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

Issue: Assessment of OTTI Based on Original Contract Terms

Check (applicable entity):

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

Description of Issue:
This agenda item intends to clarify the assessment of other than temporary impairment (OTTI) guidance in *SSAP No. 26R—Bonds*. It has been identified that there is a disconnect between SSAP No. 26R, *SSAP No. 36R—Troubled Debt Restructuring* and *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* with how modifications to debt instruments are considered for OTTI. It has been noted that this is a long-standing disconnect that has recently been identified as a result of the number of debt restructurings that have occurred in response to COVID-19.

In short summary, existing guidance in SSAP No. 26R identifies that OTTI assessments are based on the contractual terms of a debt security in effect at the date of acquisition. However, if a debt instrument has been modified pursuant to SSAP No. 36 or SSAP No. 103 (nontroubled situations), subsequent assessments of OTTI shall be based on the modified contractual terms of the debt instrument, and not revert back to the original acquisition terms.

This agenda item intends to correct this disconnect between SSAP No. 26R, SSAP No. 36 and SSAP No. 103R.

Existing Authoritative Literature:

SSAP No. 26R—Bonds

Impairment

13. An other-than-temporary(INT 06-07) impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due <u>**according to the contractual terms of a debt security in effect at the date of acquisition**</u>. A decline in fair value which is other-than-temporary includes situations where a reporting entity has made a decision to sell a security prior to its maturity at an amount below its carrying value. If it is determined that a decline in the fair value of a bond is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the entire difference between the bond's carrying value and its fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of the impairment loss shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR/IMR, the accounting for the entire amount of the realized capital loss shall be in accordance with SSAP No. 7. The other-than-temporary impairment loss shall be recorded entirely to either AVR or IMR (and not bifurcated between credit and non-credit components) in accordance with the annual statement instructions.

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): Not Applicable

Staff Recommendation:

NAIC Staff recommends that the Working Group move this item to the active listing, categorized as nonsubstantive and consider revisions to *SSAP No. 26R—Bonds* to clarify the interrelationship between SSAP No. 26R, SSAP No. 36 and SSAP No. 103 when there is a modification to a debt instrument.

SSAP No. 26R—Bonds

Impairment

13. An other-than-temporary(INT 06-07) impairment shall be considered to have occurred if it is probable that the reporting entity will be unable to collect all amounts due according to the contractual terms of a debt security in effect at the date of acquisition FN. A decline in fair value which is other-than-temporary includes situations where a reporting entity has made a decision to sell a security prior to its maturity at an amount below its carrying value. If it is determined that a decline in the fair value of a bond is other-than-temporary, an impairment loss shall be recognized as a realized loss equal to the entire difference between the bond's carrying value and its fair value at the balance sheet date of the reporting period for which the assessment is made. The measurement of the impairment loss shall not include partial recoveries of fair value subsequent to the balance sheet date. For reporting entities required to maintain an AVR/IMR, the accounting for the entire amount of the realized capital loss shall be in accordance with SSAP No. 7. The other-than-temporary impairment loss shall be recorded entirely to either AVR or IMR (and not bifurcated between credit and non-credit components) in accordance with the annual statement instructions.

New Footnote: If a bond has been modified from original acquisition, the guidance in *SSAP No. 36—Troubled Debt Restructuring* and paragraph 22 of *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* shall be followed, as applicable. After modification of original terms, future assessments to determine other-than-temporary impairment shall be based on the current contractual terms of the debt instrument.

Proposed edit for discussion on the May 20, 2020 conference call:

New Footnote: If a bond has been modified from original acquisition, the guidance in *SSAP No. 36—Troubled Debt Restructuring* and paragraph 22 of *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* shall be followed, as applicable. After modification of original terms, future assessments to determine other-than-temporary impairment shall be based on the modified ~~current~~ contractual terms of the debt instrument.

Staff Review Completed by:

Julie Gann - NAIC Staff, May 2020

Status:

On May 5, 2020, the Statutory Accounting Principles (E) Working Group exposed nonsubstantive revisions to incorporate a new footnote to SSAP No. 26R to clarify that if a debt instrument has been modified in accordance with *SSAP No. 36—Troubled Debt Restructuring* or *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, the assessment of other-than-temporary impairment shall be based on current contractual terms of the debt instrument.

On May 20, 2020, the Statutory Accounting Principles (E) Working Group adopted nonsubstantive revisions, as final, to incorporate a new footnote to *SSAP No. 26R—Bonds*, clarifying that if a debt instrument has been modified in accordance with *SSAP No. 36—Troubled Debt Restructuring* or *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, the assessment of other-than-temporary impairment shall be based on modified contractual terms of the debt instrument. (The adopted language is shown above with a noted edit to replace the word "current" with "modified" as discussed on the May 20, 2020 conference call.)

G:\FRS\DATA\Stat Acctg\3. National Meetings\A. National Meeting Materials\2020\5-20-20\Hearing (INT's and SSAP 26R Agenda Item)\Adopted Items\20-14 - Mod 5-20 - OTTI 26R.docx

