Statutory Accounting Principles (E) Working Group

**Maintenance Agenda Submission Form**

**Form A**

## **Issue: Collateral for Loans**

**Check (applicable entity):**

P/C Life Health

Modification of Existing SSAP

New Issue or SSAP

Interpretation

Description of Issue:

This agenda item has been drafted to address an inconsistency regarding the collateral loan guidance in *SSAP No. 20—Nonadmitted Assets* and *SSAP No. 21—Other Admitted Assets* (See excerpts in Authoritative Literature). These two statements contain guidance about unsecured and secured loans which is complementary.

SSAP No. 20 details the nonadmitted assets status of unsecured loans and loans secured by assets which do not qualify as investments. SSAP No. 20 also references write off and impairment guidance in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* for impaired and uncollectible loans. SSAP No. 20 provides that improperly collateralized loans include loans that do not have underlying assets that would otherwise qualify as admitted assets and stated that such loans are nonadmitted assets because the collateral would be of questionable economic value if needed to fulfill policyholder obligations. SSAP No. 20 includes similar nonadmission guidance regarding loans on personal security, cash advances to officers or agents and for travel advances.

SSAP No. 21 details the requirements for collateral loans which can qualify to be admitted assets. It provides that the collateral loan must be secured by the pledge of an investment.A footnote further describes that investment collateral would be of a type that would be in Section 3 of *Appendix A-001—Investments of Reporting Entities*. SSAP No. 21 also references the nonadmission guidance in SSAP No. 20 for collateral loans secured by assets that do not qualify as investments. The referenced guidance in SSAP No. 20 notes that the underlying assets must qualify as admitted assets.

Both SSAP No. 20 and SSAP No. 21 identify the need for adequate collateral that qualifies as an invested asset. SSAP No. 20 is explicit that the investment asset collateral must qualify as an admitted asset. Recent discussions with state regulators have highlighted that although SSAP No. 21 references the guidance in SSAP No. 20, that it would be beneficial to also note the need for the collateral to qualify as an admitted invested asset. This agenda item recommends a clarification to SSAP No. 21 that the acceptable invested asset collateral, for collateral loans must qualify as admissible invested assets.

Existing Authoritative Literature:

*SSAP No. 20—Nonadmitted Assets* (Bolding added for emphasis):

1. Consistent with paragraph 2, the following assets shall be nonadmitted:
2. Deposits in Suspended Depositories—Amounts on deposit with suspended depositories may not be fully recoverable. Any amounts not reasonably expected to be recovered shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Amounts in excess of that written off shall be nonadmitted as they are not available to satisfy obligations to policyholders;
3. **Bills Receivable Not for Premium and Loans Unsecured or Secured by Assets That Do Not Qualify As Investments**—In accordance with SSAP No. 5R, amounts determined to be uncollectible or otherwise impaired shall be written off.Amounts in excess of that written off are not considered to be properly collateralized **as there are no underlying assets which would otherwise be admitted assets. Such amounts shall be nonadmitted as they may be of questionable economic value if needed to fulfill policyholder obligations. Receivables arising from working capital finance programs designated by the Securities Valuation Office are subject to the guidance in *SSAP No. 105R—Working Capital Finance Investments*;**
4. **Loans on Personal Security, Cash Advances To, Or In The Hands Of, Officers Or Agents And Travel Advances**—In accordance with SSAP No. 5R, amounts determined to be uncollectible or otherwise impaired shall be written off. Amounts in excess of that written off typically are **unsecured and as such have no underlying assets which would otherwise be admitted assets. Such amounts shall be nonadmitted as they may be of questionable economic value if needed to fulfill policyholder obligations. Some of these items may also be considered prepaid expenses which, per *SSAP No. 29—Prepaid Expenses*, are nonadmitted;**
5. All “Non-Bankable” Checks—Examples of “non-bankable” checks are NSF (non-sufficient funds) checks, post-dated checks, or checks for which payment has been stopped. Although these checks may still maintain probable future benefits (and thus meet the definition of assets), at the date on which they are non-bankable they are not available for policyholder obligations and shall be nonadmitted until the uncertainty related to the probable future benefit is resolved and the checks are converted to available funds;
6. Trade Names And Other Intangible Assets1—These assets, by their nature, are not readily marketable and available to satisfy policyholder obligations and shall be nonadmitted;
7. Automobiles, Airplanes and Other Vehicles—Automobiles, airplanes and other vehicles meet the definition of assets established in SSAP No. 4. However, they are not readily available to satisfy policyholder obligations and as a result the undepreciated portion shall be nonadmitted. The accounting for these assets shall be consistent with the accounting for equipment provided in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements* or for commercial airplane leveraged leases, refer to the guidance in *SSAP No. 22R–Leases*;
8. Company’s Stock as Collateral for Loan—When a reporting entity lends money and accepts its own stock as collateral for the loan, it shall report the amount of the loan receivable and any related accrued interest on the loan as a nonadmitted asset. The asset is nonadmitted as the collateral could not be used to satisfy the obligation in the event of default.

**Footnote 1:** Defensible intangible assets are defined as an intangible asset acquired in a business combination or an asset acquisition that an entity does not intend to actively use but does intend to prevent others from using. These may also be referred to as a "locked-up asset" because while the asset is not being actively used, it is likely contributing to an increase in the value of other assets owned by the entity. These assets are not readily available to satisfy policyholder obligations and shall be nonadmitted.

***SSAP No. 21 – Revised—Other Admitted Assets*****(Bolding added for emphasis)**

**Collateral Loans**

1. Collateral loans are unconditional obligations1 for the payment of money secured by the pledge of an investment2 and meet the definition of assets as defined in SSAP No. 4, and are admitted assets to the extent they conform to the requirements of this statement. The outstanding principal balance on the loan and any related accrued interest shall be recorded as an admitted asset subject to the following limitations:
2. Loan Impairment—Determination as to the impairment of a collateral loan shall be based on current information and events. When it is considered probable that any portion of amounts due under the contractual terms of the loan will not be collected the loan is considered impaired. The impairment shall be measured based on the fair value of the collateral less estimated costs to obtain and sell the collateral. The difference between the net value of the collateral and the recorded asset shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*;
3. **Nonadmitted Asset—In accordance with *SSAP No. 20—Nonadmitted Assets*,** **collateral loans secured by assets that do not qualify as investments shall be nonadmitted. Further, any amount of the loan outstanding which is in excess of the permitted relationship of fair value of the pledged investment to the collateral loan shall be treated as a nonadmitted asset.**

Footnote 1: For purposes of determining a collateral loan in scope of this statement, a collateral loan does not include investments captured in scope of other statements. For example, *SSAP No. 26R—Bonds* includes securities (as defined in that statement) representing a creditor relationship whereby there is a fixed schedule for one or more future payments. Investments captured in SSAP No. 26R that are also secured with collateral shall continue to be captured within scope of SSAP No. 26R.

Footnote 2: Investment defined as those assets listed in Section 3 of *Appendix A-001—Investments of Reporting Entities*.

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 Review Completed by: Robin Marcotte – NAIC Staff ­– July 2022

Staff Recommendation: NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose the revisions to SSAP No. 21, illustrated below, which clarify that the invested assets pledged as collateral for admitted collateral loans must qualify as admitted invested assets.

Proposed revisions to ***SSAP No. 21 – Revised—Other Admitted Assets***

**Collateral Loans**

4. Collateral loans are unconditional obligations1 for the payment of money secured by the pledge of a qualifying investment2 and meet the definition of assets as defined in SSAP No. 4, and are admitted assets to the extent they conform to the requirements of this statement. The outstanding principal balance on the loan and any related accrued interest shall be recorded as an admitted asset subject to the following limitations:

1. Loan Impairment—Determination as to the impairment of a collateral loan shall be based on current information and events. When it is considered probable that any portion of amounts due under the contractual terms of the loan will not be collected the loan is considered impaired. The impairment shall be measured based on the fair value of the collateral less estimated costs to obtain and sell the collateral. The difference between the net value of the collateral and the recorded asset shall be written off in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*;
2. Nonadmitted Asset—In accordance with *SSAP No. 20—Nonadmitted Assets*, collateral loans secured by assets that do not qualify as investments which would otherwise be admitted shall be nonadmitted. Further, any amount of the loan outstanding which is in excess of the permitted relationship of fair value of the pledged investment to the collateral loan shall be treated as a nonadmitted asset.

**Footnote 1:** For purposes of determining a collateral loan in scope of this statement, a collateral loan does not include investments captured in scope of other statements. For example, *SSAP No. 26R—Bonds* includes securities (as defined in that statement) representing a creditor relationship whereby there is a fixed schedule for one or more future payments. Investments captured in SSAP No. 26R that are also secured with collateral shall continue to be captured within scope of SSAP No. 26R.

**Footnote 2:** A qualifying investment defined as those assets listed in Section 3 of *Appendix A-001—Investments of Reporting Entities* which would if held by the insurer would qualify for admittance.  For example, if the collateral would not qualify for admittance under SSAP No. 4 due to encumbrances or other third-party interests, then it does not meet the definition of "qualifying" and the collateral loan, or any portion thereof which is not adequately collateralized, is not permitted to be admitted.

**Status:**

On August 10, 2022, 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. 21R to clarify that invested assets pledged as collateral for admitted collateral loans must qualify as admitted invested assets.

On December 13, 2022, the Working Group re-exposed revisions to SSAP No. 21R to clarify that invested assets pledged as collateral for admitted collateral loans must qualify as admitted invested assets.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2023/3-22-23 - Spring/Hearing/13 - 22-11 - Collateral loans.docx