Statutory Accounting Principles (E) Working Group

**Maintenance Agenda Submission Form**

**Form A**

## **Issue: PIK Interest Disclosure Clarification**

**Check (applicable entity):**

 P/C Life Health

Modification of Existing SSAP [ ]  [x]  [ ]

New Issue or SSAP [ ]  [ ]  [ ]

Interpretation [ ]  [ ]  [ ]

Description of Issue: This agenda item has been developed to further clarify, and incorporate a practical expedient, to the paid-in-kind (PIK) interest aggregate disclosure adopted in *SSAP No. 34—Investment Income Due and Accrued* for year-2023. In response to questions received on how paydowns / disposals would impact PIK interest included in the cumulative balance, it was noted that clarifying guidance would assist with consistent application. Furthermore, without clarification it was identified that companies and investment software vendors may interpret the need to detail the retrospective PIK allocations and paydowns / disposals as evidence for the resulting amount.

To eliminate the potential inconsistent application on how paydowns / disposals impact PIK interest included in cumulative principal / par balance, as well as to streamline the calculation, this agenda item proposes the following clarifications:

* Any decreasing amounts to principal balances (paydowns / disposals / sales, etc.,) shall first be applied to any PIK interest included in the principal balance. For example, if original par was $100, PIK interest received overtime was $50 and paydowns received were $30, the resulting PIK included in the cumulative balance would be $20 - ($50 less $30). No reduction to the original principal would occur until the PIK interest had been fully eliminated from the balance. If in this scenario paydowns of $70 had occurred, the company would report zero in the disclosure for cumulative PIK interest, as the amount received would have fully eliminated the $50 in PIK interest.
* The determination of PIK interest in cumulative balance can be calculated through a practical expedient calculation of original par / principal value to current par / principal value, not to go less than zero. This calculation will determine the resulting balance from PIK interest over time as well as paydowns / disposals, etc. The intent of this calculation is to prevent companies and investment software vendors from creating a schedule that details PIK interest and paydowns received retroactively since the origination of the investment. The practical expedient calculation from the original to current par / principal value shall result with the same resulting PIK interest amount included in the cumulative balance without the retroactive scheduling required.

The adopted disclosure in SSAP No. 34 is not intended to change, but the proposed clarification and practical expedient guidance is intended to be captured in the annual statement instructions. This agenda item is being exposed at the SAPWG, as the source of the adopted disclosure, and will be used to subsequently provide a memo to blanks for year-end 2023 application and to revise the formal instructions for 2024.

**Existing Authoritative Literature:**

* **SSAP No. 34—Investment Income Due and Accrued**

Disclosures

7. The following disclosures shall be made for investment income due and accrued in the financial statements. (SSAP No. 37 captures disclosures for mortgage loans on nonaccrual status pursuant to paragraph 6.)

a. The bases by category of investment income for excluding (nonadmitting) any investment income due and accrued;

b. Disclose total amount excluded;

c. Disclose the gross, nonadmitted and admitted amounts for interest income due and accrued;

d. Disclose aggregate deferred interest;

e. Disclose cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance.

* **A/S Instructions – Life, Accident and Health / Fraternal Companies**

7. Investment Income Instruction:

Disclose the following for investment income due and accrued in the financial statements:

A. The bases, by category of investment income, for excluding (nonadmitting) any investment income due and accrued,

B. The total amount excluded.

C. The gross, nonadmitted and admitted amounts for interest income due and accrued. (1) Gross amount for interest income due and accrued. (2) Nonadmitted amount for interest income due and accrued. (3) Admitted amount for interest income due and accrued.

D. The aggregate deferred interest.

E. The cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance.

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):

* Agenda item 2022-17: Interest Income Disclosure update was adopted March 22, 2023. This disclosure data-captured existing and incorporated new disclosures, to SSAP No. 34, which included the cumulative amount of paid-in-kind (PIK) interest included in the current principal balance. The revisions were adopted for year-end 2023 and are shown in the authoritative literature section above.
* Blanks Proposal 2023-11BWG intends to adopt instructions and illustrations for the revised disclosures in May 2023.

**Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:**

None

**Convergence with International Financial Reporting Standards (IFRS):** NA

Recommendation:

NAIC staff recommend that the Working Group include this item on their maintenance agenda as a SAP clarification and expose this agenda item to clarify and incorporate a practical expedient, to the paid-in-kind (PIK) interest aggregate disclosure for SSAP No. 34 and annual statement instruction purposes. For annual statement purposes, this instruction will be an editorial change only and can be provided by the SAPWG in a memo posted on the Blanks Working (E) Group page if adopted after the deadline to incorporate into the annual statement instructions for 2023. Comments on this exposure are requested by June 30, 2023, to allow for adoption consideration at the 2023 Summer National Meeting.

Proposed Revisions to SSAP No. 34

7. The following disclosures shall be made for investment income due and accrued in the financial statements. (SSAP No. 37 captures disclosures for mortgage loans on nonaccrual status pursuant to paragraph 6.)

a. The bases by category of investment income for excluding (nonadmitting) any investment income due and accrued;

b. Disclose total amount excluded;

c. Disclose the gross, nonadmitted and admitted amounts for interest income due and accrued;

d. Disclose aggregate deferred interest;

e. Disclose cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance / par valueFN.

*New Footnote*: In disclosing the cumulative amount of PIK interest, identify the specific amounts of PIK interest by lot and aggregate the amounts by CUSIP/PPN that have a net increase to the original par value. The net increase includes PIK interest added to the par value less disposals (i.e., repayments; sales) that are first applied to any PIK interest outstanding. As a practical expedient, an insurer may calculate the cumulative amount of PIK interest on a bond by subtracting the original principal / par value from the current principal / par value, but not less than $0.

Proposed instruction for inclusion in the Annual Statement Instructions (or 2023 memo to Blanks):

7. Investment Income Instruction:

Disclose the following for investment income due and accrued in the financial statements:

A. The bases, by category of investment income, for excluding (nonadmitting) any investment income due and accrued,

B. The total amount excluded.

C. The gross, nonadmitted and admitted amounts for interest income due and accrued. (1) Gross amount for interest income due and accrued. (2) Nonadmitted amount for interest income due and accrued. (3) Admitted amount for interest income due and accrued.

D. The aggregate deferred interest.

E. The cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance.

For the PIK interest included in the current principal balance, include the amount of reported interest in which the terms permit “paid in kind” (PIK) instead of cash. The amount reported shall reflect the cumulative amount of PIK interest included in the current principal balance / par value. In disclosing the cumulative amount of PIK interest, identify the specific amounts of PIK interest by lot and aggregate the amounts by CUSIP/PPN that have a net increase to the original par value. The net increase includes PIK interest added to the par value less disposals (i.e., repayments; sales) that are first applied to any PIK interest outstanding. As a practical expedient, an insurer may calculate the cumulative amount of PIK interest on a bond by subtracting the original principal / par value from the current principal / par value, but not less than $0.

Staff Review Completed by: Julie Gann - NAIC Staff, May 2023

Status:

On May 16, 2023, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as a SAP clarification, and exposed revisions to SSAP No. 34 and the Annual Statement Instructions to clarify and incorporate a practical expedient to the paid-in-kind (PIK) interest aggregate disclosure. These SSAP No. 34 revisions, when adopted, will also result in editorial changes to the annual statement instructions.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2023/05-16-23/Exposures/B 23-13 - PIK Interest.docx