Statutory Accounting Principles (E) Working Group
Hearing Agenda
May 20, 2021
1:00 p.m. – 2:30 p.m. CT

ROLL CALL

Dale Bruggeman, Chair	Ohio	Judy Weaver	Michigan
Carrie Mears/Kevin Clark, Co-Vice Chairs	Iowa	Doug Bartlett	New Hampshire
Richard Ford	Alabama	Bob Kasinow	New York
Kim Hudson	California	Kimberly Rankin/Melissa Greiner	Pennsylvania
Kathy Belfi/William Arfanis	Connecticut	Jamie Walker	Texas
Rylynn Brown	Delaware	Doug Stolte/David Smith	Virginia
Eric Moser	Illinois	Amy Malm	Wisconsin
Stewart Guerin/Melissa Gibson	Louisiana		

NAIC Support Staff: Julie Gann, Robin Marcotte, Jim Pinegar, Fatima Sediqzad, Jake Stultz

Note: This meeting may be recorded for subsequent use.

The Statutory Accounting Principles (E) Working Group met in regulator-to-regulator session on May 4. This regulator session was pursuant to the NAIC Open Meetings Policy paragraph 3 (discussion of specific companies, entities or individuals) and paragraph 6 (consultations with NAIC staff related to NAIC technical guidance of the *Accounting Practices and Procedures Manual*). No actions were taken during this meeting - this was an informational session regarding interim progress on agenda item 2019-21, referred to as the SSAP No. 43R project.

REVIEW AND ADOPTION of NON-CONTESTED POSITIONS

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

1. Ref #2020-37: Separate Account Product Mix
2. Ref #2020-38: Pension Risk Transfer Disclosure
3. Ref #2021-02: ASU 2020-08 – Premium Amortization on Callable Debt Securities
4. Ref #2021-03: SSAP No. 103R - Disclosures
5. Ref #2021-06EP: Editorial Updates
6. Ref #2021-07: *ASU 2020-11 - Financial Services – Insurance: Effective Date*
7. Ref #2021-08: *ASU 2021-02 – Franchisors Revenue from Contracts with Customers*

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2020-37 SSAP No. 56 (Jim)	**Separate Account Product Mix**	**1 – Agenda Item**	**In Agreement**	**IP – 4**

Summary:
At the request of regulators, primarily in response to the recent growth of pension risk transfer (PRT) transactions and registered indexed linked annuity (RILA) products, improved reporting was requested so financial statement users could more readily identify and review these products, which are generally held in separate accounts. Upon review of the separate account general interrogatories in the 2019 financial statements, it was found that most

entities grouped their separate account products in 3-4 broad categories. As a result of the aggregated grouping, regulators have expressed difficulty in assessing the risk with each associated product.

Accordingly, on Nov. 12, the Working Group exposed this agenda item, primarily to solicit comments regarding the degree of product identifying details needed to adequately assess PRT and RILA product features and reserve liabilities. While this agenda item did not recommend modifications to *SSAP No. 56—Separate Accounts*, depending on the nature of the comments received, it was anticipated that a proposal would be sent to the Blanks (E) Working Group with annual statement instruction modifications regarding the separate account general interrogatories – primarily requiring disaggregation in reporting of PRT and RILA products.

On March 15, 2021, the Working Group exposed this agenda item with a concurrent Blanks (E) Working Group exposure (2021-03BWG). This exposure did not propose changes to statutory accounting however the blanks proposal added product identifiers for PRT and RILA products and provided modifications to the General Interrogatory instructions, requiring 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 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 identifier (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 to assist in regulator review so that each product (i.e., applicable transactions, guarantees and reserve assumptions), primarily products in which may potentially expose the general account to funding risk, may be independently examined.

<u>*Interested Parties' Comments:*</u>
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.

NAIC staff note – NAIC staff confirmed with interested parties via email on May 3 that the comments above support adoption.

<u>*Recommended Action:*</u>
NAIC staff recommends that the Working Group recommend 2021-03BWG for adoption by the Blanks (E) Working Group. (NAIC staff note that no comments were received by the Blanks (E) Working Group in response to the concurrent exposure). This agenda item does not result in statutory accounting revisions but adoption by the SAPWG will indicate support for the adoption at the Blanks Working Group.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2020-38 SSAP No. 56 (Jim)	**Pension Risk Transfer Disclosure**	**2– Agenda Item**	**In Agreement**	**IP - 5**

<u>*Summary:*</u>
On Nov. 12, the Working Group exposed this agenda item to solicit comments from state insurance regulators and industry regarding possible modifications to SSAP No. 56, specifically in terms of increased product identification and disclosure of pension risk transfer (PRT) transactions in the separate account financial statements. In response to the recent growth of PRT transactions, regulators expressed a desire for improved reporting so such items could

be more readily identified and analyzed. While the information request was broad, regulators discussed several possible enhancements, including separated PRT reporting and improved PRT disclosure regarding reserves, associated assets, and general account exposure.

Currently, the most specific details concerning PRT transactions are generally captured/disclosed in question 1.01 (product mix) of the separate account general interrogatories (GI 1.01). While other details of the broadly categorized products are captured in various other general interrogatories, this agenda item, at the request of regulators, proposes enhanced detailed reporting to the existing requirements for pension risk transfer products and transactions in the scope of SSAP No. 56.

On March 15, 2021, the Working Group exposed this agenda item with a concurrent Blanks (E) Working Group exposure (2021-03BWG). This exposure did not propose changes to statutory accounting however the blanks proposal added product identifiers for PRT and RILA products and provided modifications to the General Interrogatory instructions, requiring 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 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 identifier (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 to assist in regulator review so that each product (i.e., applicable transactions, guarantees and reserve assumptions), primarily products in which may potentially expose the general account to funding risk, may be independently examined.

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

NAIC staff note – NAIC staff confirmed with interested parties via email on May 3 that the comments above support adoption.

Recommended Action:
NAIC staff recommends that the Working Group recommend 2021-03BWG for adoption by the Blanks (E) Working Group. (NAIC staff note that no comments were received by the Blanks (E) Working Group in response to the concurrent exposure). This agenda item does not result in statutory accounting revisions but adoption by the SAPWG will indicate support for the adoption at the Blanks Working Group.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-02 SSAP No. 26R (Jim)	**ASU 2020-08 – Premium Amortization on Callable Debt Securities**	**3 – Agenda Item**	**In Agreement**	**IP - 7**

Summary:
On March 15, the Working Group 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. ASU 2020-08 requires that to the extent the amortized cost basis of a callable debt security exceeds the amount repayable by the issuer, any associated premium (above the call price) is to be amortized to the next effective call price/date. While the amortization requirements closely mimic existing guidance in SSAP No. 26R, it does preclude

statutory accounting's yield-to-worst concept, which requires amortizing premiums to the call or the maturity value/date in 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' Comments:
Interested parties support the rejection of ASU 2020-08 as insurers are using the yield-to-worst concept for statutory reporting.

Recommended Action:
NAIC staff recommends that the Working Group adopt the exposed nonsubstantive 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.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-03 SSAP No. 103R (Jim)	**SSAP No. 103R - Disclosures**	**4 – Agenda Item**	**In Agreement**	**IP - 7**

Summary:
This agenda item proposed additional disclosures and to data-capture certain existing disclosure elements in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*; it was drafted in response to discussions that occurred during the Working Group's continued deliberation of agenda item 2019-21: SSAP No. 43R – Equity Instruments (referred to as the SSAP No. 43R Project). Agenda item 2019-21, a substantive project to consider what investments fall within scope of *SSAP No. 43R—Loan-Backed and Structured Securities*, which was subsequently expanded to determine which investments are eligible for reporting on Schedule D-1: Long Term Bonds.

On March 15, the Working Group exposed this agenda item which proposed new disclosure elements and a data-capture template for existing disclosures in SSAP No. 103R. Consequently, a concurrent Blanks (E) Working Group (2021-05BWG) agenda item was exposed for public comment.

In response to feedback received from interested parties, on April 20, the Working Group exposed an updated agenda item, incorporating edits as jointly collaborated with Iowa regulators, interested parties and NAIC staff. While the updated exposure included minor disclosure enhancements, the primary revision included updated data-capture fields and detailed instructions to ensure filers understood the requirements of the disclosure template. Note: while an updated blanks proposal was not posted by the Blanks (E) Working Group, the updated exposed data capture template can be seen beginning on page 8 of agenda item 4.

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

Recommended Action:
NAIC staff recommends that the Working Group adopt the exposed nonsubstantive revisions to *SSAP No. 103R— Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. The revisions incorporate additional disclosure elements and a data-capture template for certain disclosures in SSAP No.

103R. The disclosures and data-capture template will assist regulators in their assessment of situations where an entity has transferred (or sold) assets but still retains a material participation in the transferred asset. The updated blanks proposal (page 8 of agenda item 4) is anticipated to be in place for 2021 year-end reporting. (In response to comments received by the Blanks (E) Working Group support staff as a result of the exposure of this agenda item, it is anticipated that minor editorial changes to the blanks proposal will occur.)

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-06EP Multiple (Jake)	**Editorial Updates**	**5 - Agenda Item**	**No Comments**	**IP - 10**

Summary:
On March 15, the Working Group exposed editorial revisions as summarized below:

- *SSAP No. 53—Property Casualty Contracts – Premiums* retitle to *SSAP No. 53—Property and Casualty Contracts – Premiums*.

- *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* - corrects grammatical errors in paragraph 54.

- SSAP Glossary - Removes the footnote noted in title and replaces it as an opening paragraph with updated verbiage.

Interested Parties' Comments:
Interested parties have no comment on the revisions.

Recommended Action:
NAIC staff recommends that the Working Group adopt the editorial revisions to SSAP No. 53, SSAP No. 97 and the SSAP Glossary as final.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-07 Appendix D (Jake)	***ASU 2020-11, Financial Services—Insurance: Effective Date and Early Application***	**6 – Agenda Item**	**No Comments**	**IP - 11**

Summary:
On March 15, the Working Group 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. ASU 2020-11 updated effective dates of recent amendments in *ASU 2019-09, Financial Services – Insurance* and *ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts,*

delaying the effective dates because of the effects of COVID-19. Both ASU 2019-09 and 2018-12 have previously been rejected for statutory accounting.

<u>*Interested Parties' Comments:*</u>
Interested parties have no comment on this item.

<u>*Recommended Action:*</u>
NAIC staff recommends the Working Group adopt the exposed nonsubstantive 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.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-08 SSAP No. 47 (Jake)	***ASU 2021-02, Franchisors—Revenue from Contracts with Customers***	**7 – Agenda Item**	**No Comments**	**IP - 11**

<u>*Summary:*</u>
On March 15, the Working Group exposed revisions to *SSAP No. 47—Uninsured Plans* to reject *ASU 2021-02, Franchisors—Revenue from Contracts with Customers (Subtopic 952-606)* for statutory accounting. ASU 2021-02 slightly amended previous guidance issued in in *ASU 2014-09, Revenue from Contracts with Customers*, as it relates to franchisors. In 2018, the Working Group rejected the guidance in ASU 2014-09 and several other accounting standards updates related to revenue recognition in *SSAP No. 47—Uninsured Plans*. Since 2018, all additional ASUs related to revenue recognition have been reviewed by NAIC staff and have been rejected for statutory accounting.

<u>*Interested Parties' Comments:*</u>
Interested parties have no comment on this item.

<u>*Recommended Action:*</u>
NAIC staff recommends the Working Group adopt the exposed nonsubstantive to *SSAP No. 47—Uninsured Plans* to reject *ASU 2021-02, Franchisors—Revenue from Contracts with Customers (Subtopic 952-606)* for statutory accounting.

<u>REVIEW of COMMENTS on EXPOSED ITEMS</u>

The following items received comments during the exposure period:

1. Ref #2020-36: Derivatives Hedging Fixed Indexed Products
2. Ref #2021-01: *ASU 2021-01, Reference Rate Reform*
3. Ref #2021-04: SSAP No. 97 – Valuation of Foreign Insurance SCAs
4. Ref #2021-05: Accounting for Cryptocurrencies
5. Ref #2021-09: State ACA Reinsurance Programs

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2020-36 SSAP No. 108 (Julie)	**Derivatives Hedging Fixed Indexed Products**	**8 – Agenda Item**	**Comments Received**	**IP - 3**

<u>Summary:</u>
This agenda item proposes the development of new guidance for the accounting and reporting of derivatives that effectively hedge the growth in interest credited for fixed indexed products (for example, fixed indexed annuity (FIA) and indexed universal life (IUL) reported in the general account. (NAIC staff is also investigating the classification of structured / registered indexed linked annuities (RILA) in the separate account, and the use of derivatives in the separate account to hedge risk related to these products. This assessment will be completed within a separate agenda item.) This agenda item is proposed to be substantive, with potential development of a new SSAP.

On Nov. 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 directs 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, the Working Group directed notification to the Life Actuarial (E) Task Force.

On March 15, 2021, the Working Group re-exposed this item to provide additional time for interested parties to develop a proposal.

<u>Interested Parties' Comments:</u>
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.

<u>Recommended Action:</u>
NAIC staff recommends the Working Group send a formal referral to the Life Actuarial (E) Task Force, seeking input regarding whether the Task Force would consider changes to the reserve framework of fixed index annuity products as their response will likely directly influence the accounting options for derivatives

hedging these products. In the interim, NAIC staff will continue to work with interested parties and Working Group members to review and discuss possible options.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-01 SSAP No. 86 (Jim)	***ASU 2021-01, Reference Rate Reform***	**9 – Agenda Item 10 - INT**	**Comments Received**	**IP - 5**

<u>Summary:</u>
In March 2020, FASB issued *ASU 2020-04, Reference Rate Reform (Topic 848) Facilitation of the Effects of Reference Rate Reform on Financial Reporting* to ensure the financial reporting of hedging relationships would reflect a continuation of the original contract and hedging relationship during the period of the market-wide transition to alternative reference rates. <u>ASU 2020-04, which was adopted by the Working Group through *INT 20-01: ASU 2020-04 - Reference Rate Reform*, provides temporary, optional, and expedient relief in that a qualifying modification (because of reference rate reform) should not be considered an event that requires contract remeasurement at the modification date or reassessment of a previous accounting determination.</u>

In January 2021, FASB issued ASU 2021-01 to clarify that all derivative instruments affected by changes to the interest rates used for discounting, margining or contract price alignment (regardless of whether they reference LIBOR or another rate that is expected to be discontinued as a result of reference rate reform) are in afforded the contract modification relief provided in ASU 2020-04. In short summary, ASU 2021-01 expands the scope of ASU 2020-04 by allowing an entity to apply the optional expedients, by stating that a change to the interest rate used for margining, discounting or contract price alignment for a derivative is not considered to be a change to the critical terms of the hedging relationship that requires dedesignation.

On March 15, the Working Group exposed interpretative guidance proposing to expand *INT 20-01: ASU 2020-04 - Reference Rate Reform* to include the new temporary (optional) expedient guidance as provided for in *ASU 2021-01, Reference Rate Reform.*

<u>*Interested Parties' Comments:*</u>
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 from Interested Parties

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.

NAIC staff note – NAIC staff confirmed with interested parties that the references to "changes noted in underline" should be disregarded entire propose paragraph is new – not just the items emphasized with underlining.

<u>*Recommended Action:*</u>
NAIC staff recommends that the Working Group adopt the INT 20-01 with the inclusion of edits as recommended by interested parties. The edits to the INT will clarify that derivative contracts that are modified by changing the reference rate used for margining, discounting, or contract price alignment that is a result of reference rate reform (regardless of whether the reference rate being modified is expected to be discontinued) are afforded the temporary, optional expedient guidance provided for in ASU 2020-04. As such, the contract modifications are not required to be considered a change in the critical terms that would require dedesignation of the hedging relationship.

Although the INT is all-encompassing for "any hedging relationships," for clarity purposes, NAIC staff agrees with <u>incorporating the additional language suggested by interested parties in paragraph 13.</u> NAIC staff believe the intent of INT 20-01 (both as currently adopted and as proposed to be modified in the current exposure) is to capture all hedging transaction types, regardless of if the transaction occurred bilaterally or through a central clearing party. The proposed addition by interested parties will simply clarify that ancillary actions taken by a central clearing party (i.e., changes in legal form of the contract or its replacement with a new contract) should not impact the accounting for the original transaction (if the modification of the original hedging transaction or replication (synthetic asset) transactions (RSAT) is as a result of reference rate reform.) This recommendation is consistent and akin to the previous action taken by the Working Group in its adoption of *INT 20-09: Basis Swaps as a Result of the LIBOR Transaction* – which directed that ancillary contracts issued by central clearing parties shall be classified as a derivative used for hedging purposes.

The INT attachment details the exposed edits, however the additional revisions proposed by interested parties are shown in grey below:

> 13. For Issue 5, the Working Group came to a tentative consensus on March 15, 2021, that ASU 2021-01 shall be applied to derivative transactions for statutory accounting. Accordingly, derivative instruments that are modified to change the reference rate used for margining, discounting, or contract price alignment that is a result of reference rate reform (regardless of whether the reference rate that is expected to be discontinued) are eligible for the exception guidance afforded in ASU 2020-04 in that such a modification is not considered a change in the critical terms that would require dedesignation of the hedging relationship. In addition, for all derivatives (those qualifying for hedge accounting, those that do not qualify for hedge accounting and replication (synthetic asset) transactions (RSAT)), a reporting entity may account for and report modifications (that are within 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 contract and its replacement with a new reference rate reform contract. This includes in-scope modifications of centrally cleared swap contracts whether they are automatically transitioned at a cessation date or voluntarily executed prior to cessation.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-04 SSAP No. 97 (Fatima)	**Valuation of Foreign Insurance SCAs**	**11 – Agenda Item**	**Comments Received**	**IP - 8 NYL - 17**

<u>*Summary:*</u>
This agenda item was created because of comments received during the March 2020 development of agenda item 2018-26 – SCA Loss Tracking – Accounting Guidance adopted revisions in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* to state that reported equity method losses of an investment in a subsidiary controlled or affiliated entity (SCA) would not create a negative value in a SCA investment, thus equity method losses would stop at zero. However, the agenda item also clarified that to the extent there was a financial guarantee or commitment, it would require recognition under *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets.* Further, in November 2020, the Working Group adopted agenda item 2020-18 - SSAP No. 97 Update which removed a lingering, superseded reference regarding negative equity method loss valuations.

Guidance in SSAP No. 97 requires specific limited statutory basis of accounting adjustments to 8.b.ii (insurance related SCA) and 8.b.iv (foreign insurance SCA) entities. These long-standing adjustments are to prevent assets held by an SCA from receiving more favorable treatment than had the assets been held directly by the insurer. (For example, if an insurer held assets that would be nonadmitted, but the SCA would not have that same restriction.) Per SSAP No. 97, the equity method of accounting for 8.b.ii and 8.b.iv entities would be a beginning point from which the limited adjustments are made (commonly referred to as SSAP No. 97, paragraph 9 adjustments). It is important to note that it was an intentional decision that the outcome of these adjustments can result in a negative equity valuation of the investment. Again, this is so assets held by an SCA are not reported at a higher value than had they been held directly by the insurer. During the discussion of the earlier agenda item, industry comments requested consideration of whether 8.b.iv entities should continue to be subject to the current explicit provisions of SSAP No. 97, specifically that paragraph 9 adjustments may result in a negative SCA valuation. While stating many positions, industry's primary response that foreign insurance operations are subject to foreign jurisdiction and should be allowed to stand independently of a domestic insurer – thus in the absence of a guarantee or commitment, equity valuation should not go negative and would stop at zero. Comments received from industry noted that the circumstances that would cause a foreign insurance reporting entity to record negative equity is uncommon, however indicated the potential to arise in the future.

The industry discussion expanded to include certain investments in scope of SSAP No. *48—Joint Ventures, Partnerships and Limited Liability Companies* and whether the required SSAP No. 97, paragraph 9 limited statutory adjustments should be modified for SSAP No. 48 investments which are foreign insurers. Under the guidance in SSAP No. 48, unless there is a minor ownership interest, those investments are to be reported using an equity method as defined in SSAP No. 97, paragraphs 8.b.i through 8.b.iv. The industry comments have indicated that foreign insurance entities including those held through a partnership, LLC or joint venture under SSAP No. 48 should also be permitted to stop the equity value at zero without reflecting a negative valuation in response to statutory adjustments.

NAIC staff notes it is important to separate the paragraph 13 equity method adjustments which stop at zero from the paragraph 9 limited statutory basis adjustments, which intentionally do not stop at zero. However, it is noted that reporting entities with investments captured under SSAP No. 48, which requires an audit for admittance, may not be completing U.S. GAAP financials. If these SSAP No. 48 investments are not audited, reporting entities may have difficulty calculating the required adjustments to be made pursuant to SSAP No. 97, paragraph 9.

Interested Parties' Comments:
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.

New York Life Comments:
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 unintendedconsequences. With that in mind, while we offer some suggested language to address such issues later inthis 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 necessaryat 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 thesame 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 furtherfinancial 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 <u>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:</u>
>
> <u>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 bebased on the guidance in SSAP No. 97, paragraph 14e;</u>
>
> <u>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.</u>
>
> <u>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.</u>

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 potentialloopholes 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, wewould 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.

Recommended Action:
NAIC staff notes that this is a unique situation and theoretical at this time however staff request regulator input on whether the limited statutory accounting adjustments in SSAP No. 97 should be revised to not result in a negative equity position for certain situations as proposed by industry comments. Staff notes there are no identified instances of BA (SSAP No. 48) or Schedule D, part 6 section 1 assets reported at a negative value. **If the Working Group is interested in considering such a limitation, NAIC staff has provided a modified version of the language proposed by New York Life illustrated below for possible exposure. This language would limit paragraph 9 adjustments for foreign insurance SCAs (8.b.iv) to stop at zero if the entity is not engaged in providing services to, or holding assets on behalf of the U.S. insurers.** In addition, staff has proposed some additional SSAP No. 48 language to clearly indicate that the equity method valuation referenced in SSAP No. 97 can result in a negative equity valuation.

Scope - Based on the comments received, NAIC staff notes the underlying issue involves both SSAP No. 97 (which reflect stock-ownership entities) as well as investments captured in SSAP No. 48, which requires audited financial statements and valuation based on of the equity method (except for those with a minor ownership interest) as defined in SSAP No. 97, paragraphs 8.b.i through 8.b.iv.

SSAP No. 97 requires traditional equity method accounting adjustments in paragraph 13 and also requires limited statutory basis of accounting adjustments (commonly referred to as paragraph 9 adjustments) for entities captured under paragraph 8.b.ii (insurance-related SCAs) and paragraph 8.b.iv (foreign insurance SCAs). **Paragraph 9 specifically indicates that "the outcome of the adjustments can result in a negative equity valuation of the investment."** This fact pattern is so that assets held in an insurance-related or foreign insurance subsidiary are not granted preferential treatment when compared to identical assets held by a U.S. insurer. While commenters reference the reliance on local jurisdictional regulations as a control mechanism to ensure only appropriate assets are recognized as admissible, the blanket adjustments required in SSAP No. 97 are in place to ensure a level playing field, consistent reporting among insurers and to recognize that jurisdictional differences may vary significantly. NAIC staff further notes that nonadmitting the SSAP No. 97 SCA/SSAP No. 48 investment does not discontinue the use of equity method accounting; equity method accounting simply determines the valuation amount that would be reported on Schedule BA or D-6-1 (and nonadmitted on the balance sheet unless the audit requirements of SSAP No. 48 and SSAP No. 97 are met.)

NAIC staff note that 8.b.iv foreign insurers are carried at audited US GAAP with paragraph 9 statutory adjustments. If an entity uses foreign basis GAAP (including IFRS), then an audited footnote reconciliation to U.S. GAAP reconciliation is required to have comparable valuations among entities. <u>NAIC staff does not recommend expanding this agenda item to address</u> comments received by New York Life, which notes that they will voluntarily discontinue application of US GAAP financial statements in 2023. While we believe this to be a limited focus issue, Working Group should provide direction regarding whether to address this question in a separate agenda item.

<u>Edits for Working Group Review (SSAP No. 97 & SSAP No. 48):</u>

SSAP No. 97, paragraph 9

9. The limited statutory basis of accounting for investments in noninsurance SCA entities, subject to paragraph 8.b.ii. and foreign insurance SCA entities, subject to paragraph 8.b.iv., shall be adjusted for the following:

a. Nonadmit assets pursuant to the following statutory accounting principles as promulgated by the NAIC in the *Accounting Practices and Procedures Manual*;

i. *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*

ii. *SSAP No. 16R—Electronic Data Processing Equipment and Software*

iii. *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

iv. *SSAP No. 20—Nonadmitted Assets*

v. *SSAP No. 21R—Other Admitted Assets* (e.g., collateral loans secured by assets that do not qualify as investments are nonadmitted under SAP)

vi. *SSAP No. 29—Prepaid Expenses*

vii. *SSAP No. 105R—Working Capital Finance Investments*

b. Expense costs that are capitalized in accordance with GAAP but are expensed pursuant to statutory accounting as promulgated by the NAIC in the *Accounting Practices and Procedures Manual* (e.g., deferred policy acquisition costs, preoperating, development and research costs, etc.);

c. Adjust depreciation for certain assets in accordance with the following statutory accounting principles:

i. *SSAP No. 16R—Electronic Data Processing Equipment and Software*

ii. *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

iii. *SSAP No. 68—Business Combinations and Goodwill*

d. Nonadmit the amount of goodwill of the SCA in excess of 10% of the audited U.S. GAAP equity of the SCA's last audited financial statements.

e. Nonadmit amount of the net deferred tax assets (DTAs) of the SCA in excess of 10% of the audited U.S. GAAP equity of the SCA's last audited financial statements.

f. Nonadmit any surplus notes held by the SCA issued by the reporting entity.

g. Adjust the U.S. GAAP annuity account value reserves of a foreign insurance SCA, with respect to the business it wrote directly, using the commissioners' annuity reserve valuation method (CARVM) as defined in paragraphs 14 and 15 of Appendix A-820 (including the reserving provisions in the various Actuarial Guidelines which support CARVM). The valuation interest rate and mortality tables to be used in applying CARVM should be that prescribed by the foreign insurance SCA's country of domicile. If the Foreign SCA's country of domicile does not prescribe the necessary tables and/or rates, no reserve adjustment shall be made.

Note that the outcome of these adjustments can result in a negative equity valuation of the investment for all 8.b.ii entities. For an 8.b.iv entity, the application of these adjustments will stop at zero, and will not result in negative equity valuation unless the 8.b.iv entity provides services to the reporting entity or its affiliates or holds assets on behalf of the reporting entity. If such services, including reinsurance transactions, are occurring, the adjustments required in this paragraph can result in a negative equity valuation. (See additional equity method application guidance in paragraph 13.e. regarding guarantees and financial support.)

SSAP No. 48, paragraph 6

6. Investments in these ventures, except for joint ventures, partnerships and limited liability companies with a minor ownership interest, shall be reported using an equity method as defined in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*, paragraphs 8.b.i. through 8.b.iv. (The equity method calculation may result with a negative valuation of the investment, therefore the SSAP No. 97 equity method calculation shall occur regardless of whether the investment is supported by an audit and the reporting entity will nonadmit the investment.) A reporting entity whose shares of losses in a SSAP No. 48 entity exceeds its investment in the SSAP No. 48 entity shall disclose the information required by SSAP No. 97, paragraph 35.a.

NAIC staff note – the proposed edits shown above in SSAP No. 48, paragraph 6 (shown above) are intended to explicitly state existing requirements that SSAP No. 48 entities are subject to the equity method of accounting as required by SSAP No. 97 paragraph 13 – which may result in a negative equity position regardless of SSAP No. 97, paragraph 9 adjustments. If the Working Group does not believe these edits are necessary, this can be removed from the proposed exposure.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-05 SSAP No. 2R (Jake)	**Accounting for Cryptocurrencies**	**12 - Agenda Item 13 - INT**	**Comments Received**	**DE Ins Dept. - 1 IP - 9**

Summary:

On March 15, the Working Group exposed interpretative guidance in *INT 20-01T: Statutory Accounting Treatment for Crypto currencies* to clarify that cryptocurrencies do not meet the definition of cash in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* and do not meet the criteria for admission as defined in *SSAP No. 4—Assets and Nonadmitted Assets.*

Crypto currency is defined as digital currency in which transactions are verified and records maintained by a decentralized system using cryptography (e.g., utilizing technology typically referred to as Blockchain), rather than by a centralized authority, such as the Federal Reserve System. The exposure also included a request for input on the extent to which companies hold (or have an interest in) crypto currencies and the manner in which they are held (e.g., held directly or held through a SCA).

Delaware Insurance Department:
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—Cash, Cash Equivalents, Drafts and Short-Term Investments.* Cryptocurrencies are not cash 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—Unaffiliated Common Stock 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—Joint Ventures, Partnerships, and Limited Liability Companies,* 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.

Interested Parties' Comments:
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 and accepted medium of exchange, 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.

Recommended Action:
NAIC staff recommends that the Working Group adopt the exposed nonsubstantive interpretative guidance provided by *INT 21-01: Statutory Accounting Treatment for Cryptocurrencies*. The INT clarifies that directly held cryptocurrencies do not meet the definition of cash in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* nor, when directly held, meet definition of an admitted asset per *SSAP No. 4—Assets and Nonadmitted Assets.* As a result of the comments received, the INT includes minor revisions to clarify that only directly held cryptocurrencies are considered nonadmitted assets, and that this does not impact the guidance for investments in funds that may hold cryptocurrencies in SSAP No. 30R, SSAP No. 48 or SSAP No. 97. The minor revisions are included below.

At this time, NAIC staff does not recommend revisions to SSAP No. 30R, SSAP No. 48 or SSAP No. 97 to restrict cryptocurrencies in funds or indirect ownership (such as in SCAs or within a joint venture, partnership or LLC). Comments are requested from regulators on whether such restrictions should be considered.

INT 21-01T

4. This Interpretation intends to clarify that directly held cryptocurrencies are nonadmitted assets for statutory accounting.

5. Directly held ~~C~~cryptocurrencies have not been identified in the *Accounting Practices and Procedures Manual* (AP&P Manual) as an admitted asset, and do not meet the definition of any admitted asset that is defined in the AP&P Manual. Accordingly, by default they are a nonadmitted asset per *SSAP No. 4—Assets and Nonadmitted Assets,* paragraph 3*,* as they are not specifically identified in the *Accounting Practices and Procedures Manual* as an admitted asset.

7. The Statutory Accounting Principles (E) Working Group reached a tentative consensus that directly held cryptocurrencies do not meet the definition of an admitted asset and are therefore considered to be a nonadmitted asset for statutory accounting. The Working Group intends to rely on this interpretation for statutory accounting and will address cryptocurrencies further once FASB has provided definitive guidance.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-09 SSAP No. 107 (Robin)	**State ACA Reinsurance Programs**	**14 – Agenda Item**	**Comments Received**	**IP - 12**

Summary:
On March 15, the Working Group moved this item to the active listing, categorized as nonsubstantive and exposed revisions to *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act* as illustrated below. These revisions would include State ACA reinsurance programs which are using Section 1332 waivers in the scope of *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*. The intent of the proposed accounting revisions is to continue to follow the SSAP No. 107 hybrid accounting approach for the state ACA programs as they operate in a similar manner.

In general, state ACA reinsurance programs provide funding to issuers in the individual market that incur high claims costs for enrollees. The programs often require assessments from issuers typically on behalf of group health plans. At a high level this hybrid accounting approach divides products into 3 broad categories. This includes:

a. Subject individual products (typically individual plans) that may pay a reinsurance funding contribution and are eligible to receive reinsurance distributions shall report similar to an involuntary reinsurance pool as described in *SSAP No. 63—Underwriting Pools*.

b. Other insured Health products (typically group plans) that are not eligible for reinsurance distributions under the terms of the state ACA reinsurance program shall treat the amounts as assessments reported in taxes, licenses and fees similar to treatment under *SSAP No. 35R—Guaranty Funds and Other Assessments*.

c. Self-insured plans where the reporting entity is acting as an administrator and will exclude the payments made on behalf of the self-insured plan from the reporting entity's operations, shall report consistent with the guidance in *SSAP No. 47—Uninsured Plans*.

Interested Parties' Comments:
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 operate to cover higher individual health claims in a manner similar to the transitional reinsurance program</u>, 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.

<u>Recommended Action:</u>
NAIC staff recommends that the Working Group direct staff to develop additional revisions for Working Group consideration that expand the principles-based guidance to address the diversity in state programs identified in the industry comments. NAIC staff provides the following preliminary comments.

1. The primary issue identified is that while some state programs have a flow of funds similar to the original federal transitional reinsurance program, other state programs have different arrangements. These arrangements include not assessing some insurers and instead using federal funds, or single assessments used by the state for multiple different programs for which the allocation of funds may not be clear to the assessed entities. In such cases, the assessed entities may not know how much of the assessment should be allocated to the reinsurance program.
2. Program reimbursements for claims costs should reduce claims incurred.
3. Timing - liabilities should be recognized when they meet the definition of a liability pursuant to SSAP No. 5R.
4. Guidance similar to the SSAP No. 107 federal receivables guidance is recommended to apply to the state ACA reinsurance programs guidance.

The comment letters are included in Attachment 15 (20 pages).

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

Issue: Separate Account – Product Identifiers

Check (applicable entity):

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

Description of Issue:
This agenda item proposes increased product identifier reporting granularity in question 1.01 (product mix) of the separate account general interrogatories (GI 1.01). At the request of regulators, primarily in response to the recent growth of pension risk transfer (PRT) transactions and registered indexed linked annuity (RILA) products that are generally held in insulated separate accounts, improved reporting was requested so regulators can more readily identify and review the products captured in the separate account. This agenda item does not anticipate modifications to *SSAP No. 56—Separate Accounts*, however if supported by the Working Group, would likely result in a proposal to the Blanks (E) Working Group for annual statement instruction modifications.

For example, upon review of the 2019 separate account annual statements filed with the NAIC, it was found that while some reporting entities included reporting details such as "XYZ Company Pension Risk Transfer" (a preferred method of disclosure), most entities grouped their separate account products in 3-4 broad categories. Common categories included variable life, variable annuity, indexed annuity and group variable annuity (the latter of which is likely where PRT's would be captured).

SSAP No. 56 requires several disclosure elements separated by "product identifier." These situations include:

- 1.01 – Separate account assets by SEC registration, guarantees, seed money, etc.
- 1.01A – Identification of private placement variable annuities / life insurance (PPVA or PPLI)
- 2.5 – Risk charges
- 4.2 – Investment Process and their treatment (e.g., to policyholder, to GA, or retained in SA)

As detailed in the separate account instructions, "a distinct product identifier shall be used for each product and shall be used consistently throughout the interrogatory." Even with this direction, most reporting entities appear to be aggregating product types for reporting. This has made it difficult to assess the reserve requirements or guarantees for the specific products. Additionally, regulators have indicated that upon their examination of the product mix general interrogatory in which the assets reflect if they are supported with a guarantee from the general account, due to the broad grouping of products, some products which do not have guarantees were grouped with those that did have guarantees.

Existing Authoritative Literature:

The disclosures for separate account assets are detailed in *SSAP No. 56—Separate Accounts*:

36. 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 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. 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), 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.

39. **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.

The annual statement instructions as well as an example of note 1.01 are below.

As the product identifier is used **throughout the interrogatory, examples of other items potentially impacted are as follows:**

1.01A For the products (and related assets) that are not registered with the SEC, identify whether the products are considered private placement variable annuity products or private placement life insurance.

1	Not Registered with SEC		
Product Identifier	2 Private Placement Variable Annuity	3 Private Placement Life Insurance	4 Other (Not PPVA or PPLI)
	$		
Totals	$		

Allocation of Investment Proceeds of Separate Account Activity

4.1 Does the reporting entity have separate account assets in which less than 100% of investment proceeds (net of contract fees and assessments) are attributed to a contract holder? (This should identify any situations where there is a ceiling on investment performance results.)

4.2 If yes, provide detail on the net investment proceeds that were attributed to the contract holder, transferred to the general account and reinvested within the separate account:

1 Product Identifier	2 Net Investment Proceeds	3 Attributed to Contract Holder	4 Transferred to General Account	5 Reinvested Within the Separate Account
	$	$	$	$
	$	$	$	$
	$	$	$	$

8.3 Identify all separate account products and identify whether each product was classified within a separate account for GAAP reporting purposes. (For non-GAAP filers, this disclosure should reflect whether the GAAP classification would have been the same if GAAP financials had been completed.) For products that were (or would have been) reported differently, identify which SOP 03-1 condition prevented separate account GAAP classification for that particular product.

1 Product Identifier	2 Same as GAAP / Condition that Requires GAAP General Account Reporting

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): N/A

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, categorized as nonsubstantive and expose 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. Additionally, feedback is requested regarding if a threshold should be established for when aggregate reporting would be permitted.

Staff Review Completed by:
Jim Pinegar - NAIC Staff, October 2020

Status:
On November 12, 2020, the Statutory Accounting Principles (E) 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. Particularly, this is requesting feedback 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 is requested regarding if a threshold should be established for when aggregate reporting would be permitted.

On March 15, 2021, the Statutory Accounting Principles (E) 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.

An excerpt from the blanks proposal is shown below:

A distinct disaggregated product identifier shall 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).

1	Separate Account Assets		4	5	6	7
	2	3				
Product Identifier	Registered with SEC	Not Registered with SEC	Guarantees Associated with the Product Yes/No	Seed Money	Fees and Expenses Due to the General Account	Additional Required Surplus Amounts
1.01A Pension Risk Transfer Group Annuities						
	$	$		$	$	$
Total Pension Risk Transfer Group Annuities	$	$		$	$	$
1.01B All Other Group Annuities						
	$	$		$	$	$
Total All Other Group Annuities	$	$		$	$	$
1.01C Registered Index Linked Annuities Individual Annuities						

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

Issue: Pension Risk Transfer – Separate Account Disclosure

Check (applicable entity):

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

Description of Issue:
This agenda item proposes increased product identification and disclosure of pension risk transfer (PRT) transactions in the separate account financial statements. At the request of regulators, in response to the recent growth of PRT, improved reporting is sought so regulators can more readily identify and analyze such transactions. Regulators requested several enhancements, including separated PRT reporting and improved PRT disclosure regarding reserves, associated assets, and general account exposure.

As a brief background, a pension risk transfer is when a defined-benefit pension provider seeks to remove some or all of its obligation to pay guaranteed retirement income to plan participants. In these transactions, the pension providers will generally transfer assets to an insurer, for which the insurer assumes the annuity risk for plan participants. According to AM Best, there were over 500 single premium pension contract buyouts totaling $28 billion in 2019. Due to organizations wanting to alleviate their pension liability, it is expected that PRT transactions will not subside in the near future.

Currently, the most specific details concerning PRT transactions are generally captured/disclosed in question 1.01 (product mix) of the separate account general interrogatories (GI 1.01). For reference, GI 1.01 is shown below:

> 1.01 Identify the product types in the separate account, quantify the assets associated with those products, indicate if there are any guarantees associated with those products, quantify seed money and quantify other fees and expenses due to the general account:

1	Separate Account Assets		4	5	6	7
	2	3				
Product Identifier	Registered with SEC	Not Registered with SEC	Guarantees Associated with the Product Yes/No	Seed Money	Fees and Expenses Due to the General Account	Additional Required Surplus Amounts
	$	$		$	$	$
Totals	$	$	XXX	$	$	$

Upon review of the 2019 separate account annual statements filed with the NAIC, it was found that most entities did not individually detail PRT activity, but rather broadly combine this product into other product categories (i.e. group variable annuity).

While other details of the broadly categorized products are captured in various other general interrogatories (as shown below in Existing Authoritative Literature), this agenda item, at the request of regulators, proposes enhanced detailed reporting requirements for pension risk transfer products and transactions in the scope of *SSAP No. 56—Separate Accounts.*

Existing Authoritative Literature:

There are numerous disclosure elements in *SSAP No. 56—Separate Accounts* that would be applicable for PRT transactions (the most relevant disclosures have been bolded below). However as described above, PRTs are generally reported in an aggregated manner with other similar products, thus the disclosures below do not currently provide the level of detail sought by regulators.

Disclosures

31. 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 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.

d. Discussion of securities lending transactions within the separate account, separately including the amount of any loaned securities within the separate account, and if policy and procedures for the separate account differ from the general account.

32. 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.

33. 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**:

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

ii. 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%;

iii. 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.

34. **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**.

35. 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.

36. 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 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. 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), 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.

37. 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 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.

38. 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.

39. 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.

As previously shown, GI 1.01 is the primary interrogatory which capture PRT transactions, however additional details are captured in the following tables.

1.01A For the products (and related assets) that are not registered with the SEC, identify whether the products are considered private placement variable annuity products or private placement life insurance.

1	Not Registered with SEC		
Product Identifier	2 Private Placement Variable Annuity	3 Private Placement Life Insurance	4 Other (Not PPVA or PPLI)
	$		
Totals	$		

Allocation of Investment Proceeds of Separate Account Activity

4.1 Does the reporting entity have separate account assets in which less than 100% of investment proceeds (net of contract fees and assessments) are attributed to a contract holder? (This should identify any situations where there is a ceiling on investment performance results.)

4.2 If yes, provide detail on the net investment proceeds that were attributed to the contract holder, transferred to the general account and reinvested within the separate account:

1 Product Identifier	2 Net Investment Proceeds	3 Attributed to Contract Holder	4 Transferred to General Account	5 Reinvested Within the Separate Account
	$	$	$	$
	$	$	$	$
	$	$	$	$

8.3 Identify all separate account products and identify whether each product was classified within a separate account for GAAP reporting purposes. (For non-GAAP filers, this disclosure should reflect whether the GAAP classification would have been the same if GAAP financials had been completed.) For products that were (or would have been) reported differently, identify which SOP 03-1 condition prevented separate account GAAP classification for that particular product.

1 Product Identifier	2 Same as GAAP / Condition that Requires GAAP General Account Reporting

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): N/A

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, categorized as nonsubstantive to solicit comments from state insurance regulators and industry regarding possible modifications to *SSAP No. 56—Separate Accounts*. Depending upon the feedback received, the Working Group would have several options available including, but not limited to, requiring the separate identification of pension risk transfer products (including transactions, guarantees, reserve assumptions, etc.) within existing disclosure requirements or the addition of a new general interrogatory (and perhaps new separate accounting reporting schedules / exhibits) to separate specific product detail that was previously reported in an aggregated format. NAIC staff is open for additional commentary and suggestions, and requests to work with industry and regulators throughout this and any subsequent exposure.

Staff Review Completed by:
Jim Pinegar - NAIC Staff, October 2020

Status:
On November 12, 2020, the Statutory Accounting Principles (E) 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 possible modifications to *SSAP No. 56—Separate Accounts* specific to pension risk transfer (PRT) products. Depending upon the feedback received, the Working Group would have several

options available including, but not limited to, requiring the separate identification of pension risk transfer products (including transactions, guarantees, reserve assumptions, etc.) within existing disclosure requirements or the addition of a new general interrogatory (and perhaps new separate accounting reporting schedules / exhibits) to separate specific product detail that was previously reported in an aggregated format.

On March 15, 2021, the Statutory Accounting Principles (E) 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.

An excerpt from the blanks proposal is shown below:

A distinct disaggregated product identifier shall 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).

1	Separate Account Assets		4	5	6	7
	2	3				
Product Identifier	Registered with SEC	Not Registered with SEC	Guarantees Associated with the Product Yes/No	Seed Money	Fees and Expenses Due to the General Account	Additional Required Surplus Amounts
1.01A Pension Risk Transfer Group Annuities						
	$	$		$	$	$
Total Pension Risk Transfer Group Annuities	$	$		$	$	$
1.01B All Other Group Annuities						
	$	$		$	$	$
Total All Other Group Annuities	$	$		$	$	$
1.01C Registered Index Linked Annuities Individual Annuities						

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

Issue: ASU 2020-08 – Premium Amortization on Callable Debt Securities

Check (applicable entity):

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

Description of Issue: In October 2020, the Financial Accounting Standards Board (FASB) issued *ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs* to clarify the amortization of premium associated with callable debt securities. In summary, ASU 2020-08 requires that to the extent the amortized cost basis of a callable debt security exceeds the amount repayable by the issuer, any associated premium (above the call price) is to be amortized to the next effective call price/date. For example, if a reporting entity held a bond at $104 in which could be called at $102 in a year, the $2 excess premium would be amortized over that particular year. Once amortized to $102, the reporting entity would then reassess for any excess premium to the next effective call price/date. If there is no remaining premium or further call dates, the effective yield is reset using the payment terms of the debt security.

Existing Authoritative Literature: The amortization of premiums related to debt securities is referenced in *SSAP No. 26R—Bonds.* While the requirements in ASU 2020-08 are very similar to statutory accounting guidance, SSAP No. 26R also requires the application of a yield-to-worst concept. With this concept, premium is amortized in a manner to produce the lowest asset value. Relevant guidance has been bolded below.

Amortized Cost

9. **Amortization of bond premium or discount shall be calculated using the scientific (constant yield) interest method taking into consideration specified interest and principal provisions over the life of the bond. Bonds containing call provisions (where the issue can be called away from the reporting entity at the issuer's discretion), except "make-whole" call provisions, shall be amortized to the call or maturity value/date which produces the lowest asset value (yield-to-worst).** Although the concept for yield-to-worst shall be followed for all callable bonds, make-whole call provisions, which allow the bond to be callable at any time, shall not be considered in determining the timeframe for amortizing bond premium or discount unless information is known by the reporting entity indicating that the issuer is expected to invoke the make-whole call provision.

Application of Yield-to-Worst

10. For callable bonds, the first call date after the lockout period (or the date of acquisition if no lockout period exists) shall be used as the "effective date of maturity" for reporting in Schedule D, Part 1. Depending on the characteristics of the callable bonds, the yield-to-worst concept in paragraph 9 shall be applied as follows:

a. For callable bonds with a lockout period, premium in excess of the next call price (subsequent to acquisition and lockout period) shall be amortized proportionally over the length of the lockout period. **After each lockout period (if more than one), remaining premium shall be amortized to the call or maturity value/date which <u>produces the lowest asset value.</u>**

b. For callable bonds without a lockout period, the book adjusted carrying value (at the time of acquisition) of the callable bonds shall equal the lesser of the next call price (subsequent to acquisition) or cost. Remaining premium shall then be amortized to the call or maturity value/date <u>which produces the lowest asset value.</u>

c. For callable bonds that do not have a stated call price, all premiums over par shall be immediately expensed. For callable bonds with a call price at par in advance of the maturity date, all premiums shall be amortized to the call date.

Balance Sheet Amount

11. Bonds, as defined in paragraph 3, shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and the designation assigned in the NAIC *Valuations of Securities* product prepared by the NAIC Securities Valuation Office (SVO).

a. Bonds, except for mandatory convertible bonds: **For reporting entities that maintain an asset valuation reserve (AVR), the bonds shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value. For reporting entities that do not maintain an AVR, bonds that are designated highest-quality and high-quality (NAIC designations 1 and 2, respectively) shall be reported at amortized cost; all other bonds (NAIC designations 3 to 6) shall be reported at the lower of amortized cost or fair value**.

b. Mandatory convertible bonds: Mandatory convertible bonds are subject to special reporting instructions and are not assigned NAIC designations or unit prices by the SVO. The balance sheet amount for mandatory convertible bonds shall be reported at the lower of amortized cost or fair value during the period prior to conversion. This reporting method is not impacted by NAIC designation or information received from credit rating providers (CRPs). Upon conversion, these securities will be subject to the accounting guidance of the statement that reflects their revised characteristics. (For example, if converted to common stock, the security will be in scope of *SSAP No. 30R—Unaffiliated Common Stock*, if converted to preferred stock, the security will be in scope of *SSAP No. 32R—Preferred Stocks*.)

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 recommends that the Working Group move this item to the active listing, categorized as nonsubstantive and expose revisions to *SSAP No. 26R—Bonds* to reject ASU 2020-08 for statutory accounting. While ASU 2020-08 closely mimics 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 in 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).

Proposed Revisions to SSAP No. 26R

33. This statement rejects the GAAP guidance for debt securities, which is contained in *ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs,* *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities, ASU 2017-08, Premium Amortization on Purchased Callable Debt* Securities, ASU *2016-01, Financial Instruments – Overall*, *FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, FASB Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with*

> *Originating or Acquiring Loans and Initial Direct Costs of Leases, FASB Emerging Issues Task Force No. 89-18, Divestitures of Certain Investment Securities to an Unregulated Commonly Controlled Entity under FIRREA,* and *FASB Emerging Issues Task Force No. 96-10, Impact of Certain Transactions on Held-to-Maturity Classifications Under FASB Statement No. 115*

Staff Review Completed by: Jim Pinegar, NAIC Staff – January 2021

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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 mimics 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).

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

Issue: SSAP No. 103R – Disclosures

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 propose additional disclosures and to data-capture certain existing disclosure elements in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.* The additional disclosures proposed herein are in response to the Working Group's continued deliberation of agenda item 2019-21: SSAP No. 43R – Equity Instruments. Agenda item 2019-21 is a substantive project to consider what investments fall within scope of *SSAP No. 43R—Loan-Backed and Structured Securities* and on Oct. 13, 2020, this project was expanded to include a review of the investments eligible for reporting on Schedule D-1: Long Term Bonds. During the continued work on this project, regulators expressed a desire to identify situations in which a reporting entity has entered into a securitization, asset-backed financing or similar transfer transaction where a significant economic interest in the transferred assets is retained by the reporting entity, its related parties or another member within the holding company group.

The existing disclosures discussed (and proposed for data-capture) are currently completed in a narrative (pdf) format. With the proposal to data-capture certain disclosures, regulators can utilize system inquiries to determine which reporting entities have a securitization, asset backed financing arrangement, or other similar transfers that have been accounted for as a sale when the transferor has continued involvement.

Note – the disclosures discussed below are only required in the event a reporting entity as entered into a securitization, asset-backed financing arrangement or other similar transfer in which it also retains a continuing involvement with the transferred financial asset. Due to the numerous circumstances that may require disclosure, data-capture of most of the applicable disclosures would not sufficiently relay the particular characteristics or circumstances of the transaction – as is required in SSAP No. 103R. <u>However, the need for regulators to have the ability to query the global population regarding the nature of these transactions remains a primary reason for this agenda item.</u> Nonetheless, certain consistent numerical disclosures are suitable for data-capture, which will significantly assist with regulator's ability to identify which reporting entities have such transactions, at which time further analysis of the narrative disclosures can be performed.

Existing Authoritative Literature:

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

28. A reporting entity shall disclose the following:

g. For securitizations, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary) with the transferred financial assets:

i. For each income statement presented:

(a) The characteristics of the transfer (including a description of the transferor's continuing involvement with the transferred financial assets, the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer, and the gain or loss from sale of transferred financial assets. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

(1) The level within the fair value hierarchy in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3)

(2) The key inputs and assumptions used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets, and anticipated credit losses, including expected static pool losses).

(b) Cash flows between a transferor and transferee, including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets, servicing fees, and cash flows received from a transferor's beneficial interests.

ii. For each statement of financial position presented, regardless of when the transfer occurred:

(a) Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk, and other risks), including:

(1) The total principal amount outstanding, the amount that has been derecognized, and the amount that continues to be recognized in the statement of financial position.

(2) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the transferee or its beneficial interest holders, including a description of any events or circumstances that could expose the transferor to loss and the amount of the maximum exposure to loss.

(3) Whether the transferor has provided financial or other support during the periods presented that it was not previously contractually required to provide to the transferee or its beneficial interest holders, including when the transferor assisted the transferee or its beneficial interest holders in obtaining support, including:

(i.) The type and amount of support

(ii.) The primary reasons for providing the support

(4) Information is encouraged about any liquidity arrangements, guarantees, and/or other commitments provided by third parties related to the transferred financial assets that may affect the transferor's exposure to loss or risk of the related transferor's interest.

(b) The entity's accounting policies for subsequently measuring assets and liabilities that relate to the continuing involvement with the transferred financial assets;

(c) The key inputs and assumptions used in measuring the fair value of assets or liabilities that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets, and anticipated credit losses, including expected static pool losses);

(d) For the transferor's interests in the transferred financial assets, a sensitivity analysis or stress test showing the hypothetical effect on the fair value of those interests (including any servicing assets or servicing liabilities) of two or more unfavorable variations from the expected levels for each key assumption that is reported under paragraph 28.g.ii.(c) independently from any change in another key assumption, and a description of the objectives, methodology, and limitations of the sensitivity analysis or stress test

(e) Information about the asset quality of transferred financial assets and any other assets that it manages together with them. This information shall be separated between assets that have been derecognized and assets that continue to be recognized in the statement of financial position. This information is intended to provide financial statement users with an understanding of the risks inherent in the transferred financial assets as well as in other assets and liabilities that it manages together with transferred financial assets. For example, information for receivables shall include, but is not limited to:

(i.) Delinquencies at the end of the period; and

(ii.) Credit losses, net of recoveries, during the period.

Current Annual Statement Illustrations for Completing Disclosures:

Note 17: Sale, Transfer and Servicing of Financial Assets and Extinguishments of Liabilities

(4) For securitizations, asset-backed financing arrangements and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary of the *Accounting Practices and Procedures Manual*) with the transferred financial assets:

a. For each income statement presented:

1. The characteristics of the transfer including a description of the transferor's continuing involvement with the transferred financial assets, the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer, and the gain or loss from the sale of transferred financial assets. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

(a) The level within the fair value hierarchy in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2) and significant unobservable inputs (Level 3).

(b) The key inputs and assumptions used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates; expected prepayments, including the expected weighted-average life of prepayable financial assets; and anticipated credit losses, including expected static pool losses)

- If an entity has aggregated multiple transfers during a period, it may disclose the range of assumptions.

  - The weighted-average life of prepayable assets in periods (for example, months or years) can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

  - Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets.

2. Cash flows between a transferor and transferee, including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets, servicing fees and cash flows received from a transferor's beneficial interests.

b. For each statement of financial position presented, regardless of when the transfer occurred:

1. Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk and other risks), including:

   (a) The total principal amount outstanding, the amount that has been derecognized and the amount that continues to be recognized in the statement of financial position.

   (b) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the transferee or its beneficial interest holders, including a description of any events or circumstances that could expose the transferor to loss and the amount of the maximum exposure to loss.

   (c) Whether the transferor has provided financial or other support during the periods presented that it was not previously contractually required to provide to the transferee or its beneficial interest holders, including when the transferor assisted the transferee or its beneficial interest holders in obtaining support, including:

   - The type and amount of support.

   - The primary reasons for providing the support.

   (d) Information is encouraged about any liquidity arrangements, guarantees and/or other commitments provided by third parties related to the transferred financial assets that may affect the transferor's exposure to loss or risk of the related transferor's interest.

2. The entity's accounting policies for subsequently measuring assets and liabilities that relate to the continuing involvement with the transferred financial assets.

3. The key inputs and assumptions used in measuring the fair value of assets or liabilities that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates; expected prepayments, including the expected weighted-average life of pre-payable financial assets; and anticipated credit losses, including expected static pool losses).

4. For the transferor's interests in the transferred financial assets, a sensitivity analysis or stress test showing the hypothetical effect on the fair value of those interests (including any servicing assets or servicing liabilities) of two or more unfavorable variations from the expected levels for each key assumption that is reported per *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* independently from any change in another key assumption, and a description of the objectives, methodology and limitations of the sensitivity analysis or stress test.

5. Information about the asset quality of transferred financial assets and any other assets that it manages together with them. This information shall be separated between assets that have been derecognized and assets that continue to be recognized in the statement of financial position. This information is intended to provide financial statement users with an understanding of the risks inherent in the transferred financial assets, as well as in other assets and liabilities that it manages together with transferred financial assets. For example, information for receivables shall include, but is not limited to:

   - Delinquencies at the end of the period.

   - Credit losses, net of recoveries, during the period.

Activity to Date (issues previously addressed by the Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): N/A

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

Convergence with International Financial Reporting Standards (IFRS) and U.S. GAAP: N/A

Staff Recommendation: NAIC staff recommends that the Working Group move this item to the active listing, categorized as nonsubstantive to 1) expose new disclosure elements and 2) propose data-capture templates for existing disclosures in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. A blanks proposal exposure is anticipated to occur concurrently with the Working Group's exposure. With inclusion of the data templates, narrative (pdf) reporting shall still occur to provide additional information regarding transfers accounted for as a sale when the transferor maintains continuing involvement in the transferred financial assets. The purpose of the data-capture templates is so regulators can perform system inquiries to identify which reporting entities have such transactions, at which time further analysis of the narrative disclosures can be performed.

Proposed disclosures to SSAP No. 103R

28. A reporting entity shall disclose the following:

g. For securitizations, asset-backed financing arrangements, and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary) with the transferred financial assets:

i. For each income statement presented:

(a) The characteristics of the transfer (including a description of the transferor's continuing involvement with the transferred financial assets, the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer, and the gain or loss from sale of transferred financial assets. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

(1) The level within the fair value hierarchy in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3)

(2) The key inputs and assumptions used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale that relate to the transferor's continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates, expected prepayments including the expected weighted-average life of prepayable financial assets, and anticipated credit losses, including expected static pool losses).

(b) Cash flows between a transferor and transferee, including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets, servicing fees, and cash flows received from a transferor's beneficial interests.

ii. For each statement of financial position presented, regardless of when the transfer occurred:

(a) Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk, and other risks), including:

(1) The total original principal amount ~~outstanding~~, the amount that has been derecognized, and the outstanding amount that continues to be recognized in the statement of financial position. The percentage of original principal held in the company group and the percentage of derecognized principal held by related parties.

(2) The terms of any arrangements that could require the transferor to provide financial support (for example, liquidity arrangements and obligations to purchase assets) to the transferee or its beneficial interest holders, including a description of any events or circumstances that could expose the transferor to loss and the amount of the maximum exposure to loss.

(3) Whether the transferor has provided financial or other support during the periods presented that it was not previously contractually required to provide to the transferee or its beneficial interest holders, including when

the transferor assisted the transferee or its beneficial interest holders in obtaining support, including:

(iii.) The type and amount of support

(iv.) The primary reasons for providing the support

(4) Information is encouraged about any liquidity arrangements, guarantees, and/or other commitments provided by third parties related to the transferred financial assets that may affect the transferor's exposure to loss or risk of the related transferor's interest.

Proposed Data Capture Template:

This data template includes aspects from SSAP No. 103R paragraphs 28g.i.(a & b), and 28.g.ii(a) as well as the new proposed disclosure elements. (While the entire proposed data capture template was new, only the additional proposed SSAP No. 103R disclosures were shown as tracked changes in the March 15th exposure, as shown immediately below).

<u>Proposed Data Capture Template:</u>

Each Material Transaction Listed Separately:

(Identification of each transaction should be consistent so that the circumstances for each item are adequately associated with the applicable transaction)

Identification of Transaction	Original Principal	<u>% of Original Principal held within the company group</u>	Amount Derecognized	<u>% of derecognized held by related parties</u>	<u>Outstanding a</u>~~A~~mount still recognized in the statement of financial position	Net cashflows between transferor and transferee	FV of proceeds received	Gain/loss from sale of transferred assets

Staff Review Completed by: Jim Pinegar – January 2021

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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.

On April 20, 2021, the Statutory Accounting Principles (E) Working Group exposed updated revisions to *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.* The updated exposure was drafted after receiving preliminary comments from interested parties and proposes 1) new disclosure elements, and 2) a data-capture template for certain existing disclosures in SSAP No. 103R to detail instances where a reporting entity has transferred (or sold) assets but still retains a material participation. An updated blanks proposal is anticipated to be concurrently exposed.

<u>April 20, 2021 Updated Exposure and Disclosure Template:</u>

<u>Drafting Note</u>: Subsequent to March exposure of this agenda item, Working Group representatives, NAIC staff and interested parties discussed regulator's desire to identify situations in which a reporting entity has entered into a securitization, asset-backed financing or similar transfer transaction where a significant economic interest in the transferred asset is retained by the reporting entity, its related parties or another member within the holding company group. Through this discussion, refinement and explanatory language which was updated and exposed by the Working Group on April 20, has been collaboratively proposed. **The updated SSAP No. 103R disclosure recommendation and the blanks proposal are shown below.**

<u>Updated Exposed Revisions to SSAP No. 103R – April 20, 2021:</u>

SSAP No. 103R, paragraph 28.g.ii

ii. For each statement of financial position presented, regardless of when the transfer occurred:

(a) Qualitative and quantitative information about the transferor's continuing involvement with transferred financial assets that provides financial statement users with sufficient information to assess the reasons for the continuing involvement and the risks related to the transferred financial assets to which the transferor continues to be exposed after the transfer and the extent that the transferor's risk profile has changed as a result of the transfer (including, but not limited to, credit risk, interest rate risk, and other risks), including:

(1) The total principal amount outstanding <u>(BACV)</u>, the amount that has been derecognized, and the amount that continues to be recognized in the statement of financial position. <u>The amount recognized (allocated fair value) by the reporting entity for the acquired participation in the transferred assets. The reporting schedules of both the transferred and reacquired assets. The percentage of beneficial interests from the reporting entity's transferred assets acquired by affiliated entities</u>.

<u>Updated Exposed Data Capture Template – April 20, 2021:</u>

<u>Instructions:</u>

<u>The purpose of this table is to provide a data capture template for certain disclosures required in *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, paragraph 28g. As detailed in paragraph 28.g.ii, disclosure is required for each statement of financial position presented, regardless of when the transfer occurred. Determination of continuing involvement shall be applied in accordance with the definition reflected in SSAP No. 103, Appendix A.</u>

<u>Columns requesting information that results in a null result (i.e., if column 5 results in a zero balance as 100% of the asset was transferred), shall indicate zero (0). In the event a column is not applicable, (i.e., if affiliated entities did not acquire an interest in the transferred asset), the column shall be referenced as zero (0).</u>

<u>In circumstances where an entity has multiple assets associated with a sale (i.e., several limited partnerships are sold as a single transaction), the assets should be aggregated and reported as a single transaction.</u>

1	2	3	4	5	6	7	8
Identification of Transaction	BACV Prior to Transfer	Original Reporting Schedule of the Transferred Assets	Amount Derecognized from Sale Transaction	Amount that continues to be recognized in the statement of financial position	BACV of acquired interests in transferred assets	Reporting Schedule of Acquired Interests	Percentage of interests of a reporting entity's transferred assets acquired by affiliated entities

Column 1 – Identification of each material transaction. Identification should be consistent across reporting periods so that the circumstances for each item are adequately associated with the applicable transaction.

Column 2 – The aggregate book value, at the time of transfer, of all assets associated with the transaction.

Column 3 – The investment schedule(s) in which the transferred assets were reported, immediately prior to the transfer. If the transferred assets were reported on multiple schedules, all reporting schedules shall be identified.

Column 4 – The aggregate book value derecognized from the investment schedules as a result of the transfer. If the assets were transferred in their entirety, Column 4 will equal Column 2.

Column 5 – The amount that continues to be recognized in the statement of financial position. This should equal Column 2 less Column 4.

Column 6 – The original BACV reported for acquired beneficial interests (or any other interest) in the previously transferred asset. (BACV for these transactions is often the allocated fair value associated with the transaction.)

Column 7 – The reporting schedule of the acquired beneficial interest reported in Column 6.

Column 8 - The percentage of interest of a reporting entity's transferred assets acquired by an affiliate as defined in *SSAP No. 25—Affiliates and Other Related Parties.*

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NAIC Accounting Practices and Procedures Manual
Editorial and Maintenance Update
March 15, 2021

Maintenance updates provide revisions to the *Accounting Practices and Procedures Manual*, such as editorial corrections, reference changes and formatting.

SSAP/Appendix	Description/Revision
SSAP No. 53	Minor modification to the SSAP title to be consistent with similar SSAP titles.
SSAP No. 97	Corrects grammatical errors in paragraph 54 of *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities.*
SSAP Glossary	Removes the footnote noted in the *Glossary to the Statements of Statutory Accounting Principles* and replaces it as an opening paragraph with updated verbiage.

Recommendation:
NAIC staff recommend that the Statutory Accounting Principles (E) Working Group move this agenda item to the active listing, categorize as nonsubstantive, and expose editorial revisions as illustrated below.

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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 as detailed below.

SSAP No. 53—Property Casualty Contracts – Premiums

Retitle to *SSAP No. 53—Property and Casualty Contracts – Premiums*. This minor modification will title SSAP No. 53 in a consistent manner with other SSAPs (i.e., *SSAP No. 62R—Property and Casualty Reinsurance).*

SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities

54. The purpose of a Sub 1 filing is to gather basic information about the SCA. If the NAIC determines that the reported transaction meets the tests specified, it will complete the filing in the VISION database. If the NAIC determines that the transaction does not meet the tests specified, it ~~shall~~ will not complete the filing in the VISION database and instead shall notify~~notifies~~ the reporting insurance company and the state of domicile in writing of its determination.

SSAP Glossary

1) Remove the footnote in the SSAP Glossary title:
GLOSSARY to the Statements of Statutory Accounting Principles ~~(FN)~~
~~FN – Note that some SSAPs may have terminology that is specific to that topic. Refer to the SSAP for clarification. Accordingly, they are not intended to be applied to other topics~~.

2) Add an opening paragraph:
The terms in this Glossary are common in most SSAPs. Some SSAPs may have terminology that is topic-specific and not intended to be applied to other topics.

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

Issue: *ASU 2020-11, Financial Services—Insurance: Effective Date and Early Application*

Check (applicable entity):

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

Description of Issue: FASB issued *ASU 2020-11, Financial Services—Insurance: Effective Date and Early Application*, which updates guidance on the effective date of the amendments in *ASU 2019-09, Financial Services – Insurance* and *ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts* because of COVID-19.

Existing Authoritative Literature: Both ASU 2019-09 and 2018-12 were rejected for statutory accounting.

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 the Working Group move this item to the active listing, categorized as nonsubstantive and expose 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. This ASU was issued to only address the effective dates of ASU 2019-09 and ASU 2018-12, which were both previously rejected by the Working Group.

Staff Review Completed by Jake Stultz, January 2021

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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.

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Statutory Accounting Principles (E) Working Group
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Issue: ***ASU 2021-02, Franchisors—Revenue from Contracts with Customers (Subtopic 952-606)***

Check (applicable entity):

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

Description of Issue:
In January 2021, the Financial Accounting Standards Board (FASB) issued *ASU 2021-02, Franchisors—Revenue from Contracts with Customers (Subtopic 952-606)*, slightly amending the guidance which was issued in *ASU 2014-09, Revenue from Contracts with Customers*, as it relates to franchisors. As a reminder, the revenue recognition updates were the result of a joint project between FASB and the International Accounting Standards Board (IASB). This project clarified the principles for recognizing revenue and develop a common revenue standard for U.S. GAAP and IFRS (the IASB issued *IFRS 15 – Revenue from Contracts with Customers*) and FASB created ASC Topic 606 – Revenue from Contracts with Customers.

In 2018, the Working Group rejected the guidance in ASU 2014-09 and several other ASUs related to Revenue Recognition in *SSAP No. 47—Uninsured Plans*. Since 2018, all additional ASUs related to revenue recognition have been reviewed by NAIC staff and have been rejected for statutory accounting. The guidance in ASU 2021-02 provides updates and clarifications to the guidance for franchisors, which include several unique accounting concepts that were not fully covered by ASU 2014-09 and ASC Topic 606.

The updates in ASU 2021-02 apply to entities that are not public business entities that are within the scope of Topic 952, which includes all entities that meet the definition of franchisor, that is, the party who grants business rights (the franchise) to the party (the franchisee) who will operate the franchised business. The amendments in this ASU were intended to reduce the cost and complexity of applying Topic 606 to pre-opening services for franchisors that are not public business entities by providing a practical expedient for applying Topic 606 to pre-opening services.

Existing Authoritative Literature:
Premium revenue recognition is detailed throughout the SSAPs, including the following: *SSAP No. 51—Life Contracts; SSAP No. 53—Property Casualty Contracts – Premiums; SSAP No. 54—Individual and Group Accident and Health Contracts* and *SSAP No. 57—Title Insurance*. The ASUs related to ASC Topic 606 have been rejected in SSAP No. 47.

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 2016-19 and 2017-37 address the main ASUs related to ASC Topic 606 and there have been several other agenda items for minor updates to revenue recognition guidance.

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

Convergence with International Financial Reporting Standards (IFRS): ASC Topic 606 and IFRS 15 are the result of the joint project between the FASB and IASB to improve financial reporting by creating common revenue recognition guidance.

Staff Recommendation:
NAIC staff recommends the Working Group move this agenda item to the active listing, categorized as nonsubstantive and expose revisions to reject ASU 2021-02 in *SSAP No. 47—Uninsured Plans*. This recommendation is consistent with how the prior ASUs related to Topic 606 have been treated.

Staff Review Completed by: Jake Stultz, February 2021

<u>Proposed Revisions to SSAP No. 47:</u>

15. This statement rejects *ASU 2014-09, Revenue from Contracts with Customers; ASU 2015-14, Revenue From Contracts With Customers; ASU 2016-08, Revenue From Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net); ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing; ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients; ~~and~~ ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers* <u>and *ASU 2021-02, Franchisors—Revenue from Contracts with Customers*</u>.

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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.*

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Statutory Accounting Principles (E) Working Group
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Issue: Derivatives Hedging Fixed Indexed Products

Check (applicable entity):

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

Description of Issue:
This agenda item proposes the development of new guidance for the accounting and reporting of derivatives that effectively hedge the growth in interest credited for fixed indexed products (for example, fixed indexed annuity (FIA) and indexed universal life (IUL) reported in the general account. (NAIC staff is also investigating the classification of structured / registered indexed linked annuities (RILA) in the separate account, and the use of derivatives in the separate account to hedge risk related to these products. This assessment will be completed within a separate agenda item.) This agenda item is proposed to be substantive, with potential development of a new SSAP.

For purposes of discussion, the following definitions apply:

- Fixed Indexed Annuity (FIA) - Zero risk of loss to the policyholder (and subject to standard nonforfeiture minimum accumulation rates), interest credited based on performance of referenced index. *(This product is addressed in this agenda item.)*

- Registered Index-Linked Annuity (RILA) - Hybrid of a fixed indexed and variable annuity. Has risk of loss to policyholder, but subject to buffers / floors. (Components may be bifurcated between the general and separate account, but aspects captured in the separate account are not subject to nonforfeiture minimums). Subject to registration as a security with the SEC. *(This product may also be referred to as a "structured" index-linked annuity. This product will be discussed in a separate agenda item.)*

Current statutory accounting guidance for the accounting and reporting for derivatives is captured in *SSAP No. 86—Derivatives* and *SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees*. The provisions of these SSAPs are briefly summarized as follows:

- SSAP No. 86 requires derivatives to be reported at fair value, with unrealized gains and losses recognized through surplus unless the derivative qualifies as an effective hedge. If the derivative qualifies as an effective hedge, the derivative follows "hedge accounting," with the derivative reported at a measurement method that mirrors the hedged item. The types of hedging relationships, and criteria that determines effective hedge treatment, generally mirror U.S. GAAP. With these provisions, derivatives used to hedge fixed indexed annuities would often not qualify as effective hedges, so the derivatives would be reported at fair value. From initial assessments, the hedge of a portfolio of FIA/IUL contracts, as well as the identification as an embedded derivative, preclude obtaining a hedge effectiveness under existing U.S. GAAP and SAP. Although FASB has issued ASU 2017-12, which is still pending full statutory accounting review, from initial review, the revisions in that ASU do not assist in qualifying these hedges as effective.

- SSAP No. 108 was issued in 2018 for the specific intent to establish guidance for derivatives that effectively hedge variable annuity guarantees. This guidance was necessary due to financial statement volatility caused by a mismatch of reporting for the derivatives and the variable annuity guarantee reserve. With the adopted provisions, all derivatives are reported at fair value, but the change in fair value is recognized differently based on when the change offsets a change in the reserve (with the use of deferred assets). This approach mitigates the financial statement volatility caused by the fair value changes in qualifying derivatives. The guidance in SSAP No. 108 is significantly different from SSAP No. 86 and U.S. GAAP as it permits qualifying effective hedging assessments in dynamic and macro hedging programs. Use of SSAP No. 108 is restricted, and is limited to annuity contracts and other contracts involving certain guaranteed annuity benefits similar to those offered with variable annuities that are reserved for in accordance with *Valuation Manual 21: Requirements for Principal-Based Reserves for Variable Annuities* (VM-21).

Accounting / Reporting Issue

It has been identified that there is a mismatch of accounting provisions when derivatives are used to hedge the growth in interest credited to reserves (liability). Although the derivative may be an effective hedge to the interest credited for the performance of a referenced index, under the provisions of SSAP No. 86, the derivative does not qualify for hedge accounting. As such, the derivative is reported at fair value, with fair value changes recognized as unrealized gains or losses through surplus. With this reporting, the results of the effective hedge do not directly offset the change in reserve recognized in the summary of operations during the hedging period. The ultimate impact is the effective hedge is not illustrated in the company's performance results within the financial statements, and the current reporting creates a presentation of additional surplus volatility from the use of derivatives, although they are effectively hedging the growth in interest that will be credited to the policy as a direct result of related indices.

Although specialized guidance was developed in SSAP No. 108 to address derivatives hedging variable annuity guarantees, the guidance in SSAP No. 108 cannot be easily adapted to incorporate derivatives hedging the growth in interest credited to FIA/IUL reserves. This is primarily because the fundamental hedging provisions in SSAP No. 108 utilize a fair value hedging approach. Under that approach, the fair value change of the hedging instruments is compared to the fair value change of the variable annuity reserves to determine effectiveness. However, for derivatives hedging the growth in interest credited for FIA/IUL reserves, determination of effectiveness is driven by a cash flow hedge assessment. Meaning, that the hedging derivative will produce cash flows that will offset the indexed-based interest crediting rate in the hedged reserves.

Although the programs may vary significantly by company, it is anticipated that the following elements may be present in these derivative arrangements:

- Designation of many hedged items that reflect bundles of FIA/IUL contracts with similar terms/crediting dates hedged with a single derivative (or portfolio of derivatives) to exactly mirror the terms of the crediting rate, resulting with the intent of a perfect hedge. (It is anticipated that a reporting entity would have many outstanding derivative structures to cover various bundles of FIA contracts.)

- Continuous assessment of hedge, noting deviations between the intended perfect match due to changes in the portfolio of hedged items (e.g., policy lapses) or slight issues with execution (e.g., timing delay in derivative acquisition) or maturity dates (e.g., 360 instead of 365 days).

- Incorporation of additional derivatives (macro/dynamic) as needed to overlay the entire structure to address deviations in the intended match and ensure effective coverage of risk of the FIA/IUL crediting rate.

Proposed Concepts to Address Reporting Mismatch:

This agenda item proposes to incorporate new statutory accounting guidance to establish accounting and reporting concepts that properly represent the use of effective hedges for indexed products in the general account. From an initial assessment, it appears that there are two potential approaches to consider:

1. Approach 1: Establish guidance that permits effective hedge treatment that is in line with SSAP No. 86. With this approach, the derivative would be reported at amortized cost, with direction that the fair value changes in the hedging derivative (at settlement) would be recognized to net investment income (or realized gains and losses) to offset the recognized change in FIA/IUL reserve. With this approach, the derivatives would change the SAP measurement method (from fair value to amortized cost) and result with a disconnect

from U.S. GAAP in the derivative reported value as all derivatives are required to be reported at fair value under U.S. GAAP. This approach would not reflect changes in the derivative position (e.g., if in a loss or gain position) in the financials, so the actual assets / liabilities from derivative activity would not be shown on the balance sheet. However, this approach would eliminate artificial volatility in derivative fair value changes through surplus while the derivative is open. The key provisions would include:

a. Establishing guidance that permits derivatives to qualify as effective hedges. As the hedged item is a portfolio of contracts resulting with an ongoing reserve liability, the guidance would likely need to consider concepts that permit structures that would not qualify as effective under existing SSAP No. 86 provisions.

b. Guidance that directs the reporting of derivative changes at settlement as net investment income (or realized gains and losses) to offset the indexed-based interest credited to FIA/IUL reserves.

This approach is partly in line with the legislation prescribed by the IA Insurance Division. However, that legislation addresses both derivative measurement method and the process to recognize the reserve change. (The IA legislation guidance permits recognizing the reserve change in the same timeframe that the contract holder is credited the reserve change.) From initial industry discussion, if only derivative measurement method is addressed under SAP, this could create greater volatility, even if using an amortized cost measurement method. Additionally, the IA approach only permits certain derivatives to be reported at amortized cost under this approach (e.g., call spreads). Futures, swaps and swaptions are required to be reported at fair value even if they are part of the overall effective hedging program.

2. <u>Approach 2: Establish guidance that permits effective hedge treatment that is in line with SSAP No. 108.</u> With this approach, the derivative would be reported at fair value, with direction that the change in fair value is bifurcated for reporting based on whether the change is an effective hedge to the interest crediting rate change in the hedged FIA/IUL reserve. This approach would be more in line with U.S. GAAP with the use of fair value for the reported value of derivatives and would be designed to recognize the derivative and reserve change at the same time through the income statement. This approach would require assessment as to any fair value fluctuation that does not offset the crediting rate and require separate reporting guidance for those changes. The key provisions would include:

   a. Establishing guidance that permits derivatives to qualify as effective hedges. As the hedged item is a portfolio of contracts resulting with an ongoing reserve liability, the guidance would likely need to consider concepts that permit structures that would not qualify as effective under existing SSAP No. 86 provisions. *(This provision is consistent between the two options.)*

   b. Incorporation of guidance that directs the reporting of fair value changes based on whether they offset the reserve crediting rate. If mirroring the concepts of SSAP No. 108:

      i. Create a timing match to offset the reserve change in the income statement with the derivative change in fair value. This option would likely utilize the "deferred asset" concept for fair value fluctuations that occur in interim periods before settlement. For example, if the product credits interest from the index changes on an annual basis, and there are effective hedges that mirrors this timeframe, the fair value change in the interim periods would be recognized as deferred assets/liabilities, rather than as unrealized gains and losses. With the recognition of the reserve change, the deferred item would be reversed for a coinciding change to net investment income (or realized gains and losses). Although similar to SSAP No. 108, it is anticipated that deferred items would be eliminated over a shorter timeframe, with reversal immediately with the policy reserve change, and not amortized over time. It is expected that most product rate changes occur annually, but variations with 2-year, 5-year and perhaps longer stated periods may exist.

ii. Review and establish guidance (as appropriate) for the recognition of derivative fair value changes, for derivatives identified to as in effective hedges, that do not offset the reserve change from interest credited. (For example, is following concepts from SSAP No. 108, those changes would continue to be reflected as unrealized gains or losses until the derivative closed.) Discussion is expected to identify the presence of such situations and differing dynamics for derivatives hedging indexed products in comparison to variable annuity products.

Existing Authoritative Literature:

- ***SSAP No. 86—Derivatives:*** This SSAP establishes statutory accounting principles for derivative instruments and hedging, income generation and replication (synthetic asset) transactions using selected concepts outlined in FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities.

  Overview of SAP Accounting – SSAP No. 86

  1. Derivative instruments used in hedging transactions that meet the criteria of a highly-effective hedge are considered "effective" and are permitted to be valued and reported in a manner consistent with the hedged asset or liability (referred to as hedge accounting). (P. 20)

  2. Derivative instruments used in hedging transactions that do not meet, or no longer meet the criteria of a highly-effective hedge, or that meets the required criteria by the entity has chosen not to apply hedge accounting, shall be accounted for at fair value, with changes in fair value recorded as unrealized gains or unrealized losses (referred to as fair value accounting). (P. 20)

  3. Entities are permitted to designate instruments to hedge changes in fair value, variations in cash flows or foreign currency exposure. Although these hedging categories are consistent with U.S. GAAP, U.S. GAAP has more restrictions than SAP for when designations may occur, and U.S. GAAP identifies specific instruments ineligible for designation as hedging instruments. (P. 23)

  4. Measurement of hedge effectiveness for a particular hedging relationship shall be consistent with the entity's risk management strategy and the method of assessing hedging effectiveness that was documented at the inception of the hedging relationship (P. 37)

  5. For contracts that qualify for hedge accounting, the change in the carrying value or cash flow of the derivative is to be recorded consistently with how changes in the carrying value or cash flow of the hedged item is recorded. Upon termination of a derivative that qualifies 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 is being hedged is subject to IMR, the gain or loss on the hedging derivative may be realized and shell be subject to IMR after termination.) Entities who choose the alternative method shall apply it consistently thereafter. (P. 22)

- ***SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees:*** This SSAP establishes statutory accounting principles for limited derivatives hedging variable annuity guarantee benefits subject to fluctuations as a result of interest rate sensitivity. The provisions within this statement are separate and distinct from the guidance in SSAP No. 86, as the items subject to the scope of this guidance, and the provisions within, would not qualify for hedge effectiveness under SSAP No. 86. The provisions within this statement are only permitted if all of the components of the statement are met and shall not be inferred as an acceptable statutory accounting approach for derivative transactions that do not meet the state qualifications or that are not specially addressed within the guidance.

Overview of SAP Accounting – SSAP No. 108

1. All derivative instruments are recognized at fair value. (P. 12)

2. Changes in fair value attributed to the hedged risk are recognized as either immediate offsets to the change in reserve liability as realized gains/losses or recognized as deferred assets and liabilities and amortized into realized gain or losses based on the duration of benefit cash flows, not to exceed 10 years. Changes in derivatives that are not attributable to the hedged risk shall be recognized as unrealized gains or losses. (Special surplus is allocated for the net deferred asset or liability.) (P. 13-14)

3. Guidance allows entities to utilize a specified derivative, or a portfolio of specified derivative as the hedging instrument. The hedging instrument can also reflect a dynamic hedging strategy in which a portfolio of derivatives can be rebalanced in accordance with changes to the hedged item in order to adhere to a the specified, documented hedging strategy. (Meaning, the derivatives can be rebalanced to reflect the annuity reserve – taking into consideration the termination / addition of annuity contracts.) (P. 5)

4. Guidance requires specific hedge effectiveness criteria, with the hedging relationship being highly effective in achieving offsetting changes in fair value attributed to the hedge risk during the period that the hedge is designated. This requires reporting entities to calculate the fair value of the hedged item at inception and on an ongoing basis and comparing the fair value change of the hedged item to the fair value change of the hedging instruments to determine whether the relationship is highly effective on a cumulative basis. (P. 10)

5. Application of SSAP No. 108 requires explicit approval from the domiciliary commissioner as well as actuarial certifications. Specific disclosures, as well as a separately Schedule DB-E reporting schedule tracks specific information for the derivatives and the recognition of deferred assets/liabilities. (P. 6 & 23.)

Overview of U.S. GAAP Accounting – U.S. GAAP guidance is based on four cornerstones (815-10-10-1):

1. Derivative instruments represent rights or obligations that meet the definitions of assets or liabilities and should be reported on the financial statements.

   In making this decision, the FASB noted that derivatives are assets or liabilities because they represent rights or obligations and that recognizing those assets and liabilities will make financial statements more complete and more informative. The FASB noted that prior to FAS 133, many derivatives were off-balance-sheet, because, unlike conventional financial instruments (such as stocks, bonds and loans), derivatives often reflect at their inception only a mutual exchange of promises with little or no transfer of tangible consideration. *FAS 133, BOC – 219.*

2. Derivative instruments should be measured at fair value, and adjustments to the carrying amount of hedged items should reflect changes in their fair value (that is gains or losses) that are attributable to the risk being hedged and that arise while the hedge is in effect.

   In making this decision, the FASB identified that fair value is the only relevant measurement attribute for derivatives. They noted that amortized cost is not a relevant measure for derivatives because the historical cost of a derivative often is zero, yet a derivative can be settled or sold at any time for an amount equivalent to its fair value. The reasoning for "held to maturity" instruments being held at amortized cost, was noted as not suitable for derivatives. *FAS 133, BOC - Paragraph 223.*

3. Only items that are assets or liabilities should be reported in the financial statements.

   In making this decision, the FASB identified that derivatives are assets and liabilities, but the gains and losses that result in changes in the fair value of derivatives are not separate assets or liabilities because they have none of the essential characteristics of assets or liabilities. The FASB identified that the act of designating a derivative as a hedging instrument does not convert a subsequent loss or gain into an asset or a liability. A loss is not an asset because no future economic benefit is associated with it. The loss cannot be exchanged for cash, a financial asset, or a nonfinancial asset used to produce something of value or used to settle liabilities. Similarly, a gain is not a liability because no obligation exists to sacrifice assets in the future. *FAS 133, BOC – 229.*

4. Special accounting for items designated as being hedged should be provided only for qualifying items. One aspect of qualification should be an assessment of the expectation of effective offsetting changes in fair value or cash flows during the term of the hedge for the risk being hedged.

   In making this decision, the FASB noted that a primary purpose of hedge accounting is to link items or transactions whose changes in fair values or cash flows are expected to offset each other. The FASB decided that one of the criteria for qualification for hedge accounting should focus on the extent to which offsetting changes in fair values or cash flows on the derivative and the hedged item or transaction during the term of the hedge are expected and ultimately achieved. *FAS 133, BOC – 230.*

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): The following items are noted as recent actions:

- SSAP No. 108 was adopted in 2018, with a Jan. 1, 2020 effective date, to establish specific guidance for derivatives hedging variable annuity guarantees.

- In August 2017, the FASB issued *ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* to improve the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements. In addition, the amendments make certain targeted improvements to simplify the application of the hedge accounting guidance in current U.S. GAAP based on feedback received from preparers, auditors, users and other stakeholders. The ASU did not make any modifications to the four U.S. GAAP cornerstones on the accounting for derivatives in ASC 815-10-10-1. Although a separate agenda item incorporated limited provisions from this ASU into SSAP No. 86 related to hedge effectiveness (Ref #2018-30), the review of this complete ASU (and overall derivatives for SAP) is a pending item for the Working Group. Although the ASU is over 400 pages, the revisions can be briefly categorized as follows:

  1. Amendments permit hedge accounting for risk components in hedging relationships involving nonfinancial risk and interest rate risk in specific scenarios.

  2. Amendments change the guidance for designating fair value hedges of interest rate risk and for measuring the change in fair value of the hedged item in fair value hedges of interest rate risk.

  3. Amendments align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements to increase the understandability of the entity's intended hedging strategies. The revisions require an entity to present the earnings effect of the hedging instrument in the same income statement line item in which the earnings effect of the hedged item

is reported. Furthermore, these amendments eliminate the separate measurements and reporting of hedge ineffectiveness.

4. Amendments expand the components in a hedging instrument allowed to be excluded in the assessment of hedge effectiveness and provide elective accounting guidance for the excluded components.

5. Amendments include targeted improvements to ease the application of assessing hedge effectiveness.

6. Amendments modify existing disclosures and incorporate a tabular disclosure related to the effect on the income statement of fair value cash flow hedges.

- In November 2018, the Working Group adopted revisions to SSAP No. 86 to incorporate revisions to reflect hedge documentation and assessment efficiencies from *ASU 2017-12, Derivatives and Hedging – Targeted Improvements to Accounting for Hedging Activities.*

- The Iowa Insurance Division has shared the following guidance that is permitted in their state: *(Per IA, although both are permitted, a majority of their domestic companies elect to follow the legislation.)*

  - Legislation / *Chapter 97: Accounting for Certain Derivative Instruments Used to Hedge the Growth in Interest Credited for Indexed Insurance Products and Accounting for the Indexed Insurance Products Reserve*. This guidance permits, at the election of the entity, amortized cost for eligible derivative assets. (It specifically excludes derivatives that do not have an amortized cost, including futures, swaps and swaptions.) Additionally, it utilizes a reserve calculation methodology in which interest credits based upon one or more indices are included in the reserve only after those interest credits have been credited to the contract holder under the terms of the annuity contract. https://www.legis.iowa.gov/docs/iac/chapter/09-26-2018.191.97.pdf

  - *Bulletin 06-01: Accounting for Derivative Instruments Used to Hedge the Growth in Interest Credited for Index Products*. This bulletin permits insurance entities to recognize changes in the fair value of derivatives in the summary of operations consistently with how changes in indexed product reserves are recorded. (Under this bulletin, derivatives continue to be reported at fair value.) https://iid.iowa.gov/documents/commissioners-bulletin/accounting-for-derivative-instruments-used-to-hedge-the-growth-in

- It is anticipated that other states may also have issued legislation or bulletins addressing derivatives hedging FIA/IUL products, and NAIC staff will review those provisions throughout the discussion process.

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

Convergence with International Financial Reporting Standards (IFRS): Pursuant to ASU 2017-12, although the language used to describe hedge accounting guidance in the ASU and *IFRS 9, Financial Instruments*, differs, there are several areas of alignment between the two standards, and it is expected that many common hedge accounting strategies will have similar outcomes related to hedging components of financial instruments and nonfinancial terms and in the measurement of hedged items in fair value hedges of interest rate risk. However, differences remain between the two standards in the criteria for qualifying for hedge accounting. Additionally, IFRS 9 retained the separate measurement and reporting of hedge ineffectiveness and does not have broad guidance on presentation.

Staff Recommendation:

NAIC Staff recommends that the Working Group move this item to the active listing, initially categorized as substantive and expose 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, NAIC staff is open for additional commentary and suggestions, and requests to work with industry throughout the process similar to the collaborative efforts that occurred when developing the guidance in SSAP No. 108. With this exposure, NAIC staff recommends notification to the Life Actuarial (E) Task Force.

Pursuant to preliminary information received, NAIC staff has an initial impression that pursuing an approach similar to SSAP No. 108 (use of fair value with deferred assets/liabilities as a mechanism to timely match effective hedge changes through the summary of operations) may be more beneficial to both industry and regulators with improved reporting in the financial statements. This is because the focus of the SAP changes will be on derivative measurement and recognition and will not encompass changing reserve calculations (or the timing of reserve impacts). NAIC staff plans to proceed with starting an issue paper during the exposure period (as time allows). As such, initial informal comments and aspects to consider are requested throughout the exposure period.

Staff Review Completed by:
Julie Gann - NAIC Staff
October 2020

Status:
On November 12, 2020, the Statutory Accounting Principles (E) 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 directs 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 Statutory Accounting Principles (E) 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.

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Statutory Accounting Principles (E) Working Group
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Issue: ***ASU 2021-01, Reference Rate Reform***

Check (applicable entity):

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

Description of Issue:
In March 2020, the Financial Accounting Standards Board (FASB) issued *ASU 2020-04, Reference Rate Reform (Topic 848) Facilitation of the Effects of Reference Rate Reform on Financial Reporting* to ensure the financial reporting of hedging relationships would reflect a continuation of the original contract and hedging relationship during the period of the market-wide transition to alternative reference rates – commonly referred to as "reference rate reform." Reference rate reform typically refers to the transition away from referencing the London Interbank Offered Rate (LIBOR), and other interbank offered rates (IBORs), and moving toward alternative reference rates that are more observable or transaction based. In July 2017, the governing body responsible for regulating LIBOR announced it would no longer require banks to continue rate submissions after 2021 – thus, likely sunsetting both the use and publication of LIBOR.

As is often the case with hedge accounting, a change to the critical terms (including reference rate modifications) typically requires remeasurement of the contract, or in the case of a hedging relationship, a dedesignation of the transaction. However, ASU 2020-04 provides temporary, optional, and expedient relief in that a qualifying modification (because of reference rate reform) should not be considered an event that requires contract remeasurement at the modification date or reassessment of a previous accounting determination. In essence, when a modification (because of reference rate reform) is made to a hedge's critical terms, a reporting entity can continue hedge accounting rather than dedesignate the hedging relationship. For fair value hedges, a reporting entity may change the hedged risk to another permitted benchmark interest rate without dedesignating the relationship; that is if the hedge is expected to remain highly effective in offsetting changes in fair value attributed to the revised hedged risk. For cash flow hedges, a reporting entity may change to another permitted benchmark interest rate without dedesignating the relationship if the forecasted hedge transaction remains probable of occurring.

The derivatives market continues to undergo various other transitions due to reference rate reform initiatives, specifically changing the reference rates used for margining, discounting, or contract price alignment (this change is referred to as a "discounting transition"). While these changes are related to reference rate reform, they are not modifying an interest rate that is expected to be discontinued (e.g., LIBOR). The most prevalent example of a discounting transition occurred in October of 2020 with Central Clearing Parties (CCP). In October of 2020, the CME Group switched to using the Secured Overnight Financing Rate (SOFR) from the Effective Federal Funds Rate (EFFR) to discount, margin and price align most U.S. Dollar based derivative products. A change in the discount rate results in an immediate increase or decrease in a derivative's fair value, which can affect required variation margin payments. In addition, using SOFR instead of EFFR impacts the amount of interest an entity will pay or receive in the related cumulative variation margin. Questions arose in that if a change in these terms would require hedge dedesignation, or if these situations should be afforded the relief offered in ASU 2020-04.

In January 2021, FASB issued *ASU 2021-01, Reference Rate Reform* to clarify that all derivative instruments affected by changes to the interest rates used for discounting, margining or contract price alignment (regardless of whether they reference LIBOR or another rate that is expected to be discontinued as a result of reference rate reform) are in scope of Topic 848. In short summary, for all derivatives affected by the discounting transition, entities may apply the optional expedients and the continuation of contract exceptions allowed in ASU 2020-04.

ASU 2021-01 expands the scope of ASU 2020-04 by allowing an entity to apply the optional expedients, by stating that a change to the interest rate used for margining, discounting or contract price alignment for a derivative is not considered to be a change to the critical terms of the hedging relationship that requires dedesignation. The entity may apply the contract modification relief provided in ASU 2020-04 and continue to account for the derivative in the same manner that existed prior to the changes resulting from reference rate reform or the discounting transition.

Other Items:
The discounting transition previously discussed was primarily driven by CCPs. In October of 2020, CCPs converted open derivative end-of-day valuation calculations from EFFR to SOFR. The process entailed CCPs conducting a standard end-of day valuation cycle based on EFFR. Then, CCPs conducted a special valuation cycle on those same positions, however utilizing SOFR as the new, ongoing discounting rate. Based on the differences between EFFR and SOFR, the CCP issued variation margin adjustments to offset the value differences arising from the change in discount rates. In addition to variation margin adjustments, CCPs issued mandatory EFFR/SOFR basis swaps, thus restoring the account holder's original risk profile. ASU 2021-01 provides guidance for the final settlement of cashflows stating that fair value hedges may adjust the fair value hedge basis while cash flow hedges may adjust accumulated other comprehensive income. The accounting, reporting, and admittance of basis swaps was previously addressed by the Working Group in *INT 20-09: Basis Swaps as a Result of the LIBOR Transition* and is further discussed in the "Activities to Date" section of this agenda item.

Informal note, feedback received from interested parties indicates that most basis swaps were liquidated prior to year-end 2020.

Finally, the effective date of ASU 2021-01 mimics the effective date of ASU 2020-04 in that the optional, expedient guidance may be applied from the beginning of an interim period that includes or is after March 12, 2020 and terminates December 31, 2022.

Existing Authoritative Literature:

ASU 2021-01 effectively increases the scope of the optional, expedient accounting guidance for derivative instruments in ASU 2020-04. Accordingly, only applicable derivative authoritative literature will be shown below. While detailed in the original agenda item (Ref #2020-12), additional SSAPS impacted by ASU 2020-04 were *SSAP No. 15—Debt and Holding Company Obligations* and *SSAP No. 22R—Leases.*

The modifications in ASU 2020-04 address hedge accounting and the allowance for a reporting entity to change the reference rate and other critical terms related to reference rate reform without having to dedesignate the hedging relationship. While alternative benchmark interest rates were previously addressed in agenda item 2018-46 – Benchmark Interest Rate, the accounting for hedged transactions is noted below, with applicable areas bolded for emphasis.

Relevant/Applicable of Overview of existing SAP Accounting – *SSAP No. 86—Derivatives*

> 12. "Benchmark Interest Rate" is a widely recognized and quoted rate in an active financial market that is broadly indicative of the overall level of interest rates attributable to high-credit-quality obligors in that market. It is a rate that is widely used in a given financial market as an underlying basis for determining the interest rates of individual financial instruments and commonly referenced in interest-rate-related transactions. In theory, the benchmark interest rate should be a risk-free rate (that is, has no risk of default). In some markets, government borrowing rates may serve as a benchmark. In other markets, the benchmark interest rate may be an interbank offered rate. In the United States, the interest rates on direct Treasury obligations of the U.S. government, the London Interbank Offered Rate (LIBOR) swap rate, the Fed Funds Effective Rate Overnight Index Swap Rate, the Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Rate, and the Secured Overnight Financing Rate (SOFR) Overnight Index Swap Rate are considered to be benchmark interest rates.

Derivatives Used in Hedging Transactions

20. Derivative instruments used in hedging transactions that meet the **criteria of a highly effective hedge shall be considered an effective hedge and are permitted to be valued and reported in a manner that is consistent with the hedged asset or liability (referred to as hedge accounting).** For instance, assume an entity has a financial instrument on which it is currently receiving income at a variable rate but wishes to receive income at a fixed rate and thus enters into a swap agreement to exchange the cash flows. **If the transaction qualifies as an effective hedge and a financial instrument on a statutory basis is valued and reported at amortized cost, then the swap would also be valued and reported at amortized cost**. Derivative instruments used in hedging transactions that do not meet or no longer meet the criteria of an effective hedge, or that meet the required criteria but the entity has chosen not to apply hedge accounting, shall be accounted for at fair value and the changes in the fair value shall be recorded as unrealized gains or unrealized losses (referred to as fair value accounting).

21. Entities shall not bifurcate the effectiveness of derivatives. A derivative instrument is either classified as an effective hedge or an ineffective hedge. Entities must account for the derivative using fair value accounting if it is deemed to be ineffective or becomes ineffective. Entities may redesignate a derivative in a hedging relationship even though the derivative was used in a previous hedging relationship that proved to be ineffective. **A change in the counterparty to a derivative instrument that has been designated as the hedging instrument in an existing hedging relationship would not, in and of itself, be considered a termination of the derivative instrument.** An entity shall prospectively discontinue hedge accounting for an existing hedge if any one of the following occurs:

a. Any criterion in paragraphs 24-36 is no longer met;

b. The derivative expires or is sold, terminated, or exercised (the effect is recorded as realized gains or losses or, for effective hedges of firm commitments or forecasted transactions, in a manner that is consistent with the hedged transaction – see paragraph 22);

c. The entity removes the designation of the hedge; or

d. The derivative is deemed to be impaired in accordance with paragraph 17. A permanent decline in a counterparty's credit quality/rating is one example of impairment required by paragraph 17, for derivatives used in hedging transactions.

22. 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 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.

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):

The Working Group has taken several actions related to reference rate reform; each are summarized below.

1. Agenda item 2018-46 – Benchmark Interest Rate, incorporated revisions to SSAP No. 86, adding the Securities Industry and Financial Markets (SIFMA) Municipal Swap Rate and the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as acceptable benchmark interest rates for hedge accounting. Prior to this change, only LIBOR and the Fed Funds Effective Swap Rate (also referred to as the Overnight Index Swap Rate) were considered acceptable benchmark interest rates.

2. Agenda item 2020-12 reviews ASU 2020-04, the foundation of which this agenda item and related ASU (2021-01) are based. Agenda item 2020-12 resulted in the Working Group adopting INT 20-01.

3. *INT 20-01: ASU 2020-04 - Reference Rate Reform,* adopted by the Working Group in April 2020, broadly adopted ASU 2020-04 for statutory accounting stating that for statutory accounting:

    - For all contracts within scope of ASU 2020-04, modifications due to reference rate reform are afforded an optional expedient to be accounted for as a continuation of the existing contract.
    - Debt and service agreement modifications, as a result of reference rate reform, should not typically rise to the level of requiring a reversal and rebooking of the liability, as *SSAP No. 15—Debt and Holding Company Obligations* states such liabilities should only be derecognized if extinguished.
    - Lease modifications, solely caused by reference rate reform and ones eligible for optional expedience, likely do not rise to the level of a modification requiring re-recognition as a new lease under *SSAP No. 22R—Leases.*
    - For derivative transactions within scope of ASU 2020-04, a change to the critical terms of the hedging relationship (due to reference rate reform), shall be afforded similar treatment in that the hedging relationship can continue the original hedge accounting rather than dedesignate the hedging relationship.

4. *INT 20-09: Basis Swaps as a Result of the LIBOR Transition*, adopted by the Working Group in July 2020, provided statutory accounting and reporting guidance for basis swaps issued by CCPs. This INT designated that basis swaps, issued by CCPs, in response to reference rate reform (i.e., the discounting transition), shall be classified as a derivative used for hedging. This categorization allowed for the basis swap derivatives to be admitted under SSAP No. 86. Additionally, the INT directed that basis swap derivatives shall not be reported as "effective" unless the instrument qualifies, with the required documentation, as highly effective under SSAP No. 86

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: N/A

Convergence with International Financial Reporting Standards (IFRS): IFRS has taken a similar approach when considering Reference Rate Reform's impact on IFRS 9 (Financial Instruments), IAS 39 (Recognition and Measurement), and IFRS 7 (Financial Instruments – Disclosures).

NAIC Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as nonsubstantive and expose 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 the interest rates used for discounting, margining or contract price alignment (regardless of whether they reference LIBOR or another rate that is expected to be discontinued as a result of reference rate reform) would be in scope of INT 20-01. This exception would allow for continuation of the existing hedge relationship and thus not requiring hedge dedesignation.

The proposed modifications to INT 20-01 temporarily override SSAP No. 86 guidance for affected policies, therefore the policy statement in Appendix F requires 2/3rd (two-thirds) of the Working Group members to be present and voting and a supermajority of the Working Group members present to vote in support of the interpretation before it can be finalized.

Staff Review Completed by: Jim Pinegar, NAIC Staff – January 2021

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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.

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Interpretation of the Statutory Accounting Principles (E) Working Group

INT 20-01: *ASUs 2020-04 & 2021-01- Reference Rate Reform*

NAIC Staff Note: Shaded revisions in paragraph 13 represent proposed revisions for Working Group discussion on May 20, 2021.

INT 20-01 Dates Discussed

Email Vote to Expose March 26, 2020; April 15, 2020; March 15, 2021

INT 20-01 References

Current:
SSAP No. 15—Debt and Holding Company Obligations
SSAP No. 22R—Leases
SSAP No. 86—Derivatives

This INT applies to all SSAPs with contracts within scope of ASU 2020-04, which allows for modifications due to reference rate reform and provides for the optional expedient to be accounted for as a continuation of the existing contract.

INT 20-01 Issue

1. This interpretation has been issued to provide statutory accounting and reporting guidance for the adoption with modification of *ASU 2020-04 – Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting* and *ASU 2021-01 – Reference Rate Reform (Topic 848)* for applicable statutory accounting principles. The Financial Accounting Standards Board (FASB) issued both ASU 2020-04 and ASU 2021-01~~in March 2020~~ to provide~~ as~~ optional, transitional and expedient guidance as a result of reference rate reform.

2. "Reference rate reform" typically refers to the transition away from referencing the London Interbank Offered Rate (LIBOR), and other interbank offered rates (IBORs), and moving toward alternative reference rates that are more observable or transaction based. In July 2017, the governing body responsible for regulating LIBOR announced it will no longer require banks to continue LIBOR submissions after 2021 – likely sunsetting both the use and publication of LIBOR. An important note is that while LIBOR is the primary interbank offering rate, other similar rates are potentially affected by reference rate reform.

3. With a significant number of financial contracts solely referencing IBORs, their discontinuance will require organizations to reevaluate and modify any contract that does not contain a substitute reference rate. A large volume of contracts and other arrangements, such as debt agreements, lease agreements, and derivative instruments, will likely need to be modified to replace all references of interbank offering rates that are expected to be discontinued. While operational, logistical, and legal challenges exist due to the sheer volume of contracts that will require modification, accounting challenges were presented as contract modifications typically require an evaluation to determine whether the modifications result in the establishment of a new contract or the continuation of an existing contract. As is often the case, a change to the critical terms (including reference rate modifications) typically requires remeasurement of the contract, or in the case of a hedging relationship, a dedesignation of the transaction.

4. The overall guidance in ASU 2020-04 is that a qualifying modification (as a result of reference rate reform) should not be considered an event that requires contract remeasurement at the modification date or reassessment of a previous accounting determination. FASB concluded that as reference rate changes are a market-wide initiative, one that is required primarily due to the discontinuance of LIBOR, it is outside the control of an entity and is the sole reason compelling an entity to make modifications to contracts or hedging strategies. As such, FASB

determined that the traditional financial reporting requirements of discontinuing such contracts and treating the modified contract as an entirely new contract or hedging relationship would 1) not provide decision-useful information to financial statement users and 2) require a reporting entity to incur significant costs in the financial statement preparation and potentially reflect an adverse financial statement impact, one of which may not accurately reflect the intent or economics of a modification to a contract or hedging transaction.

5. Guidance in ASU 2020-04 allows a method to ensure that the financial reporting results would continue to reflect the intended continuation of contracts and hedging relationships during the period of the market-wide transition to alternative reference rates – thus, generally not requiring remeasurement or dedesignation if certain criteria are met.

~~5.~~6. Guidance in ASU 2021-01 expanded the scope of ASU 2020-04 by permitting the optional, transitional, expedient guidance to also include derivative contracts that undergo a similar transition but do not specifically reference a rate that is expected to be discontinued. While these contract modifications to not reference LIBOR (or another reference rate expected to be discontinued), the changes are the direct result of reference rate reform and were deemed to be eligible for similar exception treatment. ASU 2020-01 allows for modifications in interest rates indexes used for margining, discounting or contract price alignment, as a result of reference rate reform initiatives (commonly referred to as a “discounting transition”) to be accounted for as a continuation of the existing contract and hedge accounting.

~~6.~~7. The optional, expedient and exceptions guidance provided by the amendments in ASU 2020-04 and ASU 2020-01 are applicable for all entities. However, they are only effective as of March 12, 2020 through December 31, 2022. This is because the amendments ~~in ASU 2020-04~~ are intended to provide relief related to the accounting requirements in generally accepted accounting principles (GAAP) due to the effects of the market-wide transition away from IBORs. The relief provided by the amendments is temporary in its application in alignment with the expected market transition period. However, the FASB will monitor the market-wide IBOR transition to determine whether future developments warrant any changes, including changes to the end date of the application of the amendments in this ASU. If such an update occurs, the Working Group may also consider similar action. It is not expected that the Working Group will take action prior to or in the absence of a FASB amendment.

~~7.~~8. The accounting issues are:

a. Issue 1: Should a reporting entity interpret the guidance in ASU 2020-04 as broadly accepted for statutory accounting?

b. Issue 2: Should the optional, expedient and exception guidance in ASU 2020-04 apply to debt and other service agreements addressed in SSAP No. 15?

c. Issue 3: Should the optional, expedient and exception guidance in ASU 2020-04 apply to lease transactions addressed in SSAP No. 22R?

d. Issue 4: Should the optional, expedient and exception guidance in ASU 2020-04 apply to derivative transactions addressed in SSAP No. 86?

~~d.~~e. Issue 5: Should the optional, expedient and exception guidance in ASU 2021-01 apply to derivative transactions addressed in SSAP No. 86?

INT 20-01 Discussion

~~8.~~9. For Issue 1, the Working Group came to the consensus that ASU 2020-04 shall be adopted, to include the same scope of applicable contracts or transactions for statutory accounting with the only modification related to a concept not utilized by statutory accounting, as noted below. The Working Group agreed the amendments provide appropriate temporary guidance that alleviate the following concerns due to reference rate reform:

a. Simplifies accounting analyses under current GAAP and statutory accounting principles (SAP) for contract modifications.

i. All contracts within scope of ASU 2020-04, which allows for modifications due to reference rate reform and provides for the optional expedient to be accounted for as a continuation of the existing contract.

b. Allows hedging relationships to continue without dedesignation upon a change in certain critical terms.

c. Allows a change in the designated benchmark interest rate to a different eligible benchmark interest rate in a fair value hedging relationship.

d. Suspends the assessment of certain qualifying conditions for fair value hedging relationships for which the shortcut method for assuming perfect hedge effectiveness is applied.

e. Simplifies or temporarily suspends the assessment of hedge effectiveness for cash flow hedging relationships.

f. The only SAP modification to this ASU is related to the option to sell debt currently classified held-to-maturity. This concept is not employed by statutory accounting and thus is not applicable.

~~9.~~10. For Issue 2, the Working Group came to the consensus that debt and service agreement modifications, as a result of reference rate reform, should not typically rise to the level of requiring a reversal and rebooking of the liability, as SSAP No. 15 states such liabilities should only be derecognized if extinguished. A reference rate modification should not generally require de-recognition and re-recognition under statutory accounting. Nonetheless, for clarity and consistency with ASU 2020-04, the Working Group came to the consensus that should an eligible contract be affected by reference rate reform, then the temporary guidance in ASU 2020-04 shall apply.

~~10.~~11. For Issue 3, the Working Group came to the consensus that lease modifications, solely caused by reference rate reform and ones eligible for optional expedience, likely do not rise to the level of a modification requiring re-recognition as a new lease under statutory accounting. SSAP No. 22R, paragraph 17 states only modifications in which grant the lessee additional rights shall be accounted for as a new lease. These changes are outside the scope allowed for optional expedience in ASU 2020-04. Nonetheless, for clarity and consistency with ASU 2020-04, the Working Group came to a consensus that if an eligible lease affected by reference rate reform, then the temporary guidance in ASU 2020-04 shall apply.

~~11.~~12. For Issue 4, the Working Group came to the consensus that ASU 2020-04 shall be applied to derivative transactions as the following considerations provided in the ASU are appropriate for statutory accounting:

a. For any hedging relationship, upon a change to the critical terms of the hedging relationship, allow a reporting entity to continue hedge accounting rather than dedesignate the hedging relationship.

b. For any hedging relationship, upon a change to the terms of the designated hedging instrument, allow an entity to change its systematic and rational method used to recognize the excluded component into earnings and adjust the fair value of the excluded component through earnings.

c. For fair value hedges, allow a reporting entity to change the designated hedged benchmark interest rate and continue fair value hedge accounting.

d. For cash flow hedges, adjust the guidance for assessment of hedge effectiveness to allow an entity to continue to apply cash flow hedge accounting.

~~12.~~13. For Issue 5, the Working Group came to a tentative consensus on March 15, 2021, that ASU 2021-01 shall be applied to derivative transactions for statutory accounting. Accordingly, derivative instruments that are modified to change the reference rate used for margining, discounting, or contract price alignment that is a result of reference rate reform (regardless of whether the reference rate that is expected to be discontinued) are eligible for the exception guidance afforded in ASU 2020-04 in that such a modification is not considered a change in the critical terms that would require dedesignation of the hedging relationship. In addition, for all derivatives (those qualifying for hedge accounting, those that do not qualify for hedge accounting and replication (synthetic asset) transactions (RSAT)), a reporting entity may account for and report modifications (that are within 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 contract and its replacement with a new reference rate reform contract. This includes in-scope modifications of centrally cleared swap contracts whether they are automatically transitioned at a cessation date or voluntarily executed prior to cessation.

~~13.~~14. Additionally, for GAAP purposes, if an entity has not adopted the amendments in *ASU 2017-12, Derivatives and Hedging*, it is precluded from being able to utilize certain expedients for hedge accounting. For statutory accounting purposes, only the hedge documentation requirements were adopted from ASU 2017-12, while the remainder of the items are pending statutory accounting review. The Working Group concluded that all allowed expedient methods are permitted as elections for all reporting entities under statutory accounting. However, if a reporting entity is a U.S. GAAP filer, the reporting entity may only make elections under ASU 2017-12 if such elections were also made for their U.S. GAAP financials.

INT 20-01 Status

~~14.~~15. ~~No f~~Further discussion is planned.

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

Issue: SSAP No. 97 – Valuation of Foreign Insurance SCAs

Check (applicable entity):

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

Description of Issue:
In March 2020, agenda item 2018-26 – SCA Loss Tracking – Accounting Guidance adopted guidance in *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* to state that reported equity method losses of an investment in a subsidiary controlled or affiliated entity (SCA) would not create a negative value in a SCA investment, thus equity method losses would stop at zero. However, the agenda item also clarified that to the extent there was a financial guarantee or commitment, it would require appropriate recognition under *SSAP No. 5R—Liabilities, Contingencies and Impairment of Assets.*

In November 2020, the Working Group adopted agenda item 2020-18 - SSAP No. 97 Update and removed a lingering, superseded reference regarding negative equity method loss valuations.

However guidance in SSAP No. 97 also requires specific adjustments to 8.b.ii (insurance related SCA) and 8.b.iv (foreign insurance SCA) entities. These long-standing adjustments require the non-admission of certain assets to achieve a limited statutory basis of accounting. The adjustments have typically been viewed as necessary in order to prevent assets being held by SCA receiving more favorable treatment than had the assets been held directly by the insurer. (e.g., requiring the nonadmittance of certain assets per *SSAP No. 20—Nonadmitted Assets*). Per SSAP No. 97, an equity method of accounting for 8.b.ii and 8.b.iv entities would be a beginning point which would then be adjusted by the provisions of SSAP No. 97, paragraph 9 (see "authoritative literature section"). It is important to note the outcome of these adjustments can result in a negative equity valuation of the investment. Again, this is so assets held by an SCA aren't reported at a higher value than had they been held directly by the insurer.

During the discussion of agenda item 2020-18, industry comments requested consideration of whether 8.b.iv entities should be subject to the provisions of SSAP No. 97, specifically that paragraph 9 adjustments may result in a negative equity valuation. While stating many positions, industry's primary response that foreign insurance operations are subject to foreign jurisdiction and should be allowed to stand independently of a domestic insurer – thus in the absence of a guarantee or commitment, equity valuation should not go negative and thus stop at zero. Comments were received from industry noted that the circumstances that would cause a foreign insurance reporting entity to record negative equity is not prevalent, however indicated the potential to arise in the future.

At the direction of the NAIC staff have drafted this agenda item to determine if further edits to SSAP No. 97 are required, specifically if the required statutory adjustments to 8.b.iv entities should no longer be able to result in a negative equity valuation.

One note, NAIC staff reviewed all SCA filings for the last 3 years, noting that less than 7% of all SCA filings were 8.b.iv entities. It was further noted that there was not a single instance of an 8.b.iv in a negative equity situation.

Existing Authoritative Literature:
Paragraph 9 of SSAP No. 97 details the modifications that are necessary to adjust audited U.S .Generally Accepted Accounting Principle (GAAP) financial statements to a limited statutory basis of accounting. These

long-standing adjustments ensure that assets held by an SCA are not accounted for in a more favorable manner than had the assets been held directly by the insurer.

SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities

9. The limited statutory basis of accounting for investments in noninsurance SCA entities, subject to paragraph 8.b.ii. and foreign insurance SCA entities, subject to paragraph 8.b.iv., shall be adjusted for the following:

a. Nonadmit assets pursuant to the following statutory accounting principles as promulgated by the NAIC in the *Accounting Practices and Procedures Manual*;

i. *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*

ii. *SSAP No. 16R—Electronic Data Processing Equipment and Software*

iii. *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

iv. *SSAP No. 20—Nonadmitted Assets*

v. *SSAP No. 21R—Other Admitted Assets* (e.g., collateral loans secured by assets that do not qualify as investments are nonadmitted under SAP)

vi. *SSAP No. 29—Prepaid Expenses*

vii. *SSAP No. 105R—Working Capital Finance Investments*

b. Expense costs that are capitalized in accordance with GAAP but are expensed pursuant to statutory accounting as promulgated by the NAIC in the *Accounting Practices and Procedures Manual* (e.g., deferred policy acquisition costs, preoperating, development and research costs, etc.);

c. Adjust depreciation for certain assets in accordance with the following statutory accounting principles:

i. *SSAP No. 16R—Electronic Data Processing Equipment and Software*

ii. *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

iii. *SSAP No. 68—Business Combinations and Goodwill*

d. Nonadmit the amount of goodwill of the SCA in excess of 10% of the audited U.S. GAAP equity of the SCA's last audited financial statements.

e. Nonadmit amount of the net deferred tax assets (DTAs) of the SCA in excess of 10% of the audited U.S. GAAP equity of the SCA's last audited financial statements.

f. Nonadmit any surplus notes held by the SCA issued by the reporting entity.

g. Adjust the U.S. GAAP annuity account value reserves of a foreign insurance SCA, with respect to the business it wrote directly, using the commissioners' annuity reserve valuation method (CARVM) as defined in paragraphs 14 and 15 of Appendix A-820 (including the reserving provisions in the various Actuarial Guidelines which support CARVM). The valuation interest rate and mortality tables to be used in applying CARVM should be that prescribed by the foreign insurance SCA's country of domicile. If the Foreign SCA's country of domicile does not prescribe the necessary tables and/or rates, no reserve adjustment shall be made.

Note that the outcome of these adjustments, can result in a negative equity valuation of the investment.

SSAP No. 97, Exhibit C:

7. **Q – Is it possible for an SCA investment valued using an equity method to be reported as a negative value?**

7.1 **A –** Yes, the equity method noninsurance SCA could have a negative equity. For example, SSAP No. 97, paragraph 8.b.ii., relating to noninsurance SCA entities, may require some assets to be reported as a negative value (nonadmitted) in paragraph 9. In this example, a paragraph 8.b.ii. SCA subsidiary that is only holding furniture, which is nonadmitted, would be reflected with negative equity to the extent the value of the nonadmitted asset(s) exceed(s) reported equity. It should be noted that although SSAP No. 97, paragraph 13.e., discusses some situations in which the equity method should be discontinued, this does not apply to SCA entities, which meet the requirements of paragraph 8.b.ii. In addition, SSAP No. 97, paragraph 13.e., lists some situations where the equity method for 8.b.ii and 8.b.iv entities would result in a valuation that is less than zero.

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 items 2018-26 – SCA Loss Tracking – Accounting Guidance and 2020-18 – SSAP No. 97 Update were previously adopted. Agenda item 2018-26 resulted in revisions to *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* and *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* stating that equity losses of an SCA would not go negative (thus stopping at zero), however the guaranteed liabilities would be reported to the extent there is a financial guarantee or commitment. Agenda item 2020-18 resulted in revisions with clarifying edits to Exhibit C, question 7, in SSAP No. 97, as well as removed a superseded statement that guarantees or commitments from the insurance reporting entity to the SCA could result in a negative equity valuation of the SCA.

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:
Staff recommends that the Working Group move this item to the active listing, categorized as nonsubstantive and expose the intent to move this item to the disposal listing without statutory edits. <u>Per staff's review of SCA Sub 2 filings filed with an 8b(iv) valuation method, there were no noted instances of negative value SCAs, therefore we do not recommend revisions to the existing guidance</u>. This exposure will allow industry to determine if they are aware of any prevalent examples of a negative equity valuation in a foreign insurance SCA (8.b.iv) and provide detailed information to NAIC staff for assessment.

NAIC staff highlights that if such an event (negative equity due to nonadmitted assets) was to actually occur at some point, and the company was to question whether the negative equity in the SCA should be reported, that this should be addressed directly with the state of domicile. With this approach, the domiciliary state would be able to assess the limited statutory edits that were performed, the extent to which assets are held in the SCA that would be nonadmitted if held directly by the insurer, and how the SCA obtained those assets.

Staff Review Completed by: Fatima Sediqzad - NAIC Staff
February 2021

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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 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.

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

Issue: Accounting for Cryptocurrencies

Check (applicable entity):

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

Description of Issue:
NAIC staff have received several inquiries related to the statutory accounting treatment for cryptocurrencies, which are defined as a digital currency in which transactions are verified and records maintained by a decentralized system using cryptography, rather than by a centralized authority, such as the Federal Reserve System. These questions generally inquiry whether Bitcoin is permitted to be admitted, but a recent inquiry asked whether Bitcoin is captured in the cash definition within *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments.*

The most valuable cryptocurrency as of February 2021 is Bitcoin, which has been in circulation since 2009. Cryptocurrencies are currently purchased and exchanged using a limited number of unregulated digital currency exchanges. As of February 2021, there are approximately 4,000 different cryptocurrencies available on 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 total market value and increased popularity has led to increased interest in the market by traditional financial institutions. Additionally, the recently steep increase in value has attracted speculative investors.

For statutory accounting, cash is defined in SSAP No. 2R as a "medium of exchange that a <u>bank or other similar financial institution</u> will accept for deposit and allow an immediate credit to the depositor's account." <u>**Cryptocurrencies do not meet this definition because these assets are not able to be deposited or exchanged with most U.S. banks and financial institutions**</u>. There have been some recent changes in the market as PayPal now allows users to buy, sell and hold some cryptocurrencies. 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. NAIC staff are aware that this treatment is evolving and that in the future banks may accept cryptocurrencies in the same manner as true government-backed currencies, which could then meet the statutory accounting definition of cash. However, at this time, NAIC staff note that cryptocurrencies currently do not meet the definitions of cash equivalents, drafts, or short-term investments as they are defined in SSAP No. 2R.

With regards to the inquiry on whether cryptocurrencies are considered admitted assets, pursuant to *SSAP No. 4—Assets and Nonadmitted Assets*, paragraph 3, assets are not permitted to be admitted unless specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*. As such, as cryptocurrencies are not specifically identified as admitted, these are nonadmitted assets.

At this time, no Committees or groups at the NAIC, including the Securities Valuation Office (SVO), have taken any action or established a position on cryptocurrencies. Currently, auditors must rely on guidance provided by the American Institute of Certified Public Accountants through a nonauthoritative practice guide.

Existing Authoritative Literature:
Cash is defined in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* as 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." *SSAP No. 4— Assets and Nonadmitted Assets* provides guidance that assets which are not addressed in the *Accounting Practices and Procedures Manual* default to nonadmitted status. Nonadmitted assets are detailed in *SSAP No. 20—Nonadmitted Assets*.

<u>SSAP No. 4</u>

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

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

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

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): IFRS has not yet taken a firm position on cryptocurrencies.

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as nonsubstantive and expose the interpretative guidance provided by *INT 21-01T: Statutory Accounting Treatment for Cryptocurrencies*. This guidance clarifies 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. NAIC staff will continue to monitor the evolution of cryptocurrencies and address this topic further, including addressing any statements made by FASB or the AICPA, for any significant changes in the usage and design of cryptocurrencies.

With this exposure, the Working Group requests input from Interested Parties and the insurance company trade groups that follow the Working Group to gather information from their members on current ownership of cryptocurrencies. The Working Group requests information on:

1. Extent to which companies currently hold cryptocurrencies,
2. How the acquisition in cryptocurrency is held (held directly by the insurer or indirectly through and SCA),
3. Which cryptocurrencies they are acquiring in (Bitcoin, Ethereum, Litecoin, etc.), and
4. General level of interest for future investment by both companies that currently do and do not own cryptocurrencies.

Staff Review Completed by: Jake Stultz, February 2021

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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.

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Interpretation of the Statutory Accounting Principles Working Group

INT 21-01T: Accounting for Cryptocurrencies

NAIC Staff Note: Shaded revisions in paragraphs 4, 5, and 7 represent proposed revisions for Working Group discussion on May 20, 2021.

INT 21-01T Dates Discussed

March 15, 2021

INT 21-01T References

SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments

INT 21-01T Issue

1. This agenda item is to address questions regarding statutory accounting treatment for cryptocurrencies, which are defined as a digital currency in which transactions are verified and records maintained by a decentralized system using cryptography, rather than by a centralized authority. Cryptocurrencies are purchased and exchanged using a limited number of unregulated digital currency exchanges and are not held or offered by major banks.

2. The most valuable cryptocurrency as of February 2021 is Bitcoin, which has been in circulation since 2009, and there are approximately 4,000 different cryptocurrencies available on 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 the total outstanding cryptocurrencies nearing $1 trillion as of February 2021. The total market value and increased popularity has led to increased interest in the market by traditional financial institutions and insurance companies.

3. No NAIC Committees or groups have taken any action or established a position on cryptocurrencies. Currently, auditors must rely on guidance provided by the American Institute of Certified Public Accountants through a nonauthoritative practice guide.

4. This Interpretation intends to clarify that directly held cryptocurrencies are nonadmitted assets for statutory accounting.

INT 21-01T Discussion

5. Directly held ~~C~~cryptocurrencies have not been identified in the *Accounting Practices and Procedures Manual* (AP&P Manual) as an admitted asset, and do not meet the definition of any admitted asset that is defined in the AP&P Manual. Accordingly, by default they are a nonadmitted asset per *SSAP No. 4—Assets and Nonadmitted Assets*, paragraph 3, as they are not specifically identified in the *Accounting Practices and Procedures Manual* as an admitted asset.

6. Cash is defined in *SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term Investments* as 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." Cryptocurrencies are currently not accepted by major banks and do not operate like a traditional currency, and as such do not meet the definition of cash in SSAP No. 2R.

INT 21-01T Consensus

7. The Statutory Accounting Principles (E) Working Group reached a tentative consensus that directly held cryptocurrencies do not meet the definition of an admitted asset and are therefore considered to be a nonadmitted asset for statutory accounting. The Working Group intends to rely on this interpretation for statutory accounting and will address cryptocurrencies further once FASB has provided definitive guidance.

INT 21-01T Status

8. Further discussion is planned.

9. The Statutory Accounting Principles (E) Working Group will continue to monitor the evolution of cryptocurrencies and subsequently review this interpretation as appropriate.

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
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Issue: State ACA Reinsurance Programs

Check (applicable entity):

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

Description of Issue:
SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act provides guidance regarding the three Affordable Care Act (ACA) risk sharing programs known as risk adjustment, the transitional reinsurance program and risk corridors. All three programs were to assist with rate stabilization in the individual market. Risk adjustment was originally the only permanent program and the other two were temporary. Although the 2014-2016 transitional reinsurance program has ended, several states have received approval from the Department of Health and Human Services (HHS) to run similar state ACA reinsurance programs under what are known as Section 1332 waivers.

This agenda item is to provide accounting and reporting guidance regarding State ACA reinsurance programs being run under Section 1332 waivers. Note that states can seek Section 1332 waivers to address a variety of issues such as:

- Individual and employer mandates;
- Essential health benefits (EHBs);
- Limits on cost sharing for covered benefits;
- Metal tiers of coverage;
- Standards for health insurance marketplaces, including requirements to establish a website, a call center, and a navigator program; and
- Premium tax credits and cost-sharing reductions.

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. As these programs seek to 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.

The original transitional reinsurance program and the subsequent state ACA reinsurance programs are not reinsurance in the true sense. They typically rely on group products to help fund the program, but do not typically allow the group products to receive reinsurance distributions. Therefore the group products help fund the program but are not true participants. Because of this, a hybrid approach was incorporated into the SSAP No. 107 accounting guidance. A similar hybrid approach is recommended for state ACA reinsurance programs. At a high level this approach divides products into 3 broad categories. This includes:

1. Subject individual products (typically individual plans) that may pay an insurance contribution and are eligible to receive reinsurance distributions. These programs report like an involuntary reinsurance pool as is described in *SSAP No. 63—Underwriting Pools*.

2. Other insured health products (typically group plans) that are not eligible for reinsurance distributions under the terms of the state ACA reinsurance program. These products treat the amounts as assessments reported in taxes, licenses and fees similar to treatment under *SSAP No. 35R—Guaranty Funds and Other Assessments*.

3. Self-insured plans where the reporting entity is acting as an administrator, and will exclude the payments made on behalf of the self-insured plan from the reporting entity's operations, consistent with the guidance in *SSAP No. 47—Uninsured Plans*.

Existing Authoritative Literature:
SSAP No. 35R—Guaranty Funds and Other Assessments provides guidance on assessments.

SSAP No. 63—Underwriting Pools provides guidance regarding involuntary pools.

SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act provides the following:

Transitional Reinsurance Program – Description and Overview

17. The transitional reinsurance program based on Section 1341 of the ACA is effective for plan years 2014 through 2016. Reinsurance assessments will be collected and distributions will be issued during the three-year term.

18. All issuers of major medical commercial products and third party administrators (TPAs) on behalf of uninsured group health plans are required to contribute funding at the national contribution rate to HHS. States establishing reinsurance programs may collect additional funding. Non-grandfathered individual plans are eligible to receive benefit program distributions via an excess-of-loss reinsurance system. Grandfathered plans are ineligible. Group plans are required to contribute funding, but are not eligible to receive reinsurance program distributions.

19. In general, this transitional reinsurance program provides funding to issuers in the individual market that incur high claims costs for enrollees. The program requires assessments from all issuers and TPAs on behalf of group health plans based on a per member annual fee established by HHS. The reinsurance assessment will fund reinsurance program distributions plus disbursements to the U.S. Treasury, in addition to covering administrative expenses of the program.

20. Consequently, 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. For the group plans, which are required to contribute funding but are not eligible to receive program distributions, the program is an assessment payable by the reporting entity and not a pool.

21. The national transitional reinsurance program assessment rate for all issuers and TPAs will be established by HHS and will be designed to collect more than $12 billion in 2014 to cover the required $10 billion for the reinsurance program, the $2 billion contribution to the U.S. Treasury, and additional amounts to cover the administrative costs of the federal government entity and applicable reinsurance entities. States electing to operate their own reinsurance program have the option to increase the reinsurance assessment rate to provide additional funding for the reinsurance program or to fund the administrative expenses of the applicable reinsurance entity. Assessments for the reinsurance program must fund the reinsurance program of $10 billion in 2014, $6 billion in 2015 and $4 billion in 2016, plus disbursements to the U.S. Treasury of $2 billion, $2 billion and $1 billion for years 2014 through 2016, in addition to covering administrative expenses of the applicable reinsurance entity or HHS.

22. Reinsurance program distributions will be processed either by the applicable reinsurance entity or by HHS and will be made to issuers of non-grandfathered individual market plans for high claim costs of enrollees. Distributions from the applicable reinsurance entity to insurers providing individual coverage will be calculated as a coinsurance rate multiplied by the eligible claims submitted for an individual enrollee's covered benefits between an attachment point and the reinsurance cap for each benefit year. The coinsurance rate, attachment point and

reinsurance cap are initially determined by HHS, but may be modified by the state, if the state chooses to establish its own reinsurance program.

23. Each state is eligible to establish a reinsurance program, regardless of whether the state establishes a Marketplace Exchange. If a state establishes a reinsurance program, the state must enter into a contract with an applicable reinsurance entity or entities or establish a reinsurance entity to carry out the program. If a state does not elect to establish its own reinsurance program, HHS will administer the reinsurance program on behalf of that state. HHS establishes the annual administrative portion for the fee. (For example, the 2014 fee will be $0.11 per-member per-year resulting in $20.3 million of administrative expense funding).

24. Reinsurance assessments to fund the program are made on an annual basis with billing beginning December 15, 2014. An insurer may submit claims for reimbursement when an enrollee of the reinsurance-eligible plan has met the applicable criteria as determined by either the state or HHS. Claims may be submitted through April 30 of the year following the benefit year. HHS will distribute reinsurance program funds among issuers nationally based on submitted claims. Issuers will be notified of pending reinsurance distributions by June 30 following the benefit year. If the requests for distributions exceed the actual assessments collected, HHS will reduce reinsurance distributions on a pro-rata basis. If the requests for distributions are less than actual assessments collected, HHS will increase reinsurance distributions on a pro-rata basis.

Transitional Reinsurance Program – Accounting Treatment

25. Due to the diverse elements of the transitional reinsurance program, which includes characteristics of traditional reinsurance, involuntary pools and governmental assessments, a hybrid accounting approach is required. The accounting treatment for the transitional reinsurance program outlined below is discussed in terms of the payables and receivables and the impact to the health insurance products subject to the program.

26. The following are the broad groupings of the health insurance products subject to the transitional reinsurance program:

a. Individual insured health products subject to the 2014 ACA market reforms. This excludes grandfathered and non-grandfathered 2013 products (referred to as subject individual insured products);

b. Other insured health products. This encompasses products which are not subject to the ACA market reforms including individual grandfathered and non-grandfathered (referred to as other insured health products);

c. Self-insured health products.

27. The guidance in this section will provide treatment for each of the assessments payable and program distribution receivable elements of the program listed below for the health insurance products listed in paragraph 26.

a. Assessments for reinsurance

b. Administrative costs assessments

c. Additional U.S. Treasury assessment

d. Reinsurance distributions

Subject Individual Insured Health Products

Subject Individual Insured Issuers - Assessments Payable for Reinsurance

28. Transitional reinsurance assessments attributable to enrollees in individual plans are treated as ceded reinsurance premium. This applies both to assessments made at the national assessment rate and to any state-elected additional assessments that will fund reinsurance program distributions. Ceded premiums would be

reported as a reinsurance cession and follow reinsurance accounting in accordance with SSAP No. 61R, paragraph 17 and paragraphs 25-27:

29. For the individual coverage issuers, this is an involuntary pool and under the terms of the transitional reinsurance program, the transfer of risk and timely reimbursement requirements of SSAP No. 61R are deemed to be met.

30. With regard to individual coverage issuers, the transitional reinsurance program is more similar to traditional reinsurance than it is to an assessment, because program assessments are made to and program distributions are received from the government or government-sponsored entity. Accordingly, the program is accounted for as reinsurance for individual insured products subject to the transitional reinsurance program.

31. The provisions of SSAP No. 63, paragraph 3, define involuntary pools.

32. The transitional reinsurance program differs from an involuntary pool, in that there is not a proportionate sharing of the entire results of a pool. However, the purpose is very similar: to address the additional costs associated with high-risk individuals. Furthermore, HHS has noted, *"the Affordable Care Act … requires that states eliminate or modify high-risk pools to the extent necessary to carry out the reinsurance program,"* which likewise highlights the similar purposes of the two mechanisms. Therefore, SSAP No. 63, paragraph 8, provides additional relevant guidance. As the transitional reinsurance program is a mechanism for sharing the additional costs associated with high-risk individuals, it is accounted for as traditional reinsurance.

Subject Individual Insured Issuers - Reinsurance Administrative Expense Assessments

33. The assessment payable by the reporting entity for administrative expenses attributable to individual coverage is reflected as ceded premium. This applies both to assessments made at the national assessment rate and to any state-required assessments that will provide additional funding for administrative expenses.

34. Normally reinsurance premiums are set at a level intended to cover anticipated claim costs and include an administrative charge component. Therefore, as a matter of consistency, it is appropriate to include the administrative charge component for the transitional reinsurance program in ceded premium for individual insured products.

Subject Individual Insured Issuers - U.S. Treasury Assessment

35. Because this portion of the assessment is earmarked for the U.S. Treasury and not for the reimbursement of claims or to cover the operating costs of the reinsurance program, it is a federal assessment not based on income. This portion of the assessment is not treated as ceded premium, but as an assessment under SSAP No. 35R and is reflected in the same expense category as taxes, licenses and fees. This is also consistent with annual statement expense reporting categories.

Subject Individual Insured Issuers - Reinsurance Program Distributions

36. Program distributions received from the ACA transitional reinsurance program for individual insurance is reflected as ceded claim benefit recoveries. This applies both to distributions received pursuant to the uniform federal reinsurance parameters and to any state distribution received.

37. In keeping with the rationale for reinsurance assessments above, distributions receivable from the transitional reinsurance program for individual insurance products is reflected the same as traditional reinsurance recoveries as described in SSAP No. 61R, paragraph 27.

38. Therefore, recoveries received are reported in the summary of operations and will reduce the ceding entity's reported benefits paid.

39. HHS and all applicable reinsurance entities shall be reported consistent with providers to an involuntary pool and will be treated as authorized reinsurers for the purposes of financial reporting for subject individual health products.

40. All receivables from the transitional reinsurance program are subject to the 90-day nonadmission 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.

Other Insured Health Products

Other Insured Health Products – Assessments Payable for Reinsurance

41. Transitional reinsurance program reinsurance assessments made for enrollees in fully insured plans other than individual plans are treated as an assessment payable by the reporting entity and charged to taxes, licenses and fees. This applies both to assessments made at the national assessment rate and to any state assessments that will fund reinsurance program distributions. In this case, for fully insured non-individual plans, the entity cannot, under the terms of the program, be deemed to be "participating," as funds for claim recoveries will not be re-distributed back to the issuer for the coverage that is being assessed. Therefore, issuers of other insured health products that are not for individuals are paying an involuntary fee but are not participating in an involuntary pool.

42. The treatment of the transitional reinsurance program reinsurance assessments for non-individual fully insured plans differs from the treatment for individual plans. Since the non-individual plans are not eligible for reimbursement, they are not participating in a reinsurance arrangement, and thus, the assessments are not treated as ceded premium. As an involuntary assessment, the transitional reinsurance program reinsurance assessments, consistent with SSAP No. 35R are treated as an assessment payable by the reporting entity and charged to taxes, licenses and fees expense. The expense is accrued in proportion to the other insured health enrollees base that will be used to determine the assessments payable as the premium subject to the assessment is written.

Other Insured Health Products - Reinsurance Administrative Expense Assessments

43. The reinsurance program administrative costs for other insured health products are an assessment payable by the reporting entity. This applies both to assessments made at the national assessment rate and to any state assessment that will fund administrative expenses and is reflected in the same expense category as taxes, licenses and fees.

Other Insured Health Products - U.S. Treasury Assessment

44. The additional U.S. Treasury assessment for other insured health products is a federal assessment payable by the reporting entity which is not based on income and is reflected in the same expense category as taxes, licenses and fees.

Other Insured Health Products - Reinsurance Program Distributions (not applicable)

45. Reinsurance recoveries will not occur for insured health products other than individual. Other insured health products will pay the transitional reinsurance program assessments payable but not receive program distributions for claims.

Self-Insured Health Products

Self-Insured Health Products - Assessments Payable for Reinsurance

46. Assessments made on behalf of self-insured plans which are administered by the reporting entity are uninsured plans and are excluded from the reporting entity's statement of operations, with respect to both monies received from the plans and assessments disbursed by the reporting entity. Any resulting liabilities or receivables shall be reported as liabilities and receivables held in connection with uninsured plans. This treatment is consistent with *SSAP No. 47—Uninsured Plans,* paragraphs 5 and 8-11.

47. The self-insured plan, not the reporting entity, is legally liable for assessments for the transitional reinsurance program. The funds are a bona fide pass-through by the reporting entity, which is merely providing a

service for the self-insured (uninsured) plan. Therefore, the reporting entity will not report revenues or expenses for the assessments for the transitional reinsurance program.

48. The reporting entity may have received funds from the self-insured plans in advance of making disbursements. In that event, a liability is established for funds held in connection with self-insured plans.

49. The reporting entity, depending on its arrangement with the (uninsured) plan, may make a disbursement before receiving full funding from the plan. In that event, an asset is established for amounts receivable in connection with uninsured plans. The asset would be subject to the rules for admissibility and impairment as prescribed in SSAP No. 47, paragraphs 9-10.

Self-Insured Health Products - Reinsurance Administrative Expense Assessments Payable and U.S. Treasury Assessment

50. A reporting entity providing a service for a self-insured plan that is uninsured shall apply the pass-through treatment for the transitional reinsurance program's administrative cost assessments and additional U.S. Treasury contribution amounts. The uninsured plan, not the reporting entity, is legally liable. Therefore, the reporting entity will not report revenues or expenses with respect to the transitional reinsurance program's administrative cost assessments and additional U.S. Treasury contribution amounts.

Self-Insured Health Products - Reinsurance Payments (not applicable)

51. Reinsurance recoveries will not occur for self-insured health products, as these products will pay fees but not receive claims reimbursements.

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: The following website provides a useful overview and map of existing state Section 1332 waivers.
https://www.kff.org/health-reform/fact-sheet/tracking-section-1332-state-innovation-waivers/

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 nonsubstantive and expose revisions to SSAP No. 107 as illustrated below. These revisions would include State ACA reinsurance programs which are using Section 1332 waivers in the scope of *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*. The intent of the proposed accounting revisions is to continue to follow the SSAP No. 107 hybrid accounting approach for the state ACA programs as they operate in a similar manner.

In general, state ACA reinsurance programs provide funding to issuers in the individual market that incur high claims costs for enrollees. The programs often require assessments from issuers typically on behalf of group health plans. At a high level this hybrid accounting approach divides products into 3 broad categories. This includes:

a. Subject individual products (typically individual plans) that may pay a reinsurance funding contribution and are eligible to receive reinsurance distributions shall report similar to an involuntary reinsurance pool as described in *SSAP No. 63—Underwriting Pools*.

b. Other insured Health products (typically group plans) that are not eligible for reinsurance distributions under the terms of the state ACA reinsurance program shall treat the amounts as assessments reported in taxes, licenses and fees similar to treatment under *SSAP No. 35R—Guaranty Funds and Other Assessments*.

c. Self-insured plans where the reporting entity is acting as an administrator, and will exclude the payments made on behalf of the self-insured plan from the reporting entity's operations, shall report consistent with the guidance in *SSAP No. 47—Uninsured Plans*.

Staff Review Completed by:
Robin Marcotte
NAIC Staff

SCOPE OF STATEMENT

1. The Affordable Care Act (ACA) imposes fees and premium stabilization provisions on health insurance issuers offering commercial health insurance. This statement provides accounting for three programs known as risk adjustment, reinsurance and risk corridors that take effect in 2014. Risk adjustment is a permanent risk-spreading program (ACA Section 1343). The temporary transitional reinsurance program (ACA Section 1341) and temporary risk corridors program (ACA Section 1342) are for years 2014 through 2016. Subsequent to the end of the transitional reinsurance program, several states received waivers to have state specific ACA reinsurance programs, which operate similarly to the transitional reinsurance program. These programs are addressed in this statement.

State ACA Reinsurance Programs – Overview

52. After the 2014-2016 transitional reinsurance program ended, several states received approval from the HHS to run similar state ACA reinsurance programs under what are known as Section 1332 waivers. While Section 1332 waivers can be sought on a variety of topics, state ACA reinsurance programs are the most common. These state ACA reinsurance programs have similar goals of lowering individual health insurance premium in the jurisdiction.

53. The terms of these programs will have jurisdiction-specific variations. For example, the percentage of claims covered and the cap on claims covered varies by jurisdiction and sometimes by year. The initial flow of funding and covered policies may also have differences from the original transitional reinsurance program. However, several of the state ACA programs also include excess of loss coverage for individual claims in excess of a specified amount. One example would be reimbursing 80% of claims in excess of $50,000 up to a cap of $250,000 in the individual market in a state.

54. In general, state ACA reinsurance programs provide funding to issuers in the individual market that incur high claims costs for enrollees. The programs often require assessments from issuers and TPAs typically on behalf of group health plans based on a per member annual fee established by the state specific ACA reinsurance program.

55. Consequently, 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*. These programs are similar to an involuntary pool in *SSAP No. 63—Underwriting Pools* for the individual insured health products subject to the State ACA reinsurance program. For the group plans, which are required to contribute funding but are not eligible to receive program distributions, the program is an assessment payable by the reporting entity and not a reinsurance pool.

State ACA Reinsurance Programs – Accounting Treatment

56. The state ACA reinsurance programs shall follow the same principles of accounting and reporting as the transitional reinsurance program to the extent that the state ACA reinsurance program has similar features. The state ACA reinsurance program components including the treatment of reinsurance assessments, administrative costs assessments, and the reinsurance distributions, shall follow similar accounting and reporting principles as the transitional reinsurance program.

57. Due to the diverse elements of the State ACA reinsurance programs, which include characteristics of traditional reinsurance, involuntary pools and governmental assessments, a hybrid accounting approach

is required for the state ACA reinsurance programs. The accounting treatment for the state ACA reinsurance programs is discussed in terms of the payables and receivables and the impact to the health insurance products which are subject to the program.

58. The broad groupings for health insurance products used for the original transitional programs discussed in paragraph 26 will continue to apply to the state ACA reinsurance programs with jurisdiction specific modifications regarding the scope of health products subject to the market reforms. At a high level this approach divides products into 3 broad categories which are detailed in the accounting guidance below more specifically. This includes:

a. Subject individual products (typically individual plans) that may pay a reinsurance funding contribution and are eligible to receive reinsurance distributions. These programs shall report similar to an involuntary reinsurance pool as described in *SSAP No. 63—Underwriting Pools*.

b. Other insured Health products (typically group plans) that are not eligible for reinsurance distributions under the terms of the state ACA reinsurance program. These products shall treat the amounts as assessments reported in taxes, licenses and fees similar to treatment under *SSAP No. 35R—Guaranty Funds and Other Assessments*.

c. Self-insured plans where the reporting entity is acting as an administrator, and will exclude the payments made on behalf of the self-insured plan from the reporting entity's operations, shall report consistent with the guidance in *SSAP No. 47—Uninsured Plans*.

State ACA - Subject Individual Insured Health Products

59. For subject individual insured products which are subject to reinsurance assessments and also eligible for reinsurance distributions according to the program's terms, should follow the same guidance as provided in paragraphs 28-40 to the extent the state program incorporates similar terms. For example, if the state ACA reinsurance program does not incorporate an assessment to the U.S. treasury, paragraph 35 would not apply.

60. For subject individual insured products, the accounting is similar to an involuntary reinsurance pool. The subject individual insured products will report both the state ACA reinsurance funding and State ACA reinsurance administrative assessments as premium ceded. Program distributions received from the state ACA reinsurance program for individual insurance is reflected as ceded claim benefit recoveries.

State ACA - Other Insured Health Products

61. Fully insured health products which are required to contribute to funding state ACA reinsurance programs, but are not eligible to receive reinsurance program distributions under the terms of the program, shall report the contributed reinsurance and administrative expense funding as assessments which is charged to taxes, licenses and fees expense. For these products, the accounting shall be consistent with paragraphs 41-45 to the extent the state ACA reinsurance program incorporates similar terms.

State ACA – Self-Insured Health Products

62. If a reporting entity is an administrator for a self-insured health plan, the accounting for the state ACA reinsurance program amounts for the self-insured plan administrator is similar to the accounting in SSAP No. 47. The administrator of such plans shall follow the accounting described in paragraphs 46-51 to the extent the state program incorporates similar terms. The self-insured plan, not the administrator reporting entity, is legally liable for assessments for the state ACA reinsurance program. The funds are a bona fide pass-through by the reporting entity, which is merely providing a service for the self-insured (uninsured) plan. Therefore, the reporting entity will not report revenues or expenses for the assessments for the transitional reinsurance program.

Disclosures

~~60.~~72. The financial statements shall disclose on an annual and quarterly basis beginning in the first quarter of 2014, the assets, liabilities and revenue elements by program regarding the risk-sharing provisions of the Affordable Care Act for the reporting periods which are impacted by the programs including the listing in paragraphs 60.a. through 60.c. Reporting entities shall also indicate if they wrote any accident and health insurance premium, which is subject to the Affordable Care Act risk-sharing provisions. In the event that the balances are zero, the reporting entity should provide context to explain the reasons for the zero balances, including insufficient data to make an estimate, no balances or premium was excluded from the program, etc. Asset balances shall reflect admitted asset balances. The disclosure shall include the following:

a. ACA Permanent Risk Adjustment Program

i. Premium adjustments receivable due to ACA Risk Adjustment (including high-cost risk pool payments)

ii. Risk adjustment user fees payable for ACA Risk Adjustment

iii. Premium adjustments payable due to ACA Risk Adjustment (including high-cost risk pool ceded premium)

iv. Reported as revenue in premium for accident and health contracts (written/collected) due to ACA Risk Adjustment

v. Reported in expenses as ACA risk adjustment user fees (incurred/paid)

b. ~~ACA Transitional Reinsurance Program~~ State ACA Reinsurance Program

i. Amounts recoverable for claims paid due to state ACA Reinsurance Programs

ii. Amounts recoverable for claims unpaid due to state ACA Reinsurance (contra-liability)

iii. Amounts receivable relating to uninsured plans for contributions for state ACA Reinsurance

iv. Liabilities for contributions payable due to state ACA Reinsurance - not reported as ceded premium

v. Ceded reinsurance premiums payable due to state ACA Reinsurance

vi. Liability for amounts held under uninsured plans contributions for state ACA Reinsurance

vii. Ceded reinsurance premiums due to state ACA Reinsurance

viii. Reinsurance recoveries (income statement) due to state ACA Reinsurance payments or expected payments

ix. State ACA Reinsurance Contributions – not reported as ceded premium

c. ACA Temporary Risk Corridors Program

i. Accrued retrospective premium due from ACA Risk Corridors

ii. Reserve for rate credits or policy experience rating refunds due to ACA Risk Corridors

iii. Effect of ACA Risk Corridors on net premium income (paid/received)

iv. Effect of ACA Risk Corridors on change in reserves for rate credits

Status:
On March 15, 2021, the Statutory Accounting Principles (E) 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*, as illustrated above. 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.

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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

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[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
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

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 <u>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:</u>

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

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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