

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

**Issue: Clearly Defined Hedging Strategy**

**Check (applicable entity):**

	P/C	Life	Health
Modification of Existing SSAP	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
New Issue or SSAP	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Interpretation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

**Description of Issue:** This agenda item has been prepared to update the guidance in *SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees* for a clearly defined hedging strategy (CDHS) to mirror guidance adopted by the Life Actuarial (A) Task Force in 2022, and in effect starting with the 2023 version of the Valuation Manual. The guidance previously included in SSAP No. 108 referred to the CDHS defined in VM-21, and the actuarial guidance has been modified to ensure consistent definitions of a CDHS in both VM-20 and VM-21 and is now captured within VM-01.

The proposed revisions are limited to the definition of a CDHS in paragraph 7 of SSAP No. 108 as well as references in SSAP No. 108 that refer to VM-21 as the location of the definition of a CDHS.

**Existing Authoritative Literature:**

- ***SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees***
  7. As identified in paragraph 2, eligibility for the special accounting provision within this standard is strictly limited to variable annuity contracts and other contracts involving certain guaranteed benefits similar to those offered with variable annuities that are reserved for in accordance with VM-21. This special accounting provision requires the reporting entity to engage in highly effective fair value hedges that follow a Clearly Defined Hedging Strategy, as defined in VM-21, meeting all required provisions of VM-21 allowing the reporting entity to reduce the amount of the Conditional Tail Expectation (CTE) Amount. In order to qualify as a Clearly Defined Hedging Strategy (which may be dynamic, static, or a combination thereof), the strategy must meet the principles outlined in VM-21, be in place (implemented) for at least three months<sup>1</sup>, and shall at a minimum, identify:
    - a. Specific risks being hedged<sup>2</sup>,
    - b. Hedge objectives,
    - c. Risks not being hedged,
    - d. Financial instruments that will be used to hedge the risks,
    - e. Hedge trading rules, including permitted tolerances from hedging objectives,

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<sup>1</sup> As detailed in VM-21, before a new or revised hedging strategy can be used to reduce the amount of the Conditional Tail Expectation (CTE) otherwise calculated, the hedging strategy should be in place (effectively implemented) for at least three months. As detailed in VM-21, the reporting entity may meet the time requirement by having evaluated the effective implementation of the hedging strategy for at least three months without actually having executed the trades indicated by the hedging strategy (e.g., mock testing or by having effectively implemented the strategy with similar annuity products for at least three months.)

<sup>2</sup> The specific risk being hedged shall include a measure of the hedge coverage (e.g., percentage of interest rate sensitivity being hedged).

- f. Metric(s) used for measuring hedging effectiveness,
- g. Criteria that will be used to measure effectiveness,
- h. Frequency of measuring hedging effectiveness,
- i. Conditions under which hedging will not take place, and
- j. The individuals responsible for implementing the hedging strategy.

**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):** N/A

**Staff Recommendation:**

**NAIC staff recommends that the Working Group move this item to the active listing and expose revisions to SSAP No. 108 to update the definition of a clearly defined hedging strategy (CDHS) to reflect the revised guidance pursuant to VM-01. (Only references to the CDHS are being revised to VM-01. Other references to VM-21 are product specific to variable annuity contracts and shall be retained in SSAP No. 108.)**

**Proposed revisions to SSAP No. 108:**

6.b.ii Certification by a financial officer of the company (CFO, treasurer, CIO, or designated person with authority over the actual trading of assets and derivatives) that the hedging strategy meets the definition of a Clearly Defined Hedging Strategy within ~~VM-21~~VM-01 and that the Clearly Defined Hedging Strategy is the hedging strategy being used by the company in its actual day-to-day risk mitigation efforts. This provision does not require reporting entities to use a hedging strategy in determining VM-21 reserves, nor does it require entities to use the special accounting provision within this standard. However, it does require reporting entities that use the special accounting provisions within this standard to certify that the hedging strategy within scope of this standard is a Clearly Defined Hedging Strategy and is reflected in the establishment of VM-21 reserves.

7. As identified in paragraph 2, eligibility for the special accounting provision within this standard is strictly limited to variable annuity contracts and other contracts involving certain guaranteed benefits similar to those offered with variable annuities that are reserved for in accordance with VM-21. This special accounting provision requires the reporting entity to engage in highly effective fair value hedges that follow a Clearly Defined Hedging Strategy, as defined in ~~VM-21~~VM-01, meeting all required provisions of VM-21 allowing the reporting entity to reduce the amount of the Conditional Tail Expectation (CTE) Amount. In order to qualify as a Clearly Defined Hedging Strategy (which may be dynamic, static, or a combination thereof), the strategy must meet the principles outlined in VM-21, be in place (implemented) for at least three months<sup>3</sup>, and shall at a minimum, identify:

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<sup>3</sup> As detailed in VM-21, before a new or revised hedging strategy can be used to reduce the amount of the Conditional Tail Expectation (CTE) otherwise calculated, the hedging strategy should be in place (effectively implemented) for at least three months. As detailed in VM-21, the reporting entity may meet the time requirement by having evaluated the effective implementation of the hedging strategy for at least three months without actually having executed the trades indicated by the hedging strategy (e.g., mock testing or by having effectively implemented the strategy with similar annuity products for at least three months.)

- a. The Specific risks being hedged<sup>4</sup>,
- b. The hedging~~Hedge~~ objectives,
- c. The materials ~~R~~isks that are not ~~being~~ hedged,
- d. The financial instruments ~~that will be~~ used to hedge the risks,
- e. The hedging strategy's ~~Hedge~~ trading rules, including permitted tolerances from hedging objectives,
- f. The metrics, criteria and frequency for measuring effectiveness, ~~Metric(s) used for measuring hedging effectiveness,~~
- ~~g. Criteria that will be used to measure effectiveness,~~
- ~~h. Frequency of measuring hedging effectiveness,~~
- ~~i.g. The C~~onditions under which hedging will not take place, and for how long the lack of hedging can persist,
- ~~h. The group or area, including whether internal or external,~~ The individuals responsible for implementing the hedging strategy.;
- ~~i. Areas where basis, gap or assumption risk related to the hedging strategy have been identified, and~~
- j. The circumstances under which hedging strategy will not be effective in hedging the risks.

23.a. Discussion of hedged item, including information on the guarantees sensitive to interest rate risk, along with information on the designated hedging instruments being used to hedge the risk. Discussion of the hedging instruments shall identify whether a hedging instrument is a single instrument or portfolio, as well as information on the hedging strategy (including whether there have been changes in strategy from the prior reporting period, along with detailed information on the changes), and assessment of hedging effectiveness and compliance with the “Clearly Defined Hedging Strategy” of ~~VM-21~~ VM-01. Identification shall occur on whether the hedged item is intended to be fully hedged under the hedging strategy, or if the strategy is only focused on a portion of the liability characteristics or a portion of the interest rate sensitivity. Hedging strategies shall be identified as highly effective or not highly effective. If the strategy for a particular hedging relationship excludes a specific component of the gain or loss, or related cash flows, from the assessment of hedge effectiveness, details on the excluded components shall be disclosed.

**Staff Review Completed by: Julie Gann, NAIC Staff—May 2024**

<https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2024/08-13-24SummerNationalMeeting/Meeting/F-24-17-SSAPNo.108-VM-01.docx>

<sup>4</sup> The specific risk being hedged shall include a measure of the hedge coverage (e.g., percentage of interest rate sensitivity being hedged).