims, and benefits are functions of the insurance company distinct from the separate account and shall be accounted for as transactions of the general account.

5. For those separate account contracts classified as life contracts under *SSAP No. 50—Classification of Insurance or Managed Care Contracts*, premiums and annuity considerations shall be recorded as income in the Summary of Operations of the general account, and as transfers to premiums and considerations in the separate account statement. Deposit-type contracts shall be recorded in the general account in accordance with *SSAP No. 52—Deposit-Type Contracts*.[INT 00-03] Charges (e.g., fees associated with investment management, administration, and contract guarantees) assessed on the separate accounts, as well as the net gain from operations of the separate account, shall be recorded as income in the Summary of Operations of the general account. Expenses relating to investment management, administration, and contract guarantees pertaining to separate account operations, as well as benefits and surrenders incurred on behalf of separate account contracts classified as life contracts, net transfers between separate accounts, commissions, and premium taxes (if any) shall be recorded as expenses in the Summary of Operations of the general account.

6. The general account shall include the total assets and liabilities, including transfers due or accrued, of any separate accounts business which it maintains and, therefore, the surplus, if any, of its separate accounts business. Transfers to the general account due or accrued shall be reported on a net basis so that the asset and the liability totals of the general account are not overstated. Changes in the surplus of the separate accounts business of an insurer, except for changes resulting from the net gain from operations of the separate account, shall be charged or credited directly to the unassigned funds (surplus) of the general account.

7. Where a variable annuity contract or variable life insurance contract contains a guaranteed minimum death benefit, any reserve liability for such death benefit provision shall be recorded and held in the general account based on the reserving guidance in paragraphs 25 and 26. Any differences between the benefit paid and the separate account asset value of the contract shall be charged against or credited to the general account in its net gain from operations.

8. Separate account surplus may not become negative. For example, for separate account contracts which have annuitized (i.e., contracts in the payout stage), lower than expected mortality on variable annuity contracts containing mortality guarantees may cause a deficiency in the investment funds underlying the contract reserves. Thus the general account incurs an expense and the separate account realizes revenue to cover the deficiency, if necessary. Conversely, excess funds from higher than expected mortality will result in mortality gains, which are

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included in the Summary of Operations of the separate account and are ultimately recorded as equity in net income from separate account operations as discussed in paragraph 5.

9. Separate account surplus created through the use of the commissioners' reserve valuation method (CRVM), commissioners' annuity reserve valuation method (CARVM), or other reserving methods, shall be reported by the general account as an unsettled transfer from the separate account. The net change on such transfers shall be included as a part of the net gain from operations in the general account.

10. Surplus funds transferred from the general account to the separate account, commonly referred to as seed money, and earnings accumulated thereon shall be reported as surplus in the separate accounts until transferred or repatriated to the general account. The transfer of such funds between the separate account and the general account shall be reported as surplus contributed or withdrawn during the year.

11. If an Asset Valuation Reserve (AVR) is required for investments held by separate accounts, it is combined with the general account AVR and accounted for in the general account financial statements (see *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*). The criteria for determining when an AVR is required for separate accounts are described in paragraph 18 of this statement.

12. Reporting entities collect fees for managing Separate Account Guaranteed Investment Contracts (GICs), Synthetic GICs, as well as participating separate account group annuities. These are in the form of administrative fees, risk fees and some investment management fees. For defined contribution business, these are in the form of fees related to mutual fund management. These fees are meant to offset expenses and generate some profit.

13. Amounts receivable from contractholders for separate account management fees meet the definition of assets as set forth in *SSAP No. 4—Assets and Nonadmitted Assets.*

14. An evaluation shall be made of the amounts receivable to determine any nonadmitted amounts. Next, an evaluation shall be made in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets,* to determine whether there is an impairment. This two-step process is set forth below:

a. Uncollected separate account management fees receivable over ninety days due shall be accounted for as a nonadmitted asset. Reporting entities shall begin aging the receivable when it is contractually required to be billed, or in the absence of contract specifications, when the reporting entity actually sends the bill to the contractholder;

b. Remaining amounts determined to be uncollectible shall be written off. If in accordance with SSAP No. 5R, it is "probable" the amount receivable is uncollectible, any uncollectible amount receivable shall be written off against operations in the period such determination is made. If it is "reasonably possible" the amount receivable is uncollectible, the disclosure requirements outlined in SSAP No. 5R, paragraph 32, shall be made.

Separate Account Reporting

15. The separate accounts annual statement is concerned with the flow of funds related to investment activities and obligations of the separate accounts and with the transfer of funds between the separate account and the general account. As a result, the separate account statement shall report only the assets, liabilities, and operations of the separate account and shall not include general account expenses related to investment management, administration, or contract guarantees pertaining to separate account operations which are recorded in the general account.

16. The separate account records premiums, considerations (net of loading for sales charges such as commissions and premium taxes) and receipts (other than for net investment income and realized capital gains and losses) as income transfers from the general account. Net investment income and realized and unrealized capital gains and losses relating to the investment operations of the separate account are recorded as income in the Summary of Operations. When the contract provides for such, expenses and taxes associated with the separate account

investment operations shall be deducted in the determination of net investment income. Deposits and withdrawals on deposit-type contracts shall be recorded in the Summary of Operations. Benefits and surrenders, reserve transfers, policy loans[2], policyholder charges (e.g., fees associated with investment management, administration, and contract guarantees), and federal income taxes relating to the separate account are recorded as expense transfers to the general account in the Summary of Operations. The net change in aggregate reserves relating to separate account contracts is reported as an expense in the Summary of Operations.

Measurement of Separate Account Assets

17. Assets supporting separate account contracts, except for contracts captured in paragraph 18, shall be reported at fair value, as determined under *SSAP No. 100—Fair Value*. Assets held in the separate account that reflect seed money from the general account shall follow all provisions of the SSAP to which the asset would be applicable if held in the general account. Assets that would not qualify for admittance in the general account are not permitted to be used as seed money in the separate account.

NAIC Staff Question: Information on the current measurement method for seed money is requested from industry. Although the guidance implies that seed money should be at book value, there is an assumption that companies may utilize fair value when included in a fair value separate account.

18. Assets supporting the following separate account contracts are permitted to be reported as if the assets were held in the general account. This measurement method is referred to as "book value." For these assets, measurement shall follow all provisions of the SSAP to which the asset would be applicable if held in the general account. Assets that would not qualify for admittance in the general account are not permitted in a book-value separate account. Separate account contracts that do not qualify in the following categories are not permitted at book value without a permitted or prescribed practice from the state of domicile.

a. Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation, or established or maintained by an employer, will be recorded as if the assets were held in the general account.

b. With approval of the state insurance regulator, assets supporting insulated or non-insulated separate account contracts that are similar to contracts generally found in the general account[3]. Unlike traditional separate account contracts, these contracts do not have investment directives determined by the contract holder and investment performance results are not attributed to a specific contract holder. Furthermore, unlike traditional separate account contracts, the insurance reporting entity (general account) is often ultimately obligated to provide contract benefits that are not directly tied to the performance of the underlying assets, resulting with the general account serving as an~~n~~ overall backstop or providing an implied guarantee, although a distinct performance guarantee is not specified (such as a minimum crediting rate, death benefit, etc.). Examples of contracts expected to be captured within this provision include pension risk transfer (PRT) contracts and registered index-linked annuity (RILA) contracts.

[2] Policy loans related to separate account products shall follow the guidance in *SSAP No. 49—Policy Loans*. As detailed within SSAP No. 49, as part of the expense transfer, policy loans related to separate account products require a liquidation of the separate account assets to fund the loan issued by the general account. A transfer of assets from the separate account to the general account must have occurred to fund the policy loan issuance; otherwise the policy loan is nonadmitted in the general account.

[3] The inclusion of this guidance does not imply support for these contracts within the separate account instead of the general account. The domiciliary state insurance regulator is responsible for assessing and approving separate account contract classification in accordance with state statutes.

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NAIC Staff Question: Feedback is requested on the named contracts (PRT and RILA) and whether other example contracts should be named.

~~18. Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, will be recorded as if the assets were held in the general account. Assets supporting all other contractual benefits shall be recorded at fair value on the date of valuation, or if there is no readily available market, then in accordance with the valuation procedures in the applicable contract.~~

Assets Transfers Between the General Account and Separate Account

19. Asset transfers that reflect sales for cash between the general account and separate account shall occur at fair value[4]. Specified guidance based on the measurement method of the assets in the separate account are detailed in paragraphs 20-21.

20. Asset sales for cash between the general account and "fair value" separate accounts:

a. The account (either general or separate account) selling the asset shall receive cash equal to fair value and dispose of the asset from the investment schedules at fair value.

i. Assets sold from the general account shall result in a realized gain or loss based on the difference between fair value and book adjusted carrying value (BACV). The realized gain or loss, if resulting from interest rate changes, shall be allocated to the general account IMR and amortized as if the asset had been sold to an unrelated third-party. Realized gains from these transactions shall not be deferred pursuant to *SSAP No. 25—Affiliates and Other Related Parties*, paragraph 17. Realized losses from credit-related factors shall be allocated to the AVR.

ii. Assets sold from a "fair value" separate account shall not result in a realized gain or loss.

b. The account (either general or separate account) purchasing the asset shall initially recognize the acquired asset at fair value. Subsequent measurements of the acquired asset should reflect the measurement method of the general or separate account.

21. Asset sales for cash between the general account and "book value" separate accounts:

a. Seller - The account (either general or separate account) selling the asset shall receive cash equal to fair value and dispose of the asset from the investment schedules at fair value with recognition of a realized gain or loss. The realized gain or loss, if resulting from interest rate changes, shall be allocated to IMR and amortized in the selling account as if the asset had been sold to an unrelated third-party. The transfer of an asset under this guidance that results in a gain shall not be deferred by the selling account pursuant to SSAP No. 25, paragraph 17, as such a deferral would create a mismatch in the IMR recognition between the general/separate accounts. Realized losses from credit-related factors shall be allocated to the AVR.

b. Purchaser - The account (either general or separate account) purchasing the asset shall recognize the acquired asset at the BACV from the selling account. The difference between the asset's fair value and the BACV shall be reported to IMR in the purchasing account.

[4] This guidance is specific to asset sales for cash and is not intended to reflect administration functions for the payment of amounts owed to separate account policyholders/contractholders that may occur from the general account with reimbursement from the separate account.

c. The IMR activity between the selling account and the purchasing account shall be equal and offsetting resulting in a net zero impact in the IMR between the two accounts. IMR is tracked and reported separately in the general account and the separate account, but the net impact of the two accounts shall equal zero for each transfer transaction.

d. Subsequent to initial acquisition, the purchasing account shall account for the acquired asset pursuant to the measurement method of the applicable SSAP.

22. Asset transfers that do not reflect sales for cash between the general account and separate account are subject to domiciliary state approval. 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.

NAIC Staff Question: Additional information is requested from industry on these transfers. NAIC staff recommend that these areas be expanded with consistent guidance for the treatment of transfers.

Separate Account AVR and IMR Reporting

19.23. An AVR is generally required for separate accounts when the insurerreporting 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.

20.24. Assets supporting traditional variable annuities and variable life insuranceseparate accounts 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).

21.25. 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.

22.26. "Book Value" separate accounts, pursuant to paragraph 18, Certain separate accounts are alsoare 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. OnceIf 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.

NAIC Staff Question: Clarification is requested to this guidance for seed money similar to the prior question.

~~23.~~ 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.~~

~~24.~~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.

~~25.~~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~~.

Policy Reserves

~~26.~~29. Statutory policy reserves shall be established for all contractual obligations of the insurer arising out of the provisions of the insurance contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. These statutory policy reserves are generally calculated as the excess of the present value of future benefits to be paid to or on behalf of policyholders less the present value of future net premiums. Statutory policy reserves meet the definition of liabilities as defined in SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets. The actuarial methodologies referred to in the following paragraph meet the criteria required for reasonable estimates in SSAP No. 5R.

~~27.~~30. The reserving methodologies and assumptions used in computation of policy reserves shall also meet the provisions of Appendices A-200, A-250, A-255, A-270; A-585, A-588, A-620, A-695, A-820, A-822 and the actuarial guidelines found in Appendix C of this Manual. Where separate account contracts have guaranteed elements, the basis for determining the value of the liability shall be consistent with the basis used for asset values (i.e., valuation interest rates as defined in Appendix A-820 shall be used when assets are recorded as if held in the general account and current interest rates based on market rates shall be used when assets are recorded at fair value). Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

~~28.~~31. Statutory policy reserves for those group annuity contracts or other contracts that, in whole or in part, establish the insurer's obligations by reference to a segregated portfolio of assets not owned by the insurer shall be established in accordance with the guidance in Appendix A-695. Statutory policy reserves for those contracts with nonlevel premiums or benefits, or contracts with secondary guarantees shall be established in accordance with the guidance in Appendix A-830. Statutory policy reserves for those group life contracts utilizing a separate account that meet the requirements outlined in paragraph 1 of Appendix A-200 shall be computed in accordance with the guidance in that appendix.

Other Liabilities

~~29.~~32. The separate account shall accrue as a liability, subject to contractual provisions, amounts payable, including, but not limited to:

a. Fees associated with investment management, administration, and contract guarantees;

b. Investment expenses;

c. Investment taxes, licenses, and fees (Investment taxes such as real estate taxes, licenses and fees (excluding federal income taxes) are usually paid directly by the separate account but may be transferred to the general account for payment);

d. Federal income taxes;

e. Unearned investment income;

f. Net transfer due to (from) the general account;

g. Remittances and items not allocated;

h. Payable for investments purchased;

i. Net adjustments in assets and liabilities due to foreign exchange rates.

~~**Seed Money**~~

~~30. When a new separate account is initiated, the insurer may make a temporary transfer of surplus funds commonly referred to as seed money to the separate account. Such funds and earnings accumulated thereon shall be reported as surplus in the separate accounts statement until transferred or repatriated to the general account. The transfer of such funds to and from the separate account shall be reported as surplus contributed or withdrawn during the year.~~

Disclosures

~~31.~~33. Paragraphs 31-35 detail the separate account disclosure requirements that shall be included within the Life, Accident and Health Annual Statement Blank. Paragraphs 36-38 detail the separate account disclosure requirements that shall be included within the Separate Account Annual Statement Blank.

~~32.~~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) years[5] 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-liability testing.

d. Discussion of securities lending transactions and repurchase/reverse repurchase agreements within the separate account. ~~,~~ This shall include ~~separately including~~ the amount of any loaned securities

[5] 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.

within the separate account and the amount of any sold / acquired securities under repurchase agreements, and if policy and procedures for the separate account differ from the general account.

e. Discussion of asset transfers that did not reflect sales in exchange for cash between the general account and the separate account. This shall include, but not be limited to, asset-for-asset swaps, contributions of general account assets to support separate account deficiencies, and dividends of assets from the separate account to the general account.

~~33.~~35. For each grouping (as detailed in paragraph 33), the following shall be disclosed:

a. Premiums, considerations or deposits received during the year;

b. Reserves by the valuation basis of the investments supporting the reserves at the financial statement date. List reserves for separate accounts whose assets are carried at fair value separately from those whose assets are carried at amortized cost/book value;

c. Reserves by withdrawal characteristics, including whether or not the separate account is subject to discretionary withdrawal. For reserves subject to discretionary withdrawal, the below categories are included if applicable:

i. With market value adjustment;

ii. at book value without market value adjustment and with surrender charge of 5% or more;

iii. at fair value;

iv. at book value without market value adjustment and with surrender charge of less than 5%;

d. Reserves for asset default risk, as described in paragraph 18.b., that are recorded in lieu of AVR.

~~34.~~36. For the disclosures required in paragraph 32, separate accounts shall be addressed in the following groupings (which are the same as those used for risk-based capital):

a. Separate Accounts with Guarantees:

1. Indexed separate accounts, which are invested to mirror an established index which is the basis of the guarantee;

2. Nonindexed separate accounts, with reserve interest rate at no greater than 4% and/or fund long-term interest guarantee in excess of a year that does not exceed 4%;

3. Nonindexed separate accounts, with reserve interest rate at greater than 4% and/or fund long-term interest guarantee in excess of a year that exceeds 4%.

b. Nonguaranteed Separate Accounts—Variable separate accounts, where the benefit is determined by the performance and/or fair value of the investments held in the separate account. Include variable accounts with incidental risks, nominal expense, and minimum death benefit guarantees.

~~35.~~37. Provide a reconciliation of the amount reported as transfers to and from separate accounts in the Summary of Operations of the separate accounts statement and the amount reported as net transfers to or from separate accounts in the Summary of Operations of the general accounts statement.

~~36.~~38. The disclosures in *SSAP No. 51R—Life Contracts*, and *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* related to the withdrawal characteristics of products include separate account products and shall be completed in the general account disclosures.

~~37.~~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:

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.) ~~are~~ 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.[6] 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)[7], 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

[6] 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.

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

guarantee, although a distinct performance guarantee is not specified (such as a minimum crediting rate, death benefit, etc.).

~~38.~~40. For all separate account assets not reported at fair value, indicate the measurement basis (amortized cost or other method) for each asset (or asset class) and whether the measurement method ~~was grandfathered in under the transition~~is pursuant to the guidance in this SSAP, or whether the measurement method is allowed under a prescribed or permitted practice. This disclosure shall include a comparison of the assets' reported value to fair value with identification of the resulting unrealized gain/loss that would have been recorded if the assets had been reported at fair value.

41. For all separate accounts that include securities lending transactions, disclose the reporting entity's use and policy of securities lending within the separate account, including the amount of loaned securities from the separate account at the reporting date, the percentage of separate account assets lent as of that date, a description for which type of accounts (e.g., book value accounts, market value account accounts) are lent, if the separate account policyholder is notified or approves of such practices, the policy for requiring collateral, whether the collateral is restricted and the amount of collateral for transactions that extend beyond one year from the reporting date. This disclosure requires the entity to provide the following information as of the date of the statement of financial position: (1) the aggregate amount of contractually obligated open collateral positions (aggregate amount of securities at current fair value or cash received for which the borrower may request the return of on demand) and the aggregate amount of contractually obligated collateral positions under 30-day, 60-day, 90-day, and greater than 90-day terms, (2) the aggregate fair value of all securities acquired from the sale, trade and use of the accepted collateral (reinvested collateral), and (3) information about the sources and uses of that collateral.

42. For all separate accounts that include repurchase/reverse repurchase (repo) agreements, disclose the reporting entity's use and policies of repo agreements within the separate account, including the following: (1) fair value of securities sold or acquired, (2) cash collateral and the fair value of security collateral received or provided, (3) recognized liability or receivable for the return of collateral.

~~39.~~43. Identify all products reported as a separate account product under statutory accounting principles and identify whether each product was classified differently under GAAP. For products that resulted with different classifications between GAAP and SAP, identify the characteristic(s) of the product that prevented it from receiving a separate account classification under GAAP. This disclosure is applicable for all reporting entities. Thus, if GAAP financial statements were not filed, the reporting entity should complete this disclosure as if GAAP financials had been completed.

~~40.~~44. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

~~41.~~45. This statement rejects ASU 2022-05, Transition for Sold Contracts, ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts, and AICPA Statement of Position 03-1, Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts (SOP 03-1). The disclosure elements included within this SSAP are derived from the criteria for separate account reporting under SOP 03-1; however, this SSAP does not restrict separate account reporting pursuant to the criteria established in SOP 03-1.

~~42.~~46. This statement incorporates the requirements of Appendices A-200, A-250, A-255, A-270, A-585, A-588, A-620, A-695, A-812, A-820, A-821, A-822 the Actuarial Standards Board Actuarial Standards of Practice, and the actuarial guidelines found in Appendix C of this Manual.

Effective Date and Transition

~~43.~~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 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*.

~~44.~~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.

REFERENCES

Other

- *NAIC Financial Condition Examiners Handbook*
- *Actuarial Standards Board Actuarial Standards of Practice*

Relevant Issue Papers

- *Issue Paper No. 89—Separate Accounts*
- *Issue Paper No. 110—Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts,* and *SSAP No. 56—Separate Accounts*

GLOSSARY

Guarantee represents an insurance company's general account contractual obligation to reimburse life insurance and annuity policyholders for their separate account investment losses including the return of principal, minimum crediting rates, minimum death, withdrawal, accumulation of income benefits and no-lapse guarantees, and for separate account mortality losses.

NAIC Staff Question: From informal discussions with industry reps, NAIC staff do not have the impression that the above definition of a guarantee captures the inherent guarantee when the general account is a backstop to the separate account. Rather, the above definition only captures explicit guarantees, such as a guaranteed yield, death benefit, etc. NAIC staff requests feedback on this interpretation and comments on whether revisions are necessary to ensure consistent interpretation with regulators and reporting entities.

Insulation is the legal protection of separate account assets equal to the reserves and supporting contract liabilities from the general account liabilities of the insurance enterprise ensuring that the separate account contract holder is not subjected to insurer default risk to the extent of their assets held in the separate account.

Risk Charge is the contractual amount the general account charges the separate account policyholders' account for compensation relating to the general account's guarantee on separate account assets or contract performance.

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Total Maximum Guarantee is the difference between the total amount of liability the general account is subject to reimbursing as at the balance sheet date and the policyholder's contract value referenced by the guarantee (e.g., account value). For guarantees in the event of death, it is the minimum guaranteed amount available to the contractholder upon death in excess of the contractholder's contract value referenced by the guarantee (e.g., account balance) at the balance sheet date. For guarantees of amounts at annuitization, it is the present value of the minimum guaranteed annuity payments available to the contractholder determined in accordance with the terms of the contract in excess of the contract value referenced by the guarantee (e.g., account balance).

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On December 17, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *SSAP No. 56—Separate Accounts,* as shown below as "2024 December Exposed Revisions," for a comment period ending January 31, 2025. The revisions from the prior exposure are summarized in the following bullets, included within the tracked changes, and shaded for easy identification.

Revisions reflected from the 2024 Summer National Meeting Exposure:

- 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.

2024 December Exposed Revisions to SSAP No. 56:
(The tracked changes to paragraph 18b and 22 are shaded. Paragraph references have also been shaded for subsequent confirmation. Please note that footnote references are continuing the number from the prior exposure and will be updated to restart at 1 in the adoption version.)

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for accounting and reporting for separate accounts in both the general account and separate account statements.

SUMMARY CONCLUSION

Introduction

2. Separate accounts are used to fund variable life insurance, variable annuities, modified guaranteed annuities and modified guaranteed life insurance, or various group contracts under pension or other employee benefit plans where funds are held in a separate account to support a liability. When separate accounts are established and filed accordingly, they may be used to fund guaranteed benefits. Separate account contracts may also be used to accumulate funds which are intended to be applied at some later time to provide life insurance or to accumulate proceeds applied under settlement or dividend options.

3. Assets held in separate accounts are owned by the insurer. All investment income and realized and unrealized capital gains and losses from assets allocated to a separate account, net of related investment expenses, are generally reflected in the separate account and, except for modified guaranteed annuities, modified guaranteed life insurance, and separate accounts established and filed to provide guaranteed benefits, investment performance is generally not guaranteed by the insurer. Charges relating to contract guarantees, administration, and investment management are deducted from separate accounts.

General Account Reporting

4. Insurance activities such as sales, underwriting and contract administration, premium collection and payment of premium taxes, claims, and benefits are functions of the insurance company distinct from the separate account and shall be accounted for as transactions of the general account.

5. For those separate account contracts classified as life contracts under *SSAP No. 50—Classification of Insurance or Managed Care Contracts*, premiums and annuity considerations shall be recorded as income in the Summary of Operations of the general account, and as transfers to premiums and considerations in the separate account statement. Deposit-type contracts shall be recorded in the general account in accordance with *SSAP No. 52—Deposit-Type Contracts*.[INT 00-03] Charges (e.g., fees associated with investment management, administration, and contract guarantees) assessed on the separate accounts, as well as the net gain from operations of the separate account, shall be recorded as income in the Summary of Operations of the general account. Expenses relating to investment management, administration, and contract guarantees pertaining to separate account operations, as well as benefits and surrenders incurred on behalf of separate account contracts classified as life contracts, net transfers between separate accounts, commissions, and premium taxes (if any) shall be recorded as expenses in the Summary of Operations of the general account.

6. The general account shall include the total assets and liabilities, including transfers due or accrued, of any separate accounts business which it maintains and, therefore, the surplus, if any, of its separate accounts business. Transfers to the general account due or accrued shall be reported on a net basis so that the asset and the liability totals of the general account are not overstated. Changes in the surplus of the separate accounts business of an insurer, except for changes resulting from the net gain from operations of the separate account, shall be charged or credited directly to the unassigned funds (surplus) of the general account.

7. Where a variable annuity contract or variable life insurance contract contains a guaranteed minimum death benefit, any reserve liability for such death benefit provision shall be recorded and held in the general account based on the reserving guidance in paragraphs 25 and 26. Any differences between the benefit paid and the separate account asset value of the contract shall be charged against or credited to the general account in its net gain from operations.

8. Separate account surplus may not become negative. For example, for separate account contracts which have annuitized (i.e., contracts in the payout stage), lower than expected mortality on variable annuity contracts containing mortality guarantees may cause a deficiency in the investment funds underlying the contract reserves. Thus the general account incurs an expense and the separate account realizes revenue to cover the deficiency, if necessary. Conversely, excess funds from higher than expected mortality will result in mortality gains, which are included in the Summary of Operations of the separate account and are ultimately recorded as equity in net income from separate account operations as discussed in paragraph 5.

9. Separate account surplus created through the use of the commissioners' reserve valuation method (CRVM), commissioners' annuity reserve valuation method (CARVM), or other reserving methods, shall be reported by the general account as an unsettled transfer from the separate account. The net change on such transfers shall be included as a part of the net gain from operations in the general account.

10. Surplus funds transferred from the general account to the separate account, commonly referred to as seed money, and earnings accumulated thereon shall be reported as surplus in the separate accounts until transferred or repatriated to the general account. The transfer of such funds between the separate account and the general account shall be reported as surplus contributed or withdrawn during the year.

11. If an Asset Valuation Reserve (AVR) is required for investments held by separate accounts, it is combined with the general account AVR and accounted for in the general account financial statements (see *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*). The criteria for determining when an AVR is required for separate accounts are described in paragraph 18 of this statement.

12. Reporting entities collect fees for managing Separate Account Guaranteed Investment Contracts (GICs), Synthetic GICs, as well as participating separate account group annuities. These are in the form of administrative fees, risk fees and some investment management fees. For defined contribution business, these are in the form of fees related to mutual fund management. These fees are meant to offset expenses and generate some profit.

13. Amounts receivable from contractholders for separate account management fees meet the definition of assets as set forth in *SSAP No. 4—Assets and Nonadmitted Assets.*

14. An evaluation shall be made of the amounts receivable to determine any nonadmitted amounts. Next, an evaluation shall be made in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets,* to determine whether there is an impairment. This two-step process is set forth below:

c. Uncollected separate account management fees receivable over ninety days due shall be accounted for as a nonadmitted asset. Reporting entities shall begin aging the receivable when it is contractually required to be billed, or in the absence of contract specifications, when the reporting entity actually sends the bill to the contractholder;

d. Remaining amounts determined to be uncollectible shall be written off. If in accordance with SSAP No. 5R, it is "probable" the amount receivable is uncollectible, any uncollectible amount receivable shall be written off against operations in the period such determination is made. If it is "reasonably possible" the amount receivable is uncollectible, the disclosure requirements outlined in SSAP No. 5R, paragraph 32, shall be made.

Separate Account Reporting

15. The separate accounts annual statement is concerned with the flow of funds related to investment activities and obligations of the separate accounts and with the transfer of funds between the separate account and the general account. As a result, the separate account statement shall report only the assets, liabilities, and operations of the separate account and shall not include general account expenses related to investment management, administration, or contract guarantees pertaining to separate account operations which are recorded in the general account.

16. The separate account records premiums, considerations (net of loading for sales charges such as commissions and premium taxes) and receipts (other than for net investment income and realized capital gains and losses) as income transfers from the general account. Net investment income and realized and unrealized capital gains and losses relating to the investment operations of the separate account are recorded as income in the Summary of Operations. When the contract provides for such, expenses and taxes associated with the separate account investment operations shall be deducted in the determination of net investment income. Deposits and withdrawals on deposit-type contracts shall be recorded in the Summary of Operations. Benefits and surrenders, reserve transfers, policy loans[8], policyholder charges (e.g., fees associated with investment management, administration, and contract guarantees), and federal income taxes relating to the separate account are recorded as expense transfers to the general account in the Summary of Operations. The net change in aggregate reserves relating to separate account contracts is reported as an expense in the Summary of Operations.

Measurement of Separate Account Assets

17. Assets supporting separate account contracts, except for contracts captured in paragraph 18, shall be reported at fair value, as determined under *SSAP No. 100—Fair Value*. Assets held in the separate account that reflect seed money from the general account shall follow all provisions of the SSAP to which the asset would be

[8] Policy loans related to separate account products shall follow the guidance in *SSAP No. 49—Policy Loans*. As detailed within SSAP No. 49, as part of the expense transfer, policy loans related to separate account products require a liquidation of the separate account assets to fund the loan issued by the general account. A transfer of assets from the separate account to the general account must have occurred to fund the policy loan issuance; otherwise the policy loan is nonadmitted in the general account.

applicable if held in the general account. Assets that would not qualify for admittance in the general account are not permitted to be used as seed money in the separate account.

18. Assets supporting the following separate account contracts are permitted to be reported as if the assets were held in the general account. This measurement method is referred to as "book value." For these assets, measurement shall follow all provisions of the SSAP to which the asset would be applicable if held in the general account. Assets that would not qualify for admittance in the general account are not permitted in a book-value separate account. Separate account contracts that do not qualify in the following categories are not permitted at book value without a permitted or prescribed practice from the state of domicile.

a. Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation or established or maintained by an employer, will be recorded as if the assets were held in the general account.

b. With approval of the state insurance regulator, assets supporting insulated or non-insulated separate account contracts that are similar to contracts generally found in the general account[9], 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. Unlike traditional separate account contracts, these contracts do not have investment directives determined by the contract holder and investment performance results are not attributed to a specific contract holder. ~~Furthermore, unlike traditional separate account contracts, the insurance reporting entity (general account) is often ultimately obligated to provide contract benefits that are not directly tied to the performance of the underlying assets, resulting with~~ The general account may serve ~~serving~~ as an overall backstop or may provide ~~providing~~ an implied guarantee, although a distinct performance guarantee may ~~is~~ not be specified (such as a minimum crediting rate, death benefit, etc.). Examples of contracts expected to be captured within this provision include, but are not limited to, pension risk transfer (PRT) contracts, bank-owned life insurance (BOLI) and registered index-linked annuity (RILA) contracts.

NAIC Staff Question: Although the ACLI letter only identified BOLI contracts, NAIC staff wants to confirm whether COLI contracts should also be named. Generally, references to BOLI also include COLI, but NAIC staff is not certain whether both should be captured as a common book value separate account contracts.

~~18. Assets supporting fund accumulation contracts (GICs), which do not participate in underlying portfolio experience, with a fixed interest rate guarantee, purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, will be recorded as if the assets were held in the general account. Assets supporting all other contractual benefits shall be recorded at fair value on the date of valuation, or if there is no readily available market, then in accordance with the valuation procedures in the applicable contract.~~

Assets Transfers Between the General Account and Separate Account

19. Asset transfers that reflect sales for cash between the general account and separate account shall occur at fair value[10]. Specified guidance based on the measurement method of the assets in the separate account are detailed in paragraphs 20-21.

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[9] The inclusion of this guidance does not imply support for these contracts within the separate account instead of the general account. The domiciliary state insurance regulator is responsible for assessing and approving separate account contract classification in accordance with state statutes.

[10] This guidance is specific to asset sales for cash and is not intended to reflect administration functions for the payment of amounts owed to separate account policyholders/contractholders that may occur from the general account with reimbursement from the separate account.

20. Asset sales for cash between the general account and "fair value" separate accounts:

   a. The account (either general or separate account) selling the asset shall receive cash equal to fair value and dispose of the asset from the investment schedules at fair value.

   b. Assets sold from the general account shall result in a realized gain or loss based on the difference between fair value and book adjusted carrying value (BACV). The realized gain or loss, if resulting from interest rate changes, shall be allocated to the general account IMR and amortized as if the asset had been sold to an unrelated third-party. Realized gains from these transactions shall not be deferred pursuant to *SSAP No. 25—Affiliates and Other Related Parties*, paragraph 17. Realized losses from credit-related factors shall be allocated to the AVR.

   c. Assets sold from a "fair value" separate account shall not result in a realized gain or loss.

   d. The account (either general or separate account) purchasing the asset shall initially recognize the acquired asset at fair value. Subsequent measurements of the acquired asset should reflect the measurement method of the general or separate account.

21. Asset sales for cash between the general account and "book value" separate accounts:

   a. Seller - The account (either general or separate account) selling the asset shall receive cash equal to fair value and dispose of the asset from the investment schedules at fair value with recognition of a realized gain or loss. The realized gain or loss, if resulting from interest rate changes, shall be allocated to IMR and amortized in the selling account as if the asset had been sold to an unrelated third-party. The transfer of an asset under this guidance that results in a gain shall not be deferred by the selling account pursuant to SSAP No. 25, paragraph 17, as such a deferral would create a mismatch in the IMR recognition between the general/separate accounts. Realized losses from credit-related factors shall be allocated to the AVR.

   b. Purchaser - The account (either general or separate account) purchasing the asset shall recognize the acquired asset at the BACV from the selling account. The difference between the asset's fair value and the BACV shall be reported to IMR in the purchasing account.

   c. The IMR activity between the selling account and the purchasing account shall be equal and offsetting resulting in a net zero impact in the IMR between the two accounts. IMR is tracked and reported separately in the general account and the separate account, but the net impact of the two accounts shall equal zero for each transfer transaction.

   d. Subsequent to initial acquisition, the purchasing account shall account for the acquired asset pursuant to the measurement method of the applicable SSAP.

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. 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.

NAIC Staff Question: With the revision requiring fair value measurement, comments are requested on whether additional guidance, particularly with the treatment of IMR, is needed.

Separate Account AVR and IMR Reporting

~~19.~~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.~~

~~20.~~24. Assets supporting ~~traditional variable annuities and variable life insurance~~separate accounts 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).~~

~~21.~~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.

~~22.~~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.

~~23.~~ 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.~~

~~24.~~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.

~~25.~~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~~.

Policy Reserves

~~26.~~29. Statutory policy reserves shall be established for all contractual obligations of the insurer arising out of the provisions of the insurance contract. Where separate benefits are included in a contract, a reserve for each benefit shall be established as required in Appendix A-820. These statutory policy reserves are generally calculated as the excess of the present value of future benefits to be paid to or on behalf of policyholders less the present value of future net premiums. Statutory policy reserves meet the definition of liabilities as defined in SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets. The actuarial methodologies referred to in the following paragraph meet the criteria required for reasonable estimates in SSAP No. 5R.

~~27.~~30. The reserving methodologies and assumptions used in computation of policy reserves shall also meet the provisions of Appendices A-200, A-250, A-255, A-270; A-585, A-588, A-620, A-695, A-820, A-822 and the actuarial guidelines found in Appendix C of this Manual. Where separate account contracts have guaranteed

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elements, the basis for determining the value of the liability shall be consistent with the basis used for asset values (i.e., valuation interest rates as defined in Appendix A-820 shall be used when assets are recorded as if held in the general account and current interest rates based on market rates shall be used when assets are recorded at fair value). Further, policy reserves shall be in compliance with those Actuarial Standards of Practice promulgated by the Actuarial Standards Board.

~~28.~~31. Statutory policy reserves for those group annuity contracts or other contracts that, in whole or in part, establish the insurer's obligations by reference to a segregated portfolio of assets not owned by the insurer shall be established in accordance with the guidance in Appendix A-695. Statutory policy reserves for those contracts with nonlevel premiums or benefits, or contracts with secondary guarantees shall be established in accordance with the guidance in Appendix A-830. Statutory policy reserves for those group life contracts utilizing a separate account that meet the requirements outlined in paragraph 1 of Appendix A-200 shall be computed in accordance with the guidance in that appendix.

Other Liabilities

~~29.~~32. The separate account shall accrue as a liability, subject to contractual provisions, amounts payable, including, but not limited to:

j. Fees associated with investment management, administration, and contract guarantees;

k. Investment expenses;

l. Investment taxes, licenses, and fees (Investment taxes such as real estate taxes, licenses and fees (excluding federal income taxes) are usually paid directly by the separate account but may be transferred to the general account for payment);

m. Federal income taxes;

n. Unearned investment income;

o. Net transfer due to (from) the general account;

p. Remittances and items not allocated;

q. Payable for investments purchased;

r. Net adjustments in assets and liabilities due to foreign exchange rates.

~~**Seed Money**~~

~~30. When a new separate account is initiated, the insurer may make a temporary transfer of surplus funds commonly referred to as seed money to the separate account. Such funds and earnings accumulated thereon shall be reported as surplus in the separate accounts statement until transferred or repatriated to the general account. The transfer of such funds to and from the separate account shall be reported as surplus contributed or withdrawn during the year.~~

Disclosures

~~31.~~33. Paragraphs 31-35 detail the separate account disclosure requirements that shall be included within the Life, Accident and Health Annual Statement Blank. Paragraphs 36-38 detail the separate account disclosure requirements that shall be included within the Separate Account Annual Statement Blank.

~~32.~~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) years[11] 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-liability testing.

d. Discussion of securities lending transactions and repurchase/reverse repurchase agreements within the separate account. ,This shall include separately including the amount of any loaned securities within the separate account and the amount of any sold / acquired securities under repurchase agreements, and if policy and procedures for the separate account differ from the general account.

e. Discussion of asset transfers that did not reflect sales in exchange for cash between the general account and the separate account. This shall include, but not be limited to, asset-for-asset swaps, contributions of general account assets to support separate account deficiencies, and dividends of assets from the separate account to the general account.

33.35. For each grouping (as detailed in paragraph 33), the following shall be disclosed:

a. Premiums, considerations or deposits received during the year;

b. Reserves by the valuation basis of the investments supporting the reserves at the financial statement date. List reserves for separate accounts whose assets are carried at fair value separately from those whose assets are carried at amortized cost/book value;

c. Reserves by withdrawal characteristics, including whether or not the separate account is subject to discretionary withdrawal. For reserves subject to discretionary withdrawal, the below categories are included if applicable:

v. With market value adjustment;

vi. at book value without market value adjustment and with surrender charge of 5% or more;

vii. at fair value;

[11] 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.

viii. at book value without market value adjustment and with surrender charge of less than 5%;

d. Reserves for asset default risk, as described in paragraph 18.b., that are recorded in lieu of AVR.

~~34.~~36. For the disclosures required in paragraph 32, separate accounts shall be addressed in the following groupings (which are the same as those used for risk-based capital):

a. Separate Accounts with Guarantees:

1. Indexed separate accounts, which are invested to mirror an established index which is the basis of the guarantee;

2. Nonindexed separate accounts, with reserve interest rate at no greater than 4% and/or fund long-term interest guarantee in excess of a year that does not exceed 4%;

3. Nonindexed separate accounts, with reserve interest rate at greater than 4% and/or fund long-term interest guarantee in excess of a year that exceeds 4%.

b. Nonguaranteed Separate Accounts—Variable separate accounts, where the benefit is determined by the performance and/or fair value of the investments held in the separate account. Include variable accounts with incidental risks, nominal expense, and minimum death benefit guarantees.

~~35.~~37. Provide a reconciliation of the amount reported as transfers to and from separate accounts in the Summary of Operations of the separate accounts statement and the amount reported as net transfers to or from separate accounts in the Summary of Operations of the general accounts statement.

~~36.~~38. The disclosures in *SSAP No. 51R—Life Contracts*, and *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* related to the withdrawal characteristics of products include separate account products and shall be completed in the general account disclosures.

~~37.~~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:

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.) ~~are~~ 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.[12] 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)[13], the time duration

[12] 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.

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

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.).

~~38.~~40. For all separate account assets not reported at fair value, indicate the measurement basis (amortized cost or other method) for each asset (or asset class) and whether the measurement method ~~was grandfathered in under the transition~~is pursuant to the guidance in this SSAP, or whether the measurement method is allowed under a prescribed or permitted practice. This disclosure shall include a comparison of the assets' reported value to fair value with identification of the resulting unrealized gain/loss that would have been recorded if the assets had been reported at fair value.

41. For all separate accounts that include securities lending transactions, disclose the reporting entity's use and policy of securities lending within the separate account, including the amount of loaned securities from the separate account at the reporting date, the percentage of separate account assets lent as of that date, a description for which type of accounts (e.g., book value accounts, market value account accounts) are lent, if the separate account policyholder is notified or approves of such practices, the policy for requiring collateral, whether the collateral is restricted and the amount of collateral for transactions that extend beyond one year from the reporting date. This disclosure requires the entity to provide the following information as of the date of the statement of financial position: (1) the aggregate amount of contractually obligated open collateral positions (aggregate amount of securities at current fair value or cash received for which the borrower may request the return of on demand) and the aggregate amount of contractually obligated collateral positions under 30-day, 60-day, 90-day, and greater than 90-day terms, (2) the aggregate fair value of all securities acquired from the sale, trade and use of the accepted collateral (reinvested collateral), and (3) information about the sources and uses of that collateral.

42. For all separate accounts that include repurchase/reverse repurchase (repo) agreements, disclose the reporting entity's use and policies of repo agreements within the separate account, including the following: (1) fair

value of securities sold or acquired, (2) cash collateral and the fair value of security collateral received or provided, (3) recognized liability or receivable for the return of collateral.

~~39.~~43. Identify all products reported as a separate account product under statutory accounting principles and identify whether each product was classified differently under GAAP. For products that resulted with different classifications between GAAP and SAP, identify the characteristic(s) of the product that prevented it from receiving a separate account classification under GAAP. This disclosure is applicable for all reporting entities. Thus, if GAAP financial statements were not filed, the reporting entity should complete this disclosure as if GAAP financials had been completed.

~~40.~~44. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

~~41.~~45. This statement rejects ASU 2022-05, Transition for Sold Contracts, ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts, and AICPA Statement of Position 03-1, Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts (SOP 03-1). The disclosure elements included within this SSAP are derived from the criteria for separate account reporting under SOP 03-1; however, this SSAP does not restrict separate account reporting pursuant to the criteria established in SOP 03-1.

~~42.~~46. This statement incorporates the requirements of Appendices A-200, A-250, A-255, A-270, A-585, A-588, A-620, A-695, A-812, A-820, A-821, A-822 the Actuarial Standards Board Actuarial Standards of Practice, and the actuarial guidelines found in Appendix C of this Manual.

Effective Date and Transition

~~43.~~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 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*.

~~44.~~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.

REFERENCES

Other

- *NAIC Financial Condition Examiners Handbook*
- *Actuarial Standards Board Actuarial Standards of Practice*

Relevant Issue Papers

- *Issue Paper No. 89—Separate Accounts*

- *Issue Paper No. 110—Life Contracts, Deposit-Type Contracts and Separate Accounts, Amendments to SSAP No. 51—Life Contracts, SSAP No. 52—Deposit-Type Contracts,* and *SSAP No. 56—Separate Accounts*

GLOSSARY

Guarantee represents an insurance company's general account contractual obligation to reimburse life insurance and annuity policyholders for their separate account investment losses including the return of principal, minimum crediting rates, minimum death, withdrawal, accumulation of income benefits and no-lapse guarantees, and for separate account mortality losses.

Insulation is the legal protection of separate account assets equal to the reserves and supporting contract liabilities from the general account liabilities of the insurance enterprise ensuring that the separate account contract holder is not subjected to insurer default risk to the extent of their assets held in the separate account.

Risk Charge is the contractual amount the general account charges the separate account policyholders' account for compensation relating to the general account's guarantee on separate account assets or contract performance.

Total Maximum Guarantee is the difference between the total amount of liability the general account is subject to reimbursing as at the balance sheet date and the policyholder's contract value referenced by the guarantee (e.g., account value). For guarantees in the event of death, it is the minimum guaranteed amount available to the contractholder upon death in excess of the contractholder's contract value referenced by the guarantee (e.g., account balance) at the balance sheet date. For guarantees of amounts at annuitization, it is the present value of the minimum guaranteed annuity payments available to the contractholder determined in accordance with the terms of the contract in excess of the contract value referenced by the guarantee (e.g., account balance).

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/05 - 24-10 - SSAP No 56 - BV.docx

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Derivative Premium Clarifications

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item was developed in response to two issues. First, NAIC staff noted during internal reviews of *SSAP No. 86—Derivatives* and the Annual Statement Instructions that the terminology used for derivative financing premium was inconsistent and that the guidance for derivative financing premiums could be clarified. Second, 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.

Existing Authoritative Literature:

Statement of Statutory Accounting Principles No. 86—Derivatives

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, so that the cost is paid or received throughout the derivative term or at derivative maturity, does not result with an "embedded derivative" addressed in paragraph 17.

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. Derivative premium that is not paid or received at inception represents 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.

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

Disclosure Requirements

63. Reporting entities shall disclose the following for all derivative contracts used:

a. General disclosures:

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 at the end of the derivative contract or throughout the derivative contract.);

h. For derivative contracts with financing premiums:

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.

ii. For each derivative contract with financing premiums:

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

EXHIBIT B – SPECIFIC HEDGE ACCOUNTING PROCEDURES FOR DERIVATIVES

2. Swaps, Collars, and Forwards (see also discussion in Introduction above):

c. Cash Flows and Income:

i. Where the cost of the derivative is not combined with the hedged item:

(a) Amortization of premium paid or received on derivatives is an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of the hedged item;

(b) Periodic cash flows and accruals of income/expense are to be reported in a manner consistent with the hedged item, usually as net investment income or another appropriate caption within operating income.

ii. Where the cost of the derivative is combined with the hedged item, the cash flows and income of the derivative on Schedule DB is zero. All related amortization and cash flow accounting shall be reported with the hedged item instead of with the derivative.

Annual Statement Instructions: Notes to the Financial Statements:

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 Premiums (Sum of 1 through 5)	$

b.

		Undiscounted Future Premium Commitments	Derivative Fair Value with Premium Commitments (Reported on DB)	Derivative Fair Value Excluding Impact of Future Settled Premiums
1.	Prior Year	$	$	$ ....
2.	Current Year	$	$	$ ....

Annual Statement Instructions: Schedule DB – Definitions

"Financing Premium" means that the premium cost to acquire or enter into the derivative is paid at the end of the derivative contract or throughout the derivative contract.

Annual Statement Instructions: 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 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 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 owed by the reporting entity, those "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
Agenda item 2012-17, which considered *ASU 2011-22, Disclosures about Offsetting Assets and Liabilities*, was finalized by the Working Group Nov. 29, 2012. This agenda item adopted revisions to SSAPs No. 64, 86 and 103. The adopted revisions, effective Jan. 1, 2013, 1) revise and clarify that offsetting is only allowed in accordance with SSAP No. 64, paragraphs 2-4; 2) modify the adoption of FIN 39 rejecting the ability to offset in accordance with master netting agreements and rejecting FSP FIN 39-1 and FIN 41; and 3) rejecting ASU 2011-11 for statutory accounting.

Overview of ASU 2011-11:

ASU 2011-11 was issued in December 2011 to require entities to disclose both gross information and net information about both instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting agreement. This ASU was issued as the differences in the offsetting requirements between U.S. GAAP and IFRS accounted for a significant difference in the amounts presented under those standards. These differences reduce the comparability of between U.S. GAAP and IFRS, and the users of financial statements requested that these differences be addressed expeditiously. **The objective of the ASU 2011-11 amendments is to facilitate comparison between entities that prepare financial statements under U.S. GAAP and those prepared under IFRS.** Reporting entities are required to apply the ASU 2011-11 amendments for annual reporting periods beginning on or after Jan. 1, 2013, and interim periods within those annual periods. Entities are required to provide the disclosures required by those amendments retrospectively for all comparative periods presented.

Agenda item 2013-07, which considered *ASU 2013-01: Clarifying the Scope of Disclosures About Offsetting Assets and Liabilities,* was finalized on August 24, 2013. This ASU was issued to clarify that the scope of ASU 2011-11 applies to derivatives (including embedded derivatives), repurchase and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either netted as they meet the right of setoff under ASC 210-20-45 or ASC 815-10-45, or are subject to a master netting agreement or similar agreement. The SAP adopted revisions allowed reporting entities to continue offsetting derivatives, repurchase and reverse repurchase agreements, and securities borrowing and securities lending transactions with a valid right of offset, but incorporated disclosures to illustrate the netting impact. This adoption action included a referral to the Blanks (E) Working Group for annual statement instruction revisions and to recommend development of additional schedules to reconcile the amount reported gross on DB to the amount reported net on the balance sheet.

Agenda item 2016-48 considered accounting and reporting revisions for derivatives with financing premiums. Although discussion occurred proposing a gross accounting and reporting approach, the revisions adopted on November 6, 2017 within that agenda item incorporated aggregate disclosures and new electronic columns in Schedule DB to capture the impact of financing premiums in derivative reporting.

Agenda 2019-38 considered the accounting and reporting of financing derivative transactions pursuant to a review of information from the 2018 year-end statutory financial statements. The agenda item was adopted on July 30, 2020, and included revisions to SSAP No. 86 to ensure consistency in the gross reporting of derivatives without inclusion of financing components and in reporting amounts owed to/from the reporting entity from the acquisition or writing of derivatives.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None.

Convergence with International Financial Reporting Standards (IFRS):
None.

Staff Recommendation:
NAIC Staff recommends that the Working Group move this item to the active listing of the maintenance agenda, categorized as a SAP clarification, and expose revisions to SSAP *No. 86—Derivatives* and the annual statement instructions to ensure consistent terminology for derivative financing premium and to further clarify that derivative premium costs are not to be capitalized to IMR. The proposed revisions to SSAP No. 86 and the annual statement are illustrated below.

Staff Review Completed by:
NAIC Staff – William Oden, October 2024

Status:
On November 17, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing, categorized as a SAP clarification, and exposed this agenda item proposing revisions to *SSAP No. 86—Derivatives* and the annual statement instructions to ensure consistent terminology for derivative financing premiums and to further clarify that derivative premium costs shall not be recognized as a realized gain/loss.

Proposed Edits to SSAP No. 86 - Fall National Meeting:

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 costs are not to be included in the calculation of realized losses nor capitalized to the interest maintenance reserve (IMR) as derivative premium costs are ~~is~~ not considered an underlying in the derivative contract.

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. Accordingly, derivative premium costs are not to be included in the calculation of realized losses~~capitalized to IMR~~. Derivative premiums are to be amortized over the life of the derivative contract with the amortization recorded as an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of 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 and the derivative premium amortized over the life of the derivative contract.

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 - Fall National Meeting:

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 Commitments (Reported on DB)	Derivative Fair Value Excluding Impact of ~~Future 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

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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.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Medicare Part D – Prescription Payment Program

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
This agenda item has been drafted to develop statutory accounting guidance in response to changes to the Medicare Part D (Part D) prescription drug program which goes into effect in 2025. At a high level, the Medicare Prescription Payment Program (MP3) requires insurers to pay pharmacies at the point of sale the out-of-pocket costs of enrollees who have opted into MP3. The enrollees then have the remaining policy term to make installment payments to the insurer. (The policy term typically goes from January through December, so a cost incurred in March, would be repaid through installments ending in December.)

Interpretation (INT) 05-05: Accounting for Revenues Under Medicare Part D Coverage provides high-level accounting guidance on the current Part D program. INT 05-05 includes some basic guidance, but primarily provides guidance by referring to existing statements for specific aspects of the program.

A unique aspect of the updated program is having the insurer pay the pharmacy at the point of sale and seek reimbursement from enrollees. Most of the existing statutory accounting guidance on amounts recoverable from enrollees contemplates premium receivables or amounts due from a governmental payor.

Statutory accounting questions include, 1) where to report the initial point of sale payment to the pharmacy and the related installment receivables, 2) how to account for the prescription drug point of sale payments, and 3) when to write-off and or nonadmit overdue amounts.

Starting with plan year 2025, any Part D enrollee may opt into the program. Enrollees can also opt out of the program and will have differing options to repay their outstanding balance.

The program does not change the Part D enrollee's total out of pocket costs. If a participant fails to pay the amount, they are billed by the Part D sponsor and their participation in the program may be terminated following a required two-month grace period. The Medicare Part D plan sponsor is not permitted to terminate the individual's enrollment in the Part D plan due to failure to pay MP3 bills. Part D plan sponsors must also have a reinstatement process in place to allow individuals to resume participation in the MP3 in the same plan year.

Part D sponsors are required to treat any unsettled balances owed by enrollees under the MP3 as plan losses; Centers for Medicare & Medicaid Services (CMS) considers these unsettled balances as part of the plan's administrative costs. Costs of implementing the MP3 program and program collections are included in the administrative expenses of the Part D plan and are not included in the claim expenses or claim adjustment expenses.
CMS requires several reporting requirements and ongoing monitoring.

CMS has specific guidance on the treatment of unsettled balances in the medical loss ratio (MLR). MLR is the share of revenue used for incurred claims and quality improvement activities, rather than the share of revenue used for administrative costs and profit. Therefore, **excluding unsettled balances from the numerator of the MLR calculation is consistent** with the statutory direction to treat unsettled balances as plan losses and CMS' approach to other administrative expenses incurred by Part D sponsors.

The CMS guidance notes that unsettled balances **are included in the denominator of the MLR calculation**. The Act requires Part D sponsors to treat any unsettled balances owed by participants under the MP3 as plan losses and allows Part D sponsors to include unsettled balances assumed as losses in their premium bids. Consequently, Part D sponsors will receive revenue covering these assumed losses through their direct subsidy and premium payments, which should be included in the denominator of the MLR.

Health insurance industry trades, America's Health Insurance Plans (AHIP) and Blue Cross Blue Shield Association (BCBSA) have also coordinated with NAIC staff and submitted information on the programs.

Existing Authoritative Literature:
INT 05-05: Accounting for Revenues Under Medicare Part D Coverage is an interpretation of the following statements. It provides guidance that primarily references existing guidance in the SSAPs interpreted.

- *SSAP No. 47—Uninsured Plans*
- *SSAP No. 54—Individual and Group Accident and Health Contracts*
- *SSAP No. 66—Retrospectively Rated Contracts*
- *SSAP No. 84—Health Care and Government Insured Plan Receivables*

The CMS website has several guidance documents on the updates to the program.
https://www.cms.gov/inflation-reduction-act-and-medicare/part-d-improvements/medicare-prescription-payment-plan

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Review Completed by: Robin Marcotte - NAIC Staff October 2024

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and take the actions listed below:

1. Expose the draft interpretation *INT 24-02: Medicare Part D Prescription Payment Program* and expose minor edits to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* as illustrated in the attachment. The edits to INT 05-05 adds reference to the new INT 24-02 regarding Medicare Part D prescription payment plans, but does not otherwise change the guidance in INT 05-05.
2. Send notice of the exposure to the Health Insurance (B) Committee and Health Risk-Based Capital (E) Working Group
3. Direct NAIC staff to coordinate with the Blanks (E) Working Group to develop an annual statement blanks proposal in the interim and to develop disclosures for future inclusion in relevant SSAPs. Preliminary recommendations would include the list below, but more research on CMS reporting may also identify other relevant items:
   a. Amounts recoverable on Medicare Part D installments due from enrollees.
   b. Aging of Medicare Part D installments due from enrollees more than 90 days overdue in categories similar to what is used for premium receivables.
   c. Information nonadmitted Medicare Part D installments due from enrollees.
   d. Information on write-offs of Medicare Part D installments due from enrollees.

On November 17, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing, categorized as SAP clarification, and 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*, as described above. 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.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/07 - 24-24 Medicare D RX.docx

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Interpretation of the Emerging Accounting Issues (E) Working Group and Statutory Accounting Principles (E) Working Group

INT 05-05: Accounting for Revenues Under Medicare Part D Coverage

INT 05-05 Dates Discussed

September 28, 2005; December 3, 2005; March 24, 2018; August 4, 2018; November 17, 2024

INT 05-05 References

Current:
SSAP No. 47—Uninsured Plans
SSAP No. 54—Individual and Group Accident and Health Contracts
SSAP No. 66—Retrospectively Rated Contracts
SSAP No. 84—Health Care and Government Insured Plan Receivables
INT 24-02: Medicare Prescription Payment Plan

INT 05-05 Issue

1. The Medicare Modernization Act of 2003 (MMA) created a new program, commonly known as Medicare Part D, whereby Medicare recipients may obtain prescription coverage offered by insurers who have been approved by the Centers for Medicare and Medicaid Services (CMS). Insurers who offer Medicare Part D coverage will, starting in January 2006, receive several different types of funds relating to the program. Some of these funds relate to portions of the coverage that require an annual reconciliation, resulting in the return of any excess funds received. Other funds may be received (or may be required to be returned) to offset experience that is especially unfavorable (or, respectively, favorable).

2. How should the various components of the funds received or receivable by an insurer from Medicare Part D coverage be accounted for?

INT 05-05 Discussion

3. The attached appendix provides a listing of terms to which CMS ascribes a specific meaning. This list has been enhanced to include other terms in order to facilitate consistent application for accounting and the NAIC's risk-based capital (RBC) formula. It should be noted that the terms included in the attached appendix are, for the most part, defined by CMS. Consequently, the term "reinsurance payment" does not represent actual reinsurance as defined by *SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance*.

4. The Emerging Accounting Issues (E) Working Group reached a consensus to adopt the following guidance as it applies to the various funds to be received under the Medicare Part D program. The funds should be accounted for in accordance with one of the three SSAP's outlined below:

   a. Specific funds received as reimbursements (or advance payments) for uninsured claims under a partially uninsured plan should be accounted for under SSAP No. 47. These funds include "reinsurance payments," "Coverage Gap Discount Program" payments and "low-income subsidy (cost-sharing portion)." These funds are paid by the government for a portion of claims above the out-of-pocket threshold or relate to prescription drug plan (PDP) payments for all or a portion of the deductible, the coinsurance and the co-payment amounts for low-income beneficiaries. CMS provides advance funding to the Part D sponsors. The Part D sponsor uses those advances to provide point-of-sale drug discounts to participants. CMS invoices the prescription drug manufacturers. The payment reconciliation process ensures that the Part D sponsor is paid dollar for dollar for

coverage gap discounts advanced at the point of sale, based on accepted prescription drug event (PDE) data, and that any unused excess advances from the government are repaid. The Coverage Discount Gap Program does not apply to low-income beneficiaries.

b. Specific funds received by the PDP sponsor from either the Medicare Part D enrollee or the government as payment for standard coverage that will be subject to retrospective premium adjustments should be accounted for under SSAP No. 66. These funds include "direct subsidy," "low-income subsidy (premium portion)," "beneficiary premium (standard coverage portion)," "Part D payment demonstration" and "risk corridor payment adjustment." The funds noted above have a final policy amount that is calculated based on the loss experience of the insured during the term of the policy, therefore should be treated as such.

c. Specific funds received as premiums for coverage that is not retrospectively rated should be accounted for under SSAP No. 54. These funds include "beneficiary premium (supplemental benefit portion)" as these payments are considered to be standard premium payments that do not meet the definitions under SSAP No. 47 or SSAP No. 66 as defined in paragraph 4.a. and paragraph 4.b. of this interpretation.

d. The Medicare Part D Prescription Payment Plan shall follow the guidance in *INT 24-02: Medicare Prescription Payment Plan*.

5. The collectibility and any nonadmission of amounts receivable from the government insured or uninsured plans are addressed in SSAP No. 84, paragraph 22, and SSAP No. 47, paragraph 10 and paragraph 11, respectively.

INT 05-05 Status

1. On August 4, 2018, the Statutory Accounting Principles (E) Working Group updated this interpretation to add a description of the Coverage Gap Discount Program, amend existing guidance on program payments and update definitions. On TBD, the Working Group updated this interpretation to reference guidance in INT 24-02. No further discussion is planned.

Appendix – Commonly Used Terms for Medicare Part D Coverage

The federal Centers for Medicare and Medicaid Services (CMS) oversees the Medicare Part D prescription drug coverage, including coverage provided through a stand-alone prescription drug plan (PDP) and coverage provided as part of a Medicare Advantage plan. CMS ascribed specific meaning to most of the following terms. Other terms have been defined below in order to facilitate consistent application.

Beneficiary Premium (Standard Coverage Portion) – The amount received from the Part D enrollee (directly, or from CMS after being withheld from Social Security benefits) as payment for the standard coverage. This includes any late enrollment penalties that the PDP sponsor receives for an enrollee. The beneficiary premium is accounted for as health premium.

Beneficiary Premium (Supplemental Benefit Portion) – The amount received from the Part D enrollee (directly, or from CMS after being withheld from Social Security benefits) as payment for supplemental benefits. The beneficiary premium is accounted for as health premium.

Coverage Gap Discount Program – The federal Affordable Care Act amended the Health Care and Education Act of 2010 (H. R. 4872) (HCERA) in 2011 to establish a discount program that would make manufacturer discounts available to applicable Medicare beneficiaries receiving applicable covered Part D drugs while in the coverage gap. Part D sponsors must provide the discounts for the applicable drugs in the coverage gap at point-of-sale. CMS coordinates the collection of discount payments from manufacturers and payment to Part D sponsors that provided the discount to applicable beneficiaries through a contractor. The coordination involves a standard process for paying Part D sponsors based on new information submitted to CMS on prescription drug event data. The Coverage GAP Discount Program is reconciled quarterly.

Coverage Year Reconciliation – A reconciliation made after the close of each calendar year to determine the amounts that a PDP sponsor is entitled to for the low-income subsidy (cost-sharing portion), the reinsurance payment, and the risk corridor payment adjustment. To the extent that interim payments (if any) from CMS exceeded the amounts determined by the reconciliation, the PDP sponsor must return the excess to the government; to the extent that interim payments (if any) from CMS fell short of the amounts determined by the reconciliation, the government will make an additional payment to the PDP sponsor. The coverage year reconciliation results in the low-income subsidy (cost-sharing portion) and the reinsurance payment being essentially a self-insured (by the government) component of the Part D coverage, subject to SSAP No. 47. The coverage year reconciliation also results in the treatment of the risk corridor payment adjustment as a retrospective premium adjustment, subject to SSAP No. 66.

Direct Subsidy – The amount the government pays to the PDP sponsor for the standard coverage. These payments are accounted for as health premium.

Low-Income Subsidy (Cost-Sharing Portion) – The amount the government pays to the PDP sponsor for additional benefits provided to low-income enrollees. The additional benefits may include payment for some or all of the deductible, the coinsurance, and the co-payment above the out-of-pocket threshold. These payments are accounted for as payments made under a self-insured plan.

Low-Income Subsidy (Premium Portion) – The amount the government pays to the PDP sponsor for low-income enrollees in lieu of part or all of the beneficiary premium (standard coverage portion). These payments are accounted for as health premium.

PDP Sponsor – The entity that provides stand-alone Part D coverage (as opposed to Part D coverage provided through a Medicare Advantage plan).

Reinsurance Payment – An amount paid by the government for benefit costs above the out-of-pocket threshold (see "Standard Coverage"). Generally, when costs exceed the out-of-pocket threshold, the government pays a specified percentage of the costs, the enrollee pays a percentage (or the specified co-

payments which are updated based on cost trends for generic and for brand-name prescriptions), and the PDP sponsor pays the remainder. The amount paid by the government is treated as a claim payment made by a self-insured benefit plan rather than as revenue to the PDP sponsor, and the claims do not flow through the PDP sponsor's income statement. In cases where the government prepays the reinsurance payment on an estimated basis, the prepayment is treated as a deposit, which again does not pass through the PDP sponsor's income statement. The amount paid by the enrollee is paid directly to the pharmacy; therefore there is no required accounting for this amount by the PDP sponsor.

Part D Payment Demonstration – A payment from the government to a PDP sponsor participating in CMS's Part D Payment Demonstration. The payment demonstration is a special arrangement in which the PDP sponsor receives a predetermined per-enrollee capitation payment and the government no longer provides reinsurance for the specified percentage (example 80%) of costs in excess of the out-of-pocket threshold. Rather, the PDP sponsor assumes the risk for the specified percentage (example 80%) of costs, in addition to its normal percentage (example 15%) share of costs in excess of this threshold. However, risk corridor protection does still apply to this specified percentage (example 80%) share of costs. These payments are accounted for as health premium.

Reinsurance Coverage – The Medicare Part D provision under which the PDP sponsor may receive a reinsurance payment. This does not include payments under the Part D Payment Demonstration.

Risk Corridor Payment Adjustment – An amount by which the government adjusts its payments to the PDP sponsor, based on how actual benefit costs vary from the costs anticipated in the PDP sponsor's bid for the Part D contract (the "target amount" of costs). The government establishes thresholds for symmetric risk corridors around the target amount, using percentages of the target amount. If actual costs exceed the target amount but are less than the first threshold upper limit, then no adjustment is made. Risk corridor payment adjustments are accounted for as retrospective premium adjustments on retrospectively rated contracts.

Risk Corridor Protection – The Medicare Part D provision under which the PDP sponsor may receive (or pay) a Risk Corridor Payment Adjustment. Most employer plans providing Medicare Part D are not eligible for Risk Corridor Protection.

Standard Coverage – The Part D benefit design that conforms to certain standards prescribed by the government. The standard coverage comprises: no coverage for an annual initial deductible; coverage net of a coinsurance provision (the percentage of costs are payable by the insured) for costs up to an initial coverage limit; a range beyond the initial coverage limit (sometimes called the "coverage gap") in which the insured drug manufacturers and the PDP sponsor (for example, by 2020 insureds who are eligible for drug manufacturer discounts will pay 25% for qualifying brand and generic drugs, the PDP sponsor will be responsible for 25% of qualifying brand and 75% of generic drugs, and the drug manufacturer will be responsible for 50% of qualifying brand drugs); and an annual out-of-pocket threshold above which the insured pays the greater of a specified co-payment or a specified percentage of the drug cost. The various limits and thresholds are set at specified dollar amounts, which will be increased in later years based on the growth in drug expenditures. Wherever the term "standard coverage" is used as part of these instructions, the same treatment would be applied to coverage that has been approved as actuarially equivalent coverage. With respect to amounts above the out-of-pocket threshold, see the definitions of "Reinsurance Payment" and "Part D Payment Demonstration."

Supplemental Benefits – Benefits in excess of the standard coverage. These benefits typically will cover some portion of the deductible, the co-payments, or the coverage gap between the initial coverage limit and the out-of-pocket threshold. Supplemental benefits are part of an enrollee's Part D coverage, so they are not placed in the "Other" category in the RBC formula. However, they are not subject to either the reinsurance payment or the risk corridor payment adjustment, so they receive less favorable RBC treatment than the standard coverage.

Interpretation of the
Statutory Accounting Principles (E) Working Group

INT 24-02T: Medicare Part D Prescription Payment Plan~~s~~

Drafting Note: Tracked changes reflect revisions from the November exposure which are planned for discussion.

INT 24-02T Dates Discussed

November 17, 2024; February 25, 2025

INT 24-02T References

Current:
- *SSAP No. 47—Uninsured Plans*
- *SSAP No. 54—Individual and Group Accident and Health Contracts*
- *SSAP No. 66—Retrospectively Rated Contracts*
- *SSAP No. 84—Health Care and Government Insured Plan Receivables*
- *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*

INT 24-024T Issue

1. 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 ~~help~~ offer Part D enrollees the option to ~~manage~~ 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~~3~~), ~~will become~~is effective on January 1, 2025.

~~1.~~2. The purpose of this interpretation is to provide statutory accounting and reporting guidance for aspects of ~~the MP3~~MPPP ~~program~~. This interpretation specifically addresses the ~~MP3~~MPPP components of Medicare Part D and does not intend to alter the guidance in *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*, which offers high-level accounting guidance on the current Medicare Part D program.

~~MP3~~MPPP Program Overview

3. ~~MP3~~MPPP ~~is a new program that~~ requires all Medicare prescription drug plans (Part D plan~~s~~ sponsors), including both standalone Medicare prescription drug plans and Medicare Advantage plans with prescription drug coverage, to offer its ~~members~~enrollees the option to pay their out-of-pocket prescription drug costs through monthly payments to the Part D plan sponsor over the remainder of the plan year, as opposed to paying the full amount upfront to the pharmacy.

~~2.~~4. Part D plan ~~members~~enrollees who elect to participate in ~~MP3~~MPPP (~~MP3~~MPPP ~~enrollees~~participants) will pay $0 to the pharmacy for covered Part D drugs. ~~The~~Instead, the Part D plan sponsor is required to fully pay the pharmacy the total of an ~~enrollee's~~ MPPP participant's applicable out-of-pocket amount and the Part D plan sponsor's portion of the payment in accordance with Part D prompt payment requirements. Subsequently, the Part D plan sponsor will bill the ~~MP3~~MPPP participant ~~enrollee~~ monthly for any cost-sharing incurred while enrolled in ~~MP3~~MPPP.

5. ~~MP3~~ ~~enrollees~~ MPPP participants will not ~~save money~~ reduce ~~on~~ ~~the~~ total out-of-pocket costs ~~of~~ for prescription drug purchases ~~(there are other Part D programs in place to help qualifying Part D plan members with affordability issues)~~. ~~MP3~~MPPP simply spreads the MPPP participants' out-of-pocket Part D costs into monthly payments over the remaining term of the plan year which may help ~~many~~ some ~~Part D plan~~MPPP ~~members~~participants to better manage their monthly cash flow.

~~3.~~6. Unlike other existing aspects of Medicare Part D, ~~programs~~ which involve funds due from the federal government ~~(~~for which payment is effectively assured~~)~~, ~~MP3~~MPPP installment balance recoverables are due from individual ~~enrollees~~MPPP participants. Consequently, Part D plans may pay pharmacies for ~~MP3~~MPPP ~~enrollees'~~ participants' out-of-pocket pharmacy claim costs, but some amounts billed to the ~~enrollee~~ MPPP participants might be uncollectible~~, determined~~ . ~~Reasons for the amount being uncollectable could include leaving enrollment in the Part D plan or an inability or unwillingness to pay the full outstanding balance.~~ That could occur when an MPPP participant does not pay the full outstanding balance after the required grace period. This raises statutory accounting concerns regarding potential nonadmittance of overdue amounts and impairment of ~~such~~ unpaid outstanding recoverables from MPPP participants.

~~4.~~7. To help cover potential uncollectible balances, the Centers for Medicare and Medicaid Services (CMS) allows Part D plan sponsors to include an ~~MP3 loss~~ estimate for MPPPP related losses in their ~~premium~~ plan bids. However, for the initial years, Part D plan sponsors ~~have no~~lack directly relevant prior experience in estimating the ~~MP3~~MPPP program's potential ~~expenses~~ for uncollectible amounts.

~~5.~~8. The government is responsible for the estimated ~~MP3~~MPPP ~~losses~~ losses to the extent they are included in ~~premium~~ plan bids by Part D plan sponsors. Part D plan sponsors receive additional revenue, which helps to cover uncollectible balances ~~resulting~~ from ~~MP3~~MPPP ~~enrollees~~participants. Part D plan sponsors face pricing/underwriting risk relating to the prescription needs of enrollees and may inaccurately estimate the amounts of uncollectible balances to include in ~~losses in the premium~~ plan bids. In addition, there are risks that the costs of uncollectible amounts and other aspects of implementing the ~~payment plan~~MPPP will vary from amounts that had been factored into ~~premium rates~~plan bids. ~~According to CMS guidance any losses in excess of the loss estimates included in the premium bids are the responsibility of the Part D plan sponsor.~~

~~MP3~~MPPP Program Requirements for Unpaid Balances

~~6.~~9. ~~The MP3~~ Under the MPPP, ~~Program requires~~ Part D plan sponsors ~~to~~ take on the risk for ~~of~~ uncollectible balances not covered by the plan bid. The program rules prohibit or limit many of the common methods used to mitigate loss from uncollectible ~~MP3~~MPPP balances~~. MP3 is a mandated program benefit imposed by federal law and CMS rules, with different implications for statutory accounting purposes~~. Examples of such prohibitions or limitations ~~Other key program requirements for MP3 balances~~ include the following:

a. **Late Fees, Etc. –** Under ~~MP3~~MPPP, late fees, interest payments, or other fees, such as for different payment mechanisms, are not allowed.

b. **Billing and Payment Procedures –** Part D plan sponsors can design their own billing and payment procedures for ~~MP3~~MPPP. However, they must prioritize payments towards Part D plan premiums to avoid an enrollee losing their Part D coverage. This rule applies when

it is unclear if an enrollee intended a submitted payment to cover their outstanding Part D plan premium or their ~~MP3~~MPPP balance.

c. **Pharmacies Not Responsible for Balances –** Participation in ~~MP3~~MPPP is considered an arrangement between the Part D plan sponsor and the ~~MP3 enrollee~~MPPP participant. Pharmacies are not responsible for ~~an enrollee's unsettled~~losses attributed to the uncollectibility of MPPP participants' balances or for collecting unpaid balances from the ~~MP3 enrollee~~MPPP participant on the Part D plan sponsor's behalf.

d. **Termination of Participation** – A Part D plan sponsor must terminate an enrollee's participation in ~~MP3~~MPPP if the enrollee fails to pay their monthly billed amount. An ~~MP3 enrollee~~ MPPP participant will be considered to have failed to pay their monthly billed amount only after ~~the~~ a required grace period of at least two months. The Part D plan sponsor cannot terminate ~~the~~ an enrollee~~'s membership in~~from the Part D plan for nonpayment of any of their ~~MP3~~MPPP billed amounts. Part D plan s~~S~~ponsors must continue billing amounts owed under the program in monthly amounts up to the maximum monthly cap based on the statutory formula for the remaining duration of the plan year after an enrollee has been terminated.

e. **Reinstatement of Enrollees** - Part D plan sponsors must reinstate terminated ~~MP3 enrollees~~MPPP participants if the individual demonstrates good cause for failure to pay the program billed amount within the grace period and pays all overdue amounts billed.

f. **Preclusion from Subsequent Enrollment** - A Part D plan sponsor may prevent an individual from opting in-to the ~~MP3~~MPPP program in a subsequent year if the individual owes an overdue balance to that Part D plan sponsor or to another Part D plan sponsor with the same ~~ultimate~~ parent organization. In other words, an individual who owes an overdue MPPP balance ~~under the program~~to a Part D plan sponsor cannot be barred from enrolling in ~~MP3~~ MPPP in a subsequent year ~~by~~ through a different Part D plan sponsor that does not have the same parent organization.

g. **Compliance with Federal and State Laws -** Part D plan sponsors (and any third parties that Part D plan sponsors contract) collecting unpaid balances related to the program must follow other applicable federal and state laws and requirements, including those related to other types of payment plans, credit reporting, and debt collection.

Medical Loss Ratio

~~7.~~10. The current Public Health Act outlines how to calculate medical loss ratio (MLR) rebates, which are generally based on a comparison of incurred health claims and quality improvement activities to premium revenue, considering various factors and adjustments. *SSAP No. 66—Retrospectively Rated Contracts* provides disclosures related to the MLR. The CMS MLR requirements are separate from the statutory accounting reporting requirements for MPPP. However, statutory accounting differences from CMS requirements create the need for reporting adjustments in the annual statement *Supplemental Health Care Exhibit.*

~~8.~~11. According to the CMS guidance, the losses related to uncollectible MPPP participants' ~~outstanding~~ balances ~~owed by MP3 enrollees~~are considered for MLR purposes as part of the Part D plan sponsor's administrative expenses. CMS guidance excludes ~~unsettled~~ losses attributed to uncollectible MPPP participants' balances from the numerator of the MLR calculation, ~~aligning with~~this is consistent with

CMS' treatment of other administrative expenses incurred by Part D sponsors. The CMS guidance states that ~~unsettled balances are~~the additional premium revenue attributable to the estimates of MPPP uncollectible amounts included in the Part D plan sponsor plan bids are included in the MLR calculation denominator~~ and allows Part D sponsors to account for these balances as losses in their premium bids~~. ~~The inclusion of Including enrollee losses~~~~the additional premium revenue in the denominator aligns with reporting the revenue estimated to offset~~s ~~these losses also captured in the MLR denominator.~~

Drafting Note: The ~~MP3~~MPPP program considers uncollectible ~~MP3~~ recoverables from MPPP participants as incurred plan administrative costs and does not include these amounts in the MLR numerator, so reporting guidance for other adjustments to the Supplemental Health Care Exhibit will be needed. Such reporting revisions are not addressed in this interpretation but would be anticipated to be in the annual statement reporting revisions submitted to the Blanks (E) Working Group.

INT 24-02T Discussion

Statutory Accounting and Reporting Considerations for ~~MP3~~MPPP

~~9.~~12. The Working Group reached the following tentative consensus for ~~MP3~~MPPP statutory accounting and reporting guidance. In addition, Appendix 1 illustrates some basic journal entries which help to show the intended financial statement results.

~~MP3~~ Recoverables from MPPP Participants

~~10.~~13. ~~MP3~~ R~~r~~ecoverables from MPPP participants ~~enrollees~~ shall be accrued and reported as an asset on the ~~asset~~ asset page in the line ~~24,~~ for *Health care and other amounts receivable*, when the related payment is made by the Part D plan sponsor to the pharmacy for the out-of-pocket ~~payment~~costs ~~is~~ incurred on behalf of the MPPP participant.

~~11.~~14. Current ~~MP3MPPP~~ recoverables from MPPP participants, 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 MP3 enrollees~~~~MPPP participants represents a probable future economic benefit to the Part D plan sponsor resulting from past transactions or events (i.e., paying the MP3 enrollee's~~~~MPPP participants out-of-pocket costs to the pharmacy). MP3~~ R~~r~~ecoverables from MPPP participants are also subject to impairment analysis.

~~12.~~15. Uncollected ~~MP3~~MPPP recoverables more than 90 days overdue are nonadmitted. The due date for aging of the ~~MP3~~MPPP recoverables shall follow the program billing guidelines.

~~13.~~16. If a~~n MP3~~ recoverable from an MPPP participant is fully collected, it will equal the corresponding out-of-pocket payment for a pharmaceutical claim payment. In those cases, there will not be an income statement impact regarding claims (or claims adjusting expenses)~~ if the MP3~~~~MPPP recoverable is fully collected~~.

Impairments

~~14.~~17. Uncollected ~~MP3~~ recoverables from ~~enrollees~~ MPPP participants are subject to an 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 ~~MP3~~ recoverables from MPPP

participants are ~~recorded~~written off, the expense ~~for the impairment~~ shall be reflected ~~in~~ as an incurred Medicare Part D prescription drug claims in the statutory income statement.

Out-of-Pocket ~~MP3~~MPPP Pharmacy Payments

~~15.~~18. When the Part D plan sponsor pays out-of-pocket drug claims to the pharmacy, a claims expense, a contra claims expense, and a contra claims expense account recoverable are recorded. The contra claims expense, or similar mechanism, is recorded to prevent initial claims expense recognition in the income statement so there is zero initial impact to the income statement. This is because there is an amount recoverable from the ~~enrollee~~MPPP participant, and to the extent that the ~~enrollee~~ MPPP participant pays in full, there should not be any claims recognition. This is analogous to the handling of anticipated pharmaceutical rebates or anticipated subrogation recoveries.

~~16.~~19. If the ~~enrollee~~ MPPP participant pays the amount due in full, there will be no income statement impact in claims expenses resulting from the Part D plan sponsor's payment of the ~~MP3~~MPPP participants out-of-pocket costs to the pharmacy. This is because the MPPP participant's ~~payment and enrollee~~subsequent monthly payments to the Part D plan sponsor have fully offset the initial pharmacy payments. In such cases, the ~~MP3~~MPPP recoverable will be reduced as payments are collected and there would be no income statement impact.

~~17.~~20. If the MPPP participant's ~~enrollee~~ balance ~~recoverable~~ is not repaid in whole or in part, there will be an income statement impact to reflect paid claims for the ~~amount of the~~uncollectible ~~MP3~~MPPP ~~recoverable~~ balances ~~that are~~ which have been evaluated for impairment ~~ed~~ and written off. Since there is a~~n~~ ~~MP3~~ recoverable from the ~~enrollee,~~MPPP participant there should be no income statement amount for an incurred claim until the related ~~MP3~~MPPP recoverable is written off as uncollectible based on ~~for~~ impairment analysis.

~~18.~~21. When the ~~MP3~~ recoverable from the MPPP participant is evaluated for impairment~~ed~~, the contra claims expense is decreased by the amount of the ~~MP3~~MPPP recoverable that is written off. This results in the incurred Medicare prescription claim reported reflecting the uncollectible ~~MP3~~ recoverable from MPPP participants for statutory reporting. The premium to offset these claims is included in Medicare premium bids, so reporting the ~~incurred~~ uncollectible ~~MP3~~MPPP amounts as losses allows the statutory accounting loss ratio to reflect incurred Medicare Part D prescription costs, including the ~~which include MP3~~MPPP uncollectible amounts which have been impaired and written off.

~~19. Reporting uncollectible and impaired MP3 recoverables in statutory filings as claims incurred is different than the CMS treatment of which reports such amounts as administrative expense for MLR purposes.~~

Administrative Costs

~~20.~~22. Other c~~C~~osts, e.g., those incurred by Part D plan sponsors in ~~of~~ implementing ~~the MP3~~and administering the MPPP program and ~~program~~related collections, are included in the administrative expenses of the Part D plan sponsor and are not included in the claim expenses or claim adjustment expenses.

MLR Reporting Difference

~~21.~~23. Note that the reporting of the ~~uncollectible~~written off (impaired) ~~MP3~~ recoverable from MPPP participants in Medicare prescription claims is different from CMS treatment of such amounts in the MLR. The CMS requires Part D plan sponsors to report losses from impairment write-offs ~~treatment~~ of uncollectible ~~MP3~~ recoverables from MPPP participants ~~reports such amounts~~ as administrative amounts. These administrative amounts are included in the denominator of the MLR by CMS.

INT 24-02T Status

~~22.~~24. This interpretation is tentatively effective March 30, 2025.

~~23.~~25. Further discussion is planned.

Appendix 1 - Illustrative Journal Entries

Medicare Prescription Payment Plan Scenarios			
	Claims	**Receivable**	**Cash**
Initial entries for all scenarios *Assumed to have been recorded by the ~~insurance company~~Part D plan sponsor prior to Scenarios 1 – 3.*			
DR Claims Expense *To represent claims expenses incurred on behalf of the ~~enrollee~~MPPP participant.*	$ 2,000		
CR Cash *To represent the $2,000 paid by the ~~insurance company~~Part D plan sponsor to the pharmacy on behalf of the ~~enrollee~~MPPP participant.*			$ (2,000)
DR Healthcare Receivable *To represent the amount due to the ~~insurance company~~Part D plan sponsor from the ~~enrollee~~MPPP participant, which the ~~enrollee~~MPPP participant must pay over the policy term.*		$ 2,000	
CR Claims A/R (contra-claims expense) *To be reported within the claims expense line, essentially a contra-claims expense, and represents the amount due to the ~~insurance company~~Part D plan sponsor from the ~~enrollee~~MPPP participant which the ~~enrollee~~MPPP participant must pay over the policy term. This offsets the claims expense amount, so results in a current net $0 impact ~~to~~on the income statement, but both the DR and CR on the income statement are in claims expense.*	$ (2,000)		
Scenario 1 - The ~~enrollee~~MPPP participant pays their full amount of $2,000 to the ~~insurance company~~Part D plan sponsor.			
DR Cash *To record receipt of the ~~enrollee~~MPPP participant's payment in full.*			$ 2,000
CR Healthcare Receivable *The net income statement impact remains at $0, because the original claims expense was offset by the contra-claims expense (Claims A/R), and since the full $2,000 was received from the ~~enrollee~~MPPP participant, there are no further income statement journal entry impacts.*		$ (2,000)	
Scenario 1 Net result on Financial Statements	**$ -**	**$ -**	**$ -**
Scenario 2 -- The ~~enrollee~~MPPP participant pays $1,500 out of the $2,000 to the ~~insurance company~~Part D plan sponsor and ~~doesn't~~does not pay the remaining $500.			
DR Cash			$ 1,500

To record receipt of ~~enrollee~~MPPP participant partial payment of outstanding balance.			
CR Healthcare receivable *To reduce ~~enrollee~~MPPP participant receivable for amounts paid.*		$ (1,500)	
DR Claims A/R (contra-claims expense) *To represent the write-off of the receivable. This results in the ~~insurance company~~Part D plan sponsor having a total income statement impact debit to claims expense of $500, represented as the initial $2,000 claims expense for the out-of-pocket- paid to the pharmacy by the ~~insurance company~~Part D plan sponsor, offset by the $1,500 received from the ~~enrollee~~MPPP participant.*	$ (500)		
CR Healthcare receivable *To write-off the remaining uncollectible amount as impaired*		$ (500)	
Scenario 2 Net result on Financial Statements	**$ 500**	**$**	**$ (500)**
Scenario 3 - The ~~enrollee~~MPPP participant does not pay any of the $2,000 owed to the ~~insurance company~~Part D plan sponsor.			
DR Claims A/R (contra-claims expense) *To represent the write-off of the amount anticipated to be paid by the ~~enrollee~~MPPP participant. This results in the income statement impact to the ~~insurance company~~Part D plan sponsor being a debit of $2,000, for the amount paid to the pharmacy by the ~~insurance company~~Part D plan sponsor and not reimbursed by the ~~enrollee~~MPPP participant.*	$ 2,000		
CR Healthcare receivable *To represent the write-off of the $2000 receivable.*		$ (2,000)	
Scenario 3 Net result on Financial Statements	**$ 2,000**	**$ -**	**$ (2,000)**

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Issue Papers in Statutory Hierarchy

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been drafted to capture issue papers in Level 5 of the statutory hierarchy pursuant to the direction from the 2024 Fall National Meeting. Additionally, revisions have been proposed to update the process to develop issue papers to reflect current Working Group practice.

This issue originated in response to a Sept. 27, 2024, interested parties' comment letter for the Principles-Based Bond Definition Questions and Answer Implementation Guide where interested parties suggested that issue papers should be recognized as authoritative guidance. These comments suggested inclusion of issue papers in Level 2 or Level 4 of the statutory hierarchy. However, NAIC staff identified that 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. The excerpt from the Hearing agenda discussed during the 2024 Fall National Meeting (captured within the authoritative literature) 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 was also noted that some citations in issue papers discuss proposed guidance that is evaluated and rejected. These reasons further support the identification of issue papers in Level 5 of the statutory hierarchy, as they are a source of statutory accounting, but shall be applied only to the extent that they do not conflict with a higher level of guidance.

The proposed revisions to incorporate these changes are predominantly captured in the Statutory Hierarchy reflected in the Statutory Accounting Preamble and Appendix E. Revisions have not been proposed to modify the effective date language of historical Issue Papers. Rather, a note has been included to identify the revisions to the classification of issue papers as Level 5 of the statutory hierarchy.

Excerpt from Interested Parties' Sept. 27, 2024 Comment Letter:

> First, interested parties would like to suggest that Issue Papers be recognized as authoritative guidance and included in Level 2, or alternatively Level 4, in the statutory hierarchy of authoritative guidance. Level 2 would place issue papers higher in the hierarchy than the annual statement instructions (Level 3) which arguably is 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 implies if a difference exists, and is not addressed by the SSAP, it is authoritative. If this interpretation by interested parties is not consistent with the NAIC's interpretation, it is important that the issue papers be explicitly included in the statutory hierarchy as many are drafted to include interpretative guidance not included in the SSAPs (e.g., feeder funds related to the

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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). Further, other areas of the Accounting Practices & Procedures Manual that suggest issues papers are not authoritative (e.g., Appendix E) would need to be updated for consistency.

Existing Authoritative Literature:

Statutory Accounting Principles Preamble

V. Statutory Hierarchy

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

Level 1

SSAPs, including U.S. GAAP reference material to the extent adopted by the NAIC from the FASB Accounting Standards Codification[1] *(FASB Codification or GAAP guidance)*

Level 2

Consensus positions of the Emerging Accounting Issues (E) Working Group as adopted by the NAIC (INTs adopted before 2016)

Interpretations of existing SSAPs as adopted by the Statutory Accounting Principles (E) Working Group (INTs adopted in 2016 or beyond)

Level 3

NAIC Annual Statement Instructions

Purposes and Procedures Manual of the NAIC Investment Analysis Office

Level 4

Statutory Accounting Principles Preamble and Statement of Concepts[2]

Level 5

Sources of nonauthoritative GAAP accounting guidance and literature, including: (a) practices that are widely recognized and prevalent either generally or in the industry, (b) FASB Concept Statements, (c) AICPA guidance not included in FASB Codification, (d) International Financial Reporting Standards, (e) Pronouncements of professional associations or regulatory agencies, (f)

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

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

Technical Information Service Inquiries and Replies included in the AICPA Technical Practice Aids, and (g) Accounting textbooks, handbooks and articles

43. If the accounting treatment of a transaction or event is not specified by the SSAPs, preparers, regulators and auditors of statutory financial statements should consider whether the accounting treatment is specified by another source of established statutory accounting principles. If an established statutory accounting principle from one or more sources in Level 2 or 3 is relevant to the circumstances, the preparer, regulator or auditor should apply such principle. If there is a conflict between statutory accounting principles from one or more sources in Level 2 or 3, the preparer, regulator or auditor should follow the treatment specified by the source in the higher level—that is, follow Level 2 treatment over Level 3. Revisions to guidance in accordance with additions or revisions to the NAIC statutory hierarchy should be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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

VI. Statements of Statutory Accounting Principles <u>(Bolding and underlining added for emphasis)</u>

45. This Manual consists primarily of Statements of Statutory Accounting Principles (SSAPs). SSAPs are the primary Accounting Practices and Procedures promulgated by the NAIC. These statements are the result of issue papers that have been exposed for public comment and finalized. Finalized issue papers are in Appendix E. **<u>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.</u>**

<u>Appendix E – Issue Papers (Bolding and underlining added for emphasis)</u>

Introduction

Issue papers are used as the first step in developing new or revised SSAPs, and each contains a recommended conclusion, discussion and relevant literature section. **<u>While issue papers do not constitute an authoritative level of statutory accounting guidance as defined by the statutory hierarchy, they are an important part of the *Accounting Practices and Procedures Manual* (Manual) because they reference the history and discussion of the related SSAP.</u>**

Issue papers are published in the Manual within Appendix E the first year after adoption of the related SSAP, but are then removed from the subsequent year's Manual and posted for public reference on the Statutory Accounting Principles (E) Working Group (SAPWG) web page at
https://content.naic.org/cmte_e_app_sapwg.htm.

<u>2024 Fall National Meeting Discussion</u>

NAIC staff presented a recommendation along with a review of historical guidance and references in issue papers during the 2024 Fall National Meeting. This information has been retained within this agenda item for reference purposes:

2024 Fall National Meeting Recommendation: NAIC staff recommend that the Working Group direct a new agenda item to consider capturing issue papers in Level 5 of the statutory hierarchy. Although interested parties have proposed a classification of Level 2, and an alternative classification in Level 4, NAIC staff suggest that consideration of a Level 5 classification is most appropriate to prevent any unintended conflicts with other sources of statutory guidance. The rationale for this position is that 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 deemed to reflect accounting guidance, reporting instructions or information from the SVO manual. The Level 5 classification will put issue papers on the same level as non-authoritative GAAP guidance and literature. NAIC staff believe this is appropriate, as if guidance for a topic is not specifically detailed in any other form of statutory-specific sources, adopted issue papers should be a viable source for guidance along with non-authoritative GAAP.

As detailed within, from a review of references in the issue papers, various references imply that issue papers can be applied and utilized as long as the guidance within the Issue Paper does not conflict with other guidance. There are a few explicit instances that note they are not authoritative/in the statutory hierarchy. NAIC staff notes that Issue Papers often include discussion of guidance or components that are not incorporated into SSAP, therefore it is imperative for the guidance to only be applicable if consistent with an adopted SSAP. By adding the issue papers to Level 5, this 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.

- 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 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.

NAIC staff recognizes that existing guidance presents inconsistent references to issue papers causing confusion on how/when they should apply. As noted, there are a few explicit statements that issue papers are not authoritative, but other references imply application and use of Issue Papers when there are no differences between the issue paper and the SSAP. NAIC staff believe it is imperative to stress application only when the guidance is in line with a current adopted SSAP. As SSAPs have not historically been posted publicly, NAIC staff receive questions that cite guidance in issue papers as they are posted publicly. Often in these situations, the citations have been superseded by more current SSAP, so attempting to use the issue paper guidance in those instances would not be in line with current SSAP. The following Preamble excerpt has been within the NAIC *Accounting Practices and Procedures Manual* since original codification (2000 Manual) and implies that finalized issue papers are applicable but defer to the SSAP if differences exist. (This was paragraph 41 in the 2000 Manual and is reflected as paragraph 45 in the 2024 Manual.)

> 41/45. This Manual consists primarily of Statements of Statutory Accounting Principles (SSAPs). SSAPs are the primary Accounting Practices and Procedures promulgated by the NAIC. These statements are the result of issue papers that have been exposed for public comment and finalized. **Finalized issue papers are in Appendix E. 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.**

The following Preamble excerpt has also been within the NAIC *Accounting Practices and Procedures Manual* since original codification (2000 Manual) and indicates in the absence of a SSAP or "established source of statutory accounting principles," other accounting literature may be considered. As issue papers would represent an established source of statutory guidance, this Preamble guidance could be argued to have always supported issue papers as a source that could be considered along with non-authoritative GAAP if other statutory guidance did not exist. (This is paragraph 40 in the 2000 Manual and is reflected as paragraph 44 in the 2024 Manual.)

40/44. Because of developments such as new legislation or the evolution of a new type of business transaction, there sometimes are no established statutory accounting principles for reporting a specific transaction or event. In those instances, it might be possible to report the event or transaction on the basis of its substance by selecting a statutory accounting principle that appears appropriate when applied in a manner similar to the application of an established statutory principle to an analogous transaction or event. In **the absence of a SSAP or another source of established statutory accounting principles, the preparer, regulator or auditor of statutory financial statements may consider other accounting literature, depending on its relevance in the circumstances. Other accounting literature includes the Statutory Accounting Principles Statement of Concepts and GAAP reference material and accounting literature below category c in the GAAP hierarchy as defined in SAS 69**. The appropriateness of other accounting literature depends on its relevance to the particular circumstances, the specificity of the guidance, and the general recognition of the issuer or author as an authority. For example, the Statutory Accounting Principles Statement of Concepts would be more authoritative than any other sources of accounting literature. Similarly, FASB Concepts Statements would normally be more influential than other sources below category d in the GAAP hierarchy4.

From a review of all issue papers, NAIC staff has identified that the original issue papers that correspond to the original codification of statutory accounting principles through issue papers adopted in 2000 did not include an "Effective Date" section. Beginning with *Issue Paper No. 107—Certain Health Care Receivables and Receivables Under Government Insured Plans*, which was finalized Aug. 8, 2001, an Effective Date section was included. After that issue paper, some form of "Effective Date" guidance was generally included (but not always). From Issue Paper No. 107 through Issue Paper No. 164, when effective date language was included, it was worded like the excerpts below. Although these excerpts identify that the issue papers are not in the statutory hierarchy, they also indicate an expectation that the issue paper's conclusions can be "applied" once the SSAP has been adopted.

Issue Paper No. 107: Finalized Aug. 1, 2001

28. Upon adoption of this issue paper, the NAIC will release a Statement of Statutory Accounting Principle (SSAP) for comment. The SSAP will contain the adopted Summary Conclusion of this issue paper. **Users of the Accounting Practices and Procedures Manual should note that issue papers are not represented in the Statutory Hierarchy (see Section IV of the Preamble) and therefore the conclusions reached in this issue paper should not be applied until the corresponding SSAP has been adopted by the Plenary of the NAIC.** It is expected that the SSAP will contain an effective date of years ending on or after December 31, 2001.

Issue Paper No. 164: Finalized July 30, 2020

23. The adoption of this issue paper by the Statutory Accounting Principles (E) Working Group, and the substantively revised statement of statutory accounting principles (SSAP) occurred on July 30, 2020. The substantive revisions to SSAP No. 32R are detailed in Exhibit A of this issue paper and reflected in the substantively-revised SSAP No. 32R—Preferred Stock. The effective date of the guidance will be identified in the SSAP. **Users of the Accounting Practices & Procedures Manual should note that issue papers are not represented in the Statutory Hierarchy (see**

[4] As specified by AU Section 411, paragraph 11.

Section IV of the Preamble) and therefore the conclusions reached in this issue paper should not be applied until the corresponding SSAP has been adopted by the Plenary of the NAIC.

Although the original process for issue papers was to have them adopted prior to the development and adoption of the SSAP (which could result in differences between the SSAP and issue paper), current practice more often adopts the SSAP revisions, and then uses the issue paper for historical documentation purposes, or they are completed concurrently. Note, however, that not all SSAP revisions, especially those of clarification type and not contested, have a related issue paper updated. The following effective date language is captured in more recent issue papers adopted between 2019-2023. (Noted also in Issue Papers No. 163, 165 and 167.)

Issue Paper No. 162: Finalized Aug. 3, 2019

24. As issue papers are not represented in the Statutory Hierarchy (see Section IV of the Preamble), the subsequent consideration and adoption of this issue paper will not have any impact of the effective date of the substantive revisions adopted to SSAP No. 62R during the 2018 Fall National Meeting.

NAIC staff only identified the following two issue papers that appear to have been expanded to include language as "not authoritative" in the issue paper's effective date language. These are relatively recent issue papers adopted in 2022 and 2023.

Issue Paper No. 166—Updates to the Definition of a Asset (Finalized Aug. 10, 2022)

21. **As issue papers are not authoritative** and are not represented in the Statutory Hierarchy (see Section V of the Preamble), the consideration and adoption of this issue paper will not have any impact on the SAP clarifications adopted to SSAP No. 4 by the Working Group on August 10, 2022.

Issue Paper No. 168—Updates to the Definition of a Liability (Finalized Aug. 13, 2023)

24. **As issue papers are not authoritative** and are not represented in the Statutory Hierarchy (see Section V of the Preamble), the consideration and adoption of this issue paper will not have any impact on the SAP clarifications adopted to SSAP No. 5R by the Working Group on August 13, 2023.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): None.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommend that the Working Group move this item to the active listing and expose this agenda item with proposed revisions to include issue papers within Level 5 of the statutory hierarchy. Other corresponding revisions to update references are also proposed as applicable. Upon adoption of this agenda item issue papers will not be updated but will include the following note: "On (month/year), Issue Papers were included in Level 5 of the Statutory Hierarchy."

Statutory Accounting Principles Preamble

V. Statutory Hierarchy

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

Level 1

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

Level 2

Consensus positions of the Emerging Accounting Issues (E) Working Group as adopted by the NAIC (INTs adopted before 2016)

Interpretations of existing SSAPs as adopted by the Statutory Accounting Principles (E) Working Group (INTs adopted in 2016 or beyond)

Level 3

NAIC Annual Statement Instructions

Purposes and Procedures Manual of the NAIC Investment Analysis Office

Level 4

Statutory Accounting Principles Preamble and Statement of Concepts[4]

Level 5

Statutory Accounting Issue Papers[FN]

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

New FN: With inclusion of Level 5, issue papers shall only be used and applied as authoritative guidance if they do not conflict with other sources of statutory guidance.

43. If the accounting treatment of a transaction or event is not specified by the SSAPs, preparers, regulators and auditors of statutory financial statements should consider whether the accounting treatment is specified by another source of established statutory accounting principles. If an established statutory accounting principle from one or more sources in Level 2 or 3 is relevant to the circumstances, the preparer, regulator or auditor

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

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

should apply such principle. If there is a conflict between statutory accounting principles from one or more sources in Level 2 or 3, the preparer, regulator or auditor should follow the treatment specified by the source in the higher level—that is, follow Level 2 treatment over Level 3. Revisions to guidance in accordance with additions or revisions to the NAIC statutory hierarchy should be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

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

Appendix E – Issue Papers

Introduction

Issue papers are often used ~~as the first step~~ in developing new or revised SSAPs and in documenting the discussions and issues leading to the adoption of new statutory accounting concepts. ~~, and each contains a recommended conclusion, discussion and relevant literature section. While issue papers do not constitute an authoritative level of statutory accounting guidance~~Issue papers are captured in Level 5 ~~as defined by~~of the statutory hierarchy and, as they are not typically updated after adoption, shall only be used and applied if they do not conflict with other sources of statutory guidance. SSAP clarifications, especially those non-contested, many times will not have a corresponding update to a related issue paper. Issue papers~~, they~~ are an important part of the *Accounting Practices and Procedures Manual* (Manual) because they reference the history and discussion of ~~the related~~ SSAP.

Issue papers are published in the Manual within Appendix E the first year after adoption of the related SSAP, but are then removed from the subsequent year's Manual and posted for public reference on the Statutory Accounting Principles (E) Working Group (SAPWG) web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

How to Use This Manual:

Appendix E – Issue Papers:

Appendix E includes issue papers associated with SSAPs adopted through year end prior to publication of the Manual. Issue papers are often used ~~as the first step~~ in developing new or revised SSAPs and in documenting the discussions and issues leading to the adoption of new statutory accounting concepts.~~contain a recommended conclusion, discussion and relevant literature section~~. Issue papers are captured in Level 5 of the statutory hierarchy~~,~~ and, as they are not typically updated after adoption, shall only be used and applied if they do not conflict with other sources of statutory guidance. SSAP clarifications, especially those non-contested, many times will not have a corresponding update to a related issue paper. ~~**DO NOT** constitute an authoritative level of statutory accounting, as supported by the statutory hierarchy, and should only be used as reference material. Nevertheless, i~~Issue papers are important because they reference the history and discussion of a related SSAP. The "Relevant Statutory Accounting and GAAP Guidance" section of the issue paper may contain~~s~~ excerpts of

accounting guidance considered, but not necessarily adopted, by the Statutory Accounting Principles (E) Working Group (SAPWG) when forming the conclusions reached in the resultant SSAP. Historical issue papers associated with SSAPs adopted prior to the current year are posted for public reference on the SAPWG web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

NAIC Policy Statement on Maintenance of Statutory Accounting Principles

Development of New SSAPs or New SAP Concepts[5] in an Existing SSAP

4. New SSAPs will be developed to address, but will not be limited to: 1) concepts not previously addressed by a SSAP and that do not fit within the scope of an existing SSAP; 2) concepts that fit within the scope of an existing SSAP, but the Working Group elects to supersede existing SSAPs and 3) existing concepts that warrant significant revisions. New SAP concepts to existing SSAPs will be developed to address, but will not be limited to: 1) concepts that fit within the accounting topic of an existing SSAP, but have not been addressed by the Working Group; 2) changes to the valuation and/or measurement of an existing SSAP; and 3) modifications to the overall application of existing SSAPs. The decision to undertake development of a new SSAP or a new SAP concept in an existing SSAP will rest with the Working Group. New SSAPs or a new SAP concept in an existing SSAP will have a specified effective date.

5. Research and drafting of a new SSAP or a new SAP concept in an existing SSAP will be performed by NAIC staff under the direction and supervision of the Working Group which may enlist the assistance of interested parties and/or consultants with requisite technical expertise as needed or desired. Issue papers are often used ~~The first step~~ in the process to develop ~~developing~~ new SSAPs and new SAP concepts in existing SSAPs ~~will commonly be the drafting of an issue paper, which will contain a summary of the issue, a summary conclusion, discussion, and a relevant literature section~~and to document the discussions and issues leading to the adoption of new statutory accounting concepts. Public comments will be solicited on an issue paper (at least one exposure period), and at least one public hearing will be held before the issue paper ~~is converted to a SSAP~~is adopted. Upon approval by the Working Group, all proposed SSAPs will be exposed for public comment for a period commensurate with the length of the draft and the complexities of the issue(s). After a hearing of comments, adoption of new SSAPs or new SAP concepts in existing SSAPs (including any amendments from exposure) may be made by simple majority. If no comments are received during the public comment period, the Working Group may adopt the proposal collectively (one motion/vote) with other non-contested positions after the opportunity is given during the hearing to separately discuss the proposal. All new SSAPs and new SAP concepts in existing SSAPs must be on the agenda for at least one public hearing before presentation to the Task Force for consideration. Adoption by the Task Force, its parent and the NAIC membership shall be governed by the NAIC bylaws.

Staff Review Completed by: Julie Gann, NAIC Staff—November 2024

Status:
On December 17, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing as a SAP clarification and exposed revisions, as shown above, to classify issue papers in Level 5 of the statutory hierarchy.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/09 - 24-27 - Issue Paper Stat Hierarchy.docx

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[5] Prior to December 11, 2021, the term used to describe a new SAP concept was "substantive" and the term used to describe a SAP clarification was "nonsubstantive." The new terms will be reflected in materials to describe revisions to statutory accounting principles on a prospective basis and historical documents will not be updated to reflect the revised terms.

Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Holders of Capital Notes

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been prepared in response to the direction of the Working Group during the 2024 Fall National Meeting with the adoption of *INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers*. With the adoption of the INT, and the guidance for reporting certain debt securities as capital notes in scope of *SSAP No. 41—Surplus Notes*, industry identified that slight revisions may be necessary to reflect the capital note distinctions. The Working Group directed NAIC staff to work with industry in this review and identifying necessary changes.

From the initial review and working with industry, revisions have been proposed to address the following specifically for capital notes:

1. Incorporate a definition/reference to the INT for capital notes.
2. Clarify the admittance restrictions.
3. Clarify the guidance for NAIC designations.
4. Update the impairment guidance to refer to capital notes.

In addition to these items, it was identified that an existing disclosure for surplus notes, which requires disclosure of any holder of 10% or more of an SEC-registered surplus note, is likely an extensive administrative burden, may be difficult to complete, and as a narrative disclosure only (not data-captured), is likely not often utilized. From a review of the disclosure, it predates the issuance of *SSAP No. 41—Surplus Notes*, and there are questions as to how a disclosure of certain holders of SEC-registered notes would be purposeful or used. NAIC staff has proposed to eliminate this aspect of the disclosure but retain the disclosure focusing on surplus notes with affiliates. NAIC staff requests feedback on whether this disclosure should be retained.

Existing Authoritative Literature:

- ***SSAP No. 41—Surplus Notes***

1. This statement establishes statutory accounting principles for issuers and holders of surplus notes, and for holders of capital notes. Statutory accounting principles for issuers of capital notes are provided in *SSAP No. 15—Debt and Holding Company Obligations*.

(Paragraphs 2-8 Is limited to "Issuers of Surplus Notes" so is not included.)

Holders of Capital or Surplus Notes

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

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equity instruments in the issuer held directly or indirectly by the holder of the capital or surplus note.

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. Subsequent to this nonadmittance, if any of the conditions described ceased to exist, the holder may admit the surplus note at the value determined under paragraph 11. If a surplus note was nonadmitted pursuant to this paragraph, and the 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.

10. Capital or surplus notes shall be valued in accordance with paragraph 11. Pursuant to that paragraph, the value is determined by NAIC credit rating provider (CRP) ratings. Part One – Capital and Surplus Debentures of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* provides guidance in determining the NAIC designation for these investments.

11. If the capital or surplus note has been rated by an NAIC CRP and has a designation equivalent of NAIC 1 or NAIC 2, then it shall be reported at amortized cost. If the capital or surplus note is not CRP rated or has an NAIC designation equivalent of NAIC 3 through 6, then the balance sheet amount shall be reported at the lesser of amortized cost or fair value, with fluctuations in value reflected as unrealized valuation changes.

12. For reporting entities required to maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

13. For surplus notes issued and held (directly or indirectly) between insurance reporting entities and subsidiary, controlled and affiliated entities, the guidance in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* requires adjustment to prevent double-counting of surplus notes. For example, an insurance reporting entity is not permitted to report the issuance of a surplus note as an increase in surplus and have an asset representing an investment in the SCA that includes the issued surplus note (held by an SCA). Pursuant to SSAP No. 97, the "investment in the SCA" shall be adjusted to eliminate the surplus note issued by the direct or indirect parent insurance reporting entity. This treatment shall also apply for instances in which the SCA acquires any portion of outstanding surplus notes issued by the direct or indirect parent through any means (e.g., directly acquired from the parent, acquired through a third-party broker, or via the market).

Income

14. Only interest that has been approved by the issuer's domiciliary commissioner shall be accrued as income by a holder of surplus notes. Interest income for any period consists of interest collected during the period and the change in the due and accrued interest between the beginning and end of the period approved by the issuer's domiciliary commissioner.

15. Except for the specific limitations on recognizing interest income in paragraph 14, investment income, and the recognition of uncollectible accrued interest, shall follow the guidance in *SSAP No. 34—Investment Income Due and Accrued.*

Impairment

16. An other-than-temporary impairment[(INT 06-07)] shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of the surplus note. Pursuant to the terms of a surplus note, payments of principal and interest may be delayed if the issuer's domiciliary commissioner does not approve payment. Extended delays of either principal or interest shall trigger an evaluation for an other-than-temporary impairment. An other-than-temporary impairment shall be recognized in situations when the reporting entity has made a decision to sell a surplus note prior to its maturity at an amount below its carrying value. If it is determined that a decline in fair value is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the difference between the surplus note's

carrying value and the fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of impairment shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR, realized losses shall be accounted for in accordance with SSAP No. 7.

17. In periods subsequent to the recognition of an other-than-temporary impairment loss for a surplus note, the holder of the surplus note shall account for the other-than-temporarily impaired surplus note as if the surplus note had been purchased on the measurement date of the other-than-temporary impairment. The fair value of the surplus note on the measurement date shall become the new cost basis of the surplus note and the new cost basis shall not be adjusted for subsequent recoveries in fair value. The discount or reduced premium recorded for the surplus note, based on the new cost basis, shall be amortized over the remaining life of the surplus note in the prospective manner based on the amount and timing of future estimated cash flows. The surplus note shall continue to be subject to impairment analysis for each subsequent reporting period. Future declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses.

Disclosures

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*;

d. Original issue amount of note;

e. Carrying value of note;

f. The rate at which interest accrues;

g. Maturity dates or repayment schedules, if stated;

h. Unapproved interest and/or principal;

i. Life-to-date and current year approved interest and principal recognized;

  i. Percentage interest payments offset through 'administrative offsetting' (not inclusive of amounts paid to a third-party liquidity provider). For example, if $100 in interest was recognized through the year, $10 of which was remitted to a third-party liquidity provider and the reminder $90 was offset, the reporting entity shall report 100% as offset.

j. Disclosure of whether the surplus note was issued as part of a transaction with any of the following attributes:

  i. Do surplus note/associated asset terms negate or reduce cash flow exchanges, and/or are amounts payable under surplus note and amounts receivable under other agreements contractually linked? (For example, the asset provides interest payments only when the surplus note provides interest payments.)

  ii. Are any amounts due under surplus notes and associated assets netted or offset (partially or in full) thus eliminating or reducing the exchange of cash or assets that would normally occur throughout the duration, or at maturity, of the agreement? (This may be referred to as administrative offsetting.)

iii. Were the proceeds from the issuance of a surplus note used to purchase an asset directly or indirectly from the holder of the surplus note?

k. Principle amount and fair value of assets received upon surplus note issuance, if applicable;

l. Subordination terms;

m. Liquidation preference to the reporting entity's common and preferred shareholders;

n. The repayment conditions and restrictions;

o. Information about any guarantees, support agreements or related party transactions associated with the surplus note issuance, and whether payments have been made under such agreements.

19. If a reporting entity has ceded business to a surplus note issuer that is a related party as part of a reinsurance transaction in which the surplus note meets any of the criteria in paragraph 18.j., the ceding entity shall provide a description of the transaction, including whether the criteria in paragraph 18.j. were met with respect to the surplus note issuance, as long as the reinsurance agreement remains in force. The ceding entity should provide a description of the risks reinsured, the related party reinsurer, any guarantees or support agreements, and the amount of notes outstanding.

20. If the proceeds from the issuance of a surplus note used to purchase an asset directly or indirectly from the holder of the surplus note, the following information shall be disclosed regarding the assets received:

a. Identification of asset, including the investment schedule where the asset is reported and reported NAIC designation.

b. Book/adjusted carrying value of asset as of the current reporting date.

c. A description of terms under which liquidity would be provided should a triggering event occur.

21. In addition to the above, a reporting entity shall identify all 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.

INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers

10. Q – How should hybrid securities be accounted and reported? [SSAP No. 26, paragraph 13]

10.1 A – SSAP No. 26 prior to the principles-based bond definition explicitly scoped in a class of assets referred to as "hybrid securities" which are defined as "securities whose proceeds are accorded some degree of equity treatment by one or more of the nationally recognized statistical rating organizations (NRSRO) and/or which are recognized as regulatory capital by the issuer's primary regulatory authority. Hybrid securities are designed with characteristics of debt and equity and are intended to provide protection to the issuer's senior note holders. Hybrid securities are sometimes referred to as capital securities." During the development of the principles-based bond definition, it was decided to remove the explicit scope-in and instead rely on the new principles to determine whether bond classification is appropriate. As these securities come in several forms, additional clarity on where to report such securities is warranted.

10.2 Equity Securities: Investments that represent shares, units, or an ownership interest in a company or other entity but do not reflect common stock that were previously considered hybrids under SSAP No. 26 are equity investments and shall be captured as preferred stock in scope of *SSAP No. 32—Preferred Stock*. Investments in debt securities are not permitted to be reported in scope of *SSAP No. 30—Unaffiliated Common Stock* or SSAP No. 32.

10.3 Debt Securities: Investments in debt securities previously considered hybrids under SSAP No. 26

(including those debt securities with cumulative interest features) **that qualify** under the principles-based bond definition shall be reported as bonds on Schedule D. An example may include certain debt securities which NRSROs allow to be treated as equity but for which all the principles-based bond definition requirements are present. To be clear, a set maturity date for a debt security is not a requirement for bond classification if the bond otherwise qualifies under the definition. (Perpetual bonds that qualify under the bond definition are permitted as bonds.)

10.4 Investments in debt securities treated as regulatory capital by the issuer's primary regulatory authority, and **that do not qualify** under the principles-based bond definition solely because interest can be cancelled in the event of financial stress in a non-resolution scenario without triggering an act of default are capital notes and shall be captured in *SSAP No. 41—Surplus Notes*. These capital notes are often issued by domestic or foreign banks, and the domestic or foreign bank regulator or the Issuer has the ability to cancel interest or dividends, without future interest accumulation or payment.

10.5 Debt securities other than capital notes (as defined in 10.4 above) that permit the issuing entity to cancel interest without future interest accumulation or payment and without triggering an act of default, or that incorporate other equity components that do not permit bond classification under the principles-based bond definition are non-bond debt securities and shall be captured in scope of *SSAP No. 21—Other Admitted Assets*.

10.6 Debt securities issued by regulated institutions where only the issuer's primary regulator may have regulatory power to cancel or convert to equity all or a portion of the debt and/or its related interest payments, solely in a resolution scenario were not previously considered hybrid securities and should continue to be reported as Schedule D bonds, as Issuer Credit Obligations under SSAP No. 26, so long as all principles-based bond definition requirements are met.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):
On Nov. 17, 2024, the Statutory Accounting Principles (E) Working Group adopted *INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers.* This INT addresses hybrid securities, including debt securities that are treated as regulatory capital. With the adoption of this guidance, and the reference for capital notes to be in scope of SSAP No. 41, industry identified minor revisions are needed to SSAP No.41.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:
None

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:
NAIC staff recommend that the Working Group move this item to the active listing as a SAP clarification and expose revisions to *SSAP No. 41—Surplus Notes*, to incorporate needed changes to clarify certain aspects for capital notes. As part of the review, minor other clarification revisions were also incorporated.

As there are two separate reporting lines on Schedule BA for "Surplus Notes" and "Capital Notes" with very few items currently being reported in the "Capital Note" category, this agenda item recommends annual statement instruction revisions to clarify that qualifying insurer-issued notes held by another insurance reporting entity be reported as "Surplus Notes" on Schedule BA. There is also proposed clarification on what should be included as "Capital Notes."

<u>Proposed revisions to SSAP No. 41:</u>

1. This statement establishes statutory accounting principles for issuers and holders of surplus notes, and for holders of capital notes[FN]. Statutory accounting principles for issuers of capital notes are provided in *SSAP No. 15—Debt and Holding Company Obligations*.

New Footnote: *INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers* identifies that debt securities treated as regulatory capital by the issuer's primary regulatory authority and that do not qualify under the principles-based bond definition solely because interest can be cancelled in the event of financial stress in a non-resolution scenario without triggering an event of default are capital notes in scope of this statement. For consistency in investment reporting for held securities, only insurer-issued notes that qualify under paragraph 3 shall be reported as surplus notes. As detailed within, surplus notes are subject to additional restrictions not applicable capital notes.

Holders of Capital or Surplus Notes

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. 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.

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.

10. Capital or surplus notes shall be valued in accordance with paragraph 11. Pursuant to that paragraph, the value is determined by NAIC ~~credit rating provider (CRP) ratings~~designations. ~~Part One – Capital and Surplus Debentures of t~~The *Purposes and Procedures Manual of the NAIC Investment Analysis Office* provides guidance in determining the NAIC designation for these investments.

11. If the capital or surplus note has been rated by an NAIC CRP and has a designation equivalent of NAIC 1 or NAIC 2, then it shall be reported at amortized cost. If the capital or surplus note ~~is not CRP rated~~does not have an NAIC designation or has an NAIC designation ~~equivalent~~ of NAIC 3 through 6, then the balance sheet amount shall be reported at the lesser of amortized cost or fair value, with fluctuations in value reflected as unrealized valuation changes.

12. For reporting entities required to maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

13. For surplus notes issued and held (directly or indirectly) between insurance reporting entities and subsidiary, controlled and affiliated entities, the guidance in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* requires adjustment to prevent double-counting of surplus notes. For example, an insurance reporting entity is not permitted to report the issuance of a surplus note as an increase in surplus

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and have an asset representing an investment in the SCA that includes the issued surplus note (held by an SCA). Pursuant to SSAP No. 97, the "investment in the SCA" shall be adjusted to eliminate the surplus note issued by the direct or indirect parent insurance reporting entity. This treatment shall also apply for instances in which the SCA acquires any portion of outstanding surplus notes issued by the direct or indirect parent through any means (e.g., directly acquired from the parent, acquired through a third-party broker, or via the market).

Income

14. Only interest that has been approved by the issuer's domiciliary commissioner shall be accrued as income by a holder of surplus notes. Interest income for any period consists of interest collected during the period and the change in the due and accrued interest between the beginning and end of the period approved by the issuer's domiciliary commissioner.

15. Except for the specific limitations on recognizing interest income in paragraph 14, investment income, and the recognition of uncollectible accrued interest, shall follow the guidance in *SSAP No. 34—Investment Income Due and Accrued.*

Impairment

16. An other-than-temporary impairment(INT 06-07) shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of the surplus or capital note. Pursuant to the terms ~~of a surplus note~~, payments of principal and interest may be delayed if the issuer's domiciliary commissioner or other regulatory authority does not approve payment. Extended delays of either principal or interest shall trigger an evaluation for an other-than-temporary impairment. An other-than-temporary impairment shall be recognized in situations when the reporting entity has made a decision to sell a surplus note prior to its maturity at an amount below its carrying value. If it is determined that a decline in fair value is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the difference between the surplus note's carrying value and the fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of impairment shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR, realized losses shall be accounted for in accordance with SSAP No. 7.

17. In periods subsequent to the recognition of an other-than-temporary impairment loss for a surplus or capital note, the holder of the surplus note shall account for the other-than-temporarily impaired surplus or capital note as if the ~~surplus~~ note had been purchased on the measurement date of the other-than-temporary impairment. The fair value of the ~~surplus~~ note on the measurement date shall become the new cost basis ~~of the surplus note~~ and the new cost basis shall not be adjusted for subsequent recoveries in fair value. The discount or reduced premium recorded for the surplus or capital note, based on the new cost basis, shall be amortized over the remaining life of the ~~surplus~~ note in the prospective manner based on the amount and timing of future estimated cash flows. The ~~surplus~~ note shall continue to be subject to impairment analysis for each subsequent reporting period. Future declines in fair value which are determined to be other-than-temporary shall be recorded as realized losses.

Disclosures

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*;

d. Original issue amount of note;

e. Carrying value of note;

f. The rate at which interest accrues;

g. Maturity dates or repayment schedules, if stated;

h. Unapproved interest and/or principal;

i. Life-to-date and current year approved interest and principal recognized;

i. Percentage interest payments offset through 'administrative offsetting' (not inclusive of amounts paid to a third-party liquidity provider). For example, if $100 in interest was recognized through the year, $10 of which was remitted to a third-party liquidity provider and the remainder $90 was offset, the reporting entity shall report 100% as offset.

j. Disclosure of whether the surplus note was issued as part of a transaction with any of the following attributes:

i. Do surplus note/associated asset terms negate or reduce cash flow exchanges, and/or are amounts payable under surplus note and amounts receivable under other agreements contractually linked? (For example, the asset provides interest payments only when the surplus note provides interest payments.)

ii. Are any amounts due under surplus notes and associated assets netted or offset (partially or in full) thus eliminating or reducing the exchange of cash or assets that would normally occur throughout the duration, or at maturity, of the agreement? (This may be referred to as administrative offsetting.)

iii. Were the proceeds from the issuance of a surplus note used to purchase an asset directly or indirectly from the holder of the surplus note?

k. Principle amount and fair value of assets received upon surplus note issuance, if applicable;

l. Subordination terms;

m. Liquidation preference to the reporting entity's common and preferred shareholders;

n. The repayment conditions and restrictions;

o. Information about any guarantees, support agreements or related party transactions associated with the surplus note issuance, and whether payments have been made under such agreements.

19. If a reporting entity has ceded business to a surplus note issuer that is a related party as part of a reinsurance transaction in which the surplus note meets any of the criteria in paragraph 18.j., the ceding entity shall provide a description of the transaction, including whether the criteria in paragraph 18.j. were met with respect to the surplus note issuance, as long as the reinsurance agreement remains in force. The ceding entity should provide a description of the risks reinsured, the related party reinsurer, any guarantees or support agreements, and the amount of notes outstanding.

20. If the proceeds from the issuance of a surplus note used to purchase an asset directly or indirectly from the holder of the surplus note, the following information shall be disclosed regarding the assets received:

a. Identification of asset, including the investment schedule where the asset is reported and reported NAIC designation.

b. Book/adjusted carrying value of asset as of the current reporting date.

c. A description of terms under which liquidity would be provided should a triggering event occur.

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21. In addition to the above, aA reporting entity shall identify all 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.

Proposed Revisions to Annual Statement Instructions – Schedule BA

Surplus Debentures:

Include: That portion of any subordinated indebtedness, surplus debenture, surplus note, debenture note, premium income note, or other contingent evidence of indebtedness, that qualifies as a surplus note pursuant to *SSAP No. 41—Surplus Notes*, that is reported in the surplus of the issuer.

Capital Notes:

Include: This reporting line shall be utilized for held debt securities, that do not qualify as issued surplus notes pursuant to *SSAP No. 41—Surplus Notes,* that are treated as regulatory capital by the issuer's primary regulatory authority and that do not qualify under the principles-based bond definition solely because interest can be cancelled in the event of financial stress in a non-resolution scenario without triggering an event of default. The portion of any capital note that is reported on the line for capital notes of the issuance insurance reporting entity.

Staff Review Completed by: Julie Gann, NAIC Staff—December 2024

Status:
On December 17, 2024, the Statutory Accounting Principles (E) Working Group moved this item to the active listing as a SAP clarification and exposed revisions, as shown above, 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 above.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/02-25-25/Hearing/10 - 24-28 - SSAP No. 41 - Capital Notes.docx

Statutory Accounting Principles (E) Working Group
February 25, 2025
Comment Letters Received

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Interested Parties – January 31, 2025 ○ Ref #2024-10: SSAP No. 56 – Book Value Separate Accounts ○ Ref #2024-16: Repacks and Derivative Investments ○ Ref #2024-22: ASU 2024-01, Scope Application of Profits Interest and Similar Awards ○ Ref #2024-23: Derivative Premium Clarifications ○ Ref #2024-24: Medicare Part D – Medicare Prescription Payment Programs ○ Ref #2024-25: SSAP No. 16 Clarifications ○ Ref #2024-27: Issue Papers in the Statutory Hierarchy ○ Ref #2024-28: Holders of Capital Notes *(Note: Not all items in this letter are planned for discussion on Feb. 25, 2025.)*	16-28
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December 16, 2024

Updated January 30, 2025: See Ref #2022-14 and Repurchase Agreements beginning on page 9 (both indicated by ***)

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
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RE: Interested Parties Comments on the Items Exposed for Comment by the Statutory Accounting Principles Working Group with Comments due December 16th

Dear Mr. Bruggeman:

Interested parties appreciate the opportunity to comment on the following items that were exposed for comment by the Statutory Accounting Working Group (the Working Group) with comments due December 16 th.

Ref #2022-14: ***New Market Tax Credits****

On May 16, 2023, the Working Group exposed revisions to SSAP No. 93 – *Investments in Tax Credit Structures,* and 94R – *State and Federal Tax Credit*. The revisions to SSAP No. 93 propose adoption with modification of ASU 2023-02 and expansion of the SSAP scope to include all tax credit programs and tax investment structures. The revisions to SSAP No. 94R expand the scope of the SSAP to include all state and federal tax credits whether purchased or allocated, and that tax received should be recorded at face value with losses realized immediately and gains deferred.

Interested parties have no comments on this item.

Ref #2023-24: Current Expected Credit Losses (CECL)

The Working Group exposed for comment an Issue Paper to document for the historical record the Generally Accepted Accounting Principles impairment guidance which existed prior to the implementation of *Accounting Standards Update (ASU) 2016-13, Financial Instruments—Credit Losses* (CECL). In January 2024, the Working Group rejected CECL for statutory accounting purposes and directed NAIC staff to prepare this issue paper. Since many SSAPs adopted pre-CECL impairment guidance, the Working Group wanted to ensure that any guidance which was superseded by CECL was readily available for future use.

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.

Ref #2024-04: Conforming Repurchase Agreements Assets

On August 13, 2024, the Working Group exposed this agenda item along with a memo detailing accounting and reporting guidance for repurchase agreements and securities lending transactions.

Interested parties have repeated the memo below and provided comments in italics following each section.

Overview: Fundamentally, securities lending and repurchase/reverse repurchase (Repo) transactions perform similar functions and are entered into for short-term collateralized funding/lending. Although some articles identify that the type of collateral exchanged (security or cash) is a key difference, from discussions with industry cash or securities can be used as collateral under either a security lending or repo agreement. Industry has identified that the counterparty is a key difference between the transactions.

Although similar in function, the accounting and reporting for securities lending and repurchase transactions are different under statutory accounting even when both are accounted for under the "secured borrowing" approach. (All scenarios below focus on secured borrowing accounting, and not as a "sale," as that is the more prevalent accounting approach.)

This memo intends to document the current accounting guidance and identify how NAIC staff believe accounting and reporting should be reflected. The Working Group is requesting comments on this memo, particularly within the established notes. Subsequently, NAIC staff plan to propose statutory accounting and reporting changes to reflect a consistent approach between securities lending and repurchase transactions.

The guidance for securities lending / borrowings and repo agreements are *in SAP No. 103—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. Although other aspects of the SSAP are applicable, focused guidance for these transactions are in the following paragraphs:

- Securities Lending: Paragraphs 85-92.
- Securities Borrowing: Paragraphs 93-95

- Repurchase Agreements: Paragraphs 102-104 & 113
- Reverse Repurchase Agreements: Paragraphs 111-113

Broad concepts for secured borrowing are in paragraph 19. The concepts for securities lending differ from this guidance with the requirement to recognize items on balance sheet with the ability to sell/repledge collateral. Disclosure guidelines for these transactions are in paragraph 28.
The "conforming" securities lending guidelines are captured in the RBC instructions. The full detail of the requirements is included as an appendix to this memo, but collateral requirements include:

- Cash and cash equivalents
- Direct obligations of, or securities that are fully guaranteed as to principal and interest by, the government of the United States, or any agency of the United States, or by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation.
- NAIC 1 Designated Securities
- Affiliated-issued collateral is not deemed acceptable.
- In all cases, collateral held must be permitted investments in the state of domicile for the respective insurer.

Securities Lending – Reporting Entity Lends a Security and Receives Collateral in Exchange:
A security lending transaction involves the temporary transfer of securities from one party (security lender) to another party (security borrower) and with the lender receiving collateral from the borrower to protect against the risk of loss. The lender receives a fee for the use of the security. Under statutory accounting guidance, the accounting for security lending depends on whether the reporting entity has the ability to pledge or sell the collateral received.

1. Lending Entity Cannot Sell / Repledge Security Collateral Received:

a) Reporting entity lends a security under a secured borrowing agreement. The reporting entity retains the lent security on books and codes it as a restricted asset.

b) Reporting entity lender does not recognize security collateral received as an asset and does not recognize an obligation to return the collateral.

c) If the fair value of the collateral received drops below 100% of the fair value of the loaned security, then the reporting entity (lender) is to nonadmit a portion of loaned security (which is still reported on the books). The amount nonadmitted should be the difference between the collateral and the security reported on the books. (This calculation is done at any point in time – so for a lent $100 bond, if the fair value of the bond declines to $90, then the collateral comparison would be done to the current FV of the bond, and not the FV at the time the security was lent. So, if collateral was received at $102, and declined to $90 (matching the bond), nonadmittance would not be required.) The comparison is also completed in aggregate by counterparty, so if the collateral for one security was to appreciate in value, and the collateral for another was to decline, as long as the combined collateral value continued to represent 100% of the fair value of the loaned securities, additional collateral would not be required.

The Restricted Asset / RBC Impact is as follows:

d) The retained asset lent to the counterparty should be identified as a restricted asset. This loaned asset shall be captured on general interrogatory (GI) line 25.04 or GI line 25.05 based on whether the security lending arrangement is considered to be a 'conforming' security lending program. Amounts reported on these lines flow to LR017 (Off-Balance Sheet and Other Items), lines 1 and 2. Items captured in GI line 25.04 (conforming) receive a 0.0020 RBC charge. Items captured in GI line 25.05 (nonconforming) receive a 0.0126 RBC charge. There is no current disclosure on the type of collateral received for these off-balance sheet programs. As such, regulators cannot verify from the financial statements whether the program complies with the "conforming" program requirements. However, as the collateral cannot be sold/repledged, if the collateral complies with the conforming requirements, there would be no change to that assessment over the duration of the transaction. ***(Note 1)***

e) As the collateral asset is not recognized on book of the lender, there is no RBC asset (C-1) charge. As the collateral asset is not recognized, there is no restricted asset reporting or RBC restricted asset charge. The restricted asset charge is placed on the asset that is lent but still retained on the books as discussed above in paragraph 1d. ***(Note 2)***

Note 1: Should the type of collateral received in these programs be captured in a financial statement disclosure to allow for regulator verification of the "conforming" program guidelines? Additionally, it has been noted that the admittance calculation focuses solely on the fair value comparison of the collateral received to the security lent. However, there is no current guidance that assesses admittance based on the quality/type of collateral received. Under the current guidance, residuals or low-quality assets could be received and there is no documentation of this type of collateral for certain sec lending and repo programs. Even if these programs would not qualify as conforming, there is a question on whether admittance restrictions should exist based on the collateral received from the counterparty.

Interested parties' response: Given the deferral of the conforming repo proposal, only conforming sec lending programs will be subject to the conforming guidelines. In these programs, the insurer attests to the conforming criteria. One possible additional disclosure could be footnote like footnote 5.E.8 for repo, whereby the collateral received is specified by asset type.

In typical security lending programs, the insurer receives cash in these transactions, but the master agreement between the counterparties also allows the insurer to receive high-quality collateral – restrictively defined as "acceptable collateral" - which must be marked to market regularly for ongoing margining purposes. Regardless of whether the program is conforming or not, the combination of daily margining and the restrictive definition of "acceptable collateral" should provide NAIC with sufficient comfort that additional admittance restrictions on collateral received would be duplicative.

Note 2: NAIC staff believes there is inconsistent application of the current guidance as there is a disconnect in language between RBC and the Blanks on whether the collateral received or the lent asset is identified as a restricted asset. The blanks instructions in GI 25.04 and GI 25.05 identify the

"Amount of Collateral." The lines in RBC identify "Loaned to Others." This inconsistency in terminology likely causes confusion on whether the amount reported should be the lent security or the collateral received in exchange. NAIC staff suggest clarifying terminology for consistency purposes, clarifying that the loaned asset retained on book should be the amount reported as restricted that flows through all schedules.

Interested parties' response: *We agree that consistent terminology should be established between Blanks and RBC to clarify that the loaned security is identified as a restricted asset. We suggest that Blanks references to "Amount of Collateral" in GI 25.04 and GI 25.05 should be changed to "Loaned to Others," consistent with RBC.*

2. Lending Entity Can Sell / Repledge Collateral Received – (Also Applies to Cash Collateral)

a) Reporting entity lends a security under a secured borrowing agreement. The reporting entity retains the lent security on books and codes it as a restricted asset.

b) Reporting entity lender recognizes collateral received from the counterparty on its book and recognizes a liability to return the collateral. (This collateral is reported on Schedule DL.) If security collateral is captured directly on the investment schedules, the collateral is **not** coded as a restricted asset. *(See paragraph 2f.)*

c) If the fair value of the collateral received drops below 100% of the fair value of the loaned security, then the reporting entity is to nonadmit a portion of loaned security (which is still reported on the books). The amount nonadmitted should be the difference between the collateral and the security reported on the books. (This calculation is done at any point in time – so for a lent $100 bond, if the fair value of the bond declines to $90, then the collateral comparison would be done to the current FV of the bond, and not the FV at the time the security was lent. So, if collateral was received at $102, and declined to $90 (matching the bond), nonadmittance would not be required.) The comparison is also completed in aggregate by counterparty, so if the collateral for one security was to appreciate in value, and the collateral for another was to decline, as long as the combined collateral value continued to represent 100% of the fair value of the loaned securities, additional collateral would not be required. ***(Note 3 & Note 4)***

The Restricted Asset / RBC Impact is as follows:

d) The retained asset lent to the counterparty should be identified as a restricted asset. This loaned asset shall be captured on GI line 25.04 or GI line 25.05 based on whether the security lending agreement is considered to be a 'conforming' security lending program. Amounts reported on these lines flow to LR017 (Off-Balance Sheet and Other Items), lines 1 and 2. Items captured in GI line 25.04 (conforming) receive a 0.0020 RBC charge. Items captured in GI line 25.05 (nonconforming) receive a 0.0126 RBC charge. ***(Note 5)***

e) The current collateral recognized on the balance sheet is subject to the corresponding asset (C-1) RBC charge. (This occurs directly from the investment schedule, or indirectly from

Schedule DL if the program is administered by a third-party administrator.) The RBC charge depends on the form of the collateral. (This recognition occurs regardless of whether the original collateral is reinvested.)

f) The collateral reported on book as it can be sold/repledged, is not coded as a restricted asset as there is an offsetting liability recognized for the obligation to return the collateral. Identifying both the lent security and the on-book collateral as restricted assets, particularly with the offsetting liability to return the collateral would result in a double-counting of restricted asset charges for the same transaction.

g) On day 1, both the collateral asset received and liability to return are recognized at fair value. Subsequently, the asset is measured pursuant to the applicable SSAP and the liability to return shall be adjusted as needed to reflect the current fair value of the collateral originally received. If the collateral received is reinvested, the resulting asset shall be accounted for pursuant to the applicable SSAP. As the measurement method for the collateral asset on book may not reflect fair value, this may result in a disconnect between the collateral asset and liability to return reported, but the reporting entity's liability to return the collateral shall always reflect the full obligation (fair value) to return collateral originally received.

Note 3: As the collateral can be sold/repledged, there is a question on the application of the admittance provisions in paragraphs 91-92 of SSAP No. 103. That guidance is focused on the fair value of the original collateral received in comparison to the fair value of the security lent. Once the collateral has been reinvested, the reporting entity is responsible for the reinvestment risk and the counterparty is not responsible for fair value changes of the reinvested security. Although a position could be taken that the fair value of the collateral originally received should continue to be compared to the fair value of the lent security to determine if more collateral needs to be provided, with the current financial statement reporting, this information is not captured to allow assessments once the collateral has been reinvested allowing regulators to verify the admittance provisions.

Interested parties' response: *We do not believe that there is any ongoing need to compare the fair value of the original collateral received in comparison to the fair value of the security lent. One salient feature of securities lending and repurchase agreement transactions is that exchange of variation margin covers the differences that emerge over time between the original market value of the security lent and the original market value of the collateral received. The margining process maintains equality between the market value of the collateral received – plus or minus any variation margin – and the market value of the security lent. This market structure obviates the need for regulators to generate an admittance test on whether the fair value of original collateral received compares with the fair value of the security lent.*

Existing disclosures also provide regulators with sufficient visibility:

1. *Footnote 5.E.5 b: The reinvestment portfolio acquired with cash received consisted principally of high quality, liquid, publicly traded long term bonds, short term investments, cash equivalents, or held in cash. If the securities sold or the reinvestment portfolio become*

less liquid, the Company has the liquidity resources of most of its general account available to meet any potential cash demands when securities are returned to the Company.

2. *Footnote 5.E.5 provides a maturity schedule for the collateral received.*
3. *Schedule DL provides full transparency and look-through to the assets in the reinvestment portfolio.*

In summary, existing financial statements disclose the risk and maturity summary in the footnotes and provide a full schedule for reinvested assets. The fair value security lent and collateral received continue to be matched via the margining process.

Note 4: With regards to the admittance calculation, there is also a question on application when the original collateral still covers 100% of the BACV of the loaned security but does not meet the requirement for 100% of the loaned security's fair value. As an example, if the loaned security at amortized cost has a BACV of $90, but had a fair value of $100 when loaned, the guidance in paragraph 91 requires collateral of $102 at the onset of the transaction. If the original collateral was to decrease in fair value to $98, it would no longer comply with the guidance in paragraph 91 and nonadmittance of the loaned security for $2 is expected under the guidance ($100 - $98). However, as the loaned security is reported at BACV of $90, the collateral still covers the full reported value of the loaned security. If the counterparty was to default, the reporting entity would eliminate the loaned security ($90) and the liability to return the collateral ($98) from the books and retain the collateral asset as their own. This transaction would result in an $8 gain for the reporting entity. If the loaned security had been nonadmitted by $2 prior to the default due to the FV decline of the collateral, there would have been a surplus hit of $2 for the nonadmittance. Upon the counterparty default, in addition to the $8 gain, there would have then been a surplus bump of $2 with the elimination of the nonadmitted asset. *(It is noted that if the fair value for the collateral asset had been retained, the reporting entity would have had a greater gain, but they are still fully covered based on how the loaned asset is reported.)* NAIC staff requests confirmation of the admittance guidance and its application from regulators, particularly when the fair value of the collateral continues to cover the BACV of the loaned security.

Interested parties' response: *We agree with NAIC staff's recommendation that admittance calculations should be based on the fair value of the original collateral and loaned security, as opposed to book value. As discussed above, the margining provisions of these contracts ensures that market values, rather than book values, remain aligned over the term of each transaction.*

Note 5: As the collateral received can be sold/repledged, there is a question on the application of the "conforming security lending" collateral requirements. From a broad review of financial statements, collateral reported on Schedule DL was identified as outside of the conforming parameters, but the security lending program was identified as "conforming" with the lower RBC charge. NAIC staff recommend clarification on the application of the "conforming" requirements. Particularly, if the intent is to permit a lower RBC charge due to the liquidity / stability of certain types of collateral, then it may be appropriate to require the collateral to always comply with the "conforming" provisions regardless of if it has been reinvested by the reporting entity.

Interested parties' response: *We believe that the narrow definition of "acceptable collateral," which is intended to be applied **only** to the original collateral received against the lent security, has been misapplied to the reinvestment portfolio. Acceptable asset classes in the reinvestment portfolio are defined in the portfolio's Investment Guidelines, not by the "acceptable collateral" criteria. Applying the narrow definition of "acceptable collateral" to the reinvestment portfolio could disrupt the economic viability of these programs.*

3. Securities Borrowing – Entity Borrows a Security and Provides Collateral in Exchange

a) Reporting entity borrower retains security collateral provided to counterparty on book and codes it as a restricted asset. (If providing cash in exchange for the borrowed security, then the cash is derecognized with a receivable for the return.) ***(Note 6)***

b) Reporting entity borrower does not recognize the borrowed security on their books, unless the reporting entity sells the borrowed security or the counterparty defaults. If the reporting entity sells the borrowed security, the cash received or reinvested asset is recognized with an obligation (liability) to return the borrowed security. Pursuant to paragraph 94 of SSAP No. 103, assets equivalent to the fair value of the borrowed security shall be coded as a restricted asset. Specific guidance exists in SSAP No. 103 for when borrowed securities are used to settle a short-sale. (A counterparty default would always result with an unwinding of the transaction with each party reporting the asset they have in their possession as their resulting asset.) ***(Note 7 & 8)***

The Restricted Asset / RBC Impact is as follows:

c) The retained asset (provided as collateral to a counterparty) is still on the reporting entity's investment schedules and should continue to receive the RBC asset C-1 charge. It should also be coded as a restricted asset. Due to the reporting lines available, it could be coded as "collateral held under securities lending agreements" or as an "other" restricted asset and captured in GI 26.32. If captured as a collateral within a security lending agreement, would be captured on GI line 25.04 or GI line 25.05 based on whether it is from a 'conforming' security lending program. Amounts reported on these lines flow to LR017 (Off-Balance Sheet and Other Items), lines 1 and 2. Items captured in GI line 25.04 (conforming) receive a 0.0020 RBC charge. Items captured in GI line 25.05 (nonconforming) receive a 0.0126 RBC charge. If reported as an "other" restricted asset, it would be captured on GI 26.32 with a 0.0126 RBC charge.

d) There would be no RBC impact for the borrowed security unless it is sold. At that time, the reinvested asset would be recognized and subject to an RBC asset C-1 charge. This asset (or an equivalent of other assets) would be identified as restricted. This is likely "collateral held under security lending agreement" and reported based on conforming /nonconforming in GI line 25.04 (0.0020 factor) or 25.05 (0.0126 factor).

Note 6: A security borrowing transaction is the flipside of the security lending transaction, with the reporting entity operating on the opposite side as borrower instead of lender. With this dynamic, it is

presumed that the same restricted asset categories, and whether it is a conforming program, would be determinants in reporting the restricted asset and in the resulting RBC charge. NAIC staff requests confirmation of this assessment. (A security borrowing is the transaction, and it is accounted for as a "secured borrowing" – this terminology can be confusing when discussing the design.)

Interested parties' comments on Notes 6-8: *From the insurer's perspective, securities borrowing transactions have a very different structure than securities lending transactions. Insurers have not, and do not anticipate, requesting the establishment of "conforming securities borrowing" programs with changes to RBC.*

Note 7: The guidance for a security borrowing could result with restricted asset reporting for both the collateral provided (if not cash collateral) as well as for the reinvested borrowed securities that the reporting entity has sold. NAIC staff notes that this could be a double hit of restricted asset charges and recommends comments on paragraph 94 of SSAP No. 103 on the elimination of the restricted asset requirement for the assets received from the sale of the borrowed security. It is noted that the reporting entity would already have a liability recognized to return the borrowed security to the counterparty.

See interested parties' comments above.

Note 8: For security borrowing transactions, it is identified that both a receivable and payable from the counterparty could be recognized. A receivable - if cash was originally provided as collateral for the return of the cash - and a payable - if the reporting entity sold the borrowed security for the obligation to return the security. This dynamic could result in a netting of the transactions under SSAP No. 64. If netted, then the regulators would not be able to identify these aspects within the financial statements, but the provisions that permit netting under SSAP No. 64 (legal right to offset) may be present.

See interested parties' comments above.

Repurchase Agreements***

Repurchase agreements, by definition, are agreements in which a reporting entity sells a security and simultaneously agrees to repurchase the security or a substantially similar security at a stated date and price. Repurchase agreements are functionally similar to securities lending. These transactions are generally captured as "secured borrowings" due to the requirement to repurchase the security transferred but could qualify as "sale" transactions. As very few (if any) are captured as sales under statutory accounting, this assessment will only focus on those captured as "secured borrowings."

Reporting entities can operate on both sides of repurchase agreements. If the reporting entity is selling a security and receiving cash (cash taker), it is considered a repurchase agreement. If the reporting entity is buying a security and providing cash (cash provider) it is considered a reverse repurchase agreement. SSAP No. 103 is explicit that only short-term repo agreements (with a stated short-term maturity date of 365 days or less) are allowed as admitted assets. Long-term repo agreements (with maturity dates in excess of 365 days) are nonadmitted.

There is no current concept for a "conforming repurchase agreement" and incorporating this concept, allowing for a lower RBC charge, was the request of the ACLI to the Life RBC Working Group.

4. **Repurchase Agreement – Reporting Entity Sells Security and Receives Cash / Collateral**

a) Reporting entity (cash taker) retains sold security on book and codes it as a restricted asset. This would remain an asset of the reporting entity unless the reporting entity defaults under the terms of the secured borrowing agreement. If that occurs, the reporting entity would derecognize the asset and eliminate the obligation to return the cash collateral per subparagraph (b).

b) Reporting entity recognizes cash received and obligation to return cash. (If security collateral is received, it is off-balance sheet unless that collateral is sold by the reporting entity. If sold, the reporting entity recognizes the proceeds from the sale and the obligation to return the collateral to the repo counterparty.) This process for security collateral received under a repurchase agreement is different from securities lending. Under security lending, if collateral received can be sold or repledged, even if it is not sold or repledged, the collateral is reported on balance sheet with an obligation to return. The disclosure guidance for repurchase agreements varies significantly from securities lending transactions as Schedule DL does not apply to repurchase agreements. As such, for repurchase agreements, there is no detail that identifies collateral held when the collateral can be sold/repledged. ***(Note 9)***

c) For repurchase agreements the reporting entity should receive proceeds (collateral) with a fair value of at least 95% of the fair value of the sold security. So, if the security has a FV of $100, proceeds (collateral) of $95 is required. If the FV of the proceeds (collateral) is not sufficient, then nonadmittance of the "sold" security for the amount of the shortfall is required. So, if only 93% collateral was received, the security "sold" but still reporting on-book would only be admitted for $98 with nonadmittance of $2. ***(Note 10)***

The Restricted Asset / RBC Impact is as follows:

a) The retained asset (sold to the counterparty) is still on the investment schedule and should continue to receive the RBC asset (C-1) charge. It should also be coded as a restricted asset as "subject to repurchase agreements" and captured in GI 26.21. This would then be captured in LR017 on line 3, "subject to repurchase agreements" and would receive a 0.0126 RBC charge. Under SSAP No. 103, repo agreements must be short-term to be admitted. If the repo agreement extends beyond 365 days, then the asset sold (retained on the book) would be identified as a nonadmitted asset.

b) The cash proceeds (collateral) would be recorded as cash and flow through on Schedule E - Part 1 - Cash to LR012 with a .0039 RBC charge. If the cash is used to acquire

another security, then the acquired security would be reported on the investment schedules and flow through to RBC accordingly based on the investment.

Note 9: Due to the similarities in overall function between securities lending and repurchase agreements, NAIC staff supports consistent accounting, reporting and disclosures. NAIC staff recommends expanding Schedule DL to capture repurchase agreements, and a reassessment of the repurchase agreement disclosures to determine whether the level of detail should be retained.

Interested parties' response: Extending Schedule DL to repurchase agreements makes sense only for any future "conforming repo" programs that have segregated assets in the reinvestment portfolio. In certain cases, repo can be used for secured borrowing whereby the cash is used for alternative purposes and not explicitly reinvested. Since industry is no longer requesting the establishment of conforming repo programs, we believe that Schedule DL should not be extended to repo programs at this time.

Note 10: The same concept issues exist for the nonadmittance of reported securities under repo transactions than what exist under the securities lending transactions. Under current guidance, if the fair value of the sold security was to increase, more proceeds (collateral) is required or the sold security is subject to nonadmittance. If collateral was reinvested, the comparison would have to be based on the original collateral received and not the reinvested collateral. Also, there is the question on nonadmittance when the collateral received still covers the BACV of the sold security.

Interested parties' response (similar to Note 3): One salient feature of securities lending and repurchase agreement transactions is that exchange of variation margin covers the differences that emerge over time between the original market value of the security lent and the original market value of the collateral received. The margining process therefore aligns the ***market value*** of the collateral received – plus or minus any variation margin – with the ***market value*** of the security lent. This market structure obviates the need for regulators separately to test the market value of original collateral received in comparison with the fair value of the security lent. Additionally, repo funding proceeds may be used for purposes outside of a reinvestment portfolio which results in a lack of asset base to test against for nonadmittance.

Reverse Repurchase Agreement – Reporting Entity Buys Security and Provides Cash / Collateral

a) Reporting entity (cash provider) acquires security from counterparty but does not report the security on their investment schedule. (The reporting entity would recognize the asset if the counterparty defaulted on the agreement.) ***(Note 11)***

    i. If the reporting entity sells the acquired security, the reporting entity would recognize the cash proceeds from the sale and an obligation to return the security to the counterparty. If the cash proceeds are reinvested, then the acquired investment would be on the applicable investment schedule.

b) Reporting entity derecognizes the cash provided to acquire the security and recognizes a receivable for the cash return. This is captured as a short-term investment on Schedule E-2. If the reverse repo agreement was long-term, it shall be nonadmitted.

    i. If the reporting entity provides security in exchange for the security (instead of cash), the security would remain on the reporting entity's investment schedules, coded as a restricted asset.

c) For reverse repurchase agreements the reporting entity should receive securities with a fair value of at least 102% of the purchase price (cash or securities transferred). So, if the cost of the transaction is $100, the reporting entity should receive securities worth $102. ***(Note 12)***

The Restricted Asset / RBC Impact is as follows:

d) The acquired asset is not reported unless the counterparty defaults or unless the reporting entity sells the acquired assets. Unless one of these things occurs, there is no RBC impact for the acquired asset under a reverse repo. (If those transactions occur, then the RBC is determined by the resulting security reported on the investment schedule.)

e) The receivable for the return of the cash collateral would be recorded as a short-term investment on Schedule E – Part 2 and flow through to LR012 with a .0039 RBC charge. This receivable would also be coded as restricted as an "asset subject to a reverse repurchase agreement" on GI 26.23. This would flow to LR017 line 6 and would receive a 0.0126 RBC charge. ***Note 13***

Note 11: The SSAP No. 103 guidance for reverse repo transactions does not have an explicit nonadmittance component if the % threshold is not met. Clarification on what should occur if the adequate collateral is not received / retained is recommended. Additionally, it has been noted that there is no current guidance that assesses admittance based on the quality/type of collateral received. Under the current guidance, residuals or low-quality assets could be received and there is no documentation of this type of collateral for certain sec lending and repo programs. Even if these programs would not qualify as conforming, there is a question on whether admittance restrictions should exist based on the collateral received from the counterparty.

Interested parties' comments on Notes 11-13: In terms of general quality of collateral received in reverse repo transactions, we do not believe there should be regulatory restrictions on the type of collateral that is eligible to be received, other than it being a permitted investment for the reporting entity. The yield earned on the transaction and haircut charged reflects the quality of the collateral.

Maintenance of the collateralization threshold is governed by the legal document (MRA or MSLA) between the counterparts. While collateralization threshold is one of the criteria for a conforming securities lending program, there is no intention to establish conforming reverse repo programs. We believe that regulators should derive comfort on collateralization thresholds from the existing legal agreements between counterparts.

Note 12: SAP does not currently capture details on securities acquired upon the sale of the asset acquired under a reverse repo. The note disclosures only detail aggregate amounts.

See interested parties' comments on Notes 11-13 above.

Note 13: The guidance does not explicitly indicate that the short-term receivable recorded for reverse repurchase transactions should be coded as a restricted asset and taken to GI 26.23. However, as the restricted asset note detailed in SSAP No. 1 and GI 26.23 both capture "assets subject to reverse repurchase agreements," this reference can only refer to the short-term receivable as there is no other asset reported on the books from the transaction. Assessment may be warranted on identification of restricted assets on reverse repurchase transactions.

Interested parties' comments: Interested parties do not believe that there is a cogent rationale for restricting the short term lending receivable. Other short-term lending receivables - CDs, CP and Short Term ABS – are not considered "restricted". Nothing in these short term loans implies lack of exclusive control or encumbrances or third party interests prohibiting the insurer from using these short term loans (or the collateral obtained therefrom at 102% FMV or greater) to satisfy policyholder obligations.

Appendix A – "Conforming" Securities Lending Guidance from RBC Instructions

Line (1) Securities lending programs that have all of the following elements are eligible for a lower off-balance sheet charge:

1. A written plan adopted by the Board of Directors that outlines the extent to which the insurer can engage in securities lending activities and how cash collateral received will be invested.

2. Written operational procedures to monitor and control the risks associated with securities lending. Safeguards to be addressed should, at a minimum, provide assurance of the following:

    a. Documented investment guidelines, including, where applicable, those between lender and investment manager with established procedure for review of compliance.

    b. Investment guidelines for cash collateral that clearly delineate liquidity, diversification, credit quality, and average life/duration requirements.

    c. Approved borrower lists and loan limits to allow for adequate diversification.

    d. Holding excess collateral with margin percentages in line with industry standards, which are currently 102% (or 105% for cross currency loans).

    e. Daily mark-to-market of lent securities and obtaining additional collateral needed to ensure that collateral at all times exceeds the value of the loans to maintain margin of 102% of market.

    f. Not subject to any automatic stay in bankruptcy and may be closed out and terminated immediately upon the bankruptcy of any party.

3. A binding securities lending agreement (standard "Master Lending Agreement" from Securities Industry and Financial Markets Association) is in writing between the insurer, or its agent on behalf of the insurer, and the borrowers.

4. Acceptable collateral is defined as cash, cash equivalents, direct obligations of, or securities that are fully guaranteed as to principal and interest by, the government of the United States or any agency of the United States, or by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation and NAIC 1-designated securities. Affiliate-issued collateral would not be deemed acceptable. In all cases the collateral held must be permitted investments in the state of domicile for the respective insurer.

Collateral included in General Interrogatories, Part 1, Line 25.04 of the annual statement should be included on Line (1).

* * * *

Thank you for the opportunity to comment on the above items. Please feel free to contact either one of us if you have any questions or would like to discuss further.

Sincerely,

D. Keith Bell

Rose Albrizio

cc: Interested parties
NAIC staff

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January 31, 2025

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
hut Street, Suite 1500
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RE: Interested Parties Comments on the Items Exposed for Comment by the Statutory Accounting Principles Working Group with Comments due January 31st

Dear Mr. Bruggeman:

Interested parties appreciate the opportunity to comment on the following items that were exposed for comment by the Statutory Accounting Working Group (the Working Group) with comments due January 31st.

Ref #2023-28: Collateral Loan Reporting

The Working Group re-exposed this agenda item detailing the proposed reporting lines for Schedule BA and AVR. This item was re-exposed to allow for concurrent exposure with blanks proposal 2024-19BWG. Comments received by the Blanks (E) Working Group and the SAPWG will be reviewed collectively.

Interested parties have responded (responses are in *italics*) to the following elements for which feedback was requested during the exposure:

1) Should collateral loans backed by mortgage loans be included in the new collateral loan category, or should those continue to flow through the "Investments with the Underlying Characteristics of Mortgage Loans" permitted during the interim as the long-term resolution?

Interested parties believe the 'Collateral Loans – Backed by Mortgage Loans' Schedule BA subcategory should continue to flow through the "Investments with the Underlying Characteristics of Mortgage Loans" AVR category until a permanent solution is identified.

If captured in the new collateral loan AVR category, to what extent should the underlying characteristic lines detailing quality / past due / foreclosure status (AVR lines 38-64) be duplicated?

Interested parties believe there should be just 1 category in AVR for 'Collateral Loans – Backed by Mortgage Loans' and not bifurcate between quality / past due / foreclosure status. The accounting for Collateral Loans will be able to appropriately report the fair value of the underlying collateral.

2) What additional reporting lines (breakouts) of the proposed AVR categories are necessary to ensure appropriate look-through for RBC assessment purposes?

   Interested parties believe no changes in the following breakouts are warranted at this time. We will actively engage in the RBC discussions with the appropriate NAIC Working Group on this issue.

As it relates to the corresponding Blanks Working Group exposure 2024-19BWG, we have requested a re-exposure / deferral to address this item which was exposed for the first time. Our question to the Working Group is: should Ref #2023-28 also be re-exposed / deferred to align these 2 items?

Ref #2024-10: SSAP No. 56 – Book Value Separate Accounts

During the NAIC Summer National Meeting, the Working Group exposed revisions to *SSAP No. 56—Separate Accounts,* as shown below as "2024 Summer National Meeting Exposed Revisions," to allow for initial review and consideration of potential changes to update measurement method guidance and specify the process to transfer assets for cash between the general and book-value separate accounts. The Working Group also requested comments from regulators and industry on the noted questions, which are highlighted in grey in the exposure draft. This item was originally exposed with a longer comment period ending November 8, 2024, with the comment period extended to January 31, 2025. This item was not discussed in detail during the 2024 Fall National Meeting but is planned for discussion in the interim after that meeting, or during the 2025 Spring National Meeting.

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 (change highlighted in red): "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.

Once again, the ACLI appreciates the opportunity to provide comment and looks forward to continued dialogue and collaboration on Book Value Separate Account guidance. If you have any questions regarding this letter, please do not hesitate to contact us.

Ref #2024-16: Repacks and Derivative Investments

On December 17, 2024, the Working Group exposed proposed annual statement instructions, as shown in the exposure draft under "December 2024 Proposed Revisions to 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 was requested to expose a blanks proposal sponsored by the Statutory Accounting Principles (E) Working Group at the 2024 Fall National Meeting.

Interested parties have no comments on this item.

Ref #2024-20: Restricted Asset Clarification

On November 17, 2024, the Working Group moved this item to the active listing categorized as a SAP clarification and exposed revisions illustrated in the recommended changes to SSAP No. 1 as well as corresponding proposed revisions to the Annual Statement instructions/template for the restricted asset disclosure in Note 5L to specify how Modco and FWH assets reported within a ceding company's financial statements shall be reported. The exposed revisions also include a new disclosure to identify whether Modco/FHW assets are pledged by the ceding entity as well as expanded disclosures to detail differences between what is reported in the restricted asset note and what is in the general interrogatories.

Interested parties appreciate the opportunity to comment on this item after it was re-exposed for comment by the Working Group during the NAIC Fall National Meeting in Denver.

We have split our comments below based on the section of instructions they refer to, following feedback comments related to the overall exposure.

<u>**General Feedback**</u>

Interested parties note that the instructions for SSAP No. 1, Note 5L, General Interrogatories (GI), and Risk Based Capital (RBC) do not indicate which values should be used for each of the

disclosures (i.e., Book Adjusted Carrying Value (BACV), collateral amount, Fair Value). As such, we recommend that BACV be used for all disclosures to ensure consistency.

For example, in Note 5L, columns 8 & 9, Total Admitted/Nonadmitted Assets are reported using BACV, as the assets would appear in the Assets page under the Admitted and Nonadmitted Assets columns. In lines b and c, *Collateral held under security lending agreements* and *Subject to repurchase agreements*, may be reported as collateral amounts to match the General Interrogatory (GI). Combining BACV and collateral amounts could be misleading to the reader.

Interested parties recommend that changes to the *NAIC Accounting Practices and Procedures Manual* (AP&P manual) be made concurrent with any Blanks and RBC instruction updates to ensure that all reporting is consistent.

SSAP No. 1

We have no comment on the changes in SSAP No. 1 – *Accounting Policies, Risks & Uncertainties and Other Disclosures* other than the clarification of expected reporting values.

Notes to the Financial Statements - 5L

5L(1)

- Interested parties note that instructions are not included for the new columns and rows or the newly required reconciliation. Therefore, we recommend instructions be added to the Restricted Assets section.
- We note that this section still has line o titled: *Total restricted assets,* but the new chart shows that the total is now line r. We recommend instructions be updated with the new line titles.
- We note that changes to SSAP No. 1's requirements would also require Note 5L be updated for Health and Property & Casualty companies, which have slightly different formats than Life.

Illustrations to the Financial Statements - 5L

5L(1)

- The exposure should clarify what happens if assets are pledged and may show up as restricted assets in another row.
- Interested parties recommend the removal of the reference to SSAP No. 1 Paragraph 23.c from the Restricted Assets Category in lines o-q.
- We would like to confirm that line o should exclude collateral received from security lending and repurchase agreements as these items are already included in lines b-f. We recommend clarification language to call out the exclusions.

5L(2)

- Question: Is the amount of total assets pledged under derivative contracts supposed to be on the new line (*Amount of Total pledged under derivative contracts*) and not included above

the current line "Total (c)"? If so, why would we need to remove that line from the new total line?

- We recommend that the new Total Excluding Derivatives include a formula showing it is Total (c) less Amt of total pledged under derivative contracts.
- We recommend Staff Note be included as a subnote to the table or included in the Note 5L instructions.
    - ✓ **Note: The amount of pledged under derivative contracts should agree to Schedule DB and agree to what is subtracted from the life RBC formula.**

5L(4)

- Interested parties would like clarification if the new Collateral/Modco/FWH Columns are independent of each other or are Modco/FWH subsets of the collateral amount.
- We note that the subnotes for Columns 3 and 4 were not updated and still state the formula is column 1 / Asset page. Column 1 refers to all data for BACV. The columns will need to be renumbered (i.e., 1.1 Collateral; 1.2 Modco; 1.3 FWH) and/or the subnotes for j and t would be updated.
- We note that row j currently should be column total lines, but the headers for the Separate Account (SA) section were added to the total line instead of a new row. We recommend a new line be added for the SA section headers. Line t should be numerical values rather than column headers.
- We would like to confirm that the "Recognized Obligation for Modco/FWH Assets" required in 5L(4)u and v are equal to the Modco/FWH reserve liabilities. If so, the language should be updated to read as such.

5L(4) – The second one should be renumbered to 5L(5)

- The exposure should clarify that this table applies only when the economic benefits received from pledging the asset stay with the cedant. Stated differently, if the benefit or cost associated with the restriction inures to the reinsurer, that would not be considered "purpose specific to the ceding insurance reporting entity." We recommend a principle be developed to apply the intended rules to a wide array of transactions.

Life RBC (E) Working Group Referral

Interested parties propose the following changes be made to the referral to the Life RBC (E) Working Group.

> *Basis of Factors*
> When the default risk in modified coinsurance (MODCO) and other reinsurance transactions with funds withheld is transferred, this transfer should be recognized by reducing the RBC for the ceding company and increasing it for the assuming company. **In the event that the entire asset credit or variability in statement value risk associated with the assets supporting the business reinsured is not transferred to the assuming company for the entire duration of the reinsurance treaty, the RBC for the ceding company should not be reduced. <u>For clarity, if the Modco/Funds Withheld reinsurance agreement asset held as of the year-end date has been used as a pledged asset concurrently with the</u>**

pledged asset being included as a Modco/Funds Withheld reinsurance agreement asset for any purpose specific to the ceding insurance reporting entity at any time during the year, the RBC for the ceding company shall not be reduced. For example, if the Modco/Funds Withheld reinsurance agreement asset held as of the year-end date was the collateral in a securities lending, repurchase, or FHLB transaction executed for the benefit of ~~by~~ the ceding entity at any time over the year concurrently with the pledged asset being included as a Modco/Funds Withheld reinsurance agreement asset, then ~~the reporting entity cannot assert that they have transferred the asset risk or variability and~~ RBC shall not be reduced. In situations where the economic benefit received from pledging the assets inure to the reinsurer throughout the duration of the reinsurance treaty, the cedant is allowed to reduce its RBC for those assets.

Ref #2024-21: Investment Subsidiaries

On November 17, 2024, the Working Group moved this item to the active listing and exposed this concept agenda item requesting comments on options to clarify accounting guidelines and resulting reporting impacts for investment subsidiaries.

As background, investment subsidiaries are often used by insurers as operationally efficient investment vehicles and also may be used for various legal reasons (e.g., reinsurance transactions). Using a separate legal entity to own certain types of investments may be a lot more efficient than having the insurer own the assets outright. For example, insurers may use an investment subsidiary to own residential mortgage loans. This asset type usually requires the issuance of a high volume of loans to achieve the appropriate economies of scale so that the investment is cost-effective. Insurers may create a separate legal entity to allow for licensing to purchase loans in every state and that will engage a mortgage loan servicer to administer and service all the loans. Additionally, when insurers establish an investment subsidiary in the form of a trust with a national bank as trustee, the national bank trustee is either explicitly exempted from state lending licensing requirements or entitled to federal preemption from state lending license requirements. Using an investment subsidiary in this case would allow the insurance company to invest in large volumes of residential mortgages without significant burden on internal resources and internal operations while holding a capital charge on the underlying mortgages that is commensurate with the risk of each underlying mortgage loan.

With the background above, following are our comments to the potential actions included in the exposure draft.

1. **Proposal No. 1: Revisions to SSAP No. 97 to incorporate statutory accounting guidance for SCAs that hold assets on behalf of the reporting entity and affiliate (investment subsidiaries)**

   Interested parties agree with including guidance in SSAP No. 97 to address the following items:

   a. The definition of an investment subsidiary from Schedule D should be brought over into SSAP No. 97.

b. Interested parties agree that clarification should be added on the accounting for these investments. We understand that these investments are to be reported using an equity method of accounting with U.S. GAAP audited financial statements required for admissibility. There is a current lack of clarity on how to apply the "imputed value" requirement in the investment subsidiary definition. There is inconsistency in practice as to whether the underlying investments are adjusted from a U.S. GAAP value to a U.S. SAP value in instances where U.S. GAAP and U.S. SAP differ from an investment valuation perspective. If the intent is for the investment subsidiary's assets to be recorded with a carrying value equal to what would be recorded if the assets were held directly by the insurer, more clear guidance should be included in SSAP No. 97 as to how this rule is intended to be applied.

c. There should be clarification that in no instance the RBC charges applied to the underlying assets can be more beneficial than if the assets were held directly by the insurer. This should address the Working Group's concern regarding investment subsidiaries that own bonds that do not meet the new principles-based definition and would require an SVO designation for reporting. Interested parties also request clarification in the RBC instructions that the applicable charges be applied to the accounting basis used to determine the carrying value of the investment subsidiary.

2. **Proposal No. 2: Sponsor Blanks proposals to capture new investment Schedules or perhaps expansions to existing investment schedules, to detail the underlying assets held within an investment subsidiary**

   Interested parties believe that having to include a listing of each underlying asset of the investment subsidiary will take away some of the operational efficiency that is gained by having the investment subsidiary own the underlying assets. If this is a "must have" for the Working Group, perhaps we can work together on the most efficient way to provide the data. See additional suggestions under item 3 below.

3. **Proposal No. 3: Referrals to Capital the Capital Adequacy (E) Task Force and related RBC Working Groups to incorporate details that allow regulators to verify the RBC calculation for the underlying assets in investment subsidiaries**

   Interested parties agree with providing transparency for RBC purposes. Since listing each asset individually may take away some of the benefits of creating an investment subsidiary, perhaps the assets can be provided by groupings that match AVR/RBC schedules similar to the industry's recent response on the funds withheld assets exposure. Another option may be to include detail in a note to the financial statement that would be less onerous than including it in the actual Investment schedules.

In addition to providing responses above to the specific actions detailed in the Exposure Draft, interested parties would like to provide additional comments as follows:

1. We understand from the exposure draft that the concept of an investment subsidiary is intended to be limited to Schedule D common stock and preferred stock investments. However, it is not clear to us why the concept cannot be extended to investments in subsidiaries that are legally structured as limited partnerships (LPs) or limited liability companies (LLC). The legal form of the entity should not impact whether a subsidiary meets the criteria for investment subsidiary reporting as the accounting and reporting would follow substance over form. In fact, we understand that insurance law in some states already allows the concept of an investment subsidiary to be applied to any legal entity. For example, state statutes modeled on the NAIC Holding Company System Regulatory Act refer to investment subsidiaries as "entities organized as corporations, partnerships, associations, joint stock companies, trusts, unincorporated organizations that are engaged or organized to engage exclusively in the ownership and management of assets authorized as investments for the insurer." We understand that this would require some changes to Schedule BA to add a specific line item for investment subsidiaries, which will require additional work and new AVR/RBC mapping. Another option could be to require all investment subsidiaries, regardless of legal form, to be reported on Schedule D.

2. There are entities that are not legally structured as either a corporation or LP/LLC. However, the equity they issue is more akin to a common stock investment in a corporation than it is to an equity interest in an LP/LLC. This is the case for Delaware statutory trusts (DSTs). From a legal perspective, equity investments in these types of entities are treated similarly to common stock as investors in both DSTs and corporations have limited liability. Unlike LPs/LLCs, DSTs do not maintain separate capital accounts for each investor since the ownership interest is usually represented by shares/beneficial interests similar to ownership of equity in a corporation. Any new guidance added to SSAP No. 97 should allow for the reporting entity's assessment of whether the equity investment in the investment subsidiary is more akin to common stock (Schedule D reporting) or more akin to LP/LLC interests (Schedule BA reporting). Each reporting entity needs to assess individual facts and circumstances for each investment vehicle to determine guidance applicability and the appropriate schedule in which to report the investment subsidiary.

3. Some trusts are established to hold assets such as mortgage loans that allow for direct reporting on Schedule B. We understand that this is done by including legal language in the trust certificates that specifically state that ownership in the trust represents a participation in each mortgage loan owned by the Trust. In these instances, the insurer has an undivided interest in each mortgage loan and it has the same rights as the lender of record with all proceeds from the loans as well as foreclosure rights being pari-passu with the lender of record. We believe that since ownership in the trust in this instance represents a participation in each loan as defined in SSAP No. 37, these loans are Schedule B eligible assets and are outside of the scope of the investment subsidiary guidance.

Ref #2024-22: ASU 2024-01, Scope Application of Profits Interest and Similar Awards

On November 17, 2024, the Working Group moved this item to the active listing and exposed revisions, as shown in the exposure draft, 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 have no comments on this item.

Ref #2024-23: Derivative Premium Clarifications

On November 17, 2024, the Group moved this item to the active listing, categorized as a SAP clarification, and exposed this agenda item proposing revisions to *SSAP No. 86—Derivatives* and the annual statement instructions to ensure consistent terminology for derivative financing premiums and to further clarify that derivative premium costs shall not be recognized as a realized gain/loss.

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.

Ref #2024-24: Medicare Part D - Medicare Prescription Payment Programs

On November 17, 2024, the Working Group moved this item to the active listing, categorized as a SAP clarification, and 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*, as described above. 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.

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

Ref #2024-25: SSAP No. 16 Clarifications

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 agree with the updated references in this item.

Ref #2024-27: Issue Papers in the Statutory Hierarchy

On December 17, 2024, the Working Group moved this item to the active listing as a SAP clarification and exposed revisions, as shown in the exposure draft, to classify issue papers in Level 5 of the statutory hierarchy.

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.

Ref #2024-28: Holders of Capital Notes

This agenda item has been prepared in response to the direction of the Working Group during the 2024 Fall National Meeting with the adoption of INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers. With the adoption of the INT, and the guidance for reporting certain debt securities as capital notes in scope of SSAP No. 41—Surplus Notes, industry identified that slight revisions may be necessary to reflect the capital note distinctions. The Working Group directed NAIC staff to work with industry in this review and identifying necessary changes.

From the initial review and working with industry, revisions have been proposed to address the following specifically for capital notes:

1. Incorporate a definition/reference to the INT for capital notes.

2. Clarify the admittance restrictions.

3. Clarify the guidance for NAIC designations.

4. Update the impairment guidance to refer to capital notes.

In addition to these items, it was identified that an existing disclosure for surplus notes, which requires disclosure of any holder of 10% or more of an SEC-registered surplus note, is likely an extensive administrative burden, may be difficult to complete, and as a narrative disclosure only (not data-captured), is likely not often utilized. From a review of the disclosure, it predates the issuance of SSAP No. 41—Surplus Notes, and there are questions as to how a disclosure of certain holders of SEC-registered notes would be purposeful or used. NAIC staff has proposed to eliminate this aspect of the disclosure but retain the disclosure focusing on surplus notes with affiliates. NAIC staff requests feedback on whether this disclosure should be retained. Interested parties reviewed this exposure and have the following 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 down grade 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.

* * * *

Thank you for the opportunity to comment on the above items. Please feel free to contact either one of us if you have any questions or would like to discuss further.
Sincerely,

D. Keith Bell　　　　Rose Albrizio

cc: Interested parties
NAIC staff

January 31, 2025

Mr. Dale Bruggeman
Chair, Statutory Accounting Principles (E) Working Group
National Association of Insurance Commissioners

Sent via e-mail to NAIC staff cc'd below

Re: 2024-24, Medicare Prescription Payment Plan

Dear Mr. Bruggeman:

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.

SAPWG Maintenance Agenda Submission Form, Form A

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.

* * * * * * *

The Trades thank you for this opportunity to provide our comments on SAPWG's exposure 2024-24 and would be pleased to address any questions you or other SAPWG members may have.

Sincerely,

Clay S. McClure
BCBSA, Executive Director State Affairs

Miranda Motter
AHIP, Senior Vice President, State Affairs and Policy

Cc to NAIC staff:

Julie Gann
Robin Marcotte
Jake Stultz
Jason Farr
Wil Oden

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 24-02T: Medicare ~~Part D~~ Prescription Payment ~~Plans~~Plan

INT 24-02T Dates Discussed

November 17, 2024

INT 24-02T References

Current:

- *SSAP No. 47—Uninsured Plans*
- *SSAP No. 54—Individual and Group Accident and Health Contracts*
- *SSAP No. 66—Retrospectively Rated Contracts*
- *SSAP No. 84—Health Care and Government Insured Plan Receivables*
- *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*

INT 24-024T Issue

1. The Inflation Reduction Act of 2022 introduced changes to Medicare Part D, ~~which is~~ the voluntary, outpatient prescription drug ~~program (~~benefit under Medicare. Among other changes, Part D~~), including a new program~~ sponsors are required to ~~help~~offer their Part D enrollees ~~manage~~the option to pay their ~~prescription~~out-of-pocket Part D 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 (~~MP3), will become~~MPPP), became effective on January 1, 2025.

~~1.~~2. The purpose of this interpretation is to provide statutory accounting and reporting guidance for relevant aspects of the ~~MP3 program~~MPPP. This interpretation specifically addresses the ~~MP3~~MPPP components ~~of Medicare Part D~~ (MPPP-related receivables and impairment of such balances) of Medicare Part D that prompted a need for such interpretive guidance. However, this interpretation does not intend to alter the guidance in *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*, which offers high-level accounting guidance on the current Medicare Part D program~~.~~; other than its potential impact on the *amount* of revenues, MPPP does not alter the *nature* of any revenues under the Part D program and thus there is no need to amend the existing statutory accounting guidance for such revenue in *INT 05-05.*

~~MP3~~MPPP Program Overview

1. ~~MP3 is a new program~~Under the MPPP, which launched January 1, 2025, all insurers that ~~requires all~~offer Medicare prescription drug plans (Part D ~~plans~~plan sponsors), including both standalone Medicare prescription drug plans and Medicare Advantage plans with prescription drug coverage, are required to offer ~~its members~~enrollees the option to pay their out-of-pocket prescription drug costs through monthly payments to the Part D plan sponsor over the remainder of the plan year, as opposed to paying the full amount upfront to the pharmacy.

~~2.~~3. Part D plan ~~members~~enrollees who elect to participate in ~~MP3 (MP3 enrollees~~MPPP (MPPP participants) will pay $0 to the pharmacy for covered Part D drugs. ~~The~~Instead, the Part D plan sponsor is required to fully pay the pharmacy the total of an ~~enrollee's~~MPPP participant's applicable out-of-pocket amount and the Part D plan sponsor's portion of the payment in accordance with Part D prompt payment

requirements. Subsequently, the Part D plan sponsor will bill the ~~MP3 enrollee~~MPPP participant monthly for any cost-sharing incurred while enrolled in ~~MP3~~MPPP.

~~3.~~4. ~~MP3 enrollees will~~ Participation in the MPPP does not save program participants money ~~on the total out-of-pocket~~ or otherwise lower their Part D drug costs ~~of prescription drug purchases~~ for which they are responsible (there are other ~~Part D~~ programs in place to help qualifying Part D plan ~~members~~enrollees with affordability issues). ~~MP3~~MPPP simply spreads the MPPP participants' out-of-pocket Part D costs into monthly payments over the remaining term of the plan year which may help ~~many~~some Part D plan ~~members~~enrollees to better manage their monthly cash flow.

~~4.~~5. Unlike some other existing aspects of Part D ~~programs~~, which involve funds due from the federal government ~~(~~for which payment is effectively assured~~), MP3 installment recoverables~~ , MPPP balances are due from individual ~~enrollees. Consequently, Part D plans may pay pharmacies for MP3 enrollees' out-of-pocket pharmacy claim costs, but some amounts billed~~ MPPP participants and there is the risk to the ~~enrollee~~ Part D plan sponsor that a portion of such balances might ultimately be determined to be uncollectible. ~~Reasons for the amount being uncollectable~~That could ~~include leaving enrollment in the Part D plan or an inability or unwillingness to~~ occur when an MPPP participant, for whatever reason, does not pay the full outstanding balance~~.~~ after the required grace period. This raises statutory accounting concerns ~~regarding~~ as to whether balances due from MPPP participants are admitted assets, the potential nonadmittance of overdue amounts, and how impairment of such ~~recoverables.~~unpaid outstanding balances would be reported when determined to be uncollectible

~~5.~~6. To help cover potential ~~uncollectible balances~~impairments of recoverables from MPPP participants, the Centers for Medicare and Medicaid Services (CMS) allows Part D plan sponsors to include an ~~MP3 loss~~ estimate for such MPPP-related losses in their ~~premium~~plan bids. However, and especially for the initial ~~years~~year, Part D plan sponsors ~~have no~~lack directly relevant prior experience to estimate the extent to which balances due from MPPP participants will become impaired, nor does CMS provide specific assumptions that Part D plan sponsors should use in ~~estimating the MP3 program's potential expenses~~making such estimates for inclusion in premium bids.

~~6.~~7. The government is responsible for the estimated ~~MP3~~MPPP losses to the extent they are included in ~~premium~~plan bids by Part D plan sponsors. Part D plan sponsors thus receive additional revenue, which helps to cover uncollectible/impaired balances ~~resulting from MP3 enrollees.~~of MPPP participants. However, Part D plan sponsors nonetheless face pricing/underwriting risk relating to the prescription needs of enrollees and may inaccurately estimate the amounts of uncollectible ~~losses in the premium bids.~~/impaired balances to include in plan bids, particularly in the initial years of MPPP while further experience is gained. In addition, there are risks that the costs of uncollectible/impaired amounts and other aspects of implementing ~~the payment plan~~MPPP will vary from amounts that had been factored into ~~premium rates.~~plan bids. According to CMS guidance any losses in excess of the loss estimates included in ~~the premium~~plan bids are the responsibility of the Part D plan sponsor; thus, the Part D plan sponsor bears a new element of pricing /underwriting risk that arises with MPPP.

~~MP3~~MPPP Program Requirements for Unpaid Balances

~~7.~~8. ~~The MP3 Program requires~~Under the MPPP, Part D plan sponsors are obligated to take on the risk for a portion of uncollectible balances. The program rules prohibit or limit many of the common methods ~~used~~Part D plan sponsors might otherwise use to mitigate loss from uncollectible ~~MP3 balances. MP3 is a mandated program benefit imposed by federal law and CMS rules, with different implications for statutory accounting purposes. Other key program requirements for MP3 balances~~ MPPP balances. Examples of such prohibitions or limitations include the following:

~~8.~~9. **Late Fees, Etc. –** Under ~~MP3~~MPPP, late fees, interest payments, or other fees, such as for different payment mechanisms, are not allowed.

~~9.~~10. **Billing and Payment Procedures –** Part D plan sponsors can design their own billing and payment procedures for ~~MP3~~MPPP. However, they must prioritize payments towards Part D plan premiums to avoid an enrollee losing their Part D coverage. This rule applies when it is unclear if an enrollee intended a submitted payment to cover their outstanding Part D plan premium or their ~~MP3~~MPPP balance.

~~10.~~11. **Pharmacies Not Responsible for Balances –** Participation in ~~MP3~~MPPP is considered an arrangement between the Part D plan sponsor and the ~~MP3 enrollee.~~MPPP participant. Pharmacies are not responsible for ~~an enrollee's unsettled~~losses attributed to impairment of MPPP participants' balances or for collecting unpaid balances from the ~~MP3 enrollee~~MPPP participant on the Part D plan sponsor's behalf.

~~11.~~12. **Termination of Participation –** A Part D plan sponsor must terminate an enrollee's participation in ~~MP3~~MPPP if the enrollee fails to pay their monthly billed amount. An ~~MP3 enrollee~~MPPP participant will be considered to have failed to pay their monthly billed amount only after ~~the~~a required grace period of at least two months. ~~The~~However, the Part D plan sponsor cannot terminate ~~the enrollee's membership in~~an enrollee from the Part D plan ~~for nonpayment of~~itself because the enrollee failed to fully repay their ~~MP3~~MPPP billed amounts. ~~Sponsors~~Part D plan sponsors must continue billing amounts owed under the program in monthly amounts up to the maximum monthly cap based on the statutory formula for the remaining duration of the plan year after an enrollee has been terminated.

~~12.~~13. **Reinstatement of Enrollees** - Part D plan sponsors must reinstate terminated ~~MP3 enrollees~~MPPP participants if the individual demonstrates good cause for failure to pay the program billed amount within the grace period and pays all overdue amounts billed.

~~13.~~14. **Preclusion from Subsequent Enrollment** - A Part D plan sponsor may prevent an individual from opting ~~in to~~into the ~~MP3~~MPPP program in a subsequent year if the individual owes an overdue balance to that Part D plan sponsor or to another Part D plan sponsor with the same ~~ultimate~~ parent~~.~~ organization. In other words, an individual who owes an overdue MPPP balance ~~under the program~~to a Part D plan sponsor cannot be barred from ~~MP3~~enrolling in MPPP in a subsequent year ~~by~~through a different Part D plan sponsor that does not have the same parent organization.

a. **Compliance with Federal and State Laws -** Part D plan sponsors (and any third parties that Part D plan sponsors contract) collecting unpaid balances related to the program must follow other applicable federal and state laws and requirements, including those related to other types of payment plans, credit reporting, and debt collection.

15. In essence, MPPP is a payment option that Part D plan sponsors must offer to enrollees; Part D plan sponsors are compensated by the government to the extent estimated MPPP-related losses from uncollected balances determined to be impaired are included in their plan bids; Part D plan sponsors are at risk for MPPP-related losses in excess of those estimates; and Part D plan sponsors are prohibited from using many other administrative means to mitigate such losses.

Medical Loss Ratio

~~14.~~16. Regarding the issue of how Part D plan sponsors should report MPPP-related losses in their statutory financial statement filings to state insurance regulators, a potential point of confusion is the requirement imposed by the Centers for Medicare and Medicaid Services ("CMS") that Part D plan sponsors treat any uncollected balances from MPPP participants determined to be impaired as part of their administrative costs for purposes of reporting their minimum medical loss ratio ("MLR") to CMS.

2. The current Public Health Act outlines how to calculate medical loss ratio (MLR) rebates, which are generally based on a comparison of incurred health claims and quality improvement activities to premium revenue, considering various factors and adjustments. *SSAP No. 66—Retrospectively Rated Contracts* provides disclosures related to the MLR. While the CMS MLR requirements provide interesting context, statutory reporting requirements are separate and distinct and involve their own considerations.

~~15.~~17. According to the CMS guidance, the ~~outstanding~~losses related to impairments of MPPP-related balances owed by ~~MP3 enrollees~~MPPP participants are considered for MLR purposes as part of the Part D ~~plan's~~plan sponsor's administrative expenses. CMS guidance thus excludes ~~unsettled~~losses attributed to impaired MPPP balances from the numerator of the MLR calculation, aligning with CMS' treatment of other administrative expenses incurred by Part D sponsors. The CMS guidance states that ~~unsettled balances~~ the additional premium revenue that is attributable to the estimates of MPPP-related impairments included in plan bids by Part D plan sponsors are included in the MLR calculation denominator ~~and allows Part D sponsors to account for these balances as losses in their premium bids.~~. Including ~~enrollee losses~~such premium amounts in the denominator aligns with reporting the revenue estimated to offset these losses in the MLR denominator.

18. It is noted that CMS guidance related to MLR is distinct from, and is not authoritative with respect to, statutory accounting guidance promulgated by the NAIC and its member state insurance regulators. While SAP is largely consistent with MLR reporting currently, there are some differences. This Interpretation is intended, in part, to clarify statutory accounting for MPPP-related losses and for clarity, will explain whether such treatment will or won't align with CMS guidance for the MLR.

> *Drafting Note: The ~~MP3 program~~MPPP considers uncollectible ~~MP3~~ recoverables from MPPP enrollees as incurred plan administrative costs and does not include these amounts in the MLR numerator, so reporting guidance for other adjustments to the Supplemental Health Care Exhibit will be needed. Such reporting revisions are not addressed in this interpretation but would be anticipated to be in the annual statement reporting revisions submitted to the Blanks (E) Working Group.*

INT 24-02T Discussion

Statutory Accounting and Reporting Considerations for ~~MP3~~MPPP

~~16.~~19. The Working Group reached the following tentative consensus for ~~MP3~~MPPP statutory accounting and reporting guidance. In addition, Appendix 1 illustrates some basic journal entries which help to show the intended financial statement results.

~~MP3~~ Recoverables from MPPP Participants

~~17.~~20. ~~MP3 recoverables~~Recoverables from ~~enrollees~~MPPP participants shall be accrued and reported ~~on~~as an asset on line 24, *Health care and other amounts receivable*, when the related ~~pharmacy~~ payment is made by the Part D plan sponsor to the pharmacy for the out-of-pocket ~~payment is~~costs incurred on behalf of the MPPP participant.

~~18.~~21. Current ~~MP3~~ recoverables from MPPP participants, 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 ~~MP3 enrollees~~MPPP participants represents a probable future economic benefit to the Part D plan sponsor resulting from past transactions or events (i.e., paying the ~~MP3 enrollee's~~MPPP participant's out-of-pocket costs to the pharmacy). ~~MP3~~ recoverables from MPPP participants are also subject to impairment analysis.

~~19.~~22. Uncollected ~~MP3~~ recoverables from MPPP participants more than 90 days overdue are nonadmitted. The due date for aging of ~~the MP3~~such recoverables shall follow the program billing guidelines.

~~20.~~23. If ~~an MP3~~a recoverable from an MPPP participant is fully collected, it will equal the corresponding out-of-pocket payment for pharmaceutical claim payment. In those cases, there will not be an income statement impact regarding claims (or claims adjusting expenses) if the ~~MP3~~MPPP recoverable is fully collected.

Impairments

~~21.~~24. Uncollected ~~MP3~~ recoverables from ~~enrollees~~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 ~~MP3~~ recoverables from MPPP participants are recorded, the expense for the impairment shall be reflected in as incurred Medicare Part D prescription drug claims in the statutory income statement.

Out-of-Pocket ~~MP3~~MPPP Pharmacy Payments

~~22.~~25. When the Part D plan sponsor pays out-of-pocket drug claims to the pharmacy, a claims expense, a contra claims expense, and a contra claims expense account recoverable ~~are~~may be recorded. The contra claims expense, or similar mechanism, ~~is~~could be recorded to prevent initial claims expense recognition in the income statement so there is zero initial impact to the income statement. This is because there is an amount recoverable from the ~~enrollee~~MPPP participant, and to the extent that the ~~enrollee~~MPPP participant pays in full, there should not be any claims recognition. This is analogous to the handling of anticipated pharmaceutical rebates or anticipated subrogation recoveries.

~~23.~~26. If the ~~enrollee~~MPPP participant pays the amount due in full, there will be no income statement impact in claims expenses resulting from the ~~MP3~~Part D plan sponsor's payment of the MPPP participant's out-of-pocket costs to the pharmacy ~~payment and~~which would thus have been offset by subsequent ~~enrollee~~monthly payments~~.~~ by the MPPP participant to the Part D plan sponsor. In such cases, the ~~MP3~~MPPP recoverable will be reduced as payments are collected and there would be no income statement impact.

~~24.~~27. If the ~~enrollee recoverable~~MPPP participant's balance is not repaid in whole or in part, there will be an income statement impact to reflect paid claims ~~for~~to the ~~amount~~extent of the ~~MP3 recoverable~~MPPP balance at the time that ~~are~~the balance is recognized as impaired and written off. Since there is ~~an MP3~~a recoverable from the ~~enrollee~~MPPP participant, there should be no income statement amount for an incurred claim until the related ~~MP3~~MPPP recoverable is written off for impairment.

~~25.~~28. When the ~~MP3~~ recoverable from the MPPP participant is impaired, the contra claims expense is decreased by the amount of the ~~MP3~~ recoverable that is written off. This results in the incurred Medicare prescription claim reported reflecting the uncollectible ~~MP3~~ recoverable from MPPP participants for statutory reporting. The premium to offset these claims is included in Medicare premium bids, so reporting the incurred uncollectible ~~MP3~~MPPP amounts as losses allows the statutory accounting loss ratio to reflect

incurred Medicare Part D prescription costs which include MP3MPPP uncollectible amounts. which have been impaired and written off.

3. Reporting uncollectible and impaired MP3 recoverables in statutory filings as claims incurred is different than the CMS treatment of which reports such amounts as administrative expense for MLR purposes.

Administrative Costs

26.29. Costs of Other costs, e.g., those incurred by Part D plan sponsors in implementing the MP3and administering MPPP program and programrelated collections, are included in the administrative expenses of the Part D plan sponsor and are not included in the claim expenses or claim adjustment expenses.

MLR Reporting Difference

27.30. Note that the reporting of the uncollectible (impaired) MP3 recoverable from MPPP participants in Medicare prescription claims is different from CMS treatment of such amounts in the MLR. The CMS treatmentrequires Part D plan sponsors to report losses from impairments of uncollectible MP3 recoverables reports such amountsfrom MPPP participants as administrative amounts. These administrative amounts are included in the denominator of the MLR by CMS.

INT 24-02T Status

4.3. This interpretation is tentatively effective March 30, 2025.

5.4. Further discussion is planned.

Medicare Prescription Payment Plan Scenarios			
	Claims	**Receivable**	**Cash**
Initial entries for all scenarios *Assumed to have been recorded by the ~~insurance company~~Part D plan sponsor prior to Scenarios 1 – 3.*			
DR Claims Expense *To represent claims expense incurred on behalf of the ~~enrollee~~MPPP participant.*	$ 2,000		
CR Cash *To represent the $2,000 paid by the ~~insurance company~~Part D plan sponsor to the pharmacy on behalf of the ~~enrollee~~MPPP participant.*			$ (2,000)
DR Healthcare Receivable *To represent the amount due to the ~~insurance company~~Part D plan sponsor from the ~~enrollee~~MPPP participant, which the ~~enrollee~~MPPP participant must pay over the policy term.*		$ 2,000	
CR Claims A/R (contra-claims expense) *To be reported within the claims expense line, essentially a contra-claims expense, and represents the amount due to the ~~insurance company~~Part D plan sponsor from the ~~enrollee~~MPPP participant which the ~~enrollee~~MPPP participant must pay over the policy term. This offsets the claims expense amount, so results in a current net $0 impact to the income statement, but both the DR and CR on the income statement are in claims expense.*	$ (2,000)		
Scenario 1 - The ~~enrollee~~MPPP participant pays their full amount of $2,000 to the ~~insurance company~~Part D plan sponsor.			
DR Cash *To record receipt of the ~~enrollee's~~MPPP participant's payment in full.*			$ 2,000
CR Healthcare Receivable *The net income statement impact remains at $0, because the original claims expense was offset by the contra-claims expense (Claims A/R), and since the full $2,000 was received from the ~~enrollee~~MPPP participant, there are no further income statement journal entry impacts.*		$ (2,000)	
Scenario 1 Net result on Financial Statements	**$ -**	**$ -**	**$ -**
Scenario 2 - The ~~enrollee~~MPPP participant pays $1,500 out of the $2,000 to the ~~insurance company~~Part D plan sponsor and doesn't pay the remaining $500.			
DR Cash			$ 1,500

To record receipt of ~~enrollee~~MPPP participant partial payment of outstanding balance.			
CR Healthcare receivable *To reduce ~~enrollee~~MPPP participant receivable for amounts paid.*		$ (1,500)	
DR Claims A/R (contra-claims expense) *To represent the write-off of the receivable. This results in the ~~insurance company~~Part D plan sponsor having a total income statement impact debit to claims expense of $500, represented as the initial $2,000 claims expense for the out-of-pocket ~~-~~paid to the pharmacy by the ~~insurance company~~Part D plan sponsor, offset by the $1,500 received from the ~~enrollee~~MPPP participant.*	$ (500)		
CR Healthcare receivable *To write~~-~~ off the remaining uncollectible amount as impaired*		$ (500)	
Scenario 2 Net result on Financial Statements	**$ 500**	**$**	**$ (500)**
Scenario 3 - The ~~enrollee~~MPPP participant does not pay any of the $2,000 owed to the ~~insurance company~~Part D plan sponsor.			
DR Claims A/R (contra-claims expense) *To represent the write-off of the amount anticipated to be paid by the ~~enrollee.~~MPPP participant. This results in the income statement impact to the ~~insurance company~~Part D plan sponsor being a debit of $2,000, for the amount paid to the pharmacy by the ~~insurance company~~Part D plan sponsor and not reimbursed by the ~~enrollee~~MPPP participant.*	$ 2,000		
CR Healthcare receivable *To represent the write-off of the $2000 receivable.*		$ (2,000)	
Scenario 3 Net result on Financial Statements	**$ 2,000**	**$ -**	**$ (2,000)**

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 24-02T: Medicare Prescription Payment Plan

INT 24-02T Dates Discussed

November 17, 2024

INT 24-02T References

Current:
- *SSAP No. 47—Uninsured Plans*
- *SSAP No. 54—Individual and Group Accident and Health Contracts*
- *SSAP No. 66—Retrospectively Rated Contracts*
- *SSAP No. 84—Health Care and Government Insured Plan Receivables*
- *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*

INT 24-024T Issue

1. The Inflation Reduction Act of 2022 introduced changes to Medicare Part D, the voluntary, outpatient prescription drug benefit under Medicare. Among other changes, Part D sponsors are required to offer their Part D enrollees the option to pay their out-of-pocket Part D 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), became effective on January 1, 2025.

2. The purpose of this interpretation is to provide statutory accounting and reporting guidance for relevant aspects of the MPPP. This interpretation specifically addresses the MPPP components (MPPP-related receivables and impairment of such balances) of Medicare Part D that prompted a need for such interpretive guidance. However, this interpretation does not intend to alter the guidance in *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*, which offers high-level accounting guidance on the current Medicare Part D program; other than its potential impact on the *amount* of revenues, MPPP does not alter the *nature* of any revenues under the Part D program and thus there is no need to amend the existing statutory accounting guidance for such revenue in *INT 05-05*.

MPPP Program Overview

1. Under the MPPP, which launched January 1, 2025, all insurers that offer Medicare prescription drug plans (Part D plan sponsors), including both standalone Medicare prescription drug plans and Medicare Advantage plans with prescription drug coverage, are required to offer enrollees the option to pay their out-of-pocket prescription drug costs through monthly payments to the Part D plan sponsor over the remainder of the plan year, as opposed to paying the full amount upfront to the pharmacy.

3. Part D plan enrollees who elect to participate in MPPP (MPPP participants) will pay $0 to the pharmacy for covered Part D drugs. Instead, the Part D plan sponsor is required to fully pay the pharmacy the total of an MPPP participant's applicable out-of-pocket amount and the Part D plan sponsor's portion of the payment in accordance with Part D prompt payment requirements. Subsequently, the Part D plan sponsor will bill the MPPP participant monthly for any cost-sharing incurred while enrolled in MPPP.

4. Participation in the MPPP does not save program participants money or otherwise lower their Part D drug costs for which they are responsible (there are other programs in place to help qualifying Part D plan enrollees with affordability issues). MPPP simply spreads the MPPP participants' out-of-pocket Part D costs into monthly payments over the remaining term of the plan year which may help some Part D plan enrollees to better manage their monthly cash flow.

5. Unlike some other existing aspects of Part D, which involve funds due from the federal government for which payment is effectively assured, MPPP balances are due from individual MPPP participants and there is the risk to the Part D plan sponsor that a portion of such balances might ultimately be determined to be uncollectible. That could occur when an MPPP participant, for whatever reason, does not pay the full outstanding balance after the required grace period. This raises statutory accounting concerns as to whether balances due from MPPP participants are admitted assets, the potential nonadmittance of overdue amounts, and how impairment of such unpaid outstanding balances would be reported when determined to be uncollectible

6. To help cover potential impairments of recoverables from MPPP participants, the Centers for Medicare and Medicaid Services (CMS) allows Part D plan sponsors to include an estimate for such MPPP-related losses in their plan bids. However, and especially for the initial year, Part D plan sponsors lack directly relevant prior experience to estimate the extent to which balances due from MPPP participants will become impaired, nor does CMS provide specific assumptions that Part D plan sponsors should use in making such estimates for inclusion in premium bids.

7. The government is responsible for the estimated MPPP losses to the extent they are included in plan bids by Part D plan sponsors. Part D plan sponsors thus receive additional revenue, which helps to cover uncollectible/impaired balances of MPPP participants. However, Part D plan sponsors nonetheless face pricing/underwriting risk relating to the prescription needs of enrollees and may inaccurately estimate the amounts of uncollectible/impaired balances to include in plan bids, particularly in the initial years of MPPP while further experience is gained. In addition, there are risks that the costs of uncollectible/impaired amounts and other aspects of implementing MPPP will vary from amounts that had been factored into plan bids. According to CMS guidance any losses in excess of the loss estimates included in plan bids are the responsibility of the Part D plan sponsor; thus, the Part D plan sponsor bears a new element of pricing /underwriting risk that arises with MPPP.

MPPP Program Requirements for Unpaid Balances

8. Under the MPPP, Part D plan sponsors are obligated to take on the risk for a portion of uncollectible balances. The program rules prohibit or limit many of the common methods Part D plan sponsors might otherwise use to mitigate loss from uncollectible MPPP balances. Examples of such prohibitions or limitations include the following:

9. **Late Fees, Etc. –** Under MPPP, late fees, interest payments, or other fees, such as for different payment mechanisms, are not allowed.

10. **Billing and Payment Procedures –** Part D plan sponsors can design their own billing and payment procedures for MPPP. However, they must prioritize payments towards Part D plan premiums to avoid an enrollee losing their Part D coverage. This rule applies when it is unclear if an enrollee intended a submitted payment to cover their outstanding Part D plan premium or their MPPP balance.

11. **Pharmacies Not Responsible for Balances –** Participation in MPPP is considered an arrangement between the Part D plan sponsor and the MPPP participant. Pharmacies are

not responsible for losses attributed to impairment of MPPP participants' balances or for collecting unpaid balances from the MPPP participant on the Part D plan sponsor's behalf.

12. **Termination of Participation –** A Part D plan sponsor must terminate an enrollee's participation in MPPP if the enrollee fails to pay their monthly billed amount. An MPPP participant will be considered to have failed to pay their monthly billed amount only after a required grace period of at least two months. However, the Part D plan sponsor cannot terminate an enrollee from the Part D plan itself because the enrollee failed to fully repay their MPPP billed amounts. Part D plan sponsors must continue billing amounts owed under the program in monthly amounts up to the maximum monthly cap based on the statutory formula for the remaining duration of the plan year after an enrollee has been terminated.

13. **Reinstatement of Enrollees** - Part D plan sponsors must reinstate terminated MPPP participants if the individual demonstrates good cause for failure to pay the program billed amount within the grace period and pays all overdue amounts billed.

14. **Preclusion from Subsequent Enrollment** - A Part D plan sponsor may prevent an individual from opting into the MPPP program in a subsequent year if the individual owes an overdue balance to that Part D plan sponsor or to another Part D plan sponsor with the same parent organization. In other words, an individual who owes an overdue MPPP balance to a Part D plan sponsor cannot be barred from enrolling in MPPP in a subsequent year through a different Part D plan sponsor that does not have the same parent organization.

a. **Compliance with Federal and State Laws -** Part D plan sponsors (and any third parties that Part D plan sponsors contract) collecting unpaid balances related to the program must follow other applicable federal and state laws and requirements, including those related to other types of payment plans, credit reporting, and debt collection.

15. In essence, MPPP is a payment option that Part D plan sponsors must offer to enrollees; Part D plan sponsors are compensated by the government to the extent estimated MPPP-related losses from uncollected balances determined to be impaired are included in their plan bids; Part D plan sponsors are at risk for MPPP-related losses in excess of those estimates; and Part D plan sponsors are prohibited from using many other administrative means to mitigate such losses.

Medical Loss Ratio

16. Regarding the issue of how Part D plan sponsors should report MPPP-related losses in their statutory financial statement filings to state insurance regulators, a potential point of confusion is the requirement imposed by the Centers for Medicare and Medicaid Services ("CMS") that Part D plan sponsors treat any uncollected balances from MPPP participants determined to be impaired as part of their administrative costs for purposes of reporting their minimum medical loss ratio ("MLR") to CMS.

2. The current Public Health Act outlines how to calculate medical loss ratio (MLR) rebates, which are generally based on a comparison of incurred health claims and quality improvement activities to premium revenue, considering various factors and adjustments. *SSAP No. 66—Retrospectively Rated Contracts* provides disclosures related to the MLR. While the CMS MLR requirements provide interesting context, statutory reporting requirements are separate and distinct and involve their own considerations.

17. According to the CMS guidance, the losses related to impairments of MPPP-related balances owed by MPPP participants are considered for MLR purposes as part of the Part D plan sponsor's administrative expenses. CMS guidance thus excludes losses attributed to impaired MPPP balances from the numerator of the MLR calculation, aligning with CMS' treatment of other administrative expenses incurred by Part D sponsors. The CMS guidance states that the additional premium revenue that is attributable to the estimates of MPPP-related impairments included in plan bids by Part D plan sponsors are included in the MLR calculation denominator. Including such premium amounts in the denominator aligns with reporting the revenue estimated to offset these losses in the MLR denominator.
18. It is noted that CMS guidance related to MLR is distinct from, and is not authoritative with respect to, statutory accounting guidance promulgated by the NAIC and its member state insurance regulators. While SAP is largely consistent with MLR reporting currently, there are some differences. This Interpretation is intended, in part, to clarify statutory accounting for MPPP-related losses and for clarity, will explain whether such treatment will or won't align with CMS guidance for the MLR.

Drafting Note: The MPPP considers uncollectible recoverables from MPPP enrollees as incurred plan administrative costs and does not include these amounts in the MLR numerator, so reporting guidance for other adjustments to the Supplemental Health Care Exhibit will be needed. Such reporting revisions are not addressed in this interpretation but would be anticipated to be in the annual statement reporting revisions submitted to the Blanks (E) Working Group.

INT 24-02T Discussion

Statutory Accounting and Reporting Considerations for MPPP

19. The Working Group reached the following tentative consensus for MPPP statutory accounting and reporting guidance. In addition, Appendix 1 illustrates some basic journal entries which help to show the intended financial statement results.

Recoverables from MPPP Participants

20. Recoverables from MPPP participants shall be accrued and reported as an asset on line 24, *Health care and other amounts receivable*, when the related payment is made by the Part D plan sponsor to the pharmacy for the out-of-pocket costs incurred on behalf of the MPPP participant.

21. Current recoverables from MPPP participants, 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 participant's out-of-pocket costs to the pharmacy). recoverables from MPPP participants are also subject to impairment analysis.

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

23. If a recoverable from an MPPP participant is fully collected, it will equal the corresponding out-of-pocket payment for pharmaceutical claim payment. In those cases, there will not be an income statement impact regarding claims (or claims adjusting expenses) if the MPPP recoverable is fully collected.

Impairments

24. Uncollected 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 recoverables from MPPP participants are recorded, the expense for the impairment shall be reflected in as incurred Medicare Part D prescription drug claims in the statutory income statement.

Out-of-Pocket MPPP Pharmacy Payments

25. When the Part D plan sponsor pays out-of-pocket drug claims to the pharmacy, a claims expense, a contra claims expense, and a contra claims expense account recoverable may be recorded. The contra claims expense, or similar mechanism, could be recorded to prevent initial claims expense recognition in the income statement so there is zero initial impact to the income statement. This is because there is an amount recoverable from the MPPP participant, and to the extent that the MPPP participant pays in full, there should not be any claims recognition. This is analogous to the handling of anticipated pharmaceutical rebates or anticipated subrogation recoveries.

26. If the MPPP participant pays the amount due in full, there will be no income statement impact in claims expenses resulting from the Part D plan sponsor's payment of the MPPP participant's out-of-pocket costs to the pharmacy which would thus have been offset by subsequent monthly payments by the MPPP participant to the Part D plan sponsor. In such cases, the MPPP recoverable will be reduced as payments are collected and there would be no income statement impact.

27. If the MPPP participant's balance is not repaid in whole or in part, there will be an income statement impact to reflect paid claims to the extent of the MPPP balance at the time that the balance is recognized as impaired and written off. Since there is a recoverable from the MPPP participant, there should be no income statement amount for an incurred claim until the related MPPP recoverable is written off for impairment.

28. When the recoverable from the MPPP participant is impaired, the contra claims expense is decreased by the amount of the recoverable that is written off. This results in the incurred Medicare prescription claim reported reflecting the uncollectible recoverable from MPPP participants for statutory reporting. The premium to offset these claims is included in Medicare premium bids, so reporting the incurred uncollectible MPPP amounts as losses allows the statutory accounting loss ratio to reflect incurred Medicare Part D prescription costs which include MPPP uncollectible amounts which have been impaired and written off.

Administrative Costs

29. Other costs, e.g., those incurred by Part D plan sponsors in implementing and administering MPPP program and related collections, are included in the administrative expenses of the Part D plan sponsor and are not included in the claim expenses or claim adjustment expenses.

MLR Reporting Difference

30. Note that the reporting of the uncollectible (impaired) recoverable from MPPP participants in Medicare prescription claims is different from CMS treatment of such amounts in the MLR. The CMS requires Part D plan sponsors to report losses from impairments of uncollectible recoverables from MPPP participants as administrative amounts. These administrative amounts are included in the denominator of the MLR by CMS.

INT 24-02T Status

3. This interpretation is tentatively effective March 30, 2025.

4. Further discussion is planned.

Appendix 1 - Illustrative Journal Entries

Medicare Prescription Payment Plan Scenarios			
	Claims	**Receivable**	**Cash**
Initial entries for all scenarios *Assumed to have been recorded by the Part D plan sponsor prior to Scenarios 1 – 3.*			
DR Claims Expense *To represent claims expense incurred on behalf of the MPPP participant.*	$ 2,000		
CR Cash *To represent the $2,000 paid by the Part D plan sponsor to the pharmacy on behalf of the MPPP participant.*			$ (2,000)
DR Healthcare Receivable *To represent the amount due to the Part D plan sponsor from the MPPP participant, which the MPPP participant must pay over the policy term.*		$ 2,000	
CR Claims A/R (contra-claims expense) *To be reported within the claims expense line, essentially a contra-claims expense, and represents the amount due to the Part D plan sponsor from the MPPP participant which the MPPP participant must pay over the policy term. This offsets the claims expense amount, so results in a current net $0 impact to the income statement, but both the DR and CR on the income statement are in claims expense.*	$ (2,000)		
Scenario 1 - The MPPP participant pays their full amount of $2,000 to the Part D plan sponsor.			
DR Cash T*o record receipt of the MPPP participant's payment in full.*			$ 2,000
CR Healthcare Receivable *The net income statement impact remains at $0, because the original claims expense was offset by the contra-claims expense (Claims A/R), and since the full $2,000 was received from the MPPP participant, there are no further income statement journal entry impacts.*		$ (2,000)	
Scenario 1 Net result on Financial Statements	**$ -**	**$ -**	**$ -**
Scenario 2 - The MPPP participant pays $1,500 out of the $2,000 to the Part D plan sponsor and doesn't pay the remaining $500.			
DR Cash T*o record receipt of MPPP participant partial payment of outstanding balance.*			$ 1,500
CR Healthcare receivable *To reduce MPPP participant receivable for amounts paid.*		$ (1,500)	

DR Claims A/R (contra-claims expense) *To represent the write-off of the receivable. This results in the Part D plan sponsor having a total income statement impact debit to claims expense of $500, represented as the initial $2,000 claims expense for the out-of-pocket paid to the pharmacy by the Part D plan sponsor, offset by the $1,500 received from the MPPP participant.*	$ (500)		
CR Healthcare receivable *To write off the remaining uncollectible amount as impaired*		$ (500)	
Scenario 2 Net result on Financial Statements	**$ 500**	**$**	**$ (500)**
Scenario 3 - The MPPP participant does not pay any of the $2,000 owed to the Part D plan sponsor.			
DR Claims A/R (contra-claims expense) *To represent the write-off of the amount anticipated to be paid by the MPPP participant. This results in the income statement impact to the Part D plan sponsor being a debit of $2,000, for the amount paid to the pharmacy by the Part D plan sponsor and not reimbursed by the MPPP participant.*	$ 2,000		
CR Healthcare receivable *To represent the write-off of the $2000 receivable.*		$ (2,000)	
Scenario 3 Net result on Financial Statements	**$ 2,000**	**$ -**	**$ (2,000)**