

Interpretation of the Statutory Accounting Principles Working Group

INT 20-05: Investment Income Due and Accrued

INT 20-05 Dates Discussed

Email Vote to Expose May 5, 2020; May 20, 2020; July 30, 2020; August 17, 2020

INT 20-05 References

- *SSAP No. 34—Investment Income Due and Accrue*

INT 20-05 Issue

1. A previously unknown virus began transmitting between October 2019 and March 2020, with the first deaths in the U.S. reported in early March 2020. The disease caused by the virus is known as Coronavirus Disease 2019 (COVID-19). Several states and cities have issued “stay home” orders and forced all non-essential businesses to temporarily close. This led to a significant increase in unemployment and the potential permanent closure of many businesses. Total economic damage is still being assessed however the total impact is likely to exceed \$1 trillion in the U.S. alone.

2. In response to COVID-19, temporary interpretations have been considered to provide exceptions to existing statutory accounting guidance with regards to the 90-day rule for various receivables, as well as guidance on the assessment of impairment and trouble debt restructurings. In response to these interpretations, a request to provide a temporary exception to *SSAP No. 34—Investment Income Due and Accrued* has been requested.

3. This interpretation intends to assess the requirements to review investment income due and accrued and consider whether temporary exceptions could be granted in response to COVID-19. Issues addressed within this interpretation include:

- a. Recognition and admittance of investment income under SSAP No. 34.
- b. Review of FASB staff technical inquiries and responses on investment income.

INT 20-05 Discussion

SSAP No. 34 Provisions

4. Investment income due is defined in SSAP No. 34 as the investment income earned and legally due to be paid to the reporting entity as of the reporting date. Investment income accrued is defined as investment income earned as of the reported date but not legally due to be paid to the reporting entity until subsequent to the reporting date.

5. Pursuant to SSAP No. 34, investment income due and accrued shall be recorded as an asset and assessed for impairment in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Amounts determined to be uncollectible shall be written off, and then an assessment shall be made of the remaining balance to determine nonadmitted amounts. SSAP No. 34 identifies this as a two-step process as follows:

- a. Investment income due and accrued is assessed for collectibility. If in accordance with SSAP No. 5R, it is probable the investment income due and accrued balance is uncollectible, the amount shall be written off and shall be charged against investment income in the period the determination was made.

- b. Any remaining investment income due and accrued (amounts considered probable for collection) representing either 1) amounts that are over 90-days past due (generated by any assets except mortgage loans in default) or 2) amounts designated elsewhere in the *NAIC Accounting Practices and Procedures Manual* as nonadmitted shall be considered nonadmitted. These items shall be subject to continuing assessments of collectibility and, if determined to be uncollectible, a write-off shall be recorded in the period such determination is made.

6. Pursuant to SSAP No. 34, accrued interest on mortgage loans in default shall only be recorded if deemed collectible. If uncollectible, accrued interest shall not be recorded and any previously accrued amounts shall be written off. If a mortgage loan in default has interest 180-days past due, which is assessed as collectible, all interest shall be recorded as a nonadmitted asset.

FASB Staff Technical Inquiry

7. The FASB staff received a technical inquiry regarding the recognition of interest income in response to COVID-19 when a “loan payment holiday” is provided that allows the borrowers to temporarily stop payments. The FASB Staff technical inquiry on interest income recognition was discussed April 17, 2020. In the scenario considered by the FASB staff:

- a. Interest is not accrued when the loan payment holiday is in effect.
- b. The loan modification did not represent a troubled debt restructuring.
- c. The loan modification would be accounted for as a continuation of the original lending arrangement (not as an extinguishment with a new loan recognized).

8. With this inquiry two views were presented in how interest should be recognized when a payment holiday is given and interest is not accrued:

- a. View 1 – Upon modification, a new effective interest rate is determined that equates to the revised remaining cash flows to the carrying amount of the original debt and is applied prospectively for the remaining term. That is, interest income is recognized during the payment period holiday.
- b. View 2 – Upon modification, the institution should recognize interest income on the loan in accordance with the contractual terms. Under this view, the institution would not recognize interest income during the payment holiday and would resume recognizing interest income when the payment holiday.

9. The FASB staff reviewed the submission and concluded both views to be appropriate.

INT 20-05 Consensus

10. The Working Group considered limited time collectibility assessments and admittance exceptions for investment income due and accrued and reached the following consensus:

- a. Continue with existing guidance in SSAP No. 34 that investment income shall be recorded when due (earned and legally due) or accrued (earned but not legally due until after the reporting date). If investments have been impacted by forbearance or other modification provisions, a reporting entity shall assess whether the investment income has been earned in accordance with the modified terms. Investment income shall only be recognized when earned.

- b. Continue with existing guidance in SSAP No. 34 to require an assessment of whether recorded investment income due and accrued is uncollectible.
 - i. For mortgage loans, bank loans and investment products with underlying mortgage loans impacted by forbearance or modification provisions, reporting entities may presume that borrowers and investments that were current as of Dec. 31, 2019, were not experiencing financial difficulties at the time of the forbearance or modification for purposes of determining collectibility. For these investments, further evaluation of collectibility is not required for the 1st and 2nd quarter 2020 financial statements unless other indicators that interest would not be collected are known (e.g., the entity has filed for bankruptcy).
 - ii. For investments not impacted by forbearance or modification provisions, this interpretation does not provide an assumption of collectibility and the provisions of SSAP No. 34 shall be followed in evaluating collectibility and assessing whether an impairment exists.
- c. Provide an exception for the nonadmittance of recorded investment income due and accrued that is deemed collectible and over 90-days past due. With this exception, reported investment income interest due and accrued that becomes over 90-days past due in the 1st or 2nd quarter may continue to be admitted in the June 30th, 2020 (1st and 2nd quarter) financial statements. This exception does not encompass accrued interest on mortgage loans that are in default. Mortgage loans in default shall continue to follow the SSAP No. 34 guidance. *SSAP No. 37—Mortgage Loans* identifies that determining that a loan is in default is per the contractual terms of the loan. For mortgage loans modified, determination of default shall be based on the modified contractual terms.

11. The Working Group considered the FASB technical guidance and reached a consensus consistent with the FASB staff on how interest should be recognized when a payment holiday is given and interest is not accrued. With this guidance, either of the following methods could be applied:

- a. A new effective interest rate is determined that equates the revised remaining cash flows to the carrying amount of the original debt and is applied prospectively for the remaining term. With this approach, interest income is recognized during the payment period holiday.
- b. The reporting entity should recognize interest income on the loan in accordance with the contractual terms. Under this view, the reporting entity would recognize no interest income during the payment holiday and would resume recognizing interest income when the payment holiday ends.

12. The exceptions and provisions detailed in this interpretation are applicable for the June 30th, 2020 (2nd quarter) financial statements. As the exceptions provided in this interpretation are not applicable in the September 30, 2020 (3rd quarter) financial statements, as this interpretation will automatically expire as of September 29, 2020. This interpretation will be publicly posted on the Statutory Accounting Principles (E) Working Group's website. This interpretation will be automatically nullified on September 29, 2020 and will be included as a nullified INT in Appendix H – Superseded SSAPs and Nullified Interpretations in the "as of March 2021" *Accounting Practices and Procedures Manual*.

- a. On August 17, 2020, the provisions in this INT were extended to be applicable for the September 30, 2020 (3rd quarter) financial statements. With this extension, this Interpretation will automatically expire as of December 30, 2020 (prior to the year-end 2020 financial statements). Subsequent consideration will occur to determine if an extension is needed beyond September 30, 2020.

INT 20-05 Status

13. On July 30, 2020, the Statutory Accounting Principles (E) Working Group exposed this interpretation for possible extension to September 30, 2020 (3rd quarter financial statements). If the extension were adopted, the proposed paragraph 12.a would be incorporated into the INT. On August 17, 2020, the Statutory Accounting Principles (E) Working Group extended the provisions of this INT to be applicable for the September 30, 2020 (3rd quarter) financial statements, incorporating paragraph 12.a into the INT.

14. The Statutory Accounting Principles (E) Working Group will subsequently review this interpretation to determine if an extension is needed to the effective date.

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