Statutory Accounting Principles (E) Working Group

**Maintenance Agenda Submission Form**

Form A

## **Issue: *ASU 2022-06, Reference Rate Reform (Topic 848), Deferral of the Sunset Date of Topic 848***

**Check (applicable entity):**

P/C Life Health

Modification of Existing SSAP

New Issue or SSAP

Interpretation

Description of Issue:

The Financial Accounting Standards Board (FASB) issued *ASU 2022-06, Reference Rate Reform (Topic 848), Deferral of the Sunset Date of Topic 848* to extend the sunset date of the reference rate reform guidance that was included in *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), Scope*.

As background, reference rate reform 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. An important item to note is that while LIBOR is the primary interbank offering rate, other similar rates are potentially affected by reference rate reform. For simplicity, LIBOR will be the sole IBOR referenced throughout this agenda item.

With a significant number of financial contracts referencing LIBOR, its discontinuance will require organizations to reevaluate and modify any contract which 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.

To address ASU 2020-04 the Working Group *issued INT 20-01: Reference Rate Reform*, and this interpretation was then revised to incorporate guidance from ASU 2021-01. This agenda item intends to again revise INT 20-01 to include the revised sunset date of December 31, 2024.

Existing Authoritative Literature:

The Working Group adopted INT 20-01 to address ASU 2020-04, and further revised that interpretation to address ASU 2021-01. 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. Alternative benchmark interest rates were previously addressed in agenda item 2018-46 – Benchmark Interest Rate.

ASU 2021-01 increased the scope of the optional, expedient accounting guidance for derivative instruments in ASU 2020-04 which would primarily affect *SSAP No. 86—Derivatives*. 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.*

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.
5. Agenda item 2021-09 further revised INT 20-01 and increased the scope of the optional, expedient accounting guidance for derivative instruments in ASU 2020-04.

**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 that the Working Group move this item to the active listing, categorized as SAP clarification and expose temporary (optional) expedient and exception interpretative guidance, to revise the expiration date of the guidance in *INT 20-01: ASU 2020-04 & 2021-01 - Reference Rate Reform* to be December 31, 2024.

The proposed modifications to INT 20-01 temporarily override SSAP No. 15, SSAP No. 22R and SSAP No. 86 guidance, 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: Jake Stultz—February 2023

Status:

On March 22, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and exposed temporary (optional) expedient and exception interpretative guidance, to revise the expiration date of the guidance in *INT 20-01: 2020-04, 2021-01 & 2022-06 - Reference Rate Reform* to be December 31, 2024, as reflected in INT 20-01.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2023/3-22-23 - Spring/Exposures/23-05 - ASU 2022-06 - LIBOR.docx