Attachment 15

Statutory Accounting Principles (E) Working Group
May 20 Interim Meeting
Comment Letters Received

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TRINIDAD NAVARRO
INSURANCE COMMISSIONER

April 29, 2021

Dale Bruggeman
Chair, Statutory Accounting Principles (E) Working Group
National Association of Insurance Commissioners

Re: INT 21-01T: Accounting for Cryptocurrencies; Exposure Ref #2021-05

Dear Chairman Bruggeman:

On behalf of Insurance Commissioner Navarro, please accept this letter as a recommendation that the Statutory Accounting Principles (E) Working Group (SAPWG) expand the scope of Exposure 2021-05 regarding INT 21-01T to consider the investment in cryptocurrency mutual funds by insurers. Thus far, the exposure is limited to insurers directly investing in cryptocurrencies. The exposure should expand to consider investments in mutual and other securities funds that may have cryptocurrencies within their portfolios.

Today there are approximately 4,000 different cryptocurrencies available on about 200 different cryptocurrency exchanges. Cryptocurrencies have seen significant price volatility and have experienced an extreme increase in value over the past year, with the value of total outstanding cryptocurrencies nearing $1 trillion as of February 2021. The Delaware Insurance Department's captive insurance program already has captive insurers investing in such funds. If captive insurers are doing so, it is very possible that commercial insurers are either already or considering doing the same.

SAPWG determined that if an insurer directly invests in cryptocurrencies, the investment is non-admitted under statutory accounting because cryptocurrencies are not cash under Statement of Statutory Accounting Principles (SSAP) No. 2R.[1] Cryptocurrencies are not cash

[1] National Association of Insurance Commissioners (March 2021), Statutory Statement of Accounting Principles No. 2R - *Cash, Cash Equivalents, Drafts, and Short-Term Investments.*

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under this SSAP because cryptocurrencies are not a medium of exchange that a bank or other similar financial institution will accept for deposit and allow an immediate credit to the depositor's account.

The SAPWG's decision to only consider insurers directly investing in cryptocurrencies and not indirect investments via mutual funds reveals an important distinction between what is an admitted versus non-admitted asset. SSAP No. 30R[2] does not limit an insurer's investments in mutual funds. Specifically, paragraph 4(c) includes Securities and Exchange Commission (SEC) registered funds regardless of the fund's mix or type of securities owned. If the mutual fund is not SEC registered, per SSAP No. 48[3] the investment receives treatment as a joint venture. Consequently, an insurer may indirectly invest in cryptocurrencies through a mutual fund and hold the investment as an admitted asset.

The use of cryptocurrencies is evolving. PayPal now allows users to buy, sell and hold some cryptocurrencies, but it is important to note that PayPal is not recognized as a bank. In addition to Bitcoin, some banks have shown interest in stablecoins, which trade like cryptocurrencies but are pegged to existing government-backed currencies, such as the U.S. dollar. Because the Delaware Insurance Department has experience with this evolution via captive insurers investing in cryptocurrency funds, it offers its experience to assist the working group. Captive insurers typically adopt Generally Accepted Accounting Principles (GAAP) as opposed to Statutory Accounting Principles for financial reporting. Accordingly, captive insurers report mutual fund investments at market value under GAAP. Despite this significant accounting difference, there is commonality between captive and commercial insurers for how they may invest in cryptocurrencies.

Thank you for considering this letter and the Delaware Insurance Department looks forward to assisting the SAPWG.

Sincerely,

Steve W. Kinion
Director

[2] National Association of Insurance Commissioners (March 2021), Statutory Statement of Accounting Principles No. 30R – *Unaffiliated Common Stock.*
[3] National Association of Insurance Commissioners (March 2021), Statutory Statement of Accounting Principles No. 48 – *Joint Ventures, Partnerships, and Limited Liability Companies.*

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April 30, 2021

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
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RE: Items Exposed for Comment by the Statutory Accounting Principles Working Group on March 15, 2021 with Comments due April 30, 2021

Dear Mr. Bruggeman:

Interested parties appreciate the opportunity to comment on the exposure drafts released for comment by the NAIC Statutory Accounting Principles (E) Working Group (the Working Group). We offer the following comments:

Ref #2020-36: Derivatives Hedging Fixed Indexed Products

On November 12, 2020, the Working Group moved this item to the active listing, categorized as substantive, and exposed the agenda item to solicit comment from state insurance regulators and industry on establishing accounting and reporting guidance for derivatives hedging the growth in interest for fixed indexed products. In addition to the two general options presented in the agenda item, the Working Group is open for additional commentary and suggestions, and directed NAIC staff to work with industry throughout the process similar to the collaborative efforts that occurred when developing the guidance in *SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees*. With this exposure, notification to the Life Actuarial (E) Task Force will occur.

On March 15, 2021, the Working Group re-exposed this agenda item to provide additional time for interested parties to develop a proposal. NAIC staff will work with interested parties in the interim to discuss this agenda item and potential options.

Interested parties would like to thank the Working Group for the opportunity to comment on the exposed Ref #2020-36, Derivatives Hedging Fixed Indexed Products.

We continue our work assessing the proposal and evaluating potential variances to the exposure.

As noted in 2020-36, "With this exposure, notification to the Life Actuarial (E) Task Force (LATF) will occur". We would request that a referral be made to LATF, as to whether there is interest in changing the reserve framework to accommodate the derivative approach as this may influence our view on the approach to recommend.

Interested parties are committed to working with NAIC staff and SAPWG on this very complicated and important topic, so far meeting with NAIC staff to share initial views

Ref #2020-37: Separate Account – Product Identifiers

On November 12, 2020, the Working Group moved this item to the active listing, categorized as nonsubstantive, and exposed the agenda item to solicit comments from state insurance regulators and industry regarding the degree of product identifying details needed to adequately assess the product features and reserve liabilities in the separate account. In particular, feedback was requested on how to obtain increased product identifier reporting granularity in question 1.01 (product mix) of the separate account general interrogatories (GI 1.01). Additionally, feedback was requested regarding if a threshold should be established for when aggregate reporting would be permitted.

On March 15, 2021, the Working Group exposed this agenda item with details of a proposed blanks change, which was also concurrently exposed with the Blanks (E) Working Group. With the proposed blanks changes, there were no proposed revisions to statutory accounting principles.

Consideration of this item will occur during an interim call so that the blanks changes may be reflected in the statutory financials for year-end 2021. Pursuant to this agenda item and regulator comments received, the Working Group is sponsoring blanks agenda item (2021-03BWG) to modify the current General Interrogatory instructions and require that a distinct disaggregated product identifier be used for each product represented. The disaggregation will require that each separate account product filing or policy form be separately identified. For example, if a company has 5 different separate account group annuities, each annuity shall be separately reported. Additionally, the instructions will indicate that companies may eliminate proprietary information (e.g., such as XYZ company Pension Plan), however such elimination will still require the use of a unique reporting identifiers (such as PRT #1). This disaggregation of reporting will be utilized for all applicable General Interrogatories (e.g., 1.01, 2.4, 4.1) and was at the direct request of regulators and will assist in regulator review so that each product, primarily those in which may potentially expose the general account to funding risk, may be independently examined.

NAIC staff also noted that there is inconsistency in the current reporting of the separate account general interrogatories, as some companies aggregate based on overall product type and other companies already include a disaggregation of all separate account products. With the clarification that "each product" shall be captured, the regulators will have the information necessary to complete assessments and improve consistency in reporting.

Interested parties supports the re-exposure to add pension risk transfer (PRT) and registered indexed linked annuity (RILA) product totals in the interrogatory and with the disaggregation required for each separate account product filing to be separately identified.

Ref #2020-38: Pension Risk Transfer – Separate Account Disclosure

Working Group exposed this agenda item with details of a proposed blanks change, which will also be concurrently exposed with the Blanks (E) Working Group. With the proposed blanks changes, there are no proposed revisions to statutory accounting principles.

Consideration of this item will occur during an interim call so that the blanks changes may be reflected in the statutory financials for year-end 2021. Pursuant to this agenda item and regulator comments received, the Working Group is sponsoring blanks agenda item (2021-03BWG) to modify the current General Interrogatory instructions and require that a distinct disaggregated product identifier be used for each product represented. The disaggregation will require that each separate account product filing or policy form to be separately identified. For example, if a company has 5 different separate account group annuities, each annuity shall be separately reported. Additionally, the instructions will indicate that companies may eliminate proprietary information (e.g., such as XYZ company Pension Plan), however such elimination will still require the use of a unique reporting identifiers (such as PRT #1). This disaggregation of reporting will be utilized for all applicable General Interrogatories (e.g., 1.01, 2.4, 4.1) and was at the direct request of regulators and will assist in regulator review so that each product, primarily those in which may potentially expose the general account to funding risk, may be independently examined.

NAIC staff also notes that there is inconsistency in the current reporting of the separate account general interrogatories, as some companies aggregate based on overall product type and other companies already include a disaggregation of all separate account products. With the clarification that "each product" shall be captured, the regulators will have the information necessary to complete assessments and improve consistency in reporting.

The blanks proposal includes a distinct disaggregated product identifier to be used for each product and shall be used consistently throughout the interrogatory. Disaggregation of reporting shall be such that each product filing or policy form is separately identified. For example, if a company has 5 different separate group annuities, each annuity shall be separately reported. (Companies may eliminate proprietary information however such elimination will require the use of unique reporting identifiers).

Interested parties supports the re-exposure, noting that it will provide additional detail for pension risk transfer (PRT) products in the General Interrogatories.

Ref #2021-01: *ASU 2021-01, Reference Rate Reform*

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed temporary (optional) expedient and exception interpretative guidance, with an expiration date of December 31, 2022. These optional expedients would expand the current exception guidance provided by *INT 20-01: ASU 2020-04 – Reference Rate Reform*. With this guidance, derivative instruments affected by changes to interest/reference rates because of reference rate reform (regardless of whether they reference LIBOR or another rate that is expected to be is discontinued), in which are used for discounting, margining or contract price alignment would be in scope of the exception guidance afforded in INT 20-01. This exception would allow for continuation of the existing hedge relationship and thus not requiring hedge dedesignation.

Interested parties agree with the revisions proposed in INT 20-01 to address related FASB guidance in ASU 2021-01 and we believe that it will provide significant relief to all companies that have entered into contracts that reference LIBOR (or another reference rate expected to be discontinued due to reference rate reform).

Other Comments

During the reference rate reform period there has been discussion amongst industry participants related to derivative contract modification market mechanisms and the potential unique impact on statutory accounting. Although the overarching principle of ASU 2020-04 and ASU 2021-01 and thus INT 20-01 is that contracts within scope that are modified due to reference rate reform can be accounted for as a continuation of the existing contract, the guidance only specifically addresses derivatives in the context of qualifying hedging relationships. Neither derivatives used in hedging relationships that do not qualify for hedge accounting (i.e., non-qualifying relationships) nor replication (synthetic asset) transactions (RSAT) are specifically addressed.

Addressing modifications associated with derivatives used in non-qualifying relationships or RSATs is not necessary for generally accepted accounting principles (GAAP) because under GAAP these transactions are always accounted for at market value and both unrealized and realized gains/losses are recorded within the same income statement line. Under SAP, however, gains/losses on these transactions may have different financial statement geography or may not be recognized in the income statement, for example, depending on whether they are unrealized or realized. Further, statutory reporting guidance requires detailed disclosure, through Schedule DB, of each held and terminated derivative transaction.

Exacerbating the need for clarity on this issue is the standard market mechanism for centrally cleared swaps. While bilateral derivative contracts can be amended without termination, it is typical market convention that a cleared derivative contract would be terminated and replaced with an off-market contract in order to amend terms associated with reference rate reform. Without relief, it is standard practice that these amendments would be treated as terminations within statutory accounting and reporting, with resulting impacts on the financial statements.

Although interested parties believe it is the intention of the Working Group and NAIC staff to allow all derivative contract amendments, including non-qualifying relationships and RSATs, associated with reference rate reform to be accounted for and reported as continuations under INT 20-01, we request that clarifying language be included to address the concern of industry participants. We believe this addition will provide statutory accounting and reporting clarity and ensure operational relief for all derivatives as companies plan and begin reference rate modifications.

We believe the most effective way to provide this requested clarity is the addition of the following language as subsection "e" within section 12 of the exposed revision to INT 20-01(changes noted in underline):

> For all derivatives (those qualifying for hedge accounting, those that do not qualify for hedge accounting and RSAT's), allow a reporting entity to account for and report modifications (that <u>are within</u> the scope of INT 20-01) as a continuation of the existing contract even when the legal form of the modification is a termination of the original <u>contract</u> and its replacement with a new reference rate reform contract. This includes in-scope modifications of centrally cleared swap contracts whether they are <u>automatically transitioned at a cessation date or voluntarily executed prior to cessation</u>.

We believe this additional language within INT 20-01 will provide statutory accounting and reporting clarity to companies as they prepare and begin to transition both bilateral and cleared derivatives as part of reference rate reform.

Ref #2021-02: ASU 2020-08 – Premium Amortization on Callable Debt Securities

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to *SSAP No. 26R—Bonds* to reject *ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs* for statutory accounting. While ASU 2020-08 closely mirrors existing guidance in SSAP No. 26R (amortizing applicable debt premium to the next effective call price), it does preclude statutory accounting's yield-to-worst concept, which requires amortizing premiums to the call or the maturity value/date which produces the lowest asset value. There may be scenarios, for statutory accounting, in which premiums amortized to the maturity value/date will yield a lower asset value than simply amortizing applicable premium to the next effective call date (as is required in ASU 2020-08).

Interested parties support the rejection of ASU 2020-08 as insurers are using the yield-to-worst concept for statutory reporting.

Ref #2021-03: SSAP No. 103R – Disclosures

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* to propose 1) new disclosure elements, and 2) a data-capture template for existing disclosures in SSAP No. 103R to capture disclosures for when a reporting entity has transferred (or sold) assets but still retains a material participation. A blanks proposal is anticipated to be concurrently exposed.

Interested parties thank NAIC staff for working with us in clarifying the purpose of the proposal and the requirements themselves. It was very good collaboration and we support the revised draft.

Ref #2021-04: SSAP No. 97 – Valuation of Foreign Insurance SCAs

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed the intent to move this agenda item to the disposal listing without statutory edits. Industry is requested to submit comments on any prevalent examples of a negative equity valuation in a foreign insurance subsidiary, controlled or affiliated (SCA) investment with detailed information for assessment.

As described in the exposure draft, the Working Group does not believe that any changes to SSAP No. 97 are necessary at this point. As such, the reporting entity should record negative equity in an 8.b.iv foreign insurance subsidiary if negative equity arises from the application of the SSAP No. 97 paragraph 9 adjustments even if there is no financial guarantee or commitment by the reporting entity. This approach applies the same treatment to 8.b.iv foreign insurance subsidiaries and 8.b.ii non-insurance subsidiaries.

As stated in our previous comment letter on this topic dated September 18, 2020, interested parties agree with the current accounting guidance, which requires 8.b.ii entities to report negative equity. This is because 8.b.ii entities are considered an extension of the insurance company and since 8.b.ii entities may own assets that would not be admitted if owned by the insurer, it is reasonable to require the insurer to report negative equity in those subsidiaries if negative equity arises due to the non-admission of certain assets.

Interested parties, however, do not agree that the application of the paragraph 9 adjustments should ever result in the insurer's investment in a foreign insurance subsidiary being reported at an amount less than zero. Foreign insurance subsidiaries have a true business purpose, independent from the parent insurer and are subject to significant regulations in the foreign jurisdiction in which they operate (including with respect to how they invest, the assets they are allowed to own, and the amount of capital they are required to hold). In this way, foreign insurance subsidiaries operate similarly to domestic insurance subsidiaries, and are subject to comparable levels of oversight. It does not appear reasonable to treat a foreign insurance subsidiary differently from the way a domestic insurance subsidiary is treated whereby losses are floored at zero unless the reporting entity has guaranteed obligations or is otherwise committed to provide further financial support for the domestic insurance subsidiary, as stated in SSAP No. 97, paragraph 14e.

We agree with the comments included in the exposure draft regarding the fact that in the past few years, there probably have not been instances of insurers recording negative equity in their foreign insurance subsidiaries. However, we believe that regardless of whether or not this is a common occurrence, the accounting standards should reflect the appropriate accounting treatment and provide guidance for this circumstance, which might arise in the future. As mentioned in our previous comment letter, negative equity could arise due to the non-allowance of deferred acquisition costs recorded by the foreign insurer. Since GAAP allows the explicit recognition of a DAC asset, the gross GAAP reserves are usually higher than statutory reserves, which have an implicit credit for acquisition expenses. As a result, when applying the SSAP No. 97 adjustments to non-admit DAC, we end up with a reserve that is more conservative than statutory rules. One of the reasons why this has not resulted in negative equity in the past is due to the current interest rate environment, which has caused most insurers' fixed income portfolios to be in a sustained unrealized gain position. If interest rates rise and these unrealized gains reverse out over time, it will likely result in a negative equity position.

Assuming rates stay as low as they are today, negative equity will also be very likely to occur once a foreign insurer uses the new U.S. GAAP standard on long-duration insurance contracts in the paragraph 8.b.iv valuation, since insurance liabilities will increase due to the required market value adjustment under the new standard. Under this scenario, having to report insurance liabilities at market value will then negate any unrealized gains on an insurer's bond portfolio. This change will go into effect in 2025 for non-public life insurance companies.

Finally, not all foreign insurance companies receive audited GAAP financial statements. In these situations, the investment in the foreign insurance subsidiary (cost basis) is non-admitted, and no results are reflected in surplus until the foreign insurance company distributes earnings to the parent insurance company. If a parent insurance company decides to obtain an audit of its foreign insurance company, it should not result in an impact to surplus that is worse than non-admitting the investment.

We are able and willing to work with NAIC staff to draft potential amendments to SSAP No. 97 to modify the accounting and reporting requirements of foreign insurers to address the negative equity issue.

Ref #2021-05: Accounting for Cryptocurrencies

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed the interpretative guidance in *INT 21-01T: Statutory Accounting Treatment for Cryptocurrencies* to clarify that cryptocurrencies do not meet the definition of cash in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* and are nonadmitted assets for statutory accounting. With the exposure, information from industry is requested per the above recommendation.

Interested parties would like to thank the Working Group for the opportunity to comment on Reference No. 2021-05 – *Accounting for Cryptocurrencies* and related INT 21-01T: *Statutory Accounting Treatment for Cryptocurrencies*, (together the "Exposure").

Interested parties agree that cryptocurrencies (e.g., Bitcoin) currently do not meet the definition of cash under SSAP No. 2R *Cash, Cash Equivalents, Drafts, and Short-Term Investments*. However, based on our understanding of how cryptocurrencies work, we believe that cryptocurrencies do meet the definition of an asset. As stated in SSAP No. 4 *Assets and Non-Admitted Assets*, an asset is defined as "having future economic benefits obtained or controlled by a particular entity as a result of past transactions or events." Cryptocurrencies certainly have a future economic benefit as this asset can be sold for cash or exchanged for goods and services in markets that accept cryptocurrencies as payment. In addition, to be an admitted an asset, an asset needs to be readily marketable. Interested parties note that there is an active market for cryptocurrencies as they can be purchased and/or redeemed in an open market at readily determinable fair values.

Based on interested parties' understanding, the overall extent of direct and indirect cryptocurrency ownership is unknown. We do not believe that insurers are directly investing in cryptocurrencies, nor are we aware of any companies that are currently transacting with cryptocurrencies for goods or services. However, we are aware of a very small number of insurers that are currently considering whether to directly hold cryptocurrency for purposes of investment. In addition, some companies have indicated they are interested in potentially using cryptocurrencies to transact business in the future.

Most insurers' involvement in this asset class so far seems to be limited to investments in private funds set up as limited partnerships/limited liability companies, which invest in cryptocurrency. The funds, for U.S. GAAP purposes, are generally classified as investment companies. Therefore, these funds carry their investments at fair value, and the carrying value under the statutory equity method is essentially fair value. Since the reporting entity's investment is held by a fund, the investment also results in an equity-based capital charge.

The general level of interest for future investment is difficult to gauge, however, based on what's transpiring in the financial services market and beyond, cryptocurrencies continue to gain mainstream traction as an investment[1] and accepted medium of exchange[2], with Bitcoin being the predominant cryptocurrency chosen. The level of interest for holding or transacting with cryptocurrencies may increase as blockchain technology applications are developed and deployed in the years to come. Interest may also increase as companies look to diversify their portfolios. Bitcoin can potentially be a good source of diversification as so far bitcoin appears not to have a strong correlation with the performance of other assets that are impacted by interest rate movements and government regulation for example. In addition, bitcoin may act as an inflation hedge. The supply of traditional currencies is set by a central bank or a similar institution that can run the printing presses, which can cause hyperinflation caused by the printing of too much money. In contrast, the supply of Bitcoin is set as strong incentives provide assurances that there will likely be no more than 21 million bitcoin ever created.

Ref #2021-06: NAIC Accounting Practices and Procedures Manual Editorial and Maintenance Update

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed editorial revisions to *SSAP No. 53—Property Casualty Contracts, SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* and the SSAP Glossary.

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[1] https://www.cnbc.com/2021/03/31/bitcoin-goldman-is-close-to-offering-bitcoin-to-its-richest-clients.html

[2] https://www.reuters.com/article/us-crypto-currency-visa-exclusive/exclusive-visa-moves-to-allow-payment-settlements-using-cryptocurrency-idUSKBN2BL0X9

Interested parties have no comment on the revisions.

Ref #2021-07: *ASU 2020-11, Financial Services—Insurance: Effective Date and Early Application*

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to *Appendix D—Nonapplicable GAAP Pronouncements* to reject *ASU 2020-11, Financial Services – Insurance: Effective Date and Early Application* as not applicable for statutory accounting.

Interested parties have no comment on this item.

Ref #2021-08: *ASU 2021-02, Franchisors—Revenue from Contracts with Customers (Subtopic 952-606)*

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to *SSAP No. 47—Uninsured Plans* to reject *ASU 2021-02, Franchisors – Revenue from Contracts with Customers.*

Interested parties have no comment on this item.

Ref #2021-09: State ACA Reinsurance Programs

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*. The revisions include State ACA reinsurance programs which are using Section 1332 waivers in scope of SSAP No. 107 and will provide guidance to follow the hybrid accounting approach for the state ACA programs as they operate in a similar manner.

In summary, the view of interested parties is that the principles underlying the exposure draft are appropriate. However, there are important variances among the state ACA Reinsurance Programs as to how they are funded and operate, much more so than was apparently contemplated in the drafting of the proposed guidance in the exposure draft. The significance of such variances requires additional context and guidance to assure that health plans report activity related to any particular state's ACA Reinsurance Program in a consistent manner. These points are described below, along with suggestions for such additional context and guidance for Working Group's consideration.

The proposed guidance suggested by the exposure draft is largely prefaced on the following statement therein (emphasis added):

> To date, most of the states that have sought 1332 waivers did so to implement state ACA reinsurance programs which have the goal of using the reinsurance programs to lower individual health insurance premium in the jurisdiction. <u>As these programs seek to</u>

> operate to cover higher individual health claims in a manner similar to the transitional reinsurance program, the initial recommendation is to provide guidance that such state programs should follow the guidance in SSAP No. 107 to the extent the state program has similar terms.

While interested parties agree that the goal of the various state ACA Reinsurance Programs is to lower individual health insurance premiums, the second sentence in the above passage is based on a faulty premise. In fact, the various state ACA Reinsurance Programs aim to achieve that goal in ways that differ operationally in important ways, not just from the former Federal ACA Reinsurance Program, but also from each other.

As a result of those differences, it would be difficult to apply the guidance as proposed in the exposure draft which largely mirrors the current text in SSAP No. 107 applicable to the former Federal ACA Reinsurance Program to the State ACA Reinsurance Programs. It is likely that different health plans could reach different conclusions on how to report any particular state's ACA Reinsurance Program activity notwithstanding a common set of facts and circumstances about how that state's program operates. Likewise, independent auditors and state examiners could also reach different interpretations and conclusions.

This is not to suggest that the principles from SSAP No. 107 which the exposure draft proposes to apply as well to state ACA Reinsurance Programs are necessarily flawed, rather that additional context and guidance is needed to assure that statutory accounting will be more uniformly applied by health plans with respect to the same facts and circumstances involving a particular state's ACA Reinsurance Program.

For the former Federal ACA Reinsurance Program, SSAP No. 107 recognized that additional guidance was needed, noting that:

> "… the term "reinsurance" does not represent actual reinsurance between licensed insurers as defined by *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*. This program is similar to an involuntary pool in *SSAP No. 63—Underwriting Pools* for the individual insured health products subject to the 2014 ACA market reforms."

Despite the failure of the former Federal ACA Reinsurance Program to clearly meet all the requirements of SSAP No. 61R or SSAP No. 63, SSAP No. 107 nonetheless included clarifying language to deem certain aspects of the program to be reinsurance and to be accounted for as such for statutory reporting. With subject health plans participating in a single federal program for which No. SSAP No. 107 deemed the activity as reinsurance, uniformity in reporting by health plans was more assured.

However, uniformity in reporting by health plans for their activity with the various state ACA Reinsurance Programs would not be similarly assured under the current text of the exposure draft, as each such state plan differs from the former Federal ACA Reinsurance Program – as well as from each other – in various ways. Some examples of those operational differences follow:

- Unlike the former Federal ACA Reinsurance Program, many of the state ACA Reinsurance Programs charge a single assessment that funds many other elements of healthcare affordability within the state and administration of the program, in addition to funding the reinsurance program itself. Other states may fund their program through use of existing premium taxes and have appropriated certain amounts within the state's general fund to support the reinsurance program and its administration.
- The foregoing differences in funding sources also result in differences in the amount of funding for a state's ACA Reinsurance Program that is ultimately paid by the participating health plans. In most cases, participating health plans fund a minority of the total program costs. For some state ACA Reinsurance Programs, none of the cost is borne by participating health plans. An anomalous outcome therefore is where a health plan pays very little if any of the state ACA Reinsurance Program's cost, includes no provision for such cost in its rates, and therefore does not report any premium that it could "cede" but nonetheless reports ceded claims.
- For some state ACA Reinsurance Programs, the state does not itemize the use of assessments. Application of the current proposed guidance may therefore be operationally onerous for organizations and, in some cases, may not be possible without the state providing a specific itemization of the use of the assessments. This may cause health plans to have to estimate the ceded portion versus the expense portion of payments resulting in unintended diversity in practice in treatment for the assessments, potentially reducing comparability in reporting across health plans with respect to their participation in the same state ACA Reinsurance Program.
- The assessments or fees charged are to fund more than just the reinsurance program (distributions and administration of the program); they may also include amounts related to other affordability initiatives.
- The attachment points, coinsurance, and payment caps may be more favorable to the insurer than that of the federal program particularly in the context where the fees might be lower (because the fee charged pay for more than the reinsurance program, or the fact there may be no fee at all).

SSAP No. 107, as well as the current text of the exposure draft, provides principle-based guidance that is intended to help health plans determine which of the following accounting treatments is appropriate, depending on the facts and circumstances:

- As a reinsurance cession following reinsurance accounting in accordance with *SSAP No. 61R, Life, Deposit-Type and Accident and Health Reinsurance*
- As an involuntary assessment consistent with *SSAP No. 35R, Guaranty Fund and Other Assessments*

- As an assessment made on behalf of self-insured plans which are administered by the reporting entity following the guidance of *SSAP No. 47—Uninsured Plans*

Interested parties support a similar conceptual structure to determine the appropriate statutory accounting treatment for state ACA Reinsurance Programs. However, and as a practical matter based on what is known about such programs currently in effect, reinsurance accounting would not seem to be appropriate in most cases. This is because relatively little of the cost is paid by health plans for most of the state ACA Reinsurance Programs (even zero in some cases).

That would leave as remaining options either accounting pursuant to SSAP No. 35R (assessment) or SSAP No. 47 (uninsured plan). However, for some state ACA Reinsurance Programs, the facts and circumstances may not be sufficiently clear to determine which of those would necessarily be appropriate, e.g., in the case of a state ACA Reinsurance Program for which the funding is used for a variety of health-related initiatives and which would vary by nature and amount each year based on legislative action.

As a result, it may be appropriate for the text in the exposure draft to be amended to include additional context and guidance. AHIP offers the following suggestions for the Working Group's consideration:

- Additional context to inform readers as to the nature, extent, and significance of the various ways in which state ACA Reinsurance Programs differ from the former Federal ACA Reinsurance Program, as well as from each other.
- Section 1332 Waivers should be reviewed by health plans and their auditors to see if traditional reinsurance under SSAP No. 61R would apply. Again, based on the operational aspects of the state ACA Reinsurance Programs currently in place, reinsurance accounting would not appear to be appropriate in most instances.
- If it is determined that reinsurance accounting criteria is not met, then a determination should be made as to whether the guidance of SSAP No. 47 for uninsured plans (e.g., like that under INT 05-05 for Medicare Part D), or of SSAP No. 35R (assessment reporting) would apply.
- In cases where reinsurance accounting is then not deemed appropriate, and where the facts and circumstances do not clearly indicate which of SSAP No. 35R or SSAP No. 47 should apply, include a default provision as to which of those should then apply (e.g., SSAP No. 35R). The assessments under the state ACA Reinsurance Programs are generally unavoidable if the insurer writes business within the state which is more characteristic of a business tax or similar assessment. Insurers are generally required to reduce their rates if the state reinsurance programs are in effect, and therefore, recording all of the assessment to expense is unlikely to meaningfully distort any underwriting ratios.

Timing and recognition of assessments. The updates in SSAP No. 107 currently do not address the timing of accounting recognition for the assessments. Because state ACA Reinsurance

Programs vary operationally as described above, assessments may be charged such that the current year assessment is based on prior year premiums (i.e., a premium-based assessment); this could lead to diversity in practice if health plans operating in the same state have varying views of when to recognize the assessment in the absence of specific guidance.

Additional guidance could be provided to clarify when the assessment should be recognized and recorded, e.g., by referencing within SSAP No. 107 the accounting model in SSAP No. 35R, paragraph 4a-c, and providing clarity as to how to apply the recognition criteria to the State Reinsurance assessments.

Treatment of receivables from state-based reinsurance plans as admitted assets. Under the former federal reinsurance program, SSAP No. 107 provided the following guidance:

> "All receivables from the transitional reinsurance program are subject to the 90-day non-admission rule beginning from when program receivables are due to be disbursed by the government or a government-sponsored entity. That is, the 90-day rule begins when governmental receivables are due, not from the date of initial accrual. The announced governmental or government-sponsored entity distribution date shall be the contractual due date similar to Appendix A-791, paragraph 2.h., which requires that payments due from the reinsurer are made in cash within ninety (90) days of the settlement date. The receivable is also subject to impairment analysis."

Since most of the existing state ACA Reinsurance Programs are funded by large measure based on state budgetary authority, similar guidance should apply to receivables from such programs.

*　　*　　*

Thank you for considering interested parties' comments. If you have any questions in the interim, please do not hesitate to contact us.

Sincerely,

D. Keith Bell　　　　Rose Albrizio

cc: NAIC staff
Interested parties

New York Life Insurance Company
51 Madison Avenue, New York, NY 10010

April 30, 2021

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: New York Life's Comments on Item 2021-04 *SSAP No. 97 – Valuation of Foreign Insurance SCAs*

Dear Mr. Bruggeman:

New York Life ("NYL") appreciates the opportunity to provide comments on Item 2021-04 (the "Exposure"), which was exposed by the Statutory Accounting Principles (E) Working Group (the "SAPWG") on March 15, 2021. We write to request SAPWG pursue the changes to SSAP No. 97 we detail below. We should note that we recognize amending SSAP No. 97 could bring potential unintended consequences. With that in mind, while we offer some suggested language to address such issues later in this letter, we are committed to working with SAPWG on any additional language changes deemed necessary.

As described in the Exposure, SAPWG does not believe that any changes to SSAP No. 97 are necessary at this point. As such, the reporting entity should record negative equity in an 8.b.iv foreign insurance subsidiary if negative equity arises from the application of the SSAP No. 97 paragraph 9 adjustments even if there is no financial guarantee or commitment by the reporting entity. This approach applies the same treatment to 8.b.iv foreign insurance subsidiaries and 8.b.ii non-insurance subsidiaries.

As stated in our previous comment letter on this topic dated October 27, 2020 (attached), there are significant differences between 8.b.ii and 8.b.iv subsidiaries, which, in our view, warrant different accounting treatment. 8.b.ii entities generally operate as an extension of the insurance company and own assets that for the most part would not be admitted if owned by the insurer. In those circumstances, recording negative equity makes sense. In contrast, foreign insurance subsidiaries have a true business purpose, independent from the parent insurer, and are subject to significant regulations in the foreign jurisdiction in which they operate (including with respect to how they invest and the assets they own). In this way, foreign insurance subsidiaries operate similarly to domestic insurance subsidiaries, and are subject to comparable levels of oversight. It does not appear reasonable to treat a foreign insurance subsidiary differently from the way a domestic insurance subsidiary is treated whereby losses are floored at zero unless the reporting entity has guaranteed obligations or is otherwise committed to provide further financial support for the domestic insurance subsidiary, as stated in SSAP No. 97, paragraph 14e.

Furthermore, if the foreign insurer is solvent and has positive capital on a local statutory basis, recording negative equity only due to the SSAP No. 97 paragraph 9 adjustments does not appear to provide the right accounting result. We agree with the comments included in the Exposure regarding the fact that in the past few years, there probably have not been instances of insurers recording negative equity in their foreign insurance subsidiaries. However, just because it hasn't happened recently, does not mean it cannot happen in the future under very realistic scenarios. Accordingly, we believe the accounting standards should reflect the appropriate accounting treatment and provide guidance for this likely circumstance.

As mentioned in our previous comment letter, negative equity could arise due to the non-allowance of deferred acquisition costs ("DAC") recorded by the foreign insurer. Since GAAP allows the explicit recognition of a DAC asset, the gross GAAP reserves are usually higher than statutory reserves, which have an implicit credit for acquisition expenses. As a result, when applying the SSAP No. 97 adjustments to non-admit DAC, we end up with a reserve that is more conservative than statutory rules. One of the reasons why this has not resulted in negative equity in the past is due to the current interest rate environment, which has caused most insurers' fixed income portfolios to be in a sustained unrealized gain position. If interest rates rise and these unrealized gains reverse out over time, it will likely result in a negative equity position. We have included an example below to illustrate the sensitivity to interest rates of certain foreign insurers' fixed income portfolios. It is possible that other foreign insurers might have different interest rate sensitivity due to differences in their current GAAP equity and underlying portfolios. This example is based on a sensitivity analysis performed by NYL using certain assumptions regarding asset composition. Based on our analysis, an increase of as little as 50 basis points in the 10-year treasury rate can deplete about $200 million of unrealized gains.

Reconciliation from U.S. GAAP to statutory admitted equity (in millions)	**Admitted equity at 12/31/20**		**Assumes a 0.5% increase in the 10-year treasury rate**	**Assumes a 1.5% increase in the 10-year treasury rate**
SCA GAAP Equity*	1,300		1,100	700
Less para. 9 adjustments				
DAC	570		570	570
Other non-admitted assets	44		44	44
Goodwill	90		90	90
Adjusted Equity	**596**		**396**	**(4)**

*GAAP equity includes $900 million of unrealized gains on the foreign insurer's bond portfolio at 12/31/20

In light of the fact that negative equity can occur realistically in the near term, we believe that changes are needed to the accounting standards to address this issue. At the same time, we understand the need to protect against potential abuses that could arise if SSAP No. 97 is updated to remove the negative equity concept for a foreign insurance subsidiary. As suggested in our previous comment letter, we have crafted the below underlined language, which we would propose inserting into the last sentence of paragraph 9:

> Note that the outcome of these adjustments can result in a negative equity valuation of the investment for all 8.b.ii SCA entities. For an 8.b.iv SCA entity, the application of these adjustments will not result in negative equity unless either of the following circumstances arises:

1) The reporting entity has guaranteed obligations of the 8.b.iv SCA entity or is otherwise committed to provide further financial support for the 8.b.iv SCA entity. In this case, accounting for the equity pick-up after application of the paragraph 9 adjustments, should be based on the guidance in SSAP No. 97, paragraph 14e;
2) The 8.b.iv SCA entity provides services to, or holds assets on behalf of, the reporting entity. In this case, negative equity has to be recorded.

   Note – if there are any reinsurance transactions between the reporting entity and the foreign insurance subsidiary, the adjustments required in paragraph 8.b.iv of SSAP No. 97 must be followed.

We believe this language addresses the two competing interests described above: (1) reflect the appropriate accounting for an 8.b.iv entity and (2) prevent potential abuses from allowing an 8.b.iv entity's equity to be floored at zero. However, we are open to any other language SAPWG believes would help distinguish true operating foreign insurance subsidiaries that are independent from the U.S. insurer and have a true business purpose from entities that operate to shield the reporting entity from U.S. statutory accounting rules. Our intent is not to amend SSAP No. 97 in a way that creates loopholes – instead we want to incorporate changes that contain sufficient guardrails while also appropriately accounting for foreign insurance subsidiaries. We will be happy to work with you on re-drafting our proposal to address potential loopholes and prevent any abuses from occurring.

We would also like to take this opportunity to raise another issue related to the accounting and reporting of foreign insurance subsidiaries. Due to the high cost of implementing new U.S. GAAP standards related to credit losses and long duration insurance contracts, NYL has decided to discontinue the preparation of financial statements on a U.S. GAAP basis in 2023, which will include our Mexican subsidiary. Once that occurs, it is unclear to us which accounting basis to use to record our investment in the foreign insurance subsidiary, which would then be non-admitted since there is no U.S. GAAP audit. In that scenario, we would have to record our investment at cost or local statutory equity. To that end, we would appreciate the opportunity to engage in a conversation with you and SAPWG staff regarding the ability to potentially allow for foreign insurance subsidiaries without U.S. GAAP financial statements to be admitted and to be carried at the lower of cost or local audited statutory basis, adjusted for paragraph 9 requirements, but flooring those adjustments at zero if negative equity arises. Our understanding of the current guidance in SSAP No. 97 paragraph 8.b.iv is that we are allowed to use audited foreign statutory basis financial statements of the foreign insurer, but the foreign insurer's financial statements still need to include a reconciliation to U.S. GAAP, which means that U.S. GAAP books and records still need to be prepared.

Thank you for considering our comments on this topic. If you have any questions in the interim, please do not hesitate to contact us.

Sincerely,

Robert M. Gardner
Senior Vice President and Controller

Douglas A. Wheeler

Douglas A. Wheeler
Senior Vice President, Office of Governmental Affairs

Robert Gardner
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October 27, 2020

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: New York Life's Comments on Item 2020-18 SSAP 97 Update

Dear Mr. Bruggeman:

New York Life ("NYL") appreciates the opportunity to provide comments on Item 2020-18 (the "Exposure"), which was exposed by the Statutory Accounting Principles (E) Working Group (the "Working Group") during the NAIC 2020 Summer National Meeting.

NYL agrees with the comments provided in the September 18, 2020 Interested Party letter. This letter provides additional background on those comments as well as a potential path to resolution by suggesting wording changes that could be incorporated into SSAP No. 97 Investments in Subsidiaries, Controlled and Affiliated Entities to address the issues that have been identified.

NYL has been closely watching SAPWG's exposure of revisions to SSAP No. 97, including the most recent exposure that makes some updates to the last sentence of paragraph 9. That exposure caused us to re-examine our understanding of the SSAP and the potential for a foreign insurance subsidiary to record negative equity in the future. As expressed in the Interested Parties comment letter, we believe that it makes sense for SSAP No. 97 to differentiate in its treatment of 8.b.iv foreign insurance subsidiaries and 8.b.ii SCAs.

At a high level, 8.b.ii entities generally operate as an extension of the insurance company and own assets that for the most part would not be admitted if owned by the insurer. In those circumstances, recording negative equity makes sense. In contrast, foreign insurance subsidiaries have a true business purpose, independent from the parent insurer, and are subject to significant regulations in the foreign jurisdiction in which they operate. From our perspective, foreign insurance subsidiaries are closer to 8.b.iii subsidiaries in that they are real operating companies that are independent of the domestic insurer.

While the circumstances that could cause an insurer to record negative equity in a foreign insurance subsidiary are probably not very common, they could come to pass in the future. This could be due to the non-allowance of deferred acquisition costs recorded by the foreign insurer, while still requiring the foreign insurer subsidiary to hold the higher gross GAAP reserve that has no implicit credit for acquisition expenses that is inherent in statutory reserves. Therefore, we believe that changes are needed to prevent this situation from occurring in the future.

At the same time, we want to prevent against any potential abuses that could arise if SSAP No. 97 is updated to remove the negative equity concept for a foreign insurance subsidiary. We have therefore crafted the below underlined language, which we would propose inserting into the last sentence of paragraph 9:

Note that the outcome of these adjustments can result in a negative equity valuation of the investment for all 8.b.ii SCA entities. For an 8.b.iv SCA entity, recording negative equity depends on whether or not the parent insurer has issued a guarantee to fund losses of the 8.b.iv SCA entity or whether the 8.b.iv entity provides services to the parent or affiliated insurer. If the parent insurer has committed to fund losses of the 8.b.iv SCA entity, the accounting described in paragraph 13e should be followed. If the 8.b.iv SCA entity does not provide services to, or holds assets on behalf of, the parent insurer or affiliate, the valuation of the investment in the SCA would be floored at zero if negative equity arises due to the application of these adjustments. For an 8.b.iv SCA entity that provides services to, or holds assets on behalf of, the parent insurer or affiliate, negative equity has to be recorded due to the application of these adjustments for the total amount of the non-admitted assets used to provide services to, or held on behalf of, the parent insurer or affiliate.

We believe this language addresses the two competing interests described above. Thank you for considering our comments on this topic. If you have any questions in the interim, please do not hesitate to contact us.

Sincerely,

Robert M. Gardner
Senior Vice President and Controller

Douglas a. Wheeler

Douglas A. Wheeler
Senior Vice President, Office of Governmental Affairs