

Chapter 16B - Asset Valuation Reserve

All U.S. life insurance companies and fraternal benefit societies must include as a liability in their statutory financial statement an Asset Valuation Reserve (AVR) on fixed income and equity investments. The AVR is calculated in accordance with instructions promulgated by the Valuation of Securities (EX4) Task Force of the National Association of Insurance Commissioners and contained in the Life, Accident and Health Annual Statement Instructions and the Valuation of Securities manual. Because the instructions for the calculation of the AVR are periodically revised, the current publications should be consulted.

The purpose of the AVR is to establish a provision for the volatile incidence of asset losses and recognize appropriately the long term return expectations for equity type investments. The AVR provides a mechanism to absorb unrealized and credit-related realized gains and losses on all invested asset categories excluding cash, policy loans, premium notes, collateral notes and income receivable.

The AVR contains two components, default and equity, each designed to address specific asset risk areas. The default component is further divided into the bond and preferred stock subcomponent and the mortgage subcomponent; the equity component is comprised of the common stock subcomponent and the real estate and other invested asset subcomponent. Increases or decreases to the reserve are charged or credited directly to surplus. The AVR is limited to maximums by subcomponent, and no subcomponent of the AVR may be less than zero. Transfers between subcomponents or between components may be required or may be allowed without commissioner approval when negative or certain maximum subcomponent balances occur.

RELEVANT LITERATURE

Statutory Accounting

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- *Purposes and Procedures Manual of the NAIC Securities Valuation Office*, Section 6. Interest Maintenance Reserve and Asset Valuation Reserve for Life Insurance Companies and Fraternal Benefit Societies
- Accounting Practices and Procedures Manual for Life and Accident and Health Insurance Companies, Chapter 16, *Asset Valuation Reserve and Interest Maintenance Reserve*

Generally Accepted Accounting Principles

- *FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*
- *FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities*

State Regulations

- Texas Administration Code, Title 28 - Insurance, Chapter 7, *Corporate and Finance*

Other Sources of Information

- Draft discussion material from previous Life Codification projects, Chapter 16A, *Interest Maintenance Reserve*, and Chapter 16B, *Asset Valuation Reserve*