

Statutory Issue Paper No. 90

Nonadmitted Assets

STATUS

Finalized March 16, 1998

Original SSAP and Current Authoritative Guidance: SSAP No. 20

Type of Issue:

Common Area

SUMMARY OF ISSUE

1. As described in *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets* (Issue Paper No. 4), one of the cornerstones of statutory accounting is the use of nonadmitted assets. The use of nonadmitted assets is consistent with the recognition concept in the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).
2. Current statutory accounting guidance for nonadmitted assets is provided throughout the Accounting Practices and Procedures Manuals for Life and Accident and Health Insurance Companies and Property and Casualty Insurance Companies (Life/A&H and P&C Accounting Practices and Procedures Manuals).
3. The purpose of this issue paper is to establish statutory accounting principles for nonadmitted assets which are not specifically addressed in other issue papers, consistent with the Statement of Concepts and Issue Paper No. 4.

SUMMARY CONCLUSION

4. The definition and accounting treatment for nonadmitted assets is outlined in paragraph 3 of Issue Paper No. 4 as follows:

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 may be unavailable due to encumbrances or other third party interests should not be recognized on the balance sheet”, and are, therefore, considered nonadmitted.

Issue Paper No. 4 defines nonadmitted assets as follows:

An asset meeting the criteria in paragraph 2 above which is accorded limited or no value in statutory reporting and is one which is:

- a. Specifically identified within the Codification as a nonadmitted asset or
- b. Not specifically identified within the Codification as an admitted asset.

If an asset meets one of these criteria, the asset shall be reported as a nonadmitted asset and charged against surplus unless otherwise specifically addressed within the Codification. The asset shall be depreciated or amortized against net income as the estimated economic benefit expires.

5. This paper shall not be considered an all-inclusive list of nonadmitted assets. Certain admitted assets and nonadmitted assets are addressed in other issue papers. Assets not addressed in specific issue papers are nonadmitted until specifically authorized.

6. Consistent with paragraph 4, the following assets shall be nonadmitted and shall be reported in accordance with Issue Paper No. 4.

Deposits in Suspended Depositories

7. Amounts on deposit with suspended depositories may not be fully recoverable. Any amounts not reasonably expected to be recovered shall be written off in accordance with *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets* (Issue Paper No. 5). Amounts in excess of that written off shall be nonadmitted as they are not available to satisfy obligations to policyholders.

Bills Receivable Not for Premium and Loans Unsecured or Secured by Assets That Do Not Qualify As Investments

8. In accordance with Issue Paper No. 5, amounts determined to be uncollectible or otherwise impaired shall be written off. Amounts in excess of that written off are not considered to be properly collateralized as there are no underlying assets which would otherwise be admitted assets. Such amounts shall be nonadmitted as they may be of questionable economic value if needed to fulfill policyholder obligations.

Loans on Personal Security, Cash Advances To, Or In The Hands Of, Officers Or Agents And Travel Advances

9. In accordance with Issue Paper No. 5, amounts determined to be uncollectible or otherwise impaired shall be written off. Amounts in excess of that written off typically are unsecured and as such have no underlying assets which would otherwise be admitted assets. Such amounts shall be nonadmitted as they may be of questionable economic value if needed to fulfill policyholder obligations. Some of these items may also be considered prepaid expenses which, per *Issue Paper No. 29—Prepaid Expenses (excluding deferred policy acquisition costs and other underwriting expenses, income taxes, and guaranty fund assessments)*, are nonadmitted.

All “Non-Bankable” Checks

10. Examples of “non-bankable” checks are NSF (non-sufficient funds) checks, post dated checks, or checks for which payment has been stopped. Although these checks may still maintain probable future benefits (and thus meet the definition of assets), at the date on which they are non-bankable they are not available for policyholder obligations and shall be nonadmitted until the uncertainty related to the probable future benefit is resolved and the checks are converted to available funds.

Trade Names And Other Intangible Assets

11. These assets, by their nature, are not readily marketable and available to satisfy policyholder obligations and shall be nonadmitted.

Automobiles, Airplanes and Other Vehicles

12. Automobiles, airplanes and other vehicles meet the definition of assets established in Issue Paper No. 4. However, they are not readily available to satisfy policyholder obligations and as a result the undepreciated portion shall be nonadmitted. The accounting for these assets shall be consistent with the accounting for equipment provided in *Issue Paper No. 19—Furniture, Fixtures and Equipment*.

Company's Stock as Collateral for Loan

13. When a reporting entity lends money and accepts its own stock as collateral for the loan, it shall report the amount of the loan receivable and any related accrued interest on the loan as a nonadmitted asset. The asset is nonadmitted as the collateral could not be used to satisfy the obligation in the event of default.

DISCUSSION

14. For those items specifically addressed within this issue paper the principles established are consistent with current statutory accounting practices except as follows:

- a. With respect to the principles outlined in paragraphs 7, 8 and 9, current statutory accounting nonadmits a portion of or the entire amount of the asset. The conclusion above requires the write-off of the portion not expected to be recoverable in accordance with Issue Paper No. 5 with any remaining amounts being nonadmitted as outlined above.
- b. In relation to paragraph 7, such treatment is consistent with current statutory accounting for life and accident and health insurance companies but is a change for property and casualty insurance companies as current statutory accounting requires only "the amounts on deposit in excess of what reasonably can be estimated as recoverable" to be nonadmitted.
- c. Paragraphs 12 and 13 identify assets that are to be treated as nonadmitted assets. These assets are generally recognized as nonadmitted assets in current statutory accounting practice although they were not previously specifically stated as such.

15. The statutory accounting principles outlined above are consistent with the conservatism and recognition concepts in the Statement of Concepts, current statutory accounting guidance and Issue Paper No. 4.

Conservatism

Conservative valuation procedures provide protection to policyholders against adverse fluctuations in financial condition or operating results. Statutory accounting should be reasonably conservative over the span of economic cycles and in recognition of the primary responsibility to regulate for financial solvency.

Recognition

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 but rather should be charged against surplus when acquired or when availability otherwise becomes questionable.

Accounting treatments which tend to defer expense recognition do not generally represent acceptable SAP treatment.

16. Statutory treatment differs from GAAP in that GAAP does not have a concept of nonadmitted assets and would recognize the items addressed above as assets to the extent they remain collectible or recoverable.

Drafting Notes/Comments

- Issue Paper No. 5 discusses and outlines the appropriate treatment for the impairment of assets.

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

17. The Life/A&H and P&C Accounting Practices and Procedures Manuals, page iv and page v, respectively, provide the following guidance:

ASSETS

paragraph 1

Because of the conservatism intrinsic to insurance accounting, certain assets may be accorded limited or no value in statutory reporting, i.e., nonadmitted assets.

18. Chapter 9, Nonadmitted Assets, of the P&C Accounting Practices and Procedures Manual provides guidance as outlined below. Many of the items given as examples in Chapter 9 have been addressed in separate issue papers and therefore are not addressed in the conclusion of this issue paper. Additionally, the accounting treatment for such items addressed in separate issue papers may no longer be consistent with the accounting treatment outlined in Chapter 9.

Because, in many respects, the statutory balance sheet is presented on a conservative basis, certain assets (which may have a recognized value in noninsurance corporations) are accorded no value and thus reduce the reported surplus of the insurance company. Some assets may be nonadmitted because they do not conform to the laws and regulations of the various states and other assets may be nonadmitted because they are not readily convertible to liquid assets. Changes in the amount of nonadmitted assets are charged or credited directly to surplus.

The following are examples of nonadmitted assets:

1. Excess of Book Value over Market Value of Securities: In keeping with the concept of presenting the balance sheet on a conservative basis, the unrealized loss on stocks and impaired bonds reduces the admitted asset value on the annual statement.
2. Deposits in Suspended Depositories (less the estimated recoverable amount): The amounts on deposit in excess of what reasonably can be estimated as recoverable are nonadmitted.
3. Agents' Balances or Uncollected Premiums Over Three Months Due: The statutes of most states require that agents' balances or uncollected premiums over three months due be nonadmitted because of the uncertainty of collection. The over three months rule does not apply to ceded reinsurance premiums payable due from solvent insurance companies provided the assuming insurer maintains sufficient reserves as to the ceding insurer to apply the principles of offset accounting or the ceding insurer is licensed and in good standing in the state of the assuming insurer's domicile.
4. Future installments on all policies for which one or more installments are over three months due.
5. Accrued retrospective premiums from any person for whom any agents' balances or uncollected premiums are classified as nonadmitted.

6. Bills Receivable, Taken for Premiums: Bills or notes receivable are used as methods of financing premiums usually in states where installment premiums are not permitted or customary. If any portion of a bill or note receivable is unpaid past the due date of the installment, the entire bill or note is classified as nonadmitted. Also, on bills or notes not past due, the excess of the balance due over the unearned premium on the underlying policy or policies is classified as a nonadmitted asset. To the extent bills receivable are taken for premium for retrospectively rated policies, such bills must meet the same criteria required of accrued retrospective premiums to be reported as an admitted asset.
 7. Electronic Data Processing Equipment: Application systems software may be expensed when purchased or established as a nonadmitted asset and written off over a period of years not to exceed the software's expected useful life.
 8. Equipment, Furniture and Supplies: The company may record furniture and equipment as a ledger asset, depreciate it, and nonadmit it in the exhibit of assets in the statutory financial statements, or the company may expense the furniture and equipment when it is purchased. Supplies are normally expensed when purchased.
 9. Bills Receivable, Not Taken for Premiums: All bills or notes receivable - except those from an insured for premiums, or those fully secured by collateral- are classified as nonadmitted.
 10. Loans on Personal Security: Loans on personal security by definition are not properly secured by collateral. Therefore, they are classified as nonadmitted.
 11. Prepaid Expenses.
 12. Cash Advances To, or In the Hands Of, Officers or Agents: These amounts are not secured by collateral and are, therefore, nonadmitted.
 13. Travel Advances: Travel advances are nonadmitted since they are unsecured balances due from employees.
 14. Surplus Notes: Insurers sometimes make subordinated surplus contributions to other insurers via an instrument variously referred to as "surplus notes", "surplus debentures", "contribution certificates", "capital notes", etc. Generally, these instruments allow for payment of interest and repayment of principal only with the approval of the commissioner of the domiciliary jurisdiction of the insurer receiving the surplus infusion and issuing the instrument. The form and content of such instruments are also subject to regulatory approval. Where such approval conditions exist, insurers should report these instruments as admitted assets only in an amount as determined by the Securities Valuation Office (SVO) of the National Association of Insurance Commissioners. The holders of such instruments should never be allowed an admitted asset value more than that which would be allowed by considering the instruments as equity instruments and adding same to any other equity investments in the issuer held directly or indirectly by the holder of the instruments. In addition, such instruments shall be considered in the limitations on investments in affiliates. Investment income on these instruments shall not be reported as accrued until payment by the issuer has been approved by the insurer's domiciliary commissioner.
19. Chapter 9, Nonadmitted Assets, of the Life/A&H Accounting Practices and Procedures Manual provides the following guidance:

Some assets or portions thereof may be nonadmitted because they do not conform to the laws and regulations of the various states. As a result, certain assets which normally would be accorded value in noninsurance corporations are accorded no value and thus reduce the reported surplus of the insurance company. In addition, state regulations require that certain

expenditures which could normally be capitalized by a noninsurance company be charged as an expense.

Common Examples

Some examples of assets which are nonadmitted due to either an uncertainty as to their collectibility or an insufficient basis for determining their valuation or other reasons are:

1. deposits in suspended depositories;
2. agents' debit balances;
3. bills receivable which are not properly secured by collateral;
4. loans on personal security (endorsed or not) which are not properly secured by collateral;
5. cash advance to or in the hands of officers or agents;
6. travel advances;
7. depreciated cost of applications software;
8. depreciated cost of equipment and furniture;
9. prepaid loss adjustment expenses;
10. other prepaid expenses;
11. all "NSF", post dated, payment stopped or otherwise non-bankable checks;
12. group accident and health premiums more than 90 days past due;
13. individual accident and health premiums which are more than one modal premium past due;
14. the excess of premium notes over policy reserves on individual policies;
15. collateral loans secured by assets which do not qualify as investments.

RELEVANT LITERATURE

Statutory Accounting Practices and Procedures

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- Accounting Practices and Procedures Manual for Life and Accident and Health Insurance Companies, page iv and Chapter 9
- Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies, page v and Chapter 9
- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*
- *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets*
- *Issue Paper No. 19—Furniture, Fixtures and Equipment*
- *Issue Paper No. 29—Prepaid Expenses (excluding deferred policy acquisition costs and other underwriting expenses, income taxes, and guaranty fund assessments)*

Generally Accepted Accounting Principles

None

State Regulations

- No additional guidance obtained from state statutes or regulations.