Statutory Accounting Principles (E) Working Group

**Maintenance Agenda Submission Form**

**Form A**

## **Issue:** Enhanced Goodwill Disclosures

**Check (applicable entity):**

 P/C Life Health

Modification of Existing SSAP [x]  [x]  [x]

New Issue or SSAP [ ]  [ ]  [ ]

Interpretation [ ]  [ ]  [ ]

Description of Issue: This agenda item was drafted to request additional goodwill information and to clarify reporting on Schedule D, Part 6, Section 1 – Valuation of Shares of Subsidiary, Controlled and Affiliated Companies.

1. With the adoption of agenda item 2017-18: Goodwill Limitations in *SSAP No. 68—Business Combinations and Goodwill* and *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*, the information reported regarding goodwill, as provided in Annual Statement Footnote 3 – Business Combinations and Goodwill, has improved. This agenda item proposes additional disclosures to enhance the reporting of an SCA’s book adjusted carrying value (BACV). As goodwill is a significant component of many SCAs’ BACV, this agenda item will assist in facilitating review and disclosure of each balance.

1. During a review of SCA Sub 2 filings, it is noted that many companies do not calculate the amortization of goodwill correctly, which sometimes overstates the value of the SCA. Many companies also do not provide additional information to verify beginning goodwill and purchase price; as such NAIC staff rely on a review of Footnote 3 for these details. If the goodwill amount is not verifiable, it is not be allowed to be admitted as part of the SCA’s value.
2. The goodwill limitation of 10% of the insurance reporting entity’s goodwill is a calculation that all reporting entities who have goodwill must perform. While the admitted result is in the Annual Statement, the details of the calculation are not easily identifiable This agenda item proposes the addition of a disclosure to capture the admissibility information, to ensure transparency in the admission of goodwill.

Additionally, feedback is requested in terms of the proposed edits to Schedule D – Part 6 – Sections 1 and 2. As detailed in the proposal below, two column headings and related Blanks instruction refer to “Intangible Assets,” however NAIC staff believe the original intent of these disclosures were to capture goodwill. FASB defines intangible assets as assets (not including financial assets) that lack physical substance and refer to assets other than goodwill. Feedback is requested from regulators and interested parties regarding what has historically been included in this disclosure and if changing the definition to articulate goodwill is warranted. Upon a sampled review by NAIC staff, it appears as though goodwill is the sole number currently being reported in these applicable columns.

Existing Authoritative Literature:

Goodwill calculation and admittance limitations are detailed in *SSAP No. 68—Business Combinations and Goodwill.* Relevant areas in relation to this agenda item have been bolded for emphasis.

### Statutory Purchases of SCA Investments

1. The statutory purchase method of accounting is defined as accounting for a business combination as the acquisition of one entity by another. It shall be used for all purchases of SCA entities including partnerships, joint ventures, and limited liability companies. The acquiring reporting entity shall record its investment at cost. Cost is defined as the sum of: (a) any cash payment, (b) the fair value of other assets distributed, (c) the fair value of any liabilities assumed, and (d) any direct costs of the acquisition.(INT 00-28) Contingent consideration issued in a purchase business combination that is embedded in a security or that is in the form of a separate financial instrument shall be recorded by the issuer at fair value at the acquisition date.
2. For those acquired SCA entities accounted for in accordance with paragraphs 8.b.i., 8.b.ii., 8.b.iii. or 8.b.iv. of SSAP No. 97, and joint venture, partnership or limited liability company entities accounted for in accordance with paragraph 8 of SSAP No. 48, goodwill is defined as the difference between the cost of acquiring the entity and the reporting entity’s share of the book value of the acquired entity. **When the cost of the acquired entity is greater than the reporting entity’s share of the book value, positive goodwill exists.**  When the cost of the acquired entity is less than the reporting entity’s share of the book value, negative goodwill exists. **Goodwill resulting from assumption reinsurance shall be recorded as a separate write-in for other-than-invested assets. All other goodwill shall be reported in the carrying value of the investment.**
3. A business combination accounted for under the statutory purchase method and in which the acquired entity is valued in accordance with paragraphs 8.b.ii., 8.b.iii. or, 8.b.iv. of SSAP No. 97 shall determine the amount of positive goodwill or negative goodwill created by the combination using the reporting entity’s share of the GAAP net book value of the acquired entity, adjusted to a statutory basis of accounting in accordance with paragraph 9 of SSAP No. 97 in the case of acquired entities valued in accordance paragraphs 8.b.ii. or 8.b.iv. of SSAP No. 97. Business combinations accounted for under the statutory purchase method and in which the acquired entity is valued in accordance with, paragraph 8.b.i. of SSAP No. 97 shall determine the amount of positive or negative goodwill created by the business combination using the insurer’s share of the statutory book value of the acquired entity.
4. For those acquired SCA entities accounted for in accordance with paragraph 8.b.i. of SSAP No. 97 under the statutory purchase method, the historical bases of the acquired entity shall continue to be used in preparing its statutory financial statements. Therefore, pushdown accounting is not permitted.
5. Positive goodwill recorded under the statutory purchase method of accounting shall be admitted subject to the following limitation: **Positive goodwill from all sources, including life, accident and health, and deposit-type assumption reinsurance and goodwill resulting from the acquisition of an SCA by the insurance reporting entity that is reported on the SCA’s financial statements (resulting from the application of pushdown accounting), is limited in the aggregate to 10% of the acquiring[[1]](#footnote-1) entity’s capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for its most recently filed statement with the domiciliary state commissioner adjusted to exclude any net positive goodwill, EDP equipment and operating system software, and net deferred tax assets.** Additionally, all positive goodwill shall be nonadmitted when the underlying investment in the SCA or partnership, joint venture and limited liability company is nonadmitted[[2]](#footnote-2). When negative goodwill exists, it shall be recorded as a contra-asset.
6. Positive or negative goodwill resulting from the purchase of an SCA, joint venture, partnership or limited liability company shall be amortized to unrealized capital gains and losses on investments over the period in which the acquiring entity benefits economically, not to exceed 10 years. Positive or negative goodwill resulting from life, accident and health, and deposit-type assumption reinsurance shall be amortized to operations as a component of general insurance expenses over the period in which the assuming entity benefits economically, not to exceed 10 years. Goodwill shall be evaluated separately for each transaction.(INT 01-18)

**Disclosures:**

1. For business combinations accounted for under the statutory purchase method, the financial statements shall disclose the following for as long as unamortized goodwill is reported as a component of the investment:
	1. The name and brief description of the acquired entity;
	2. Method of accounting, that is the statutory purchase method;
	3. Acquisition date, cost of the acquired entity and the original amount of admitted goodwill; and
	4. The amount of amortization of goodwill recorded for the period; the admitted goodwill as of the reporting date, and admitted goodwill as a percentage of the SCA’s book adjusted carrying value (gross of admitted goodwill).
2. For business combinations taking the form of a statutory merger, the financial statements shall disclose:
	1. The names and brief description of the combined entities;
	2. Method of accounting, that is the statutory merger method;
	3. Description of the shares of stock issued or cancelled in the transaction;
	4. Details of the results of operations of the previously separate entities for the period before the combination is consummated that are included in the current combined net income, including revenue, net income, and other changes in surplus; and
	5. A description of any adjustments recorded directly to surplus for any entity that previously did not prepare statutory statements.
3. The financial statements shall disclose the following information regarding goodwill resulting from assumption reinsurance:
	1. The name of the ceding entity;
	2. The type of business assumed;
	3. The cost of the acquired business and the amount of goodwill; and
	4. The amount of amortization of goodwill recorded for the period.
4. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:
	1. A description of the impaired assets and the facts and circumstances leading to the impairment; and
	2. The amount of the impairment charged to realized capital gains and losses and how fair value was determined.

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

In March 2018, the Working Group adopted agenda item 2017-18: Goodwill Limitations in SSAP Nos. 68 and 97, requiring additional goodwill disclosures in Footnote 3 – Business Combinations and Goodwill (shown below).

Additional goodwill items under consideration by the Working Group relate to the currently exposed, agenda items:

1. Agenda item 2019-14: Attribution of Goodwill. This agenda item proposes the expansion of statutory guidance regarding the attribution of purchase price and goodwill from an acquisition and to add explicit language regarding the accounting treatment for situations in which an insurance company acquires a holding company that owns multiple companies.
2. Agenda item 2019-17: Pushdown Accounting. This agenda item reviewed the guidance in *ASU 2014-17, Business Combinations – Pushdown Accounting* and its applicability for statutory accounting. Three options were suggested for consideration which included complete rejection, allowance of pushdown for non-insurance entities, or allowance of pushdown only if previously elected (for SEC Registrants).

Also, in December 2019, the Working Group adopted an edit to *SSAP No. 68—Business Combinations and Goodwill* to clarify that all goodwill from an insurance entity’s acquisition of SCAs, regardless of whether pushdown accounting is applied, is subject to the existing 10% admittance limitation.

**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 this agenda item with nonsubstantive revisions to *SSAP No. 68—Business Combinations and Goodwill,* as detailed below, to add additional goodwill disclosures. The proposed disclosures will improve the validity and accuracy of numbers currently being reported and will assist with the regulators’ review of reported assets not readily available for the payment of policyholder claims.

Proposed additional disclosures in *SSAP No. 68—Business Combinations and Goodwill:*

### Disclosures

1. For business combinations accounted for under the statutory purchase method, the financial statements shall disclose the following for as long as unamortized goodwill is reported as a component of the investment:
	1. The name and brief description of the acquired entity;
	2. Method of accounting, that is the statutory purchase method;
	3. Acquisition date, cost of the acquired entity, the original amount of goodwill and the original amount of admitted goodwill;
	4. Each SCA’s book value, the amount of amortization of goodwill recorded for the period; the SCA’s admitted goodwill as of the reporting date;
	5. ,Total admitted goodwill as of the reporting date; and
	6. Admitted goodwill as a percentage of the SCA’s book adjusted carrying value (gross of admitted goodwill).
2. For business combinations taking the form of a statutory merger, the financial statements shall disclose:
3. The names and brief description of the combined entities;
4. Method of accounting, that is the statutory merger method;
5. Description of the shares of stock issued or cancelled in the transaction;
6. Details of the results of operations of the previously separate entities for the period before the combination is consummated that are included in the current combined net income, including revenue, net income, and other changes in surplus; and
7. A description of any adjustments recorded directly to surplus for any entity that previously did not prepare statutory statements.
8. The financial statements shall disclose the following information regarding goodwill resulting from assumption reinsurance:
9. The name of the ceding entity;
10. The type of business assumed;
11. The cost of the acquired business and the amount of goodwill; and
12. The amount of amortization of goodwill recorded for the period.
13. A reporting entity that recognizes an impairment loss shall disclose the following in the financial statements that include the period of the impairment write-down:
14. A description of the impaired assets and the facts and circumstances leading to the impairment; and
15. The amount of the impairment charged to realized capital gains and losses and how fair value was determined.
16. A reporting shall disclose the subcomponents and calculation of adjusted surplus and total admitted goodwill as a percentage of adjusted surplus:

Proposed Blank updates related to SSAP No. 68 include the following:

Footnote 3 (A) Illustration:

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Purchased Entity | Acquisition Date | Cost of Acquired Entity | Original Amount of Goodwill | Original Amount of Admitted Goodwill | Admitted Goodwill as of the Reporting Date | Amount of Goodwill Amortized During the Reporting Period | Book Value of SCA | Admitted Goodwill as a % of SCA BACV, Gross of Admitted Goodwill |
| XYZ Insurance Company | 6/30/\_\_ | $ |  | $ | $ | $ |  | % |
| Total |  |  |  |  | XXX |  |  |  |

New Footnote, proposed to be numbered 3(E):

|  |  |  |
| --- | --- | --- |
|  | Calculation of Limitation using Prior Quarter Numbers |  Current reporting period |
| Capital & Surplus | XXX. |  |
| Less Admitted Positive Goodwill | <XXX.> |  |
| Less Admitted EDP Equipment & Operating System Software | <XXX.> |  |
| Less Admitted Net Deferred Taxes | <XXX.> |  |
| Adjusted Capital and Surplus | XXX. |  |
|  |  |  |
| Limitation on amount of goodwill (adjusted capital and surplus times 10%) |  |  |
|  |  |  |
| Current period reported Admitted Goodwill |  | XXX, |
| Current Period Admitted Goodwill as a % of prior period Adjusted Capital and Surplus |  | % |

In addition to the above, changes are proposed for the following schedules which detail the Valuation of Shares of Subsidiary, Controlled of Affiliated Companies. As previously addressed, column clarifications regarding the reporting of Goodwill as opposed to Intangible Assets (as currently indicated).

Schedule D – Part 6 – Section 1 (Original) – Valuation of Shares of Subsidiary, Controlled or Affiliated Companies

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| 1CUSIPIdentification | 2Description NameOf Subsidiary, Controlled orAffiliated Company | 3Foreign | 4NAIC Company Code | 5ID Number | 6NAIC Valuation Method |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| 7Do Insurer's AssetsInclude IntangibleAssets Connected withHolding ofSuch Company's Stock? | 8Total Amount of SuchIntangible Assets | 9Book /AdjustedCarrying Value | 10Nonadmitted Amount | Stock of Such Company Owned by Insurer on Statement Date |
| 11Number of Shares | 12% of Outstanding |

Schedule D – Part 6 – Section 1 (Proposed Tracked Changes) – Valuation of Shares of Subsidiary, Controlled or Affiliated Companies

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| 1CUSIPIdentification | 2Description NameOf Subsidiary, Controlled orAffiliated Company | 3Foreign | 4NAIC Company Code | 5ID Number | 6NAIC Valuation Method | 7Book /AdjustedCarrying Value |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | 8Total Amount of Goodwill included in Book / Adjusted Carrying Value |  | 9Nonadmitted Amount | Stock of Such Company Owned by Insurer on Statement Date |
| 10Number of Shares | 11% of Outstanding |

Note 1 in Schedule D-Part 6-Section 1 (below), is proposed for removal due to the addition of footnote 3 (D). It is anticipated that if adopted as exposed, both changed would occur simultaneously.

 1. Total amount of goodwill nonadmitted $

For brevity, only instructions for affected columns have been included. Remaining paragraph numbers will be renumbered accordingly.

Column 8 – Total Amount of Goodwill

Report the total amount of goodwill whether admitted or nonadmitted. The intangible assets shown for the SCA Company should include any intangible assets that are included in the SCA Company’s carrying value of the stock of one or more lower-tier companies controlled by the SCA Company. In all cases, the goodwill equals goodwill calculated at purchase, as defined in *SSAP No. 68—Business Combinations and Goodwill*, minus any impairments/write-off thereof between the date of purchase and the statement date. If any portion of the total amount of goodwill is required to be nonadmitted for all SCA companies combined in accordance with *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* and *SSAP No. 68—Business Combinations and Goodwill* state the total amount nonadmitted in the footnote at the bottom of the this section of the schedule.

Schedule D – Part 6 – Section 2 – Valuation of Shares of Subsidiary, Controlled or Affiliated Companies

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| 1CUSIPIdentification | 2Name of Lower-Tier Company | 3Name of Company Listed in Section 1 Which Controls Lower-Tier Company | 4Total Goodwill Included in Amounts Shown in Column 8, Section 1 | Stock in Lower-Tier Company Owned Indirectly by Insurer on Statement Date |
| 5Number of Shares | 6% of Outstanding |

For brevity, only instructions for affected columns have been included.

Column 4 – Total Amount of Goodwill Included in Amount Shown in Column 8, Section 1

As explained in the instructions for Section 1, this amount is based on the goodwill purchase of the stock of the lower-tier company, reduced by any subsequent impairment/write-off. The reporting entity also bases the amount shown on the proportionate ownership of the lower-tier company.

Staff Review Completed by: Jim Pinegar & Fatima Sediqzad, NAIC Staff – January 2020

**Status:**

On March 18, 2020, the Statutory Accounting Principles (E) Working Group moved this item to the active listing, categorized as nonsubstantive, and exposed revisions to *SSAP No. 68—Business Combinations and Goodwill*, as illustrated above,to add additional goodwill disclosures. The proposed disclosures will improve the validity and accuracy of numbers currently being reported and will assist with the regulators’ review of reported assets not readily available for the payment of policyholder claims. Revisions to Schedule D, Part 6, Section 1 - Valuation of Shares of Subsidiary, Controlled and Affiliated Companies and Schedule D, Part 6, Section 2 - Valuation of Shares of Subsidiary, Controlled and Affiliated Companies primarily focus on the current reference to intangible assets. This item has a comment period deadline ending May 29, 2020.

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1. The “acquiring” entity is intended to reflect the insurance reporting entity that reports the investment resulting in goodwill. The goodwill limitation test shall be completed at the individual reporting company level. [↑](#footnote-ref-1)
2. This includes, but is not limited to, situations in which the investment is nonadmitted as the audited financial statements for the SCA, joint venture, partnership or limited liability company includes substantial doubt on the entity’s ability to continue as a going concern, or on the basis/contents of the audit opinion pursuant to paragraph 21 of SSAP No. 97. [↑](#footnote-ref-2)