Statutory Accounting Principles (E) Working Group

**Maintenance Agenda Submission Form**

**Form A**

## **Issue: Updates to SSAP No. 27**

**Check (applicable entity):**

P/C Life Health

Modification of existing SSAP

New Issue or SSAP

Interpretation

Description of Issue: During February 2024, it came to NAIC staffs’ attention that *SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures* references *Risk and Financial Instruments with Concentrations of Credit Risk* references *FASB Statement No. 105, Disclosure of Information about Financial Instruments with Off-Balance-Sheet* (FAS 105) which was superseded by *FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities* (FAS 133). By accident, FAS 133 did not include any guidance on non-derivative financial instruments with off-balance sheet risk and guidance on this issue had to be re-drafted and added back in during 2001 with *Statement of Position 01-6 Accounting by Certain Entities (Including Entities With Trade Receivables) That Lend to or Finance the Activities of Others* (SOP 01-6) which was then incorporated into FASB codification Topic 825-10 in 2009. Additionally, NAIC staff noted that the annual statement instructions only provide disclosures for derivative swaps, futures, and options, however the guidance in SSAP No. 27 is intended to be applicable to all derivative instruments and financial instruments, except those specifically carved out in FAS 105 paragraphs 14 and 15.

NAIC staff suggest amending SSAP No. 27 to specifically list financial instruments excluded from the SSAP rather than referencing FAS 105, which is significantly out of date as it was superseded by FAS 133 prior to the creation of the Accounting Standards Codification which in turn superseded FAS 133. The only change made to these exclusions from FAS 105 was that financial instruments denominated in foreign currency would now be within scope of SSAP No. 27 as there did not appear to be a compelling reason for this exclusion from off-balance sheet risk reporting as financial instruments in foreign currency were not excluded from the scope of SOP 01-6. Staff also suggests updating the annual statement instructions to add an “Other” derivatives category and disclosure examples and instructions for non-derivative financial instruments with off-balance sheet credit risks.

Existing Authoritative Literature:

*SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments*, paragraph 18b, requires concentration risk disclosures in accordance with SSAP No. 27.

*SSAP No. 26R—Bonds*, paragraph 30b, requires concentration risk disclosures in accordance with SSAP No. 27.

*SSAP No. 86R—Derivatives*, paragraph 30b, note that derivatives meet the definition of financial instrument under SSAP No. 27, meaning that disclosures for off-balance sheet and concentration of credit risk are required for all derivatives.

*SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, glossary, defines a Derivative Financial Instruments as “A derivative instrument (as defined in SSAP No. 86—Derivatives) that is a financial instrument (refer to SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures, paragraph 2).”

*SSAP No. 105R—Working Capital Finance Investments*, paragraph 30b, requires concentration risk disclosures in accordance with SSAP No. 27.

*SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures Risk and Financial Instruments with Concentrations of Credit Risk:*

**SCOPE OF STATEMENT**

1. This statement establishes statutory accounting principles for disclosure of information about financial instruments with off-balance-sheet risk and financial instruments with concentration of credit risk.

**SUMMARY CONCLUSION**

2. A financial instrument shall be defined as cash, evidence of an ownership interest in an entity, or a contract that both:

1. Imposes on one entity a contractual obligation (i) to deliver cash or another financial instrument to a second entity or (ii) to exchange other financial instruments on potentially unfavorable terms with the second entity; and
2. Conveys to that second entity a contractual right (i) to receive cash or another financial instrument from the first entity or (ii) to exchange other financial instruments on potentially favorable terms with the first entity.

3. Examples of the financial instruments, which encompass both assets and liabilities recognized and not recognized in the financial statement, to which this statement applies include, but are not limited to, short-term investments, bonds, common stocks, preferred stocks, mortgage loans, derivatives[[1]](#footnote-2), financial guarantees written, standby letters of credit, notes payable and deposit-type contracts.

**Disclosure of Extent, Nature, and Terms of Financial Instruments with Off-Balance-Sheet Risk**

4. For financial instruments1 with off-balance-sheet risk, except as noted in paragraphs 14 and 15 of *FASB Statement No. 105, Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk* (FAS 105), a reporting entity shall disclose in the financial statements the following information by class of financial instrument:

1. The face or contract amount (or notional principal amount if there is no face or contract amount); and
2. The nature and terms including, at a minimum, a discussion of (i) the credit and market risk of those instruments, (ii) the cash requirements of those instruments, and (iii) the related accounting policy pursuant to the requirements of *APB Opinion No. 22,* *Disclosure of Accounting Policies*.

5. Additional disclosures related to derivatives and embedded credit derivatives are addressed in *SSAP No. 86—Derivatives*.

**Disclosure of Credit Risk of Financial Instruments with Off-Balance-Sheet Credit Risk**

6. For financial instruments1 with off-balance-sheet credit risk, except as noted in paragraphs 14 and 15 of FAS 105, an entity shall disclose in the financial statements the following information by class of financial instrument:

1. The amount of accounting loss the entity would incur if any party to the financial instrument failed completely to perform according to the terms of the contract and the collateral or other security, if any, for the amount due proved to be of no value to the entity; and
2. The entity’s policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity’s access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

**Disclosure of Concentrations of Credit Risk of All Financial Instruments**

7. Except as noted in paragraph 14 of FAS 105, a reporting entity shall disclose all significant concentrations of credit risk arising from all financial instruments1 whether from an individual or group. Group concentrations of credit risk exist if a number of individuals or groups are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The following shall be disclosed in the financial statements about each significant concentration:

1. Information about the (shared) activity, region, or economic characteristic that identifies the concentration;
2. The amount of the accounting loss due to credit risk the entity would incur if parties to the financial instruments that make up the concentration failed completely to perform according to the terms of the contracts and the collateral or other security, if any, for the amount due proved to be of no value to the entity; and
3. The entity’s policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity’s access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

**Annual and Quarterly Disclosure Requirements**

8. Refer to the Preamble for further information regarding disclosure requirements. The disclosures in paragraph 7 shall be included in the annual audited statutory financial reports only.

**Relevant Literature**

9. This statement adopts the provisions of FAS 105 with the following modifications:

1. The disclosures required in paragraph 17 of FAS 105 shall distinguish between derivatives entered into for hedging purposes and for other-than-hedging purposes.
2. Paragraph 19 of FAS 105 is rejected. It addresses voluntary disclosures not required by this statement.

**Effective Date and Transition**

10. This statement is effective for years beginning January 1, 2001.

**REFERENCES**

**Relevant Issue Papers**

1. *Issue Paper No. 27—Disclosure of Information about Financial Instruments with Concentration of Credit Risk*
2. *Issue Paper No. 33—Disclosures about Fair Value of Financial Instruments*
3. *Issue Paper No. 85—Derivative Instruments (as it relates to disclosure about financial instruments with off-balance-sheet risk)*

**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):**

None.

Staff Recommendation:

NAIC staff recommends that the Working Group move this item to the active listing of the maintenance agenda categorized as a SAP Clarification and expose revisions, as detailed below, to SSAP No. 27 and the Annual Statement Instructions.

Staff Review Completed by:

NAIC Staff – William Oden, February 2024

Status:

On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to *SSAP No. 27—* *Off-Balance-Sheet and Credit Risk Disclosures Risk and Financial Instruments with Concentrations of Credit Risk* which would remove references to FAS 105 and instead specify the assets excluded from SSAP No. 27. Additionally, revisions were exposed to the Annual Statement Instructions for Note 16 to add an “other” category to the derivatives tabular disclosure, add a non-derivative financial instrument disclosure and additional narrative disclosure examples for non-derivative financial instruments.

**Proposed Revisions to SSAP No. 27:**

## SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for disclosure of information about financial instruments with off-balance-sheet risk and financial instruments with concentration of credit risk.

## SUMMARY CONCLUSION

1. A financial instrument shall be defined as cash, evidence of an ownership interest in an entity, or a contract that both:
2. Imposes on one entity a contractual obligation (i) to deliver cash or another financial instrument to a second entity or (ii) to exchange other financial instruments on potentially unfavorable terms with the second entity; and
3. Conveys to that second entity a contractual right (i) to receive cash or another financial instrument from the first entity or (ii) to exchange other financial instruments on potentially favorable terms with the first entity.
4. Examples of the financial instruments, which encompass both assets and liabilities recognized and not recognized in the financial statement, to which this statement applies include, but are not limited to, short-term investments, bonds, common stocks, preferred stocks, mortgage loans, derivativesfn, financial guarantees written, standby letters of credit, notes payable and deposit-type contracts.
5. The following types of financial instruments are not within the scope of this statement:
6. Insurance contracts, not held as an investment.
7. Unconditional purchase obligations.
8. Obligations and financial instruments within the scope of *SSAP No. 92—Postretirement Benefits Other Than Pensions* and *SSAP No. 102—Pensions*.
9. Substantively extinguished liabilities as defined within *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*.
10. Leases as defined within *SSAP No. 22R—Leases.*

### Disclosure of Extent, Nature, and Terms of Financial Instruments with Off-Balance-Sheet Risk

1. For financial instruments with off-balance-sheet risk, the reporting entity shall disclose in the financial statements the following information by class of financial instrument:
2. The face or contract amount (or notional principal amount if there is no face or contract amount); and
3. The nature and terms including, at a minimum, a discussion of (i) the credit and market risk of those instruments, (ii) the cash requirements of those instruments, and (iii) the related accounting policy pursuant to the requirements of *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*.
4. Additional disclosures related to derivatives and embedded credit derivatives are addressed in *SSAP No. 86—Derivatives*.

### Disclosure of Credit Risk of Financial Instruments with Off-Balance-Sheet Credit Risk

1. For financial instrumentsfn with off-balance-sheet credit risk, the reporting entity shall disclose in the financial statements the following information by class of financial instrument:
2. The amount of accounting loss the entity would incur if any party to the financial instrument failed completely to perform according to the terms of the contract and the collateral or other security, if any, for the amount due proved to be of no value to the entity; and
3. The entity’s policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity’s access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

### Disclosure of Concentrations of Credit Risk of All Financial Instruments

1. The reporting entity shall disclose all significant concentrations of credit risk arising from all financial instruments whether from an individual or group. Group concentrations of credit risk exist if a number of individuals or groups are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The following shall be disclosed in the financial statements about each significant concentration:
2. Information about the (shared) activity, region, or economic characteristic that identifies the concentration;
3. The amount of the accounting loss due to credit risk the entity would incur if parties to the financial instruments that make up the concentration failed completely to perform according to the terms of the contracts and the collateral or other security, if any, for the amount due proved to be of no value to the entity; and
4. The entity’s policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity’s access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

### Annual and Quarterly Disclosure Requirements

1. Refer to the Preamble for further information regarding disclosure requirements. The disclosures in paragraph 8 shall be included in the annual audited statutory financial reports only.

### Relevant Literature

1. This statement adopts the provisions of FAS 105 with the following modifications:
2. The disclosures required in paragraph 17 of FAS 105 shall distinguish between derivatives entered into for hedging purposes and for other-than-hedging purposes.
3. Paragraph 19 of FAS 105 is rejected. It addresses voluntary disclosures not required by this statement.

### Effective Date and Transition

1. This statement is effective for years beginning January 1, 2001.

## REFERENCES

### Relevant Issue Papers

1. Issue Paper No. 27—Disclosure of Information about Financial Instruments with Concentration of Credit Risk
2. Issue Paper No. 33—Disclosures about Fair Value of Financial Instruments
3. Issue Paper No. 85—Derivative Instruments (as it relates to disclosure about financial instruments with off-balance-sheet risk)

**Proposed Revisions to Annual Statement Instructions:**

**16. Information About Financial Instruments With Off-Balance-Sheet Risk And Financial Instruments With Concentrations of Credit Risk**

Refer to *SSAP No. 27—Off‑Balance-Sheet and Credit Risk Disclosures* for accounting guidance.

Instruction:

For financial instruments with off-balance-sheet risk, a reporting entity shall disclose in the financial statements the following information by class of financial instrument:

(1) The face or contract amount (or notional principal amount if there is no face or contract amount).

(2) The nature and terms, including, at a minimum, a discussion of (i) the credit and market risk of those instruments, (ii) the cash requirements of those instruments, and (iii) the related accounting policy pursuant to the requirements of *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*.

(3) The amount of accounting loss the entity would incur if any party to the financial instrument failed completely to perform according to the terms of the contract and the collateral or other security, if any, for the amount due proved to be of no value to the entity.

(4) The entity’s policy of requiring collateral or other security to support financial instruments subject to credit risk, information about the entity’s access to that collateral or other security, and the nature and a brief description of the collateral or other security supporting those financial instruments.

Illustration:

**THIS EXACT FORMAT MUST BE USED IN THE PREPARATION OF THIS NOTE FOR THE TABLE BELOW. REPORTING ENTITIES ARE NOT PRECLUDED FROM PROVIDING CLARIFYING DISCLOSURE BEFORE OR AFTER THIS ILLUSTRATION.**

**(NOTE: THIS DOES NOT INCLUDE THE ENDING NARRATIVE.)**

(1) The table below summarizes the face amount of the Company’s financial instruments with off‑balance‑sheet risk.

Assets Liabilities

20\_\_\_ 20\_\_\_ 20\_\_\_ 20\_\_\_

Derivatives Contracts:

a. Swaps $ $ $ $

b. Futures $ $ $ $

c. Options $ $ $ $

d. Other $ $ $ $

e. Total (a+b+c+d) $$ **$** $

Other Financial Instruments:

1. Loan

Commitments $ $ $ $

b. Standby Letters

of Credit $ $ $ $

c. Financial

Guarantees $ $ $ $

d. Other $ $ $ $

e. Total (a+b+c+d) $$ **$** $

See Schedule DB of the Company’s annual statement for additional detail on derivative contracts.

(2) The Company uses interest rate swaps to reduce market risks from changes in interest rates and to alter interest rate exposures arising from mismatches between assets and liabilities. Under interest rate swaps, the Company agrees with other parties to exchange, at specified intervals, the difference between fixed-rate and floating-rate interest amounts calculated by reference to an agreed notional principal amount. Generally, no cash is exchanged at the outset of the contract and either party makes no principal payments. These transactions are entered into pursuant to master agreements that provide for a single net payment to be made by one counterparty at each due date.

Under exchange-traded currency futures and options, the Company agrees to purchase a specified number of contracts with other parties and to post variation margin on a daily basis in an amount equal to the difference in the daily fair values of those contracts. The parties with whom the Company enters into exchange-traded futures and options are regulated futures commissions merchants who are members of a trading exchange.

(3) The Company is exposed to credit-related losses in the event of nonperformance by counterparties to financial instruments, but it does not expect any counterparties to fail to meet their obligations given their high credit ratings. The credit exposure of interest rate swaps and currency swaps is represented by the fair value (market value) of contracts with a positive fair value (market value) at the reporting date. Because exchange-traded futures and options are affected through a regulated exchange and positions are marked to market on a daily basis, the Company has little exposure to credit-related losses in the event of nonperformance by counterparties to such financial instruments.

(4) The Company is required to put up collateral for any futures contracts that are entered. The amount of collateral that is required is determined by the exchange on which it is traded. The Company currently puts up cash and U.S. Treasury Bonds to satisfy this collateral requirement.

The current credit exposure of the Company’s derivative contracts is limited to the fair value at the reporting date. Credit risk is managed by entering into transactions with creditworthy counterparties and obtaining collateral where appropriate and customary. The Company also attempts to minimize its exposure to credit risk through the use of various credit monitoring techniques. Approximately \_\_\_\_\_% of the net credit exposure for the Company from derivative contracts is with investment-grade counterparties.

(5) The Company’s credit exposure related to outstanding derivatives contracts reported in “Other” consist of Treasury Lock and Forward contracts of $\_\_\_\_ and $\_\_\_\_, respectively.

(6) The Company’s non-derivative off-balance sheet exposures consist of loan commitments, standby letters of credits, and financial guarantees and in accordance with Statutory Accounting Principles are not recorded on the Company’s balance sheet. The amounts shown do not necessarily reflect actual future settlement value but rather the maximum liability the Company may incur from these contracts. The amounts shown for loan commitments and letters of credit represent the total credit available to be drawn upon with these instruments. The amounts shown for financial guarantees represent the Company’s guarantee to pay the balance of the Affiliate’s note payable due to an unrelated shareholder. The Company does not anticipate any material losses from its off-balance sheet arrangements.

(7) Approximately \_\_\_\_% of the Company’s all premium receivables are due from policyholders which reside in the state of Missouri. The Company is in good standing with the Missouri Department of Insurance and is not aware of any circumstances which would impair its ability to continue operating within the state of Missouri. Approximately, \_\_\_% of mortgage loan assets, totaling $\_\_\_, are due from a single borrower which operates in the biomedical industry within the state of Kansas. Were there to be a downturn within this economic space and the borrower becomes delinquent, the Company would have the ability to seize collateral of $\_\_\_. The borrower is current on its mortgage payments and the Company is not aware of any circumstances which would indicate the borrower will be unable to meet its debt service obligations.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Hearing/19 - 24-12 - Updates to SSAP No 27.docx

1. The financial instruments captured within this statement shall include financial instruments that contain embedded derivatives that are not separately recognized as financial instruments with derivatives under SSAP No. 86, and that expose the holder to the possibility (however remote) of making future payments. [↑](#footnote-ref-2)