Meeting Agenda

Statutory Accounting Principles (E) Working Group
Meeting Agenda
November 17, 2024

A. <u>Consideration of Maintenance Agenda – Pending List</u>

1. Ref #2024-20: Restricted Asset Clarification
2. Ref #2024-21: Investment Subsidiary Classification
3. Ref #2024-22: *ASU 2024-01, Scope Application of Profits Interest and Similar Awards*
4. Ref #2024-23: Derivative Premium Clarifications
5. Ref #2024-24: Medicare Part D – Prescription Payment Plan
6. Ref #2024-25: SSAP No. 16 ASU Clarification
7. Ref #2024-26EP: Fall 2024 Editorial Revisions

Ref #	Title	Attachment #
2024-20 (Julie)	**Restricted Asset Clarifications**	**A – Form A**

<u>*Summary:*</u>
This agenda item has been prepared to clarify how assets held under modified coinsurance (Modco) or funds withheld (FWH) agreements shall be reflected within the restricted asset disclosure in paragraph 23 of *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures* and in the corresponding disclosures in Note 5L of the statutory financial statements. It also proposes enhanced disclosures to fully identify the extent of restricted assets reported on balance sheet within a single disclosure as well as identify differences between the "restricted asset" annual statement disclosure and the amount reported in the general interrogatories, which is pulled directly into the RBC formulas. Lastly, this agenda item suggests a referral to propose revisions to the life RBC instructions to clarify that if the reporting entity uses any assets held under a modco or FWH agreement as collateral or as a pledged asset for a purpose unrelated to the reinsurance agreement (securing an exposure that has not been ceded to the reinsurer), then the reporting entity should not take any Modco/FWH reduction in RBC charges (credit) for those assets in the life RBC formula. This clarification is consistent with the existing life RBC instruction that does not permit RBC credit when the asset risk has not been transferred to the assuming entity for the entire duration of the reinsurance treaty. This referral to life RBC intends to make it clear that if the insurance entity has utilized Modco/FWH assets as collateral or as a pledged item for their own repurchase agreements, securities lending transactions, FHLB agreements/borrowings, or any other purpose specific to the ceding insurer's use, then the asset risk/benefit has not been sufficiently transferred to the assuming entity warranting RBC credit for those assets.

As a key item to note, this agenda item does not propose to capture modco/FWH assets in the restricted asset reporting that flows through to the general interrogatories (GI) that results with an additional "noncontrolled" asset RBC charge. As the RBC formula allows credit for modco/FWH assets held, if these were included in the "noncontrolled asset" category, more complexity and adjustments to the RBC formula would be required to also provide credit against the additional noncontrolled asset charge. Instead, as detailed within, this agenda item proposes modifications to capture modco/FWH assets in the existing restricted asset disclosure (SSAP No. 1, paragraph 23c) that currently focuses on collateral received reported on balance sheet for when there is an corresponding liability reported. By including at this location and expanding disclosures to provide a complete view of restricted assets in comparison to total assets and total admitted assets, there is no additional RBC impact and regulators have a better picture of the assets that are restricted as pledged, not under the exclusive control of the reporting entity or that are earmarked (such as modco/FWH) for a specific purpose.

NAIC staff is aware that some companies report modco/FWH assets held in the existing restricted asset disclosure as "pledged collateral not captured in other categories" or as "other restricted assets," but not all companies report these assets as restricted. (In the RBC formulas, there are adjustments for these assets that are reported that incur additional "noncontrolled" asset RBC.) This agenda item specifies the disclosure location and category to promote consistency and comparability across insurers in the reporting of these assets. NAIC staff supports the inclusion of these assets in the restricted asset disclosure (even when an offsetting liability is reported), as it allows for a full comparison of such assets to total assets. NAIC staff believes the total restricted assets may be considered by financial statement users when assessing available assets, and this disclosure could impact the extent to which borrowing is permitted. If Modco/FWH assets are not captured, it may present a picture of available assets that is not accurate.

As noted in the introduction, this agenda item also proposes additional disclosures to identify differences between what is captured as restricted in SSAP No. 1, paragraph 23b, in Note 5L(1), and what is captured in the general interrogatories. Although the categories are identical, NAIC staff is aware that amounts are reported differently between the two locations. NAIC staff believes this is due to the amounts that are reported in the GI are pulled for the additional noncontrolled asset RBC charge. Over time NAIC staff has received information that these discrepancies may be directed by the domiciliary state regulator for situations that have been identified not to warrant the additional "restricted asset" / "noncontrolled asset" RBC charge. Since the amount is pulled directly from the GI to the RBC formula it is not considered a permitted practice in RBC, however, it results in a mismatch between the note disclosure and the GI although the categories are identical. (NAIC staff has not identified any permitted practices for the differences between the Note and GI reporting. Regulator comments are requested on whether the two reporting locations are interpreted to have different parameters as the language appears identical in both locations.) At this time, this proposal is strictly a disclosure element to make it easy to identify variations and the explanation between the Note and GI reporting so that future assessments can occur. If certain restricted assets are supported for general exclusion from the GI reporting (and the RBC factor), then those situations should be considered by the Working Group so that all insurers are following the same provisions.

The following paragraphs detail how the existing disclosure in SSAP No. 1, paragraph 23b (reported in Note 5L(1)) compares to the information reported in the GI:

- As detailed in SSAP No. 1, paragraph 23b and in Note 5L(1), admitted and nonadmitted assets that are pledged or otherwise restricted in the general account and separate account are to be disclosed along with a comparison of the total restricted assets to total assets and total admitted assets. With specific categories for certain uses, the note also includes broad categories for "pledged as collateral not captured in other categories" and "other restricted assets" to capture items not covered within the specific lines. Note 5L(2) and 5L(3) captures information on these generic categories, and includes examples of reinsurance and derivatives contracts on what should be captured. This disclosure instruction indicates that contracts that share similar characteristics (such as reinsurance and derivatives) are to be reported in the aggregate.

- The restricted asset categories in Note 5L(1) are duplicated in the annual statement general interrogatories (GI), and the amounts reported in the GI are pulled directly into the RBC formula and incur an additional "noncontrolled asset" RBC charge. NAIC staff is aware that there are discrepancies between the amounts of restricted assets reported in Note 5L(1) and what is captured in the same categories within the GI. (These are lines 25.04, 25.05 and 26.21-26.32 in the GI.)

The following details how these items are pulled into RBC from the general interrogatories:

- In the life formula, the restricted assets captured in the GI are pulled directly from the GI to LR017. The standard "noncontrolled asset" charge on that page is 0.0126, except for conforming security lending programs which receive a charge of 0.0020. (Assets pledged as collateral to the FHLB are adjusted in the formula based on various factors.)

- In the P/C and health RBC formula, the restricted assets captured in the GI are pulled directly to PR014 and XR005 respectively, with a 0.010 charge except for conforming security lending programs which receive a 0.002 charge.

The specific excerpts from SSAP No. 1, Note 5L, the applicable GIs and RBC formulas have been captured in the authoritative language section. The categories are also listed in the table below. The terminology at each location is also included below to show the intended consistency in classifications.

<u>Assets identified as "Not Controlled" or "Restricted Assets":</u>

- <u>SSAP No. 1: Restricted Assets / Not Under Exclusive Control</u>: Defined in paragraph 23b as "not under the exclusive control, subject to a put option contract, etc." Footnote 3 of SSAP No. 1 includes the following: The aggregate information captured within this disclosure is intended to reflect the information reported in the Annual Statement Investment Schedules in accordance with the coding of investments **<u>that are not under the exclusive control of the reporting entity, including assets loaned to others and the information reported in the General Interrogatories, as well as information on restricted cash, cash equivalents and short-term investments</u>**.

- <u>Note 5L</u>: Matches terminology and language as SSAP No. 1.

- <u>General Interrogatories: Exclusive Control</u>: GI 25 asks if the company has "exclusive control" over all securities, other than securities lending detailed in 25.03. The instructions define this guidance as "exclusive control means that the company has the exclusive right to dispose of the investment at will, without the necessity of making a substitution therefore." GI 26 that captures the statement value of investments that are not under the exclusive control of the reporting entity. **<u>These categories mirror what is captured in SSAP No. 1 and Note 5L.</u>**

- <u>RBC: Noncontrolled Assets</u>: The RBC instructions have separate lines to capture collateral from conforming and non-conforming securities lending programs and "noncontrolled assets." **<u>The instructions indicate "noncontrolled assets are any assets reported on the balance sheet that are not under the exclusively under the control of the company, or assets that have been sold or transferred subject to put option contract currently in force."</u>** *(Although not detailed in this agenda item, the RBC instructions include specific guidance on what to include (or exclude). Examples include assets related to the Federal Reserve's Asset Loan Facility (TALF) and for restricted assets in excess of FHLB borrowing.)*

<u>Recommendation:</u>
NAIC staff recommends that the Working Group move this item to the active listing and expose SAP clarification revisions to *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures* as well as corresponding proposed revisions to the Annual Statement (A/S) instructions/template for the restricted asset disclosure in Note 5L to more clearly identify how Modco and FWH assets reported within a ceding company's financial statements shall be captured.

In addition to the revisions that explicitly address Modco/FWH, the A/S revisions propose a new component to the existing disclosure to identify and explain differences between the note and what is captured in the general interrogatories. Although it was originally anticipated that the note and the GI would agree, NAIC staff is aware that there are often differences and that in some instances domiciliary states have directed specific items to be removed from the GI reporting because of the resulting RBC pull / factor impact. This disclosure will highlight those differences to ensure ease of regulator comparisons as well as allow NAIC staff

to assess consistency across companies and enable future discussions. NAIC staff recommends that the SAPWG sponsor a blanks proposal to incorporate Annual Statement instruction revisions.

Although there is a separate agenda item to identify Modco and FWH assets with more granularity, and to assist with RBC impact, this clarification of the aggregate restricted asset disclosure has been recommended to move forward to ensure the restricted asset disclosure is consistently reported.

Upon adoption of revisions, this agenda item recommends a referral to the Life RBC (E) Working Group to clarify that Modco assets held by a ceding entity that at any time during the year are pledged or used by the ceding entity for their own purpose, such as being used in assets reported to or as collateral to the FHLB or in a repurchase or securities lending agreement, are not permitted to be reported as an RBC charge reduction from the RBC formula for invested assets. Such uses would reflect circumstances in which the "entire asset credit or variability in statement value risk associated with the assets supporting the business reinsurance was not transferred to the assuming company for the entire duration of the reinsurance treaty." This referral will also identify the direction to capture modco/FWH assets in SSAP No. 1, paragraph 23c, therefore these assets should not be captured in the RBC reporting of "noncontrolled assets," therefore the existing elements in the RBC formula to adjust modco/FWH from the "noncontrolled" reporting lines may no longer be necessary.

Ref #	Title	Attachment #
2024-21 (Julie)	**Investment Subsidiary Classification**	**B – Form A**

<u>*Summary:*</u>
This agenda item has been prepared as questions have been received on the classification of investments as "investment subsidiaries" in schedule D-6-1: Valuation of Shares of Subsidiary, Controlled or Affiliated Companies and in the Life RBC formula on pages LR042, LR043 and LR044.

For background, the concept of an investment subsidiary was reflected in *SSAP No. 46—Investments in Subsidiary, Controlled and Affiliated Entities* as "investments in noninsurance subsidiary, controlled or affiliated (SCA) entities that have no significant ongoing operations other than to hold assets that are primarily for the direct or indirect benefit or use of the reporting entity or its affiliates." For these SCAs, the guidance in SSAP No. 46 required an equity measurement method adjusted to the statutory basis of accounting. With this adjustment to the statutory basis of accounting, the measurement of the SCA under SSAP No. 46 was intended to be consistent to the accumulated measurement of the underlying assets if they had been held directly. SSAP No. 46 was superseded by SSAP No. 88 as of Jan. 1, 2005, and the concept of an "investment subsidiary" (or a subsidiary designed to hold assets for the entity) was eliminated from statutory accounting guidance. SSAP No. 88 was then superseded by *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* as of Dec. 31, 2007, and is the current authoritative guidance for SCAs. Similar to SSAP No. 88, the concept of an "investment subsidiary" (or an SCA designed just to hold assets for the benefit of the reporting entity and its affiliates) is not in SSAP No. 97.

Under current guidance in SSAP No. 97, the concept of an SCA that simply holds assets is not reflected. Unless the SCA is an insurance subsidiary or engages in specific transactions on behalf of the entity, the SCA will be captured under paragraph 8.b.iii in SSAP No. 97 and reported based on the audited US GAAP equity value. Admittance is permitted if the parameters of the SSAP are met, which includes an audited financial statement supporting the US GAAP equity value. It is noted that the concept of an investment sub is still reflected in *SSAP No. 25—Affiliates and Other Related Parties*. The example of an entity only holding assets for the benefit of the insurer is an example of a non-economic transaction, where the assets are transferred/recognized at fair value, but any gain from the transfer is deferred until permanence can be verified.

From questions received and a review of financial statement reporting, the following list identifies issues:

- Situations have been identified in which companies have reported Schedule BA items (in scope of SSAP No. 48) as "investment subs" for RBC look through although those investments should not be captured within the classification. The concept for an "investment subsidiary" is for items reported as SCAs in scope of SSAP No. 97 with common and/or preferred stock ownership.

- Questions have been raised on whether companies can utilize the concept of an "investment sub" to avoid statutory accounting provisions for underlying assets but receive favorable RBC impact as if the SSAP criteria had been met. (For example, whether a company utilize the bond RBC factors for a debt security held within an investment subsidiary without verifying that the debt security would qualify as a bond under *SSAP No. 26—Bonds* or use CRP ratings to determine RBC when the asset may have required an SVO-assigned designation if held directly.)

- Questions have been received on how companies comply with Life RBC LR044 instruction for Affiliate Type 4 "*The risk-based capital charge for the ownership of an investment subsidiary is based on the risk-based capital of the underlying assets, pro-rated for the degree of ownership. The basis for this calculation is the assumption that the charge should be the same as it would be if the life insurer held the assets directly.*" Specifically, the measurement method for the SCA pursuant to *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* (audited U.S. GAAP equity) would not be consistent with the measurement of the assets if the assets were held directly (statutory basis). Questions arise whether the underlying assets within the investment subsidiary are converted to statutory basis of accounting prior to computation of RBC charge. In addition, there were questions as to how the RBC after covariance is calculated for investment subsidiaries.

- According to Annual Statement instructions, investment subsidiaries also need to apply a "look-through" approach in Asset Valuation Reserve (AVR) calculation. However, diversity in practice has been observed and for companies that utilize Lines 5 – 14 of the AVR Equity and Other Invested Asset Component table to calculate AVR, the computation is not transparent.

- Questions have been raised on the current annual statement instructions for D-6-1 regarding the "imputed value on a statutory basis" and the direction for nonadmittance of the excess or reclassification in the "all other affiliates" category. Schedule D-6-1 does not determine the amount reported on balance sheet, as that amount is pulled from *Schedule D-2-2, Common Stocks*. Further, the A/S instructions for D-6-1 would not override the SSAP guidance that prescribes the measurement and admittance requirement as that is governed by SSAP No. 97, which is higher in the statutory hierarchy. These A/S instructions regarding the "imputed statutory value" appear to come from historical RBC guidance, and it is assumed that the calculation of the "imputed statutory value" was intended to be a pre-requisite for classifying as an investment sub. However, as the A/S guidance does not override SSAP, and what is captured would seemingly create a disconnect from what is reported on balance sheet, it seems to be causing confusion on application, as companies are not consistently reporting "investment subsidiaries" throughout the schedule, AVR and the RBC formula.

- From a review of the financial statements, the amounts reported for "investment subsidiaries" vary between D-6-1, AVR and RBC. From the 2023 filing, the amount reported in the RBC formula (which allows company RBC calculation based on the underlying assets) is significantly greater than the amount reported on D-6-1 and what is reported through the equity component of AVR.

<u>*Recommendation:*</u>
NAIC staff recommend that the Working Group move this item to the active listing and expose this agenda item with a request for comments on the options offered to clarify statutory accounting guidelines (and resulting reporting impacts) for investment subsidiaries. As noted, with the exception of possible revisions to SSAP No. 97, the other possible actions are to sponsor blanks proposals or send referrals to the Capital

Adequacy (E) Task Force and related RBC groups with a request for revisions. (Determination on whether this is a SAP classification or a new SAP concept will be based on the action directed.)

Potential Actions:

1) **Revisions to SSAP No. 97 to incorporate statutory accounting guidance for SCAs that hold assets on behalf of the reporting entity and affiliate (investment subsidiaries).** By incorporating in SSAP, consideration can be given as to prescribing the measurement method and potential nonadmittance thresholds if the assets within the investment subsidiary would be nonadmitted if held directly. (As detailed within, the existing reference to measurement and nonadmittance in the instructions for D-6-1 would not overrule the guidance in SSAP No. 97. If the revisions to SSAP No. 97 are not supported, then the Working Group could consider sponsoring a blanks proposal to clarify the instructions in D-6-1 to prescribe allocation of the underlying investments in a manner that coincides with the SCA measurement and admittance under SSAP No. 97.)

2) **Sponsor blanks proposals to capture new investment schedules, or perhaps expansions to existing investment schedules, to detail the underlying assets held within an investment subsidiary.** As the RBC and AVR calculations require reporting entities to calculate RBC and AVR based on the underlying assets, this information should be readily available. If revisions are not incorporated into SSAP No. 97, these proposals can also clarify requirements for reporting as an investment subsidiary.

3) **Referrals to the Capital Adequacy (E) Task Force and related RBC Working Groups to incorporate details that allow regulators to verify the RBC calculation for the underlying assets in investment subsidiaries.** If blanks reporting revisions are incorporated that provide this detail, then the RBC formula can likely pull from those sources. If reporting revisions are not incorporated, then additional schedules or reporting lines would be necessary within the RBC formula.

Ref #	Title	Attachment #
2024-22 (Wil)	**ASU 2024-01, Scope Application of Profits Interest and Similar Awards**	**C – Form A**

<u>*Summary:*</u>
In March 2024, FASB issued *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards,* which includes amendments to Topics 718 to provide clarifications on the application of guidance on stock compensation in the form of profits interest. The primary changes made were the creation of application examples and amendments to certain language in the Scope and Scope Exceptions Section of Topic 718 to improve clarity and operability without changing the guidance.

Because profits interest holders only participate in future profits and/or equity appreciation and have no rights to the existing net assets of the partnership, it can be complex to determine whether a profits interest award should be accounted for as a share-based payment arrangement (Topic 718) or similar to a cash bonus or profit-sharing arrangement (Topic 710, Compensation—General, or other Topics).

For statutory accounting assessments, prior U.S. GAAP guidance related to share-based payments has been predominantly adopted with modification in *SSAP No. 104—Share-Based Payments*. Statutory accounting modifications to the U.S. GAAP guidance have mostly pertained to statutory terms and concepts. (For example, statutory reporting lines, nonadmittance of prepaid assets, etc.)

<u>*Recommendation:*</u>
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 to adopt with modification *ASU 2024-01, Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards* within *SSAP No. 104—Share-Based Payments.* The proposed revisions to SSAP No. 104 are illustrated within the Form A.

Ref #	Title	Attachment #
2024-23 (Wil)	**Derivative Premium Clarifications**	**D – Form A**

<u>*Summary:*</u>
This agenda item was developed in response to two issues. First, NAIC staff noted during internal reviews of *SSAP No. 86—Derivatives* and the Annual Statement Instructions that the terminology used for derivative financing premium was inconsistent and that the guidance for derivative financing premiums could be clarified. Second, as part of the ongoing Interest Maintenance Reserve (IMR) Ad Hoc Group meetings NAIC staff learned that there is some confusion within industry regarding whether statutory accounting guidance allows derivative premium costs to be captured in the calculation of realized losses for the derivative transaction. NAIC staff noted that within SSAP No. 86 there are several sections which provide derivative specific accounting guidance, and within these sections the guidance is clear that companies are to amortize derivative premiums over the life of the derivative contract. With amortization of the derivative premium, the derivative premium costs would not be a component in determining realized losses at expiration. As noted within the Definitions section of SSAP No. 86, derivative premiums represent the cost to acquire or write a derivative contract and is not an “underlying” in a derivative contract. As SSAP No. 86 only allows for the change in value attributable to the derivative underlying to be capitalized to IMR as a realized loss and as derivative premium costs are NOT a component of the derivative underlying, the guidance is clear that derivative premium costs should not be included in losses capitalized into IMR. To ensure this is abundantly clear, revisions have been recommended to both the “Definitions” and “Derivative Premium” sections to add language which specifically states that derivative premium costs cannot be capitalized into IMR.

<u>*Recommendation:*</u>
NAIC staff recommend that the Working Group move this item to the active listing of the maintenance agenda, categorized as a SAP clarification, and expose revisions to SSAP *No. 86—Derivatives* and the annual statement instructions to ensure consistent terminology for derivative financing premium and to further clarify that derivative premium costs are not to be capitalized to IMR. The proposed revisions to SSAP No. 86 and the annual statement instructions are illustrated within the Form A.

Ref #	Title	Attachment #
2024-24 (Robin)	**Medicare Part D – Prescription Payment Plan**	**E – Form A F – INT**

<u>*Summary:*</u>
This agenda item is drafted to develop statutory accounting guidance in response to changes to the Medicare Part D (Part D) prescription drug program which goes into effect in 2025. At a high level, the Medicare Prescription Payment Program (MP3) requires insurers to pay pharmacies at the point of sale the out-of-pocket costs of enrollees who have opted into MP3. The enrollees then have the remaining policy term to make installment payments to the insurer. (The policy term typically goes from January through December, so a cost incurred in March, would be repaid through installments ending in December.)

Interpretation (INT) 05-05: Accounting for Revenues Under Medicare Part D Coverage provides high-level accounting guidance on the current Part D program. INT 05-05 includes some basic guidance, but primarily provides guidance by referring to existing statements for specific aspects of the program.

A unique aspect of the updated program is having the insurer pay the pharmacy at the point of sale and seek reimbursement from enrollees. Most of the existing statutory accounting guidance on amounts recoverable from enrollees contemplates premium receivables or amounts due from a governmental payor.

Statutory accounting questions include 1) where to report the initial point of sale payment to the pharmacy and the related installment receivables, 2) how to account for the prescription drug point of sale payments, and 3) when to write-off and or nonadmit overdue amounts.

The program does not change the Part D enrollee's total out of pocket costs. If a participant fails to pay the amount, they are billed by the Part D sponsor, their participation in the program may be terminated following a required two-month grace period. The Part D plan sponsor is not permitted to terminate the individual's enrollment in the Part D plan due to failure to pay MP3 bills. Part D plan sponsors must also have a reinstatement process in place to allow individuals to resume participation in the MP3 in the same plan year.

Part D sponsors are required to treat any unsettled balances owed by enrollees under the MP3 as plan losses; Centers for Medicare & Medicaid Services (CMS) considers these unsettled balances as part of the plan's administrative costs. The other costs of Costs of implementing the MP3 program and program collections are included in the administrative expenses of the Part D plan and are not included in the claim expenses or claim adjustment expenses. CMS requires several reporting requirements and ongoing monitoring.

CMS has specific guidance on the treatment of unsettled balances in the medical loss ratio (MLR). MLR is the share of revenue used for incurred claims and quality improvement activities, rather than the share of revenue used for administrative costs and profit. Therefore, excluding unsettled balances from the numerator of the MLR calculation is consistent with the statutory direction to treat unsettled balances as plan losses and CMS' approach to other administrative expenses incurred by Part D sponsors.

The CMS guidance notes that unsettled balances are included in the denominator of the MLR calculation. The Act requires Part D sponsors to treat any unsettled balances owed by participants under the MP3 as plan losses and allows Part D sponsors to include unsettled balances assumed as losses in their premium bids. Consequently, Part D sponsors will receive revenue covering these assumed losses through their direct subsidy and premium payments, which should be included in the denominator of the MLR.

Health insurance industry trades, America's Health Insurance Plans (AHIP) and Blue Cross Blue Shield Association (BCBSA) have also coordinated with NAIC staff and submitted information on the programs and recommendations which are included in the Hearing comments.

Recommendation:

NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and take the actions listed below:

1. Expose the draft interpretation *INT 24-02: Medicare Part D Prescription Payment Program* and expose minor edits to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* as illustrated in the agenda item. The edits to INT 05-05 adds reference the new INT 24-02 regarding Medicare Part D prescription payment plans.
2. Send notice of the exposure to the Health Insurance (B) Committee and Health Risk Based Capital (E) Working Group
3. Direct NAIC staff to coordinate with Blanks (E) Working Group to develop a annual statement blanks proposal in the interim and to develop disclosures for future inclusion in relevant SSAPs. Preliminary

recommendations would include the list below, but more research on CMS reporting may also identify other relevant items:

a. Amounts recoverable on Medicare Part D installments due from enrollees.
b. Aging of Medicare Part D installments due from enrollees more than 90 days overdue in categories similar to what is used for premium receivables.
c. Information nonadmitted Medicare Part D installments due from enrollees.
d. Information on write-offs of Medicare Part D installments due from enrollees.

Ref #	Title	Attachment #
2024-25 (Jake)	**SSAP No. 16 ASU Clarification**	**G – Form A**

<u>*Summary:*</u>
This agenda item was developed when staff noted instances in SSAP No. 16 where the FASB ASC Topic has been referenced directly instead of the ASU. When guidance is adopted by FASB, it is issued through an accounting standards update which formally adopts the guidance into the FASB Accounting Codification. The Working Group will then address the guidance in the ASU, which is the guidance at a moment in time instead of the actual ASC, which represents guidance that will change over time as other ASUs are adopted. As the guidance stands now, a new ASU could be issued that impacts the ASC sections that are referenced in the SSAP, thereby changing statutory accounting guidance without the Working Group addressing and considering the issue. This agenda item proposes to add the effective ASUs to each of these references where it is missing in SSAP No. 16.

<u>*Recommendation:*</u>
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 to *SSAP No. 16—Electronic Data Processing Equipment and Software* to clarify the references to ASC sections in the SSAP. The proposed revisions to SSAP No. 16 are illustrated within the Form A.

Ref #	Title	Attachment #
2024-26EP (Julie)	**Fall 2024 Editorial Revisions**	**H – Form A**

<u>*Summary:*</u>
The disclosure in SSAP No. 26, paragraph 39e is an existing disclosure (pre-bond-definition revisions). However, the pre-bond-definition version of the disclosure included direction for disclosure by Schedule D broad reporting categories, with categories listed in the SSAP. These reporting categories were removed from the adopted revised SSAP No. 26 disclosure effective Jan. 1, 2025. Although this disclosure is satisfied by the completion of Schedule D-1-1 and D-1-2 for statutory accounting purposes, comments have been made that the adopted revised language could require a listing of all bonds in the audited financial statements. As such, editorial revisions have been proposed to reinstate the prior language for "receiving bond treatment" (as adopted, revised *SSAP No. 43—Asset-Back Securities*, paragraph 44m points to this SSAP No. 26 disclosure for ABS items), and to include reference to reporting categories. A listing of the reporting categories is not deemed necessary within the SSAP.

<u>*Recommendation:*</u>
NAIC staff recommend that the Statutory Accounting Principles (E) Working Group move this agenda item to the active listing, categorize as a SAP Clarification, and expose editorial revisions as illustrated within for a shortened comment period ending December 9, 2024. It is anticipated that this item will be considered during the December 17 SAPWG virtual meeting.

B. Any Other Matters

a. Review of U.S. GAAP Exposures (Jason – Attachment I)

The attachment details the items currently exposed by the FASB. Comments are not recommended at this time – NAIC staff recommend review of the final issued ASU under the SAP Maintenance Process as detailed in *Appendix F—Policy Statements.*

b. Update on the IMR Ad Hoc Subgroup – (Julie)

The IMR Ad Hoc group has met regularly since their first meeting in Oct. 2023. Since the Summer National Meeting, the discussions have focused on IMR from reinsurance transactions. The reinsurance discussion is complex, and after assessing application/interpretation of existing guidance, the group has directed a reassessment of guidance. With this approach, it is intended that principles for accounting/reporting of IMR in response to reinsurance transactions (including for the cedent, assuming entity and in the event of recapture) will be established for application.

c. Update on the Bond Project Implementation / Bond Small Group – (Julie)

The Bond Small Group has currently concluded their regular meetings. The group addressed the items presented and referred the question-and-answer guide to the Working Group. The group may resume future discussions as necessary based on issues or questions raised.

d. Use of 3rd Party Vendors / Checklists to Determine Bond Definition Compliance / Classification

e. IAIS Audit and Accounting Working Group (AAWG Update) – (Julie)

Julie Gann and Maggie Chang (NAIC) monitor IAIS discussions. There have been no significant discussions since the Summer National Meeting. Beginning in November 2024, it is anticipated that NAIC staff will be involved in reviewing comments received on the exposed IAIS climate risk materials and proposing revisions to the application paper.

This update simply intends to inform the SAPWG regulators and interested parties of these ongoing NAIC staff actions to monitor and participate in the IAIS AAWG. Any questions on discussions or if additional information is requested, please contact NAIC staff.

f. Update on Reinsurance Exposures (Robin)

Three reinsurance-related agenda items (2024-05, A-791, Paragraph 2.c., 2024-06, Risk Transfer Analysis on Combination Reinsurance Contracts, 2024-07, Reporting of Funds Withheld and Modco Assets) were exposed at the Summer National Meeting. Agenda items 2024-05 and 2024-06 are related to referrals from the Valuation Analysis (E) Working Group and 2024-07 is for the new modco disclosures. All three of these items have had delayed comment deadlines at the request of the ACLI, and they have been asked to provide a short update at this meeting.

g. December 17 Meeting

The Working Group has scheduled a meeting for December 17th for items with a November 8th and December 9th comment deadlines.

Comment Deadlines:

- **Comment Deadline for Ref #2024-26EP – Monday, December 9, 2024**

- **Comment Deadline for all other items – Friday, January 31, 2025**

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

Issue: Restricted Asset Disclosure Clarification

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been prepared to clarify how assets held under modified coinsurance (Modco) or funds withheld (FWH) agreements shall be reflected within the restricted asset disclosure in paragraph 23 of *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures* and in the corresponding disclosures in Note 5L of the statutory financial statements. It also proposes enhanced disclosures to fully identify the extent of restricted assets reported on balance sheet within a single disclosure as well as identify differences between the "restricted asset" annual statement disclosure and the amount reported in the general interrogatories, which is pulled directly into the RBC formulas. Lastly, this agenda item suggests a referral to propose revisions to the life RBC instructions to clarify that if the reporting entity uses any assets held under a modco or FWH agreement as collateral or as a pledged asset for a purpose unrelated to the reinsurance agreement (securing an exposure that has not been ceded to the reinsurer), then the reporting entity should not take any Modco/FWH reduction in RBC charges (credit) for those assets in the life RBC formula. This clarification is consistent with the existing life RBC instruction that does not permit RBC credit when the asset risk has not been transferred to the assuming entity for the entire duration of the reinsurance treaty. This referral to life RBC intends to make it clear that if the insurance entity has utilized Modco/FWH assets as collateral or as a pledged item for their own repurchase agreements, securities lending transactions, FHLB agreements/borrowings, or any other purpose specific to the ceding insurer's use, then the asset risk/benefit has not been sufficiently transferred to the assuming entity warranting RBC credit for those assets.

As a key item to note, this agenda item does not propose to capture modco/FWH assets in the restricted asset reporting that flows through to the general interrogatories (GI) that results with an additional "noncontrolled" asset RBC charge. As the RBC formula allows credit for modco/FWH assets held, if these were included in the "noncontrolled asset" category, more complexity and adjustments to the RBC formula would be required to also provide credit against the additional noncontrolled asset charge. Instead, as detailed within, this agenda item proposes modifications to capture modco/FWH assets in the existing restricted asset disclosure (SSAP No. 1, paragraph 23c) that currently focuses on collateral received reported on balance sheet for when there is an corresponding liability reported. By including at this location and expanding disclosures to provide a complete view of restricted assets in comparison to total assets and total admitted assets, there is no additional RBC impact and regulators have a better picture of the assets that are restricted as pledged, not under the exclusive control of the reporting entity or that are earmarked (such as modco/FWH) for a specific purpose.

NAIC staff is aware that some companies report modco/FWH assets held in the existing restricted asset disclosure as "pledged collateral not captured in other categories" or as "other restricted assets," but not all companies report these assets as restricted. (In the RBC formulas, there are adjustments for these assets that are reported that incur additional "noncontrolled" asset RBC.) This agenda item specifies the disclosure location and category to promote consistency and comparability across insurers in the reporting of these assets. NAIC staff supports the inclusion of these assets in the restricted asset disclosure (even when an offsetting liability is reported), as it allows for a full comparison of such assets to total assets. NAIC staff believes the total restricted assets may be considered by financial statement users when assessing available assets, and this disclosure could impact the extent to which borrowing is permitted. If Modco/FWH assets are not captured, it may present a picture of available assets that is not accurate.

As noted in the introduction, this agenda item also proposes additional disclosures to identify differences between what is captured as restricted in SSAP No. 1, paragraph 23b, in Note 5L(1), and what is captured in the general interrogatories. Although the categories are identical, NAIC staff is aware that amounts are reported differently between the two locations. NAIC staff believes this is due to the amounts that are reported in the GI are pulled for the additional noncontrolled asset RBC charge. Over time NAIC staff has received information that these discrepancies may be directed by the domiciliary state regulator for situations that have been identified not to warrant the additional "restricted asset" / "noncontrolled asset" RBC charge. Since the amount is pulled directly from the GI to the RBC formula it is not considered a permitted practice in RBC, however, it results in a mismatch between the note disclosure and the GI although the categories are identical. (NAIC staff has not identified any permitted practices for the differences between the Note and GI reporting. Regulator comments are requested on whether the two reporting locations are interpreted to have different parameters as the language appears identical in both locations.) At this time, this proposal is strictly a disclosure element to make it easy to identify variations and the explanation between the Note and GI reporting so that future assessments can occur. If certain restricted assets are supported for general exclusion from the GI reporting (and the RBC factor), then those situations should be considered by the Working Group so that all insurers are following the same provisions.

The following paragraphs detail how the existing disclosure in SSAP No. 1, paragraph 23b (reported in NoteL(1)) compares to the information reported in the GI:

- As detailed in SSAP No. 1, paragraph 23b and in Note 5L(1), admitted and nonadmitted assets that are pledged or otherwise restricted in the general account and separate account are to be disclosed along with a comparison of the total restricted assets to total assets and total admitted assets. With specific categories for certain uses, the note also includes broad categories for "pledged as collateral not captured in other categories" and "other restricted assets" to capture items not covered within the specific lines. Note 5L(2) and 5L(3) captures information on these generic categories, and includes examples of reinsurance and derivatives contracts on what should be captured. This disclosure instruction indicates that contracts that share similar characteristics (such as reinsurance and derivatives) are to be reported in the aggregate.

- The restricted asset categories in Note 5L(1) are duplicated in the annual statement general interrogatories (GI), and the amounts reported in the GI are pulled directly into the RBC formula and incur an additional "noncontrolled asset" RBC charge. NAIC staff is aware that there are discrepancies between the amounts of restricted assets reported in Note 5L(1) and what is captured in the same categories within the GI. (These are lines 25.04, 25.05 and 26.21-26.32 in the GI.)

The following details how these items are pulled into RBC from the general interrogatories:

- In the life formula, the restricted assets captured in the GI are pulled directly from the GI to LR017. The standard "noncontrolled asset" charge on that page is 0.0126, except for conforming security lending programs which receive a charge of 0.0020. (Assets pledged as collateral to the FHLB are adjusted in the formula based on various factors.)

- In the P/C and health RBC formula, the restricted assets captured in the GI are pulled directly to PR014 and XR005 respectively, with a 0.010 charge except for conforming security lending programs which receive a 0.002 charge.

The specific excerpts from SSAP No. 1, Note 5L, the applicable GIs and RBC formulas have been captured in the authoritative language section. The categories are also listed in the table below. The terminology at each location is also included below to show the intended consistency in classifications.

<u>Assets identified as "Not Controlled" or "Restricted Assets":</u>

- <u>SSAP No. 1: Restricted Assets / Not Under Exclusive Control</u>: Defined in paragraph 23b as "not under the exclusive control, subject to a put option contract, etc." Footnote 3 of SSAP No. 1 includes the following: The aggregate information captured within this disclosure is intended to reflect the information reported in the Annual Statement Investment Schedules in accordance with the coding of investments **<u>that are not under the exclusive control of the reporting entity, including assets loaned to others and the information reported in the General Interrogatories, as well as information on restricted cash, cash equivalents and short-term investments</u>**.

- <u>Note 5L</u>: Matches terminology and language as SSAP No. 1.

- <u>General Interrogatories: Exclusive Control</u>: GI 25 asks if the company has "exclusive control" over all securities, other than securities lending detailed in 25.03. The instructions define this guidance as "exclusive control means that the company has the exclusive right to dispose of the investment at will, without the necessity of making a substitution therefore." GI 26 that captures the statement value of investments that are not under the exclusive control of the reporting entity. **<u>These categories mirror what is captured in SSAP No. 1 and Note 5L.</u>**

- <u>RBC: Noncontrolled Assets</u>: The RBC instructions have separate lines to capture collateral from conforming and non-conforming securities lending programs and "noncontrolled assets." **<u>The instructions indicate "noncontrolled assets are any assets reported on the balance sheet that are not under the exclusively under the control of the company, or assets that have been sold or transferred subject to put option contract currently in force."</u>** *(Although not detailed in this agenda item, the RBC instructions include specific guidance on what to include (or exclude). Examples include assets related to the Federal Reserve's Asset Loan Facility (TALF) and for restricted assets in excess of FHLB borrowing.)*

	SSAP No. 1	***Note 5L***	***GI***	***Life RBC[2]***
23.a	Amounts not in the financial statements that represent segregated funds held for others.	None	None	None
23.b.i	Subject to contractual obligation for which liability is not shown	5.L(1)a	None	None
23.b.ii	Collateral Under Security Lending[1]	5.L(1)b	25.0 4 & 25.05	LR017 (1) & LR017 (2)
23.b.iii	Subject to Repurchase Agreements	5.L(1)c	26.21	LR017 (3)
23.b.iv	Subject to Reverse Repurchase Agreements	5.L(1)d	26.22	LR017 (4)
23.b.iv	Subject to Dollar Repurchase	5.L(1)e	26.23	LR017 (5)
23.b.v	Subject to Dollar Reverse Repurchase	5.L(1)f	26.24	LR017 (6)
23.b.vi	Placed Under Option Contracts	5.L(1)g	26.25	LR017 (7)
23.b.vii	Stock or Securities Restricted as to Sale – Excluding FHLB	5.L(1)h	26.26	LR017 (8)
23.b.ix	FHLB Capital Stock	5.L(1)i	26.27	LR017 (9)
23.b.x	On Deposits with States	5.L(1)j	26.28	LR017 (10)
23.b.xi	On Deposit with Regulatory Bodies	5.L(1)k	26.29	LR017 (11)
23.b.xii	Pledged Collateral to FHLB	5.L(1)l	26.31	LR017 (13)
23.b.xiii	Pledged Collateral Not Captured in Other Categories	5.L(1)m	26.30	LR017 (12.1)
	Less Derivative Collateral Pledged[3]			LR017 (12.2)
23.b.xiv	Other Restricted Assets	5.L(1)n	26.32	LR017 (14)
23.c	Assets received as collateral, reflected as assets within the F/S and the recognized liability to return.	5.L(4)		
	1 – In the life blank, this reads “loaned to others,” but the RBC instructions indicate “collateral.” This agenda item proposes to update this terminology in the life blank for consistency.			
	2 – These items are duplicated in the P/C and Health RBC blank on page PR014 and XR005, except for 3) below.			
	3 – This reduction is in the RBC Life Formula Only. Derivative collateral pledged is subject to a lower RBC charge of .0039 and is captured separately.			

Existing Authoritative Literature:

SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures

Other Disclosures

23. Reporting entities shall disclose[1] the following information in the financial statements:

a. Amounts not recorded in the financial statements that represent segregated funds held for others, the nature of the assets and the related fiduciary responsibilities associated with such assets. One example of such an item is escrow accounts held by title insurance companies; and

b. The total combined (admitted and nonadmitted) amount of restricted assets by category, with separate identification of the admitted and nonadmitted restricted assets by category, and nature of any assets pledged to others as collateral or otherwise restricted (e.g., not under the exclusive control, assets subject to a put option contract, etc.)[2] in the general and separate accounts[3] by the reporting entity in comparison to total assets and total admitted assets. (Pursuant to SSAP No. 4, paragraph 6, all assets pledged as collateral or otherwise restricted shall be reported in this disclosure regardless if the asset is considered an admitted asset.) This disclosure shall include the following restricted asset categories:

   i. Reported assets subject to contractual obligation for which liability is not shown;
   ii. Collateral held under security lending agreements;
   iii. Assets subject to repurchase agreements;
   iv. Assets subject to reverse repurchase agreements;
   v. Assets subject to dollar repurchase agreements;
   vi. Assets subject to dollar reverse repurchase agreements;
   vii. Assets placed under option contracts;
   viii. Letter stock or securities restricted as to sale[4] – excluding FHLB stock;
   ix. FHLB capital stock;
   x. Assets on deposit with states;
   xi. Assets on deposit with other regulatory bodies;
   xii. Pledged as collateral to the FHLB (including assets backing funding agreements);
   xiii. Assets pledged as collateral not captured in other categories; and

[1] Disclosure of restricted assets shall be included in the annual financial statements and, pursuant to the Preamble, in the interim financial statements if significant changes have occurred since the annual statement. If significant changes have occurred, the entire disclosure shall be reported in the interim financial statements.

[2] The aggregate information captured within this disclosure is intended to reflect the information reported in the Annual Statement Investment Schedules in accordance with the coding of investments that are not under the exclusive control of the reporting entity, including assets loaned to others and the information reported in the General Interrogatories, as well as information on restricted cash, cash equivalents and short-term investments.

[3] Restricted assets in the separate account are not intended to reflect amounts "restricted" only because they are insulated from the general account or because they are attributed to specific policyholders. Separate account assets shall be captured in this disclosure only if they are restricted outside of these characteristics.

[4] The nature, description and amount of the restriction are required in the disclosure.

xiv. Other restricted assets.

c. The amount and nature of any assets received as collateral, reflected as assets within the reporting entity's financial statements, and the recognized liability to return these collateral assets, in the general and separate accounts in comparison to total assets and admitted assets.

2024 Annual Statement Instructions – Note 5L: Restricted Assets

L. Restricted Assets

(1) Restricted Assets (Including Pledged)

Disclose the total gross (admitted and nonadmitted) amount of restricted assets by category, with separate identification of the admitted and nonadmitted restricted assets by category and nature of any assets pledged to others as collateral or otherwise restricted (e.g., not under the exclusive control, assets subject to a put option contract, etc.) by the reporting entity. Provide the gross amount of restricted assets (total general account, general account assets supporting separate account activity, total separate account, separate account assets supporting general account activity and sum of the general account and the separate account for current year, prior year and the change between years), the total admitted of restricted assets and the percentage the restricted asset amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 28 of the asset page (gross and admitted respectively) by the following categories:

a. Subject to contractual obligation for which liability is not shown

b. Collateral held under security lending agreements

c. Subject to repurchase agreements

d. Subject to reverse repurchase agreements

e. Subject to dollar repurchase agreements

f. Subject to dollar reverse repurchase agreements

g. Placed under option contracts

h. Letter stock or securities restricted as to sale – excluding FHLB capital stock

i FHLB capital stock

j. On deposit with states

k. On deposit with other regulatory bodies

l. Pledged collateral to FHLB (including assets backing funding agreements)

m. Pledged as collateral not captured in other categories

n. Other restricted assets

o. Total restricted assets

(2) Detail of Assets Pledged as Collateral Not Captured in Other Categories

For assets pledged as collateral not captured in other categories reported in aggregate in Note 5L(1) above, provide the gross (admitted and nonadmitted) amount of restricted assets (total general account, general account assets supporting separate account activity, total separate account, separate account assets supporting general account activity and sum of the general account and the separate account for current year, prior year and the change between years), the total admitted of restricted assets and the percentage the restricted asset amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 28 of the asset page (gross and admitted respectively) with a narrative summary of each collateral agreement included in the aggregate number in Note 5L(1) above. Contracts that share similar characteristics, such as reinsurance and derivatives, are to be reported in the aggregate. (Note: This would be the detail for what was reported as "Pledged as Collateral Not Captured in Other Categories" for 5L(1) above.)

(3) Detail of Other Restricted Assets

For other restricted assets reported in aggregate in Note 5L(1) above, provide the gross (admitted and nonadmitted) amount of restricted assets (total general account, general account assets supporting separate account activity, total separate account, separate account assets supporting general account activity and sum of the general account and the separate account for current year, prior year and the change between years), the total admitted of restricted assets and the percentage the restricted asset amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 28 of the asset page (gross and admitted respectively) with a description of each of the other restricted assets included in the aggregate number in Note 5L(1) above. Contracts that share similar characteristics, such as reinsurance and derivatives, are to be reported in the aggregate. (Note: This would be the detail for what was reported as "Other Restricted Assets" for 5L(1) above.)

(4) Collateral Received and Reflected as Assets Within the Reporting Entity's Financial Statements

Disclose the following for the general account and separate account:

- Nature of any assets received as collateral reflected as assets within the reporting entity's financial statements

- Book/adjusted carrying value (BACV) of the collateral

- Fair value of the collateral

- The recognized liability to return these collateral assets

- The percentage the collateral asset BACV amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 26 of the asset page (gross and admitted, respectively).

NOTE: The information captured within this disclosure is intended to aggregate the information reported in the Annual Statement Investment Schedules in accordance with the coding of investments that are not under the exclusive control of the reporting entity, including assets loaned to others, and the information reported in the General Interrogatories.

Restricted assets in the separate account are not intended to capture amounts "restricted" only because they are insulated from the general account or because they are attributed to specific policyholders. Separate account assets shall be captured in this disclosure only if they are restricted outside of these characteristics.

(1) Restricted Assets (Including Pledged)

Restricted Asset Category	Gross (Admitted & Nonadmitted) Restricted						
	Current Year					6	7
	1 Total General Account (G/A)	2 G/A Supporting S/A Activity (a)	3 Total Separate Account (S/A) Restricted Assets	4 S/A Assets Supporting G/A Activity (b)	5 Total (1 plus 3)	Total From Prior Year	Increase/ (Decrease) (5 minus 6)
a. Subject to contractual obligation for which liability is not shown	$	$	$	$	$	$	$
b. Collateral held under security lending agreements	....		....				
c. Subject to repurchase agreements	....		....				
d. Subject to reverse repurchase agreements	....		....				
e. Subject to dollar repurchase agreements	....		....				
f. Subject to dollar reverse repurchase agreements	....		....				
g. Placed under option contracts	....		....				
h. Letter stock or securities restricted as to sale – excluding FHLB capital stock	....		....				
i. FHLB capital stock	....		....				
j. On deposit with states	....		....				
k. On deposit with other regulatory bodies	....		....				
l. Pledged as collateral to FHLB (including assets backing funding agreements)	....		....				
m. Pledged as collateral not captured in other categories	....		....				
n. Other restricted assets	....		....				
o. Total Restricted Assets (Sum of a through n)	$	$	$	$	$	$	$

(a) Subset of Column 1
(b) Subset of Column 3

Restricted Asset Category	Current Year			
	8	9	Percentage	
	Total Nonadmitted Restricted	Total Admitted Restricted (5 minus 8)	10 Gross (Admitted & Nonadmitted) Restricted to Total Assets (c)	11 Admitted Restricted to Total Admitted Assets (d)
a. Subject to contractual obligation for which liability is not shown			%	%
b. Collateral held under security lending agreements				
c. Subject to repurchase agreements				
d. Subject to reverse repurchase agreements				
e. Subject to dollar repurchase agreements				
f. Subject to dollar reverse repurchase agreements				
Placed under option contracts				
h. Letter stock or securities restricted as to sale – excluding FHLB capital stock				
i. FHLB capital stock				
j. On deposit with states				
k. On deposit with other regulatory bodies				
l. Pledged as collateral to FHLB (including assets backing funding agreements)				
m. Pledged as collateral not captured in other categories				
n. Other restricted assets				
o. Total Restricted Assets (Sum of a through n)			%	%

(c) Column 5 divided by Asset Page, Column 1, Line 28
(d) Column 9 divided by Asset Page, Column 3, Line 28

(2) Detail of Assets Pledged as Collateral Not Captured in Other Categories (Contracts that Share Similar Characteristics, Such as Reinsurance and Derivatives, Are Reported in the Aggregate)

	Gross (Admitted & Nonadmitted) Restricted							8	Percentage	
	Current Year					6	7		9	10
	1	2	3	4	5					
Description of Assets	Total General Account (G/A)	G/A Supporting S/A Activity (a)	Total Separate Account (S/A) Restricted Assets	S/A Assets Supporting G/A Activity (b)	Total (1 plus 3)	Total From Prior Year	Increase/ (Decrease) (5 minus 6)	Total Current Year Admitted Restricted	Gross (Admitted & Nonadmitted) Restricted to Total Assets	Admitted Restricted to Total Admitted Assets
....	$	$	$	$	$	$	$	$	.... %	............%
....	....	....	....	....	....	....	....	....	....	....
....	....	....	....	....	....	....	....	....	....	....
Total (c)	$	$	$	$	$	$	$	$	.... %	............%

(a) Subset of column 1
(b) Subset of column 3
(c) Total Line for Columns 1 through 7 should equal 5L(1)m Columns 1 through 7 respectively and Total Line for Columns 8 through 10 should equal 5L(1)m Columns 9 through 11 respectively

(3) Detail of Other Restricted Assets (Contracts that Share Similar Characteristics, Such as Reinsurance and Derivatives, Are Reported in the Aggregate)

	Gross (Admitted & Nonadmitted) Restricted							8	Percentage	
	Current Year					6	7		9	10
	1	2	3	4	5					
Description of Assets	Total General Account (G/A)	G/A Supporting S/A Activity (a)	Total Separate Account (S/A) Restricted Assets	S/A Assets Supporting G/A Activity (b)	Total (1 plus 3)	Total From Prior Year	Increase/ (Decrease) (5 minus 6)	Total Current Year Admitted Restricted	Gross (Admitted & Nonadmitted) Restricted to Total Assets	Admitted Restricted to Total Admitted Assets
....	$	$	$	$	$	$	$	$	.... %	............%
....	....	....	....	....	....	....	....	....	....	....
....	....	....	....	....	....	....	....	....	....	....
Total (c)	**$ ....**	**$ ....**	**$ ....**	**$ ....**	**$ ....**	**$ ....**	**$ ....**	**$ ....**	**........... %**	**............%**

(a) Subset of column 1
(b) Subset of column 3
(c) Total Line for Columns 1 through 7 should equal 5L(1)n Columns 1 through 7 respectively and Total Line for Columns 8 through 10 should equal 5L(1)n Columns 9 through 11 respectively

(4) Collateral Received and Reflected as Assets Within the Reporting Entity's Financial Statements

	1	2	3	4
Collateral Assets	Book/Adjusted Carrying Value (BACV)	Fair Value	% of BACV to Total Assets (Admitted and Nonadmitted *	% of BACV to Total Admitted Assets **
General Account:				
a. Cash, Cash Equivalents and Short-Term Investments	$	$	..................%	.... %
b. Schedule D, Part 1	....	....	..................%	.... %
c. Schedule D, Part 2, Section 1	....	....	..................%	.... %
d. Schedule D, Part 2, Section 2	....	....	..................%	.... %
e. Schedule B	....	....	..................%	.... %
f. Schedule A	....	....	..................%	.... %
g. Schedule BA, Part 1	....	....	..................%	.... %
h. Schedule DL, Part 1	....	....	..................%	.... %
i. Other			%	%
j. Total Collateral Assets (a+b+c+d+e+f+g+h+i)	$	$	%	%
Separate Account:				
k. Cash, Cash Equivalents and Short-Term Investments	$	$	..................%	.... %
l. Schedule D, Part 1	....	....	..................%	.... %
m. Schedule D, Part 2, Section 1	....	....	..................%	.... %
n. Schedule D, Part 2, Section 2	....	....	..................%	.... %
o. Schedule B	....	....	..................%	.... %
p. Schedule A	....	....	..................%	.... %
q. Schedule BA, Part 1	....	....	..................%	.... %

r. Schedule DL, Part 1	....	....	..................%	.... %
s. Other			%	%
t. Total Collateral Assets (k+l+m+n+o+p+q+r+s)	$	$	%	%

* j = Column 1 divided by Asset Page, Line 26 (Column 1)
t = Column 1 divided by Asset Page, Line 27 (Column 1)

** j = Column 1 divided by Asset Page, Line 26 (Column 3)
t = Column 1 divided by Asset Page, Line 27 (Column 3)

	1 Amount	2 % of Liability to Total Liabilities *
u. Recognized Obligation to Return Collateral Asset (General Account)	$	%
v. Recognized Obligation to Return Collateral Asset (Separate Account)	$	%

* u = Column 1 divided by Liability Page, Line 26 (Column 1)
v = Column 1 divided by Liability Page, Line 27 (Column 1)

ANNUAL STATEMENT GENERAL INTERROGATORIES

Instructions – Part 1 – Common Interrogatories

INVESTMENT

25. For the purposes of this interrogatory, "exclusive control" means that the company has the exclusive right to dispose of the investment at will, without the necessity of making a substitution thereof. For purposes of this interrogatory, securities in transit and awaiting collection, held by a custodian pursuant to a custody arrangement or securities issued subject to a book entry system are considered to be in actual possession of the company.

If bonds, stocks and other securities owned December 31 of the current year, over which the company has exclusive control are: (1) securities purchased for delayed settlement, or (2) loaned to others, the company should respond "NO" to 25.01 and "YES" to 26.1.

25.03 Describe the company's securities lending program, including value for collateral and amount of loaned securities, and whether the collateral is held on- or off-balance sheet. Note 17 of Notes to Financial Statement provides a full description of the program.

25.04 Report amount of collateral for conforming programs as outlined in the Risk-Based Capital Instructions.

25.05 Report amount of collateral for other programs.

25.091 The fair value amount reported should equal the grand total of Schedule DL, Part 1, Column 5 plus Schedule DL, Part 2, Column 5. The fair value amount reported amount should also equal the fair value amount reported in Note 5E(5)a1(m).

25.092 The book adjusted/carrying value amount reported should equal the grand total of Schedule DL, Part 1,
Column 6 plus Schedule DL, Part 2, Column 6.

25.093 The payable for securities lending amount reported should equal current year column for payable for securities lending line on the liability page.

26. Disclose the statement value of investments that are not under the exclusive control of the reporting entity within the categories listed in 26.2.

Excerpt – Annual Statement Blank

25.01	Were all the stocks, bonds and other securities owned December 31 of current year, over which the reporting entity has exclusive control, in the actual possession of the reporting entity on said date? (other than securities lending programs addressed in 25.03)	Yes [ ] No [ ]
25.02	If no, give full and complete information, relating thereto..	
25.03	**For securities lending programs, provide a description of the program including value for collateral and amount of loaned securities, and whether collateral is carried on or off-balance sheet. (an alternative is to reference Note 17 where this information is also provided)................ ....**	
25.04	**For the reporting entity's securities lending program, report amount of collateral for conforming programs as outlined in the Risk-Based Capital Instructions.**	$ ____________
25.05	For the reporting entity's securities lending program, report amount of collateral for other programs.	$ ____________
25.06	Does your securities lending program require 102% (domestic securities) and 105% (foreign securities) from the counterparty at the outset of the contract?	Yes [ ] No [ ] N/A [ ]
25.07	Does the reporting entity non-admit when the collateral received from the counterparty falls below 100%?	Yes [ ] No [ ] N/A [ ]
25.08	Does the reporting entity or the reporting entity's securities lending agent utilize the Master Securities Lending Agreement (MSLA) to conduct securities lending?	Yes [ ] No [ ] N/A [ ]
25.09	For the reporting entity's securities lending program, state the amount of the following as of December 31 of the current year:	
	25.091 Total fair value of reinvested collateral assets reported on Schedule DL, Parts 1 and 2	$ ____________
	25.092 Total book/adjusted carrying value of reinvested collateral assets reported on Schedule DL, Parts 1 and 2	$ ____________
	25.093 Total payable for securities lending reported on the liability page	$ ____________
26.1	**Were any of the stocks, bonds or other assets of the reporting entity owned at December 31 of the current year not exclusively under the control of the reporting entity or has the reporting entity sold or transferred any assets subject to a put option contract that is currently in force? (Exclude securities subject to Interrogatory 21.1 and 25.03).**	**Yes [ ] No [ ]**
26.2	**If yes, state the amount thereof at December 31 of the current year:**	
	26.21 Subject to repurchase agreements	**$____________**
	26.22 Subject to reverse repurchase agreements	**$____________**
	26.23 Subject to dollar repurchase agreements	**$____________**
	26.24 Subject to reverse dollar repurchase agreements	**$____________**
	26.25 Placed under option agreements	**$____________**
	26.26 Letter stock or securities restricted as to sale – excluding FHLB Capital Stock	**$____________**
	26.27 FHLB Capital Stock	**$____________**
	26.28 On deposit with states	**$____________**
	26.29 On deposit with other regulatory bodies	**$____________**
	26.30 Pledged as collateral – excluding collateral pledged to an FHLB	**$____________**
	26.31 Pledged as collateral to FHLB – including assets backing funding agreements	**$____________**
	26.32 Other	**$____________**
26.3	**For category (26.26) provide the following:**	

1 **Nature of Restriction**	**2** **Description**	**3** **Amount**

<u>Excerpt from Life RBC Instructions – Bolded for Emphasis</u>

MODCO OR FUNDS WITHHELD REINSURANCE AGREEMENTS
LR045, LR046, LR047 and LR048

References to MODCO and funds withheld reinsurance agreements apply to all treaties in effect.

Basis of Factors
When the default risk in modified coinsurance (MODCO) and other reinsurance transactions with funds withheld is transferred, this transfer should be recognized by reducing the RBC for the ceding company and increasing it for the assuming company. **In the event that the entire asset credit or variability in statement value risk associated with the assets supporting the business reinsured is not transferred to the assuming company for the entire duration of the reinsurance treaty, the RBC for the ceding company should not be reduced.**

Assets
The total RBC related to assets (i.e., bonds, mortgages, unaffiliated preferred and common stock, separate accounts, real estate and other long-term assets) in MODCO or Funds Withheld reinsurance agreements, should be reduced (increased) by the amounts of RBC ceded (assumed). There is a separate line in each asset section to achieve this reduction (i.e., "Reduction in RBC for MODCO or Funds Withheld reinsurance ceded agreements")**.** The amount ceded is determined using the assets supporting the ceded liabilities as of Dec. 31. (In some instances, there may be assets in a trust that exceed the amount needed to support the liabilities; only the portion of assets used to support the ceded liabilities is used to determine the ceded RBC).

The ceding company will need to supply the assuming company with sufficient information in order for the assuming company to determine the amount of RBC assumed. With the exception of the impact of the size factor, the amount of RBC ceded should be equal to the amount of RBC assumed. Put another way, there should be “mirror imaging” of RBC, except for the impact of the size factor. For MODCO or Funds Withheld reinsurance agreements, there will be no specific, line-by-line inventory of ceded assets and corresponding ceded RBC; however, ceding and assuming companies must keep detailed records and be prepared to produce those records upon request. The ceding company is required to supply the assuming company with sufficient information in order for the assuming company to determine the amount of RBC assumed.

A reinsurer that has not received such information shall calculate MODCO adjustments for reinsurance assumed as follows:

- If the reinsurer has received data for periods prior to the effective date of the RBC filing, a “MODCO liability ratio” will be developed by comparing the MODCO liabilities at the filing date to the MODCO liabilities as of the last date for which data were received. The required capital for MODCO assumed is the required capital as calculated based on these data multiplied by the “MODCO liability ratio.”
- • If the reinsurer has never received data from the ceding company, a “MODCO liability ratio” will be developed by comparing the MODCO liabilities at the filing date to the reinsurer’s total invested assets (Page 2, Line 12 of the blue blank, or its equivalent). The required capital for MODCO assumed is the reinsurer’s required capital as calculated prior to MODCO ceded and assumed adjustments multiplied by the “MODCO liability ratio.”

Adjustments for MODCO or Funds Withheld reinsurance agreements should be based on pre-tax factors.

Size Factor
Companies with MODCO or Funds Withheld reinsurance agreements should adjust the company’s year-end size factors according to the way the bonds are handled in the treaties. The assuming company includes the bonds that support its share of the liabilities; the ceding company includes the bonds that support its share of the liabilities. No adjustment is made for bonds purchased subsequent to June 30 of the valuation year and that solely support ceded liabilities.

Mortgages
The amount of RBC for mortgages is based upon the ceding company’s calculation for the mortgages, or portion of these mortgages, which support the ceded liabilities. Thus, the amount of RBC ceded is equal to the amount of RBC assumed.

Specific Instructions for Application of the Formula

MODCO OR FUNDS WITHHELD REINSURANCE AGREEMENTS
Reinsurance Ceded - Bonds C-1o
LR045

Column 4: Enter by reinsurer, the amount of C-1o RBC the insurance company has ceded that is attributable to bonds. The “total” should equal the total amount of the reduction in C-1o RBC shown on Line (19) of page LR002 Bonds.

MODCO OR FUNDS WITHHELD REINSURANCE AGREEMENTS
Reinsurance Assumed - Bonds C-1o
LR046

Column 4: Enter by ceding company, the amount of C-1o RBC the insurance company has assumed that is attributable to bonds. The “total” should equal the total amount of the increase in C-1o RBC shown on Line (20) of page LR002 Bonds.

MODCO OR FUNDS WITHHELD REINSURANCE AGREEMENTS
Reinsurance Ceded – All Other Assets C-0, C-1o And C-1cs
LR047

Column 4: Enter by reinsurer, the amount of C-0, C-1o And C-1cs RBC the company has ceded that is attributable to all assets except bonds. The “total” should equal the total amount of the reduction of C-0, C-1o And C-1cs RBC attributable to all assets except bonds for MODCO and funds withheld agreements.

MODCO OR FUNDS WITHHELD REINSURANCE AGREEMENTS
Reinsurance Assumed – All Other Assets C-0, C-1o And C-1cs
LR048

Column 4: Enter by ceding company, the amount of C-0, C-1o And C-1cs RBC the insurance company has assumed that is attributable to all assets except bonds. The "total" should equal the total amount of the increase in C-0, C-1o And C-1cs RBC attributable to all assets except bonds for MODCO and funds withheld agreements.

Excerpt from Health RBC (Identical to P/C RBC)

Confidential when Completed

OFF-BALANCE SHEET AND OTHER ITEMS

		Annual Statement Source	(1) Bk/Adj Carrying Value	(2) Factor	(3) RBC Requirement	(4) Yes/No Response
	Noncontrolled Assets					
(1)	Loaned to Others - Conforming Securities Lending Programs	General Interrogatories Part 1 Line 25.04		0.002		
(2)	Loaned to Others - Securities Lending Programs - Other	General Interrogatories Part 1 Line 25.05		0.010		
(3)	Subject to Repurchase Agreements	General Interrogatories Part 1 Line 26.21		0.010		
(4)	Subject to Reverse Repurchase Agreements	General Interrogatories Part 1 Line 26.22		0.010		
(5)	Subject to Dollar Repurchase Agreements	General Interrogatories Part 1 Line 26.23		0.010		
(6)	Subject to Reverse Dollar Repurchase Agreements	General Interrogatories Part 1 Line 26.24		0.010		
(7)	Placed Under Option Agreements	General Interrogatories Part 1 Line 26.25		0.010		
(8)	Letter Stock or Securities Restricted as to Sale - Excluding FHLB Capital Stock	General Interrogatories Part 1 Line 26.26		0.010		
(9)	FHLB Capital Stock	General Interrogatories Part 1 Line 26.27		0.010		
(10)	On Deposit with States	General Interrogatories Part 1 Line 26.28		0.010		
(11)	On Deposit with Other Regulatory Bodies	General Interrogatories Part 1 Line 26.29		0.010		
(12)	Pledged as Collateral - Excluding Collateral Pledged to an FHLB	General Interrogatories Part 1 Line 26.30		0.010		
(13)	Pledged as Collateral to FHLB (Including Assets Backing Funding Agreements)	General Interrogatories Part 1 Line 26.31		0.010		
(14)	Other	General Interrogatories Part 1 Line 26.32		0.010		
(15)	Total Noncontrolled Assets	Sum of Lines (1) through (14)				
(16)	Guarantees for Affiliates	Notes to Financial Statements 14A(03C1), Column 2		0.010		
(17)	Contingent Liabilities	Notes to Financial Statements 14A(1), Column 2		0.010		
(18)	Is the entity responsible for filing the U.S. Federal income tax return for the reporting insurer a regulated insurance company?	"Yes", "No" or "N/A" in Column (4)				
(19)	SSAP No. 101 Paragraph 11a Deferred Tax Assets	Notes to Financial Statements, Item 9A2(a), Column 3		†		
(20)	SSAP No. 101 Paragraph 11b Deferred Tax Assets	Notes to Financial Statements, Item 9A2(b), Column 3		0.010		
(21)	Total Miscellaneous Off-Balance Sheet and Other Items	Lines (15) + (16) + (17) + (19) + (20)				

† If Line (18) Column (4) is "Yes", then the factor is 0.005. If Line (18) Column (4) is "No", then the factor is 0.010. If Line (18) Column (4) is "N/A", then the factor is 0.000.

Denotes items that must be manually entered on filing software.

Excerpt from Life RBC

OFF-BALANCE SHEET AND OTHER ITEMS

		Annual Statement Source	(1) Statement Value	(2) Less Noncontrolled Assets Funding Guaranteed Separate Accounts, Synthetic GIC's and Certain FHLB Liabilities	(3) Subtotal		(4) Factor			(5) RBC Requirement
	Noncontrolled Assets									
(1)	Loaned to Others - Conforming Securities Lending Program	General Interrogatories Part 1 Line 25.04	$0	$0	$0	X	0.002		=	$0
(2)	Loaned to Others - Securities Lending Programs - Other	General Interrogatories Part 1 Line 25.05	$0	$0	$0	X	0.0126		=	$0
(3)	Subject to Repurchase Agreements	General Interrogatories Part 1 Line 26.21	$0	$0	$0	X	0.0126		=	$0
(4)	Subject to Reverse Repurchase Agreements	General Interrogatories Part 1 Line 26.22	$0	$0	$0	X	0.0126		=	$0
(5)	Subject to Dollar Repurchase Agreements	General Interrogatories Part 1 Line 26.23	$0	$0	$0	X	0.0126		=	$0
(6)	Subject to Reverse Dollar Repurchase Agreements	General Interrogatories Part 1 Line 26.24	$0	$0	$0	X	0.0126		=	$0
(7)	Placed Under Option Agreements	General Interrogatories Part 1 Line 26.25	$0	$0	$0	X	0.0126		=	$0
(8)	Letter Stock or Other Securities Restricted as to sale - excluding FHLB Capital Stock	General Interrogatories Part 1 Line 26.26	$0	$0	$0	X	0.0126		=	$0
(9)	FHLB Capital Stock	General Interrogatories Part 1 Line 26.27	$0	$0	$0	X	0.0126		=	$0
(10)	On Deposit with States	General Interrogatories Part 1 Line 26.28	$0	$0	$0	X	0.0126		=	$0
(11)	On Deposit with Other Regulatory Bodies	General Interrogatories Part 1 Line 26.29	$0	$0	$0	X	0.0126		=	$0
(12.1)	Pledged as Collateral - excluding Collateral Pledged to an FHLB	General Interrogatories Part 1 Line 26.30	$0	$0	$0					
(12.2)	Less Derivative Collateral Pledged	Schedule DB Part D Section 2 Column 7, Line 0199999999	$0	$0	$0	X	0.0039		=	$0
(12.3)	Pledged as Collateral - excluding Collateral Pledged to an FHLB Less Derivatives Collateral Pledged	Line (12.1) - (12.2)	$0	$0	$0	X	0.0126		=	$0
(13)	Pledged as Collateral to FHLB - including Assets Backing Funding Agreements	General Interrogatories Part 1 Line 26.31	$0	$0 †	$0	X	0.000	#	=	$0
(14)	Other	General Interrogatories Part 1 Line 26.32	$0	$0	$0	X	0.0126		=	$0
(15)	Total Noncontrolled Assets	Sum of Lines (1) through (11) Plus Lines (12.2) through (14)	$0	$0	$0					$0

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 SAP clarification revisions to SSAP No. 1 as well as corresponding proposed revisions to the Annual Statement (A/S) instructions/template for the restricted asset disclosure in Note 5Lto more clearly identify how Modco and FWH assets reported within a ceding company's financial statements shall be captured.

In addition to the revisions that explicitly address Modco/FWH, the A/S revisions propose a new component to the existing disclosure to identify and explain differences between the note and what is captured in the general interrogatories. Although it was originally anticipated that the note and the GI would agree, NAIC staff is aware that there are often differences and that in some instances domiciliary states have directed specific items to be removed from the GI reporting because of the resulting RBC pull / factor impact. This disclosure will highlight those differences to ensure ease of regulator comparisons as well as allow NAIC staff to assess consistency across companies and enable future discussions. NAIC staff recommends that the SAPWG sponsor a blanks proposal to incorporate the Annual Statement instruction revisions.

Although there is a separate agenda item to identify Modco and FWH assets with more granularity, and to assist with RBC impact, this clarification of the aggregate restricted asset disclosure has been recommended to move forward to ensure the restricted asset disclosure is consistently reported.

Upon adoption of the revisions, this agenda item recommends a referral to the Life RBC (E) Working Group to clarify that Modco assets held by a ceding entity that at any time during the year are pledged or used by the ceding entity for their own purpose, such as being used in assets reported to or as collateral to the FHLB or in a repurchase or securities lending agreement, are not permitted to be reported as an RBC charge reduction from the RBC formula for invested assets. Such uses would reflect circumstances in which the

"entire asset credit or variability in statement value risk associated with the assets supporting the business reinsurance was not transferred to the assuming company for the entire duration of the reinsurance treaty." This referral will also identify the direction to capture modco/FWH assets in SSAP No. 1, paragraph 23c, therefore these assets should not be captured in the RBC reporting of "noncontrolled assets," therefore the existing elements in the RBC formula to adjust modco/FWH from the "nonconrolled" reporting lines may no longer be necessary.

Proposed Revisions:

SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures

23. Reporting entities shall disclose[5] the following information in the financial statements:

a. Amounts not recorded in the financial statements that represent segregated funds held for others, the nature of the assets and the related fiduciary responsibilities associated with such assets. One example of such an item is escrow accounts held by title insurance companies; and

b. The total combined (admitted and nonadmitted) amount of restricted assets by category, with separate identification of the admitted and nonadmitted restricted assets by category, and nature of any assets pledged to others as collateral or otherwise restricted (e.g., not under the exclusive control, assets subject to a put option contract, etc.)[6] in the general and separate accounts[7] by the reporting entity in comparison to total assets and total admitted assets. (Pursuant to SSAP No. 4, paragraph 6, all assets pledged as collateral or otherwise restricted shall be reported in this disclosure regardless if the asset is considered an admitted asset.) Reporting entities shall also disclose differences in the amounts reported in this note versus the amounts reported for the same categories in the general interrogatories. This disclosure shall include the following restricted asset categories:

   i. Reported assets subject to contractual obligation for which liability is not shown;

   ii. Collateral held under security lending agreements;

   iii. Assets subject to repurchase agreements;

   iv. Assets subject to reverse repurchase agreements;

   v. Assets subject to dollar repurchase agreements;

   vi. Assets subject to dollar reverse repurchase agreements;

   vii. Assets placed under option contracts;

[5] Disclosure of restricted assets shall be included in the annual financial statements and, pursuant to the Preamble, in the interim financial statements if significant changes have occurred since the annual statement. If significant changes have occurred, the entire disclosure shall be reported in the interim financial statements.

[6] The aggregate information captured within this disclosure is intended to reflect the information reported in the Annual Statement Investment Schedules in accordance with the coding of investments that are not under the exclusive control of the reporting entity, including assets loaned to others and the information reported in the General Interrogatories, as well as information on restricted cash, cash equivalents and short-term investments.

[7] Restricted assets in the separate account are not intended to reflect amounts "restricted" only because they are insulated from the general account or because they are attributed to specific policyholders. Separate account assets shall be captured in this disclosure only if they are restricted outside of these characteristics.

viii. Letter stock or securities restricted as to sale[8] – excluding FHLB stock;

ix. FHLB capital stock;

x. Assets on deposit with states;

xi. Assets on deposit with other regulatory bodies;

xii. Pledged as collateral to the FHLB (including assets backing funding agreements);

xiii. Assets pledged as collateral not captured in other categories[FN1]; and

xiv. Other restricted assets.

New Footnote 1: Items captured in this category shall include assets reported within the financial statements that are pledged to a counterparty that have not been captured in other categories or within paragraph 23.c. Items reported should include, but not be limited to, assets pledged under derivative arrangements.

c. The amount and nature of any assets received as collateral or assets that are held under modified coinsurance or funds withheld reinsurance agreements, reflected as assets within the reporting entity's financial statements, for which there is a ~~and the~~ recognized liability to return these collateral assets or for the dedicated use of those assets under the modco/funds withheld agreement, in the general and separate accounts in comparison to total assets and admitted assets.

Note to the Financial Statements – 5L

(1) Restricted Assets (Including Pledged)

Disclose the total gross (admitted and nonadmitted) amount of restricted assets by category, with separate identification of the admitted and nonadmitted restricted assets by category and nature of any assets pledged to others as collateral or otherwise restricted (e.g., not under the exclusive control, assets subject to a put option contract, etc.) by the reporting entity. Provide the gross amount of restricted assets (total general account, general account assets supporting separate account activity, total separate account, separate account assets supporting general account activity and sum of the general account and the separate account for current year, prior year and the change between years), the total admitted of restricted assets and the percentage the restricted asset amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 28 of the asset page (gross and admitted respectively) by the following categories:

a. Subject to contractual obligation for which liability is not shown
b. Collateral held under security lending agreements
c. Subject to repurchase agreements
d. Subject to reverse repurchase agreements
e. Subject to dollar repurchase agreements
f. Subject to dollar reverse repurchase agreements
g. Placed under option contracts
h. Letter stock or securities restricted as to sale – excluding FHLB capital stock

[8] The nature, description and amount of the restriction are required in the disclosure.

i FHLB capital stock

j. On deposit with states

k. On deposit with other regulatory bodies

l. Pledged collateral to FHLB (including assets backing funding agreements)

m. Pledged as collateral not captured in other categories

n. Other restricted assets

o. Total restricted assets

Note: Items captured "pledged as collateral not captured in other categories" shall include, but not be limited to, assets pledged under derivative arrangements.

(2) Detail of Assets Pledged as Collateral Not Captured in Other Categories

For assets pledged as collateral not captured in other categories reported in aggregate in Note 5L(1) above, provide the gross (admitted and nonadmitted) amount of restricted assets (total general account, general account assets supporting separate account activity, total separate account, separate account assets supporting general account activity and sum of the general account and the separate account for current year, prior year and the change between years), the total admitted of restricted assets and the percentage the restricted asset amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 28 of the asset page (gross and admitted respectively) with a narrative summary of each collateral agreement included in the aggregate number in Note 5L(1) above. Contracts that share similar characteristics, such as reinsurance and derivatives, are to be reported in the aggregate. (Note: This would be the detail for what was reported as "Pledged as Collateral Not Captured in Other Categories" for 5L(1) above.)

(3) Detail of Other Restricted Assets

For other restricted assets reported in aggregate in Note 5L(1) above, provide the gross (admitted and nonadmitted) amount of restricted assets (total general account, general account assets supporting separate account activity, total separate account, separate account assets supporting general account activity and sum of the general account and the separate account for current year, prior year and the change between years), the total admitted of restricted assets and the percentage the restricted asset amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 28 of the asset page (gross and admitted respectively) with a description of each of the other restricted assets included in the aggregate number in Note 5L(1) above. Contracts that share similar characteristics, such as reinsurance and derivatives, are to be reported in the aggregate. (Note: This would be the detail for what was reported as "Other Restricted Assets" for 5L(1) above.)

(4) Collateral Received and Assets Held under Modco/Funds Withheld Reinsurance Agreements Reflected as Assets Within the Reporting Entity's Financial Statements

Disclose the following for the general account and separate account regarding collateral received and assets held under modco/funds withheld reinsurance agreements under SSAP No. 1, paragraph 23c:

- Nature of ~~any~~ assets ~~received as collateral~~ reflected ~~as assets~~ within the reporting entity's financial statements

- Book/adjusted carrying value (BACV) of the ~~collateral~~assets

- Fair value of the ~~collateral~~assets

- The recognized liability to return ~~these~~ collateral assets or obligation under the Modco/Funds Withheld Reinsurance Agreements

- The percentage the ~~collateral~~ asset BACV amount (gross and admitted) is of the reporting entity's total assets amount reported on Line 26 of the asset page (gross and admitted, respectively).

Illustrations to the Financial Statements – 5L

This illustration includes the presentation of all restricted assets reported on the financial statements for a total comparison to total assets. This includes the items captured in SSAP No. 1, paragraph 23b and 23c. (Items captured in paragraph 23c should have a corresponding liability recognized, therefore there is no capture within the general interrogatories or capture as a noncontrolled asset in the RBC formula.)

	Current Year						
	8	9	Percentage				
Restricted Asset Category	Total Nonadmitted Restricted	Total Admitted Restricted (5 minus 8)	10 Gross (Admitted & Nonadmitted) Restricted to Total Assets (c)	11 Admitted Restricted to Total Admitted Assets (d)	12 Amount Reported in General Interrogatories	13 Difference from Note and GI	14 GI Ref
a. Subject to contractual obligation for which liability is not shown	$	$	..................%	..................%			
b. Collateral held under security lending agreements	....	....	....	....			25.04+25.05
c. Subject to repurchase agreements	....	....	....	....			26.21
d. Subject to reverse repurchase agreements	....	....	....	....			26.22
e. Subject to dollar repurchase agreements	....	....	....	....			26.23
f. Subject to dollar reverse repurchase agreements	....	....	....	....			26.24
g. Placed under option contracts	....	....	....	....			26.25
h. Letter stock or securities restricted as to sale – excluding FHLB capital stock	....	....	....	....			26.26
i. FHLB capital stock	....	....	....	....			26.27
j. On deposit with states	....	....	....	....			26.28
k. On deposit with other regulatory bodies	....	....	....	....			26.29
l. Pledged as collateral to FHLB (including assets backing funding agreements)	....	....	....	....			26.31
m. Pledged as collateral not captured in other categories	....	....	....	....			26.30
n. Other restricted assets	....	....	....	....			26.32
o. Collateral Assets Received and on Balance Sheet *(SSAP 1. Paragraph 23.c)*					XXX	XXX	N/A
p. Assets held under Modco Reinsurance Agreements *(SSAP 1. Paragraph 23.c)*					XXX	XXX	N/A
q. Assets held under Funds Withheld Reinsurance Agreements. *(SSAP 1. Paragraph 23.c)*					XXX	XXX	N/A
~~o~~r. Total Restricted Assets (Sum of a through n)	$	$	..................%	..................%	XXX	XXX	

(c) Column 5 divided by Asset Page, Column 1, Line 28
(d) Column 9 divided by Asset Page, Column 3, Line 28

Reporting entities shall explain the differences between amounts reported in Note 5L(1) and the general interrogatories. This shall include all instances in which an amount is reported in column 13 above.

GI Reference	Difference between Note and GI (Per Column 12 above)	Explanation
25.04+25.05		
26.21		
26.22		

26.23		
26.24		
26.25		
26.26		
26.27		
26.28		
26.29		
26.31		
26.30		
26.32		

(2) Detail of Assets Pledged as Collateral Not Captured in Other Categories (Contracts that Share Similar Characteristics, Such as Reinsurance (excluding modco/FWH) and Derivatives, Are Reported in the Aggregate)

	Gross (Admitted & Nonadmitted) Restricted							8	Percentage	
	Current Year					6	7		9	10
	1	2	3	4	5					
Description of Assets	Total General Account (G/A)	G/A Supporting S/A Activity (a)	Total Separate Account (S/A) Restricted Assets	S/A Assets Supporting G/A Activity (b)	Total (1 plus 3)	Total From Prior Year	Increase/ (Decrease) (5 minus 6)	Total Current Year Admitted Restricted	Gross (Admitted & Nonadmitted) Restricted to Total Assets	Admitted Restricted to Total Admitted Assets
....	$	$	$	$	$	$	$	$	.... %	...........%
....	....	....	....	....	....	....	....	....	....	....
....	....	....	....	....	....	....	....	....	....	....
Total (c)	$	$	$	$	$	$	$	$	.... %	...........%
Amount of Total pledged under derivative contracts										
Total Excluding Derivative Collateral										

(a) Subset of column 1
(b) Subset of column 3
(c) Total Line for Columns 1 through 7 should equal 5L(1)m Columns 1 through 7 respectively and Total Line for Columns 8 through 10 should equal 5L(1)m Columns 9 through 11 respectively

Staff Note – The amount pledged under derivative contracts should agree to Schedule DB and agree to what is subtracted from the life RBC formula.

(3) Detail of Other Restricted Assets (Contracts that Share Similar Characteristics, Such as Reinsurance (exclude modco/FWH) and Derivatives, Are Reported in the Aggregate)

	Gross (Admitted & Nonadmitted) Restricted							8	Percentage	
	Current Year					6	7		9	10
	1	2	3	4	5					
Description of Assets	Total General Account (G/A)	G/A Supporting S/A Activity (a)	Total Separate Account (S/A) Restricted Assets	S/A Assets Supporting G/A Activity (b)	Total (1 plus 3)	Total From Prior Year	Increase/ (Decrease) (5 minus 6)	Total Current Year Admitted Restricted	Gross (Admitted & Nonadmitted) Restricted to Total Assets	Admitted Restricted to Total Admitted Assets
....	$	$	$	$	$	$	$	$	.... %	...........%
....	....	....	....	....	....	....	....	....	....	....
....	....	....	....	....	....	....	....	....	....	....
Total (c)	$	$	$	$	$	$	$	$	.... %	...........%

(a) Subset of column 1
(b) Subset of column 3
(c) Total Line for Columns 1 through 7 should equal 5L(1)n Columns 1 through 7 respectively and Total Line for Columns 8 through 10 should equal 5L(1)n Columns 9 through 11 respectively

Staff Question – Are there other broad categories that should be captured in aggregate subtotals?

(4) Collateral Received and Assets Held under Modco/Funds Withheld (FWH) Reinsurance Agreements Reflected as Assets Within the Reporting Entity's Financial Statements

~~Collateral~~ Assets	1 Book/Adjusted Carrying Value (BACV)			2 Fair Value			3 % of BACV to Total Assets (Admitted and Nonadmitted *	4 % of BACV to Total Admitted Assets **
	Collateral	Modco	FWH	Collateral	Modco	FWH		
General Account:								
a. Cash, Cash Equivalents and Short-Term Investments	$			$			%	%
b. Schedule D, Part 1				....			%	%
c. Schedule D, Part 2, Section 1				....			%	%
d. Schedule D, Part 2, Section 2				....			%	%
e. Schedule B				....			%	%
f. Schedule A				....			%	%
g. Schedule BA, Part 1				....			%	%
h. Schedule DL, Part 1	....			....			%	%
i. Other							%	%
j. Total ~~Collatera~~l Assets (a+b+c+d+e+f+g+h+i)	Collateral	Modco	FWH	Collateral	Modco	FWH	%	%
Separate Account:								
k. Cash, Cash Equivalents and Short-Term Investments	$			$			%	%
l. Schedule D, Part 1	....			....			%	%
m. Schedule D, Part 2, Section 1	....			....			%	%
n. Schedule D, Part 2, Section 2	....			....			%	%
o. Schedule B	....			....			%	%
p. Schedule A	....			....			%	%
q. Schedule BA, Part 1	....			....			%	%
r. Schedule DL, Part 1	....			....			%	%
s. Other							%	%
t. Total ~~Collateral~~ Assets	Collateral	Modco	FWH	Collateral	Modco	FWH	%	%

(k+l+m+n+o+p+q+r +s)								

* j = Column 1 divided by Asset Page, Line 26 (Column 1)
t = Column 1 divided by Asset Page, Line 27 (Column 1)

** j = Column 1 divided by Asset Page, Line 26 (Column 3)
t = Column 1 divided by Asset Page, Line 27 (Column 3)

	1 Amount	2 % of Liability to Total Liabilities *
u. Recognized Obligation to Return Collateral Asset (General Account)	$	%
v. Recognized Obligation to Return Collateral Asset (Separate Account)	$	%

* u = Column 1 divided by Liability Page, Line 26 (Column 1)
v = Column 1 divided by Liability Page, Line 27 (Column 1)

u. Recognized Obligation for Modco assets (General Account)	$	%
v. Recognized Obligation for Modco assets (Separate Account)	$	%

* u = Column 1 divided by Liability Page, Line 26 (Column 1)
v = Column 1 divided by Liability Page, Line 27 (Column 1)

u. Recognized Obligation for FWH (excluding Modco) assets (General Account)	$	%
v. Recognized Obligation for FWH (excluding Modco) assets (Separate Account)	$	%

* u = Column 1 divided by Liability Page, Line 26 (Column 1)
v = Column 1 divided by Liability Page, Line 27 (Column 1)

(4) Disclose whether any of the assets held as collateral or under modified coinsurance (Modco) or funds withheld reinsurance (FWH) agreements have been pledged for another purpose specific to the insurance reporting entity. For example, if the insurance reporting entity has used these assets as the collateral in a securities lending agreement, a repo transaction, pledged as collateral to the FHLB, etc. (For Modco/FWH assets, items pledged on behalf of the reinsurer shall not be captured.)

	Collateral Held	**Modco**	**FWH**
a. Securities Lending	....		
b. Repo / repurchase Agreements	....		
c. Placed under option contracts	....		
d. On deposit with states	....		
e. On deposit with other regulatory bodies	....		
f. Pledged as collateral to FHLB (including assets backing funding agreements)	....		

g. Pledged as collateral not captured in other categories	....		
Total			

Proposed Language for a Referral to the Life RBC (E) Working Group:

MODCO OR FUNDS WITHHELD REINSURANCE AGREEMENTS
LR045, LR046, LR047 and LR048

References to MODCO and funds withheld reinsurance agreements apply to all treaties in effect.

Basis of Factors
When the default risk in modified coinsurance (MODCO) and other reinsurance transactions with funds withheld is transferred, this transfer should be recognized by reducing the RBC for the ceding company and increasing it for the assuming company. **In the event that the entire asset credit or variability in statement value risk associated with the assets supporting the business reinsured is not transferred to the assuming company for the entire duration of the reinsurance treaty, the RBC for the ceding company should not be reduced. For clarity, if the Modco / Funds Withheld reinsurance agreement asset held as of the year-end date has been used as a pledged asset for any purpose specific to the ceding insurance reporting entity at any time during the year, the RBC for the ceding company shall not be reduced. For example, if the Modco / Funds Withheld reinsurance agreement asset held as of the year-end date was the collateral in a securities lending, repurchase or FHLB transaction by the ceding entity at any time over the year, then the reporting entity cannot assert that they have transferred the asset risk or variability and RBC shall not be reduced.**

Staff Review Completed by: Julie Gann, NAIC Staff—October 2024

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/Maintenance/Active Form A's/2024/24-XX - Restricted Asset Clarification.docx

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

Issue: Investment Subsidiary Classification

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item has been prepared as questions have been received on the classification of investments as "investment subsidiaries" in schedule D-6-1: Valuation of Shares of Subsidiary, Controlled or Affiliated Companies and in the Life RBC formula on pages LR042, LR043 and LR044.

For background, the concept of an investment subsidiary was reflected in *SSAP No. 46—Investments in Subsidiary, Controlled and Affiliated Entities* as "investments in noninsurance subsidiary, controlled or affiliated (SCA) entities that have no significant ongoing operations other than to hold assets that are primarily for the direct or indirect benefit or use of the reporting entity or its affiliates." For these SCAs, the guidance in SSAP No. 46 required an equity measurement method adjusted to the statutory basis of accounting. With this adjustment to the statutory basis of accounting, the measurement of the SCA under SSAP No. 46 was intended to be consistent to the accumulated measurement of the underlying assets if they had been held directly. SSAP No. 46 was superseded by SSAP No. 88 as of Jan. 1, 2005, and the concept of an "investment subsidiary" (or a subsidiary designed to hold assets for the entity) was eliminated from statutory accounting guidance. SSAP No. 88 was then superseded by SSAP No. 97 as of Dec. 31, 2007, and is the current authoritative guidance for SCAs. Similar to SSAP No. 88, the concept of an "investment subsidiary" (or an SCA designed just to hold assets for the benefit of the reporting entity and its affiliates) is not in SSAP No. 97.

Under current guidance in SSAP No. 97, the concept of an SCA that simply holds assets is not reflected. Unless the SCA is an insurance subsidiary or engages in specific transactions on behalf of the entity, the SCA will be captured under paragraph 8.b.iii in SSAP No. 97 and reported based on the audited US GAAP equity value. Admittance is permitted if the parameters of the SSAP are met, which includes an audited financial statement supporting the US GAAP equity value. It is noted that the concept of an investment sub is still reflected in *SSAP No. 25—Affiliates and Other Related Parties*. The example of an entity only holding assets for the benefit of the insurer is an example of a non-economic transaction, where the assets are transferred/recognized at fair value, but any gain from the transfer is deferred until permanence can be verified.

From questions received and a review of financial statement reporting, the following list identifies issues:

- Situations have been identified in which companies have reported Schedule BA items (in scope of SSAP No. 48) as "investment subs" for RBC look through although those investments should not be captured within the classification. The concept for an "investment subsidiary" is for items reported as SCAs in scope of SSAP No. 97 with common and/or preferred stock ownership.

- Questions have been raised on whether companies can utilize the concept of an "investment sub" to avoid statutory accounting provisions for underlying assets but receive favorable RBC impact as if the SSAP criteria had been met. (For example, whether a company utilize the bond RBC factors for a debt security held within an investment subsidiary without verifying that the debt security would qualify as a bond under SSAP No. 26 or use CRP ratings to determine RBC when the asset may have required an SVO-assigned designation if held directly.)

- Questions have been received on how companies comply with Life RBC LR044 instruction for Affiliate Type 4 "*The risk-based capital charge for the ownership of an investment subsidiary is based on the risk-based capital of the underlying assets, pro-rated for the degree of ownership. The basis for this calculation is the assumption that the charge should be the same as it would be if the life insurer held the assets directly.*" Specifically, the measurement method for the SCA pursuant to *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities* (audited U.S. GAAP equity) would not be consistent with the measurement of the assets if the assets were held directly (statutory basis). Questions arise whether the underlying assets within the investment subsidiary are converted to statutory basis of accounting prior to computation of RBC charge. In addition, there were questions as to how the RBC after covariance is calculated for investment subsidiaries.

- According to Annual Statement instructions, investment subsidiaries also need to apply a "look-through" approach in Asset Valuation Reserve (AVR) calculation. However, diversity in practice has been observed and for companies that utilize Lines 5 – 14 of the AVR Equity and Other Invested Asset Component table to calculate AVR, the computation is not transparent.

- Questions have been raised on the current annual statement instructions for D-6-1 regarding the "imputed value on a statutory basis" and the direction for nonadmittance of the excess or reclassification in the "all other affiliates" category. Schedule D-6-1 does not determine the amount reported on balance sheet, as that amount is pulled from *Schedule D-2-2, Common Stocks*. Further, the A/S instructions for D-6-1 would not override the SSAP guidance that prescribes the measurement and admittance requirement as that is governed by SSAP No. 97, which is higher in the statutory hierarchy. These A/S instructions regarding the "imputed statutory value" appear to come from historical RBC guidance, and it is assumed that the calculation of the "imputed statutory value" was intended to be a pre-requisite for classifying as an investment sub. However, as the A/S guidance does not override SSAP, and what is captured would seemingly create a disconnect from what is reported on balance sheet, it seems to be causing confusion on application, as companies are not consistently reporting "investment subsidiaries" throughout the schedule, AVR and the RBC formula.

- From a review of the financial statements, the amounts reported for "investment subsidiaries" vary between D-6-1, AVR and RBC. From the 2023 filing, the amount reported in the RBC formula (which allows company RBC calculation based on the underlying assets) is significantly greater than the amount reported on D-6-1 and what is reported through the equity component of AVR.

The RBC background was noted from the 1995 "Raising the Safety Net" publication for RBC for P/C Insurance Companies is included as follows:

> The general principle in determining the RBC of … investment affiliates is to do so as if the affiliate were fully consolidated with the insurer. The committee recognizes that there is not necessarily any legal obligation for a parent to assist a subsidiary nor maintain adequate capital in the subsidiary; vice versa, a parent which wishes to remove excess capital from a subsidiary might sometimes face barriers in doing so. Nonetheless, the committee believes that the consolidation approach is the best way to measure the RBC of the parent, particularly when both the parent and the affiliate are going concerns. One particular advantage of this approach is that where there is a choice of whether to have ownership of an asset or placement of particular insurance business in either the parent or the subsidiary, the RBC calculation for the parent remains the same whichever choice is made. The committee believes that this makes the RBC calculation less manipulable with respect to affiliate transactions.
>
>> D. Investment Affiliates - Investment affiliates are investment conduits whose function it is to hold and invest assets of the insurance company.* Note that money management subsidiaries are not investment affiliates for this purpose. The RBC for an investment conduit is determined on a

consolidated or "see through" basis by applying the appropriate asset factors to the assets owned by the affiliate.

* An affiliate qualifies as an investment conduit if the following criteria are met:

i. 95 percent or more of the affiliate's assets would qualify as admitted assets if directly owned by the insurer.
ii. 95 percent or more of the affiliate's liabilities are paid-in capital, retained earnings or debt.
iii. Combining the prorata ownership share of the asset so fall the investment conduit affiliates with the owning insurer's assets does not violate any state requirements concerning diversification of investments or limitations on investments in a single entity.
iv. The investment conduit's statement value does not exceed the imputed value of the investment conduit using statutory accounting methodology admit the excess or move the affiliate to the "All Other Affiliated Common Stock" category.

Although the RBC calculation is within the purview of the Capital Adequacy (E) Task Force and its related RBC Working Groups, with the questions received for "investment subsidiaries," as well as the current lack of detail on the underlying assets used to determine RBC, this agenda item proposes the following potential actions:

1) Revisions to SSAP No. 97 to incorporate statutory accounting guidance for SCAs that hold assets on behalf of the reporting entity and affiliate (investment subsidiaries). By incorporating in SSAP, consideration can be given as to prescribing the measurement method and potential nonadmittance thresholds if the assets within the investment subsidiary would be nonadmitted if held directly. (As detailed within, the existing reference to measurement and nonadmittance in the instructions for D-6-1 would not overrule the guidance in SSAP No. 97. If the revisions to SSAP No. 97 are not supported, then the Working Group could consider sponsoring a blanks proposal to clarify the instructions in D-6-1 to prescribe allocation of the underlying investments in a manner that coincides with the SCA measurement and admittance under SSAP No. 97. (For example, if the equity measurement reported on balance sheet per SSAP No. 97 is $100, but the imputed statutory value would be lower at $80 (or higher at $120), what should be reported on D-6-1 and how should that flow to RBC?)

2) Sponsor blanks proposals to capture new investment schedules, or perhaps expansions to existing investment schedules, to detail the underlying assets held within an investment subsidiary. As the RBC and AVR calculations require reporting entities to calculate RBC and AVR based on the underlying assets, this information should be readily available. If revisions are not incorporated into SSAP No. 97, these proposals can also clarify requirements for reporting as an investment subsidiary.

3) Referrals to the Capital Adequacy (E) Task Force and related RBC Working Groups to incorporate details that allow regulators to verify the RBC calculation for the underlying assets in investment subsidiaries. If blanks reporting revisions are incorporated that provide this detail, then the RBC formula can likely pull from those sources. If reporting revisions are not incorporated, then additional schedules or reporting lines would be necessary within the RBC formula.

Existing Authoritative Literature:

SSAP No. 46—Investments in Subsidiary, Controlled and Affiliated Entities –
Superseded by SSAP No. 88 as of Jan. 1, 2005.

7.b.ii Investments in noninsurance SCA entities that have no significant ongoing operations other than to hold assets that are primarily for the direct or indirect benefit or use of the reporting entity or its affiliates, shall be recorded based on the underlying equity of the respective entity's financial statements adjusted to a statutory basis of accounting and the resultant proportionate share of the subsidiary's adjusted surplus, adjusted for unamortized goodwill as provided for in SSAP No. 68. Examples include but are not limited to: (i) an insurer and a SCA entity that leases autos, furniture, office equipment, or computer equipment to the insurer; (ii) an insurer and a SCA entity that owns real estate property that is leased to the insurer for office space; and (iii) an insurer and an SCA entity that holds investments that an insurer could acquire directly (i.e., "look through" investment subsidiary);

SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities –
The current guidance requirement prescribes measurement based on the market value approach (8a) or an equity method (8b). The following guidance is divided as follows: 8bi: insurance subsidiaries, 8.b.ii: non-insurance subsidiaries that meet the activity and revenue test, 8bii: non-insurance subsidiaries not captured in 8a or 8bii, and 8biv: foreign insurance subsidiaries. There is no current guidance for an "investment subsidiary" and those SCAs would be captured under 8.b.iii and measured at the audited US GAAP equity.

8. The admitted investments in SCA entities shall be valued using either the market valuation approach (as described in paragraph 8.a.), or one of the equity methods (as described in paragraph 8.b.) adjusted as appropriate in accordance with the guidance in *SSAP No. 25—Affiliates and Other Related Parties*, paragraph 18.d.

a. In order to use the market valuation approach for SCA entities, the following requirements apply:

i. The subsidiary must be traded on one of the following major exchanges: (1) the New York Stock Exchange, (2) the NASDAQ, or (3) the Japan Exchange Group;

ii. The reporting entity must submit subsidiary information to the NAIC SCA analysts for calculation of the subsidiary's market value. Such calculation could result in further discounts in market value above the established base discounts based on ownership percentages detailed below;

iii. Ownership percentages for determining the discount rate shall be measured at the holding company level;

iv. If an investment in a SCA results in an ownership percentage between 10% and 50%, a base discount percentage between 0% and 20% on a sliding scale basis is required;

v. If an investment in a SCA results in an ownership percentage greater than 50% up to and including 80%, a base discount percentage between 20% and 30% on a sliding scale basis is required;

vi. If an investment in a SCA results in an ownership percentage greater than 80% up to and including 85%, a minimum base discount percentage of 30% is required.

vii. Further, the SCA must have at least two million shares outstanding, with a total market value of at least $50 million in the public's control; and

viii. Any ownership percentages exceeding 85% will result in the SCA being recorded on an equity method.

b. If a SCA investment does not meet the requirements for the market valuation approach in paragraph 8.a. or, if the requirements are met, but a reporting entity elects not to use that approach, the reporting entity's proportionate share of its investments in SCAs shall be recorded as follows:

i. Investments in U.S. insurance SCA entities shall be recorded based on either 1) the underlying audited statutory equity of the respective entity's financial statements, adjusted for any unamortized goodwill as provided for in SSAP No. 68—Business Combinations and Goodwill1 or 2) the underlying audited statutory equity of the respective entity's financial statements, adjusted for any unamortized goodwill, modified to remove the impact of any permitted or prescribed accounting practices that depart from the NAIC Accounting Practices and Procedures Manual. Reporting entities shall record investments in U.S. insurance SCA entities on at least a quarterly basis, and shall base the investment value on the most recent quarterly information available from the SCA. Entities may recognize their investment in U.S. insurance SCA entities based on the unaudited statutory equity in the SCAs year-end annual statement if the annual SCA audited financial statements are not complete as of the filing deadline. The recorded statutory equity shall be adjusted for audit adjustments, if any, as soon as the annual audited financial statements have been completed. Annual consolidated or combined audits are allowed if completed in accordance with the Model Regulation Requiring Annual Audited Financial Reports as adopted by the SCA's domiciliary state;

ii. Investments in both U.S. and foreign noninsurance SCA entities that are engaged in the following transactions or activities:

(a) Collection of balances as described in *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers*

(b) Sale/lease or rental of EDP Equipment and Software as described in *SSAP No. 16—Electronic Data Processing Equipment and Software*

(c) Sale/lease or rental of furniture, fixtures, equipment or leasehold improvements as described in *SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements*

(d) Loans to employees, agents, brokers, representatives of the reporting entity or SCA as described in *SSAP No. 20—Nonadmitted Assets*

(e) Sale/lease or rental of automobiles, airplanes and other vehicles as described in *SSAP No. 20—Nonadmitted Assets*

(f) Providing insurance services on behalf of the reporting entity including but not limited to accounting, actuarial, auditing, data processing, underwriting, collection of premiums, payment of claims and benefits, policyowner services

(g) Acting as an insurance or administrative agent or an agent for a government instrumentality performing an insurance function (e.g. processing of state workers compensations plans, managing assigned risk plans, Medicaid processing etc).

(h) Purchase or securitization of acquisition costs

[1] If the insurance SCA employs accounting practices that depart from the NAIC accounting practices and procedures, and the reporting insurance entity has not adjusted the valuation of the insurance SCA to be consistent with the NAIC accounting practices and procedures, (i.e., retains the effect of the permitted or prescribed practice in its valuation), disclosure about those accounting practices that affect the insurance SCA's net income and surplus shall be made pursuant to paragraph 37. If the reporting entity has adjusted the investment in the insurance SCA with the resulting valuation being consistent with the accounting principles of the AP&P Manual, the disclosures in paragraph 37 are not required.

and if 20% or more of the SCA's revenue is generated from the reporting entity and its affiliates, then the underlying equity of the respective entity's audited U.S. Generally Accepted Accounting Principles (GAAP) financial statements shall be adjusted to a limited statutory basis of accounting in accordance with paragraph 9. For purposes of this section, revenue means GAAP revenue reported in the audited U.S. GAAP financial statements excluding realized and unrealized capital gains/losses. Foreign SCA entities are defined as those entities incorporated or otherwise legally formed under the laws of a foreign country. Paragraphs 22-27 provide guidance for investments in holding companies;

iii. Investments in both U.S. and foreign noninsurance SCA entities that do not qualify under paragraph 8.b.ii., shall be recorded based on the audited U.S. GAAP equity of the investee. Foreign SCA entities are defined as those entities incorporated or otherwise legally formed under the laws of a foreign country. Additional guidance on investments in downstream holding companies is included in paragraphs 22-27. Additional guidance on the use of audited foreign GAAP basis financial statements for the U.S. GAAP equity valuation amount is included in paragraph 23.b.

iv. Investments in foreign insurance SCA entities shall be recorded based on the underlying U.S. GAAP equity from the audited U.S. GAAP basis financial statements, adjusted to a limited statutory basis of accounting in accordance with paragraph 9, if available. If the audited U.S. GAAP basis financial statements are not available, the investment can be recorded on the audited foreign statutory basis financial statements of the respective entity adjusted to a limited statutory basis of accounting in accordance with paragraph 9 and adjusted for reserves of the foreign insurance SCA with respect to the business it assumes directly and indirectly from a U.S. insurer using the statutory accounting principles promulgated by the NAIC in the *Accounting Practices and Procedures Manual*. The audited foreign statutory basis financial statements must include an audited footnote that reconciles net income and equity on the foreign statutory basis of accounting to the U.S. GAAP basis. Foreign insurance SCA entities are defined as alien insurers formed according to the legal requirements of a foreign country.

<u>2024 Annual Statement Instructions – Schedule D-6-1</u>

If a reporting entity has any common stock or preferred stock reported for any of the following required categories or subcategories, it shall report the subtotal amount of the corresponding category or subcategory, with the specified subtotal line number appearing in the same manner and location as the pre-printed total or grand total line and number:

Category	Line Number
Preferred Stocks:	
Parent	0199999
U.S. Property & Casualty Insurer	0299999
U.S. Life Insurer	0399999
U.S. Health Entity #	0499999
Alien Insurer	0599999
Non-Insurer Which Controls Insurer	0699999
***Investment Subsidiary**	**0799999**
Other Affiliates	0899999
Subtotals – Preferred Stocks	0999999
Common Stocks:	
Parent	1099999
U.S. Property & Casualty Insurer	1199999
U.S. Life Insurer	1299999
U.S. Health Entity #	1399999
Alien Insurer	1499999

Non-Insurer Which Controls Insurer 1599999
***Investment Subsidiary 1699999**
Other Affiliates 1799999
Subtotals – Common Stocks 1899999
Totals – Preferred and Common Stocks 1999999

*NOTE: Investment Subsidiary shall mean any subsidiary, other than a holding company, engaged or organized primarily in the ownership and management of investments for the reporting entity. An investment subsidiary shall not include any broker dealer or a money management fund managing funds other than those of the parent company. The following criteria are applicable:

1. 95% or more of the investment subsidiary's assets would qualify as admitted assets;
2. The investment subsidiary's total liabilities are 5% or less of total assets;
3. Combining the pro-rata ownership shares of the assets of all the investment subsidiaries with the owning reporting entity's assets does not violate any state requirements concerning diversification of investments or limitations on investments in a single entity; and
4. **The investment subsidiary's book/adjusted carrying value does not exceed the imputed value on a statutory accounting basis. If the book/adjusted carrying value does exceed the imputed statutory value, the reporting entity may either nonadmit the excess or categorize such subsidiary in the "All Other Affiliates" category.**

<u>2023 RBC Forecasting and Instructions:</u>

AFFILIATED/SUBSIDIARY STOCKS – LR042, LR043, and LR044

(Only key excerpts included – bolded for emphasis.)

Affiliated/Subsidiary investments fall into two broad categories: (A) Insurance Affiliates/Subsidiaries that are Subject to risk-based capital; and (B) Affiliates/Subsidiaries that are Not Subject to risk-based capital. The risk-based capital for these two broad groups differs. **Investment subsidiaries are a subset of category A in that they are subject to a risk-based capital charge that includes the life RBC risk factors applied only to the investments held by the investment subsidiary for its parent insurer.** Publicly traded insurance affiliates/subsidiaries held at market value have characteristics of both broader categories. As a result, there is a two-part RBC calculation. The general treatment for each is explained below.

4. Investment Subsidiaries

An investment subsidiary is a subsidiary that exists only to invest the funds of the parent company. The term "investment subsidiary" is defined in the NAIC's Annual Statement Instructions as any subsidiary, other than a holding company, engaged or organized primarily to engage in the ownership and management of investments for the insurer. An investment subsidiary shall not include any broker-dealer or a money management fund managing funds other than those of the parent company. **The risk-based capital charge for the ownership of an investment subsidiary is based on the risk-based capital of the underlying assets, pro-rated for the degree of ownership. The basis for this calculation is the assumption that the charge should be the same as it would be if the life insurer held the assets directly.** Report information regarding any investment subsidiaries. Subsidiaries reported in this section will be assigned an affiliate code of "4" for investment subsidiaries. The amount of reported common stock should be the same as Schedule D, Part 6, Section 1, Line 1699999. Preferred stock information should be the same as Schedule D, Part 6, Section 1, Line 0799999.

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 recommend that the Working Group move this item to the active listing and expose this agenda item with a request for comments on the options offered to clarify statutory accounting guidelines (and resulting reporting impacts) for investment subsidiaries. As noted, with the exception of possible revisions to SSAP No. 97, the other possible actions are to sponsor blanks proposals or send referrals to the Capital Adequacy (E) Task Force and related RBC groups with a request for revisions. (Determination on whether this is a SAP classification or a new SAP concept will be based on the action directed.)

Potential Actions:

1) **Revisions to SSAP No. 97 to incorporate statutory accounting guidance for SCAs that hold assets on behalf of the reporting entity and affiliate (investment subsidiaries).** By incorporating in SSAP, consideration can be given as to prescribing the measurement method and potential nonadmittance thresholds if the assets within the investment subsidiary would be nonadmitted if held directly. (As detailed within, the existing reference to measurement and nonadmittance in the instructions for D-6-1 would not overrule the guidance in SSAP No. 97. If the revisions to SSAP No. 97 are not supported, then the Working Group could consider sponsoring a blanks proposal to clarify the instructions in D-6-1 to prescribe allocation of the underlying investments in a manner that coincides with the SCA measurement and admittance under SSAP No. 97.)

2) **Sponsor blanks proposals to capture new investment schedules, or perhaps expansions to existing investment schedules, to detail the underlying assets held within an investment subsidiary.** As the RBC and AVR calculations require reporting entities to calculate RBC and AVR based on the underlying assets, this information should be readily available. If revisions are not incorporated into SSAP No. 97, these proposals can also clarify requirements for reporting as an investment subsidiary.

3) **Referrals to the Capital Adequacy (E) Task Force and related RBC Working Groups to incorporate details that allow regulators to verify the RBC calculation for the underlying assets in investment subsidiaries.** If blanks reporting revisions are incorporated that provide this detail, then the RBC formula can likely pull from those sources. If reporting revisions are not incorporated, then additional schedules or reporting lines would be necessary within the RBC formula.

Staff Review Completed by: Julie Gann, NAIC Staff—November 2024

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Meeting/B - 24-21 - Investment Sub.docx

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

Issue: ASU 2024-01, Scope Application of Profits Interest and Similar Awards

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: In March 2024, FASB issued *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards,* which includes amendments to Topics 718 to provide clarifications on the application of guidance on stock compensation in the form of profits interest. The primary changes made were the creation of application examples and amendments to certain language in the Scope and Scope Exceptions Section of Topic 718 to improve clarity and operability without changing the guidance.

Because profits interest holders only participate in future profits and/or equity appreciation and have no rights to the existing net assets of the partnership, it can be complex to determine whether a profits interest award should be accounted for as a share-based payment arrangement (Topic 718) or similar to a cash bonus or profit-sharing arrangement (Topic 710, Compensation—General, or other Topics).

For statutory accounting assessments, prior U.S. GAAP guidance related to share-based payments has been predominantly adopted with modification in *SSAP No. 104—Share-Based Payments*. Statutory accounting modifications to the U.S. GAAP guidance have mostly pertained to statutory terms and concepts. (For example, statutory reporting lines, nonadmittance of prepaid assets, etc.)

Existing Authoritative Literature:
Stock compensation is addressed by *SSAP No. 104—Share-Based Payments* and *SSAP No. 95—Nonmonetary Transactions*.

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 2018-35 adopted with modification *ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting* and incorporated the U.S. GAAP amendments from that ASU into SAP.

Agenda items 2016-19 and 2017-37 address the main ASUs related to *ASC Topic 606 Contracts with Customers* and there have been several other agenda items for minor updates to revenue recognition guidance, which have been rejected *in SSAP No. 47—Uninsured Plans*.

Agenda item 2023-07 addressed *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*, which was adopted with modification in 2023 to SSAP Nos. 47, 95, and 104.

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 to adopt with modification *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards* within *SSAP No. 104—Share-Based Payments*. The proposed revisions to SSAP No. 104 are illustrated below.

Proposed Revisions* to *SSAP No. 104—Share-Based Payments

Scope and Scope Exceptions

4. This statement applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in the grantor's own operations or provides consideration payable to a customer by either of the following:

a. I~~i~~ssuing (or offering to issue) its shares, share options, or other equity instruments to an employee or nonemployee.~~or by~~

~~a.~~b. I~~i~~ncurring liabilities to an employee or nonemployee that meet either of the following conditions:

i. The amounts are based, at least in part[1], on the price of the entity's shares or other equity instruments.

ii. The awards require or may require settlement by issuing the entity's equity shares or other equity instruments.

5. Share-based payments awarded to a grantee by a related party or other holder of an economic interest in the entity as compensation for goods or services provided to the reporting entity are share-based payment transactions to be accounted for under this statement unless the transfer is clearly for a purpose other than compensation for goods or services to the reporting entity. The substance of such a transaction is that the economic interest holder makes a capital contribution to the reporting entity, and that entity makes a share-based payment to the grantee in exchange for services rendered or goods received. An example of a situation in which such a transfer is not compensation is a transfer to settle an obligation of the economic interest holder to the grantee that is unrelated to goods or services to be used or consumed in a grantor's own operations. Reporting entities which issue profits interest or similar awards as compensation to either employees and nonemployees in exchange for goods or services shall apply the guidance in paragraph 4 in determining whether the award is a share-based payment transaction and in scope of this statement.

NAIC Drafting Note: Some of the relevant guidance added by ASU 2024-01 is included in illustrative examples. As SSAP No. 104 does not have illustrative examples, NAIC Staff drafted language (see tracked changes immediately above) using the guidance provided in the ASU illustrative examples and commentary.

Relevant Literature

127. This statement adopts with modification the U.S. GAAP guidance for share-based payment transactions reflected in FASB *Accounting Standards Codification (ASC) Topic 718, Compensation – Stock Compensation*, as modified by the ASUs listed in paragraphs 127.a. through 127.e., excluding the guidance in *ASC Subtopic 718-40, Employee Stock Ownership Plans* (ESOPs). Statutory accounting guidance for ESOPs is addressed in *SSAP No.*

[1] The phrase "at least in part" is used as an award of share-based compensation may be indexed to both the price of an entity's shares and something else that is neither the price of the entity's shares nor a market, performance, or service condition.

12—Employee Stock Ownership Plans. This adoption with modification includes the related implementation guidance reflected within the FASB Codification Topic 718 not reflected within this standard. The U.S. GAAP guidance adopted with modification reflects the adoption with modification of the following ASUs:

a. *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards*. The statutory modification did not incorporate the application examples and added additional language to clarify that profits interest and similar awards needed to be considered under this SSAP.

~~a.~~b. *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer.*

~~b.~~c. *ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting*. The revisions from ASU 2018-07 expand the scope of ASC 718 to include share-based payment transactions for acquiring goods and services from nonemployees. With ASU 2018-17, *ASC 505-50, Equity – Equity Payments to Nonemployees* was superseded.

~~c.~~d. *ASU 2017-09, Scope of Modification Accounting*

~~d.~~e. *ASU 2016-09, Improvements to Employee Share-Based Payment Accounting*

~~e.~~f. *ASU 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*

~~f.~~g. *ASU 2010-13, Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Current of the Market in Which the Underlying Equity Security Trades*

Effective Date and Transition

132. Since the initial adoption of SSAP No. 104, subsequent revisions were effective as follows:

a. *ASU 2024-01 Compensation—Stock Compensation (Topic 718), Scope Application of Profits Interest and Similar Awards* was adopted with modifications. This SAP clarification is effective December 31, 2025.

~~a.~~b. *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*. The SAP clarification is effective August 10, 2022.

Staff Review Completed by:
NAIC Staff – William Oden, September 2024

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Meeting/C - 24-22 - ASU 2024-01 - Scope Application of Profits Interest and Similar Awards.docx

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

Issue: Derivative Premium Clarifications

Check (applicable entity):

	P/C	Life	Health
Modification of existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: This agenda item was developed in response to two issues. First, NAIC staff noted during internal reviews of *SSAP No. 86—Derivatives* and the Annual Statement Instructions that the terminology used for derivative financing premium was inconsistent and that the guidance for derivative financing premiums could be clarified. Second, as part of the ongoing Interest Maintenance Reserve (IMR) Ad Hoc Group meetings NAIC staff learned that there is some confusion within industry regarding whether statutory accounting guidance allows derivative premium costs to be captured in the calculation of realized losses for the derivative transaction. NAIC staff noted that within SSAP No. 86 there are several sections which provide derivative specific accounting guidance, and within these sections the guidance is clear that companies are to amortize derivative premiums over the life of the derivative contract. With amortization of the derivative premium, the derivative premium costs would not be a component in determining realized losses at expiration. As noted within the Definitions section of SSAP No. 86, derivative premiums represent the cost to acquire or write a derivative contract and is not an "underlying" in a derivative contract. As SSAP No. 86 only allows for the change in value attributable to the derivative underlying to be capitalized to IMR as a realized loss and as derivative premium costs are NOT a component of the derivative underlying, the guidance is clear that derivative premium costs should not be included in losses capitalized into IMR. To ensure this is abundantly clear, revisions have been recommended to both the "Definitions" and "Derivative Premium" sections to add language which specifically states that derivative premium costs cannot be capitalized into IMR.

Existing Authoritative Literature:

Statement of Statutory Accounting Principles No. 86—Derivatives

6. "Derivative Premium" is the cost to acquire or write a derivative contract. Derivative premium is not an "underlying" in a derivative contract and is not impacted by changes in an underlying interest of the derivative agreement. A derivative with contract terms that finance the derivative premium, so that the cost is paid or received throughout the derivative term or at derivative maturity, does not result with an "embedded derivative" addressed in paragraph 17.

Derivative Premium

19. Derivative premium is the amount paid (acquired derivative) or received (written derivative) to enter into a derivative contract. At inception, the premium generally represents the fair value of the derivative. Derivative premium that is not paid or received at inception represents a liability or receivable for the reporting entity. Derivatives with premiums not remitted at acquisition are considered "financed derivatives." Financed derivatives shall be reported in accordance with the following provisions:

a. At acquisition and subsequently, the gross reported fair value of the derivative shall exclude the impact of financing premiums. Only market changes in the actual fair value of the derivative shall be reflected as unrealized gains or losses.

b. At acquisition and subsequently, premiums payable (acquired derivative) and premiums receivable (written derivatives) shall be separately reported as "payable for securities" and "receivables for securities."

Disclosure Requirements

63. Reporting entities shall disclose the following for all derivative contracts used:

a. General disclosures:

v. Identification of whether the reporting entity has derivative contracts with financing premiums. (For purposes of this term, this includes scenarios in which the premium cost is paid at the end of the derivative contract or throughout the derivative contract.);

h. For derivative contracts with financing premiums:

i. Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums excluding the impact of the deferred or financing premiums.

ii. For each derivative contract with financing premiums:

(a) Whether premium cost is paid throughout the contract, or at derivative maturity;
(b) Next premium cost payment date;
(c) Total premium cost;
(d) Premium cost paid in prior years;
(e) Current year premium cost paid;
(f) Future unpaid premium cost;

EXHIBIT B – SPECIFIC HEDGE ACCOUNTING PROCEDURES FOR DERIVATIVES

2. Swaps, Collars, and Forwards (see also discussion in Introduction above):

c. Cash Flows and Income:

i. Where the cost of the derivative is not combined with the hedged item:

(a) Amortization of premium paid or received on derivatives is an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of the hedged item;

(b) Periodic cash flows and accruals of income/expense are to be reported in a manner consistent with the hedged item, usually as net investment income or another appropriate caption within operating income.

ii. Where the cost of the derivative is combined with the hedged item, the cash flows and income of the derivative on Schedule DB is zero. All related amortization and cash flow accounting shall be reported with the hedged item instead of with the derivative.

Annual Statement Instructions: Notes to the Financial Statements:

<u>NOTE 8.A.(8)</u> Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums, excluding the impact of the deferred or financing premiums.

Illustration:

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

A. Derivatives under *SSAP No. 86—Derivatives*

(8)

a.

	Fiscal Year	Derivative Premium Payments Due
1.	2025	$ ....
2.	2026	....
3.	2027	....
4.	2028	....
5.	Thereafter	
6.	Total Future Settled Premiums (Sum of 1 through 5)	$

b.

		Undiscounted Future Premium Commitments	Derivative Fair Value with Premium Commitments (Reported on DB)	Derivative Fair Value Excluding Impact of Future Settled Premiums
1.	Prior Year	$	$	$ ....
2.	Current Year	$	$	$ ....

Annual Statement Instructions: Schedule DB – Definitions

"Financing Premium" means that the premium cost to acquire or enter into the derivative is paid at the end of the derivative contract or throughout the derivative contract.

Annual Statement Instructions: Schedule DB – Part A – Section 1

Column 30 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted future settled premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of future financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 30 shall reflect the fair value of the derivative without an offset for the future financing premiums.)

Column 31 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted future settled premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing cost owed by the reporting entity, those "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

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 2012-17, which considered *ASU 2011-22, Disclosures about Offsetting Assets and Liabilities*, was finalized by the Working Group Nov. 29, 2012. This agenda item adopted revisions to SSAPs No. 64, 86 and 103. The adopted revisions, effective Jan. 1, 2013, 1) revise and clarify that offsetting is only allowed in accordance with SSAP No. 64, paragraphs 2-4; 2) modify the adoption of FIN 39 rejecting the ability to offset in accordance with master netting agreements and rejecting FSP FIN 39-1 and FIN 41; and 3) rejecting ASU 2011-11 for statutory accounting.

Overview of ASU 2011-11:

ASU 2011-11 was issued in December 2011 to require entities to disclose both gross information and net information about both instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting agreement. This ASU was issued as the differences in the offsetting requirements between U.S. GAAP and IFRS accounted for a significant difference in the amounts presented under those standards. These differences reduce the comparability of between U.S. GAAP and IFRS, and the users of financial statements requested that these differences be addressed expeditiously. **The objective of the ASU 2011-11 amendments is to facilitate comparison between entities that prepare financial statements under U.S. GAAP and those prepared under IFRS.** Reporting entities are required to apply the ASU 2011-11 amendments for annual reporting periods beginning on or after Jan. 1, 2013, and interim periods within those annual periods. Entities are required to provide the disclosures required by those amendments retrospectively for all comparative periods presented.

Agenda item 2013-07, which considered *ASU 2013-01: Clarifying the Scope of Disclosures About Offsetting Assets and Liabilities,* was finalized on August 24, 2013. This ASU was issued to clarify that the scope of ASU 2011-11 applies to derivatives (including embedded derivatives), repurchase and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either netted as they meet the right of setoff under ASC 210-20-45 or ASC 815-10-45, or are subject to a master netting agreement or similar agreement. The SAP adopted revisions allowed reporting entities to continue offsetting derivatives, repurchase and reverse repurchase agreements, and securities borrowing and securities lending transactions with a valid right of offset, but incorporated disclosures to illustrate the netting impact. This adoption action included a referral to the Blanks (E) Working Group for annual statement instruction revisions and to recommend development of additional schedules to reconcile the amount reported gross on DB to the amount reported net on the balance sheet.

Agenda item 2016-48 considered accounting and reporting revisions for derivatives with financing premiums. Although discussion occurred proposing a gross accounting and reporting approach, the revisions adopted on November 6, 2017 within that agenda item incorporated aggregate disclosures and new electronic columns in Schedule DB to capture the impact of financing premiums in derivative reporting.

Agenda 2019-38 considered the accounting and reporting of financing derivative transactions pursuant to a review of information from the 2018 year-end statutory financial statements. The agenda item was adopted on July 30, 2020, and included revisions to SSAP No. 86 to ensure consistency in the gross reporting of derivatives without inclusion of financing components and in reporting amounts owed to/from the reporting entity from the acquisition or writing of derivatives.

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 to SSAP *No. 86—Derivatives* and the annual statement instructions to ensure consistent terminology for derivative financing premium and to clarify that derivative premium costs are not to be capitalized to IMR. The proposed revisions to SSAP No. 86 and the annual statement are illustrated below.

Proposed Edits to SSAP No. 86:

6. “Derivative Premium” is the cost to acquire or write a derivative contract. Derivative premium is not an “underlying” in a derivative contract and is not impacted by changes in an underlying interest of the derivative agreement. A derivative with contract terms that finance the derivative premium (financing premium), so that the ~~cost is~~premiums are paid or received throughout the derivative term or at derivative maturity, does not result with an “embedded derivative” which is addressed in paragraph 17. For the purposes of this statement, unpaid or deferred premiums are considered synonymous with financing premium. Derivative premium costs are not to be included in realized losses capitalized to the Interest Maintenance Reserve (IMR) as derivative premium is not considered an underlying in the derivative contract.

Derivative Premium

19. Derivative premium is the amount paid (acquired derivative) or received (written derivative) to enter into a derivative contract. At inception, the premium generally represents the fair value of the derivative but does not represent an underlying in the derivative contract. Accordingly, derivative premium costs are not to be included in realized losses capitalized to IMR. Derivative premiums are to be amortized over the life of the derivative contract, with the amortization recorded as an adjustment to net investment income or another appropriate caption within operating income consistent with the reporting of the derivative contract. Derivative premium that is not paid or received at inception of the derivative contract represents financing premium and shall be recorded as a liability or receivable for the reporting entity. Derivatives with premiums not remitted at acquisition are considered “financed derivatives.” Financed derivatives shall be reported in accordance with the following provisions:

a. At acquisition and subsequently, the gross reported fair value of the derivative shall exclude the impact of financing premiums. Only market changes in the actual fair value of the derivative shall be reflected as unrealized gains or losses. Even if the derivative premium is fully financed, a derivative contract asset/liability must be recorded and the derivative premium amortized over the life of the derivative contract.

b. At acquisition and subsequently, financing premiums payable (acquired derivative) and financing premiums receivable (written derivatives) shall be separately reported as “payable for securities” and “receivables for securities.”

24. For those derivatives which qualify for hedge accounting, the change in the carrying value or cash flow of the derivative shall be recorded consistently with how the changes in the carrying value or cash flow of the hedged asset, liability, firm commitment or forecasted transaction are recorded. Upon termination of a derivative that qualified for hedge accounting, the gain or loss shall adjust the basis of the hedged item and be recognized in income in a manner that is consistent with the hedged item (alternatively, if the item being hedged is subject to ~~Interest Maintenance Reserve (~~IMR~~)~~, the gain or loss on the hedging derivative may be realized and shall be subject to IMR upon termination.) Entities who choose the alternative method shall apply it consistently thereafter.

63.a.v. Identification of whether the reporting entity has derivative contracts with financing premiums. (For purposes of this term, this includes scenarios in which the premium cost is paid/received at the end of the derivative contract or throughout the derivative contract.);

63.h.i. Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums excluding the impact of ~~the deferred or~~ financing premiums.

63.h.ii. For each derivative contract with financing premiums:

(a) Whether premium cost is paid/received throughout the contract, or at derivative maturity;
(b) Next premium cost payment date;
(c) Total premium cost;
(d) Premium cost paid/received in prior years;
(e) Current year premium cost paid/received;
(f) Future unpaid/unreceived premium cost;

Footnote [3] Pursuant to paragraph 19, the gross reported value of a derivative and the determination of unrealized gains or losses shall exclude the impact of financing premiums. Financing ~~P~~premiums payable or receivable from the acquisition or writing of a derivative shall not be reflected in the gross reporting of derivatives or in determining the fair value change in a derivative.

Proposed Edits to Annual Statement Instructions:

NOTE 8.A.(8) Disclose the aggregate, non-discounted total premium cost for these contracts and the premium cost due in each of the following four years, and thereafter. Also disclose the aggregate fair value of derivative instruments with financing premiums, excluding the impact of ~~the deferred or~~ financing premiums.

Illustration:

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

A. Derivatives under *SSAP No. 86—Derivatives*

(8)

a.

	Fiscal Year	Derivative Premium Payments Due
1.	2025	$ ....
2.	2026	....
3.	2027	....
4.	2028	....
5.	Thereafter	
6.	Total ~~Future Settled~~Financing Premiums (Sum of 1 through 5)	$

b.

		Undiscounted Future Premium Commitments	Derivative Fair Value with Premium Commitments (Reported on DB)	Derivative Fair Value Excluding Impact of ~~Future Settled~~ Financing Premiums
1.	Prior Year	$	$	$ ....
2.	Current Year	$	$	$ ....

SCHEDULE DB – PART A – SECTION 1

Column 30 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~ financing premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 30 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 31 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~ financing premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premiums owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

SCHEDULE DB – PART A – SECTION 2

Column 29 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~financing premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 29 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 30 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~financing premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premiums owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

SCHEDULE DB – PART B – SECTION 1

Column 28 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~financing premiums. For example, if the fair value of the derivative reported in Column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in Column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in Column 28 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 29 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~financing premiums. For example, if the valuation increase/valuation decrease reported in Column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premiums owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

SCHEDULE DB – PART B – SECTION 2

Column 24 – Fair Value of Derivative, Excluding Impact of Financing Premiums

Reflect the fair value of the derivative adjusted to exclude the impact of discounted ~~future settled~~financing premiums. For example, if the fair value of the derivative reported in column 16 has been reduced due to expected cash outflows representing the reporting entity's future payment of financing premiums, the consideration of those future premium cash outflows shall be removed from the reported fair value of the derivative captured in this column.

(At acquisition, a derivative may be reported with a net zero fair value in column 16 as the value of the derivative and the net present value of ~~future~~ financing premiums owed from the acquisition of the derivative may offset. The fair value reported in column 30 shall reflect the fair value of the derivative without an offset for the ~~future~~ financing premiums.)

Column 25 – Unrealized Valuation Increase/(Decrease), Excluding Impact of Financing Premiums

Reflect the unrealized gain or unrealized loss reported for the derivative adjusted to exclude the impact from discounted ~~future settled~~ financing premiums. For example, if the valuation increase/valuation decrease reported in column 17 includes "losses" to recognize the net present value of the financing ~~cost~~ premium owed by the reporting entity, those future "losses" shall be removed from the unrealized valuation increase/decrease reflected in this column.

Staff Review Completed by:
NAIC Staff – William Oden, October 2024

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Meeting/D - 24-23 - Derivative Premium Clarification.docx

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

Issue: Medicare Part D – Prescription Payment Program

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 develop statutory accounting guidance in response to changes to the Medicare Part D (Part D) prescription drug program which goes into effect in 2025. At a high level, the Medicare Prescription Payment Program (MP3) requires insurers to pay pharmacies at the point of sale the out-of-pocket costs of enrollees who have opted into MP3. The enrollees then have the remaining policy term to make installment payments to the insurer. (The policy term typically goes from January through December, so a cost incurred in March, would be repaid through installments ending in December.)

Interpretation (INT) 05-05: Accounting for Revenues Under Medicare Part D Coverage provides high-level accounting guidance on the current Part D program. INT 05-05 includes some basic guidance, but primarily provides guidance by referring to existing statements for specific aspects of the program.

A unique aspect of the updated program is having the insurer pay the pharmacy at the point of sale and seek reimbursement from enrollees. Most of the existing statutory accounting guidance on amounts recoverable from enrollees contemplates premium receivables or amounts due from a governmental payor.

Statutory accounting questions include 1) where to report the initial point of sale payment to the pharmacy and the related installment receivables, 2) how to account for the prescription drug point of sale payments, and 3) when to write-off and or nonadmit overdue amounts.

Starting with plan year 2025, any Part D enrollee may opt into the program. Enrollees can also opt out of the program and will have differing options to repay their outstanding balance.

The program does not change the Part D enrollee's total out of pocket costs. If a participant fails to pay the amount, they are billed by the Part D sponsor and their participation in the program may be terminated following a required two-month grace period. The Medicare Part D plan sponsor is not permitted to terminate the individual's enrollment in the Part D plan due to failure to pay MP3 bills. Part D plan sponsors must also have a reinstatement process in place to allow individuals to resume participation in the MP3 in the same plan year.

Part D sponsors are required to treat any unsettled balances owed by enrollees under the MP3 as plan losses; Centers for Medicare & Medicaid Services (CMS) considers these unsettled balances as part of the plan's administrative costs. Costs of implementing the MP3 program and program collections are included in the administrative expenses of the Part D plan and are not included in the claim expenses or claim adjustment expenses.
CMS requires several reporting requirements and ongoing monitoring.

CMS has specific guidance on the treatment of unsettled balances in the medical loss ratio (MLR). MLR is the share of revenue used for incurred claims and quality improvement activities, rather than the share of revenue used for administrative costs and profit. Therefore, **excluding unsettled balances from the numerator of the MLR calculation is consistent** with the statutory direction to treat unsettled balances as plan losses and CMS' approach to other administrative expenses incurred by Part D sponsors.

The CMS guidance notes that unsettled balances **are included in the denominator of the MLR calculation**. The Act requires Part D sponsors to treat any unsettled balances owed by participants under the MP3 as plan losses and allows Part D sponsors to include unsettled balances assumed as losses in their premium bids. Consequently, Part D sponsors will receive revenue covering these assumed losses through their direct subsidy and premium payments, which should be included in the denominator of the MLR.

Health insurance industry trades, America's Health Insurance Plans (AHIP) and Blue Cross Blue Shield Association (BCBSA) have also coordinated with NAIC staff and submitted information on the programs.

Existing Authoritative Literature:
INT 05-05: Accounting for Revenues Under Medicare Part D Coverage is an interpretation of the following statements. It provides guidance that primarily references existing guidance in the SSAPs interpreted.

- *SSAP No. 47—Uninsured Plans*
- *SSAP No. 54R—Individual and Group Accident and Health Contracts*
- *SSAP No. 66—Retrospectively Rated Contracts*
- *SSAP No. 84—Health Care and Government Insured Plan Receivables*

The CMS website has several guidance documents on the updates to the program.
https://www.cms.gov/inflation-reduction-act-and-medicare/part-d-improvements/medicare-prescription-payment-plan

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 Review Completed by: Robin Marcotte - NAIC Staff October 2024

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and take the actions listed below:

1. Expose the draft interpretation *INT 24-02: Medicare Part D Prescription Payment Program* and expose minor edits to *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage* as illustrated below. The edits to INT 05-05 adds reference the new INT 24-02 regarding Medicare Part D prescription payment plans.
2. Send notice of the exposure to the Health Insurance (B) Committee and Health Risk Based Capital (E) Working Group
3. Direct NAIC staff to coordinate with Blanks (E) Working Group to develop a annual statement blanks proposal in the interim and to develop disclosures for future inclusion in relevant SSAPs. Preliminary recommendations would include the list below, but more research on CMS reporting may also identify other relevant items:
   a. Amounts recoverable on Medicare Part D installments due from enrollees.
   b. Aging of Medicare Part D installments due from enrollees more than 90 days overdue in categories similar to what is used for premium receivables.
   c. Information nonadmitted Medicare Part D installments due from enrollees.
   d. Information on write-offs of Medicare Part D installments due from enrollees.

Exposed revisions to INT 05-05: Accounting for Revenues Under Medicare Part D Coverage:

INT 05-05 Dates Discussed
September 28, 2005; December 3, 2005; March 24, 2018; August 4, 2018; November 17, 2024

INT 05-05 References
Current:
SSAP No. 47—Uninsured Plans
SSAP No. 54—Individual and Group Accident and Health Contracts
SSAP No. 66—Retrospectively Rated Contracts
SSAP No. 84—Health Care and Government Insured Plan Receivables
INT 24-02: Medicare Prescription Payment Plan

4. The Emerging Accounting Issues (E) Working Group reached a consensus to adopt the following guidance as it applies to the various funds to be received under the Medicare Part D program. The funds should be accounted for in accordance with one of the three SSAP's outlined below:

a. Specific funds received as reimbursements (or advance payments) for uninsured claims under a partially uninsured plan should be accounted for under SSAP No. 47. These funds include "reinsurance payments," "Coverage Gap Discount Program" payments and "low-income subsidy (cost-sharing portion)." These funds are paid by the government for a portion of claims above the out-of-pocket threshold or relate to prescription drug plan (PDP) payments for all or a portion of the deductible, the coinsurance and the co-payment amounts for low-income beneficiaries. CMS provides advance funding to the Part D sponsors. The Part D sponsor uses those advances to provide point-of-sale drug discounts to participants. CMS invoices the prescription drug manufacturers. The payment reconciliation process ensures that the Part D sponsor is paid dollar for dollar for coverage gap discounts advanced at the point of sale, based on accepted prescription drug event (PDE) data, and that any unused excess advances from the government are repaid. The Coverage Discount Gap Program does not apply to low-income beneficiaries.

b. Specific funds received by the PDP sponsor from either the Medicare Part D enrollee or the government as payment for standard coverage that will be subject to retrospective premium adjustments should be accounted for under SSAP No. 66. These funds include "direct subsidy," "low-income subsidy (premium portion)," "beneficiary premium (standard coverage portion)," "Part D payment demonstration" and "risk corridor payment adjustment." The funds noted above have a final policy amount that is calculated based on the loss experience of the insured during the term of the policy, therefore should be treated as such.

c. Specific funds received as premiums for coverage that is not retrospectively rated should be accounted for under SSAP No. 54R. These funds include "beneficiary premium (supplemental benefit portion)" as these payments are considered to be standard premium payments that do not meet the definitions under SSAP No. 47 or SSAP No. 66 as defined in paragraph 4.a. and paragraph 4.b. of this interpretation.

~~c.~~d. The Medicare Part D Prescription Payment Plan shall follow the guidance in *INT 24-02: Medicare Prescription Payment Plan.*

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 24-02T: Medicare Part D Prescription Payment Plans

INT 24-02T Dates Discussed

November 17, 2024

INT 24-02T References

Current:
- *SSAP No. 47—Uninsured Plans*
- *SSAP No. 54—Individual and Group Accident and Health Contracts*
- *SSAP No. 66—Retrospectively Rated Contracts*
- *SSAP No. 84—Health Care and Government Insured Plan Receivables*
- *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*

INT 24-024T Issue

1. The Inflation Reduction Act of 2022 introduced changes to Medicare Part D, which is the prescription drug program (Part D), including a new program to help Part D enrollees manage their prescription drug payments. This program, known as the Medicare Prescription Payment Plan (MP3), will become effective on January 1, 2025. The purpose of this Interpretation is to provide statutory accounting and reporting guidance for aspects of the MP3 program. This Interpretation specifically addresses the MP3 components of Medicare Part D and does not intend to alter the guidance in *INT 05-05: Accounting for Revenues Under Medicare Part D Coverage*, which offers high-level accounting guidance on the current Medicare Part D program.

MP3 Program Overview

2. MP3 is a new program that requires all Medicare prescription drug plans (Part D plans) – including both standalone Medicare prescription drug plans and Medicare Advantage plans with prescription drug coverage – to offer their members the option to pay their out-of-pocket prescription drug costs through monthly payments over the remainder of the plan year, as opposed to paying the full amount upfront to the pharmacy.

3. Part D plan members who elect to participate in MP3 (MP3 enrollees) will pay $0 to the pharmacy for covered Part D drugs. The Part D plan sponsor is required to fully pay the pharmacy the total of an enrollee's applicable out-of-pocket amount and the Part D plan sponsor's portion of the payment in accordance with Part D prompt payment requirements. Subsequently, the Part D plan sponsor will bill the MP3 enrollee monthly for any cost-sharing incurred while enrolled in MP3.

4. MP3 enrollees will not save money on the total out-of-pocket costs of prescription drug purchases (there are other Part D programs in place to help qualifying Part D plan members with affordability issues). MP3 simply spreads payments over the remaining term of the plan year which may help many Part D plan members to better manage their monthly cash flow.

5. Unlike existing Part D programs which involve funds due from the federal government (for which payment is effectively assured), MP3 installment recoverables are due from individual enrollees.

Consequently, Part D plans may pay pharmacies for MP3 enrollees' out-of-pocket pharmacy claim costs, but some amounts billed to the enrollee might be uncollectible. Reasons for the amount being uncollectable could include leaving enrollment in the Part D plan or an inability or unwillingness to pay the full outstanding balance. This raises statutory accounting concerns regarding potential nonadmittance of overdue amounts and impairment of such recoverables.

6. To help cover potential uncollectible balances, CMS allows Part D plan sponsors to include an MP3 loss estimate in their premium bids. However, for the initial years, Part D plan sponsors have no prior experience in estimating the MP3 program's potential expenses.

7. The government is responsible for the estimated MP3 losses included in premium bids by Part D plan sponsors. Part D plan sponsors receive additional revenue, which helps to cover uncollectible balances resulting from MP3 enrollees. Part D plan sponsors face pricing/underwriting risk relating to the prescription needs of enrollees and may inaccurately estimate the amounts of uncollectible losses in the premium bids. In addition, there are risks that the costs of uncollectible amounts and other aspects of implementing the payment plan will vary from amounts that had been factored into premium rates. According to CMS guidance any losses in excess of the loss estimates included in the premium bids are the responsibility of the Part D plan sponsor.

MP3 Program Requirements for Unpaid Balances

8. The MP3 Program requires Part D plan sponsors to take on the risk of uncollectible balances. The program rules prohibit many of the common methods used to mitigate loss from uncollectible MP3 balances. MP3 is a mandated program benefit imposed by federal law and CMS rules, with different implications for statutory accounting purposes. Other key program requirements for MP3 balances include the following:

a. **Late fees, etc. –** Under MP3, late fees, interest payments, or other fees, such as for different payment mechanisms, are not allowed.

b. **Billing and Payment Procedures -** Part D plan sponsors can design their own billing and payment procedures for MP3. However, they must prioritize payments towards Part D plan premiums to avoid an enrollee losing their Part D coverage. This rule applies when it is unclear if an enrollee intended a submitted payment to cover their outstanding Part D plan premium or their MP3 balance.

c. **Pharmacies Not Responsible for Balances -** Participation in MP3 is considered an arrangement between the Part D plan sponsor and the MP3 enrollee. Pharmacies are not responsible for an enrollee's unsettled balances or for collecting unpaid balances from the MP3 enrollee on the Part D plan sponsor's behalf.

d. **Termination of Participation -** A Part D plan sponsor must terminate an enrollee's participation in MP3 if the enrollee fails to pay their monthly billed amount. An MP3 enrollee will be considered to have failed to pay their monthly billed amount only after the required grace period of at least two months. The Part D plan sponsor cannot terminate the enrollee's membership in the Part D plan for nonpayment of their MP3 billed amounts. Sponsors must continue billing amounts owed under the program in monthly amounts up to the maximum monthly cap based on the statutory formula for the remaining duration of the plan year after an enrollee has been terminated.

e. **Reinstatement of Enrollees -** Part D plan sponsors must reinstate terminated MP3 enrollees if the individual demonstrates good cause for failure to pay the program billed amount within the grace period and pays all overdue amounts billed.

f. **Preclusion from Subsequent Enrollment -** A Part D plan sponsor may prevent an individual from opting into the MP3 program in a subsequent year if the individual owes an overdue balance to that Part D plan sponsor or to another Part D plan sponsor with the same ultimate parent. In other words, an individual who owes an overdue balance under the program cannot be barred from MP3 in a subsequent year by a different Part D plan sponsor that does not have the same parent organization.

g. **Compliance with Federal and State Laws -** Part D plan sponsors (and any third parties that Part D plan sponsors contract) collecting unpaid balances related to the program must follow other applicable federal and state laws and requirements, including those related to payment plans, credit reporting, and debt collection.

Medical Loss Ratio

9. The current Public Health Act outlines how to calculate medical loss ratio (MLR) rebates, which are generally based on a comparison of incurred health claims and quality improvement activities to premium revenue, considering various factors and adjustments. *SSAP No. 66—Retrospectively Rated Contracts* provides disclosures related to the MLR.

10. According to the CMS guidance, the outstanding balances owed by MP3 enrollees are considered part of the Part D plan's administrative expenses. CMS guidance excludes unsettled balances from the numerator of the MLR calculation, aligning with CMS' treatment of other administrative expenses incurred by Part D sponsors. The CMS guidance states that unsettled balances are included in the MLR calculation denominator and allows Part D sponsors to account for these balances as losses in their premium bids. Including enrollee losses in the denominator aligns with reporting the revenue estimated to offset these losses in the MLR denominator.

Drafting Note: The MP3 program considers uncollectible MP3 recoverables as incurred plan administrative costs and does not include these amounts in the Medical Loss Ratio numerator, so reporting guidance for other adjustments to the Supplemental Health Care Exhibit will be needed. Such reporting revisions are not addressed in this Interpretation but would be anticipated to be in the annual statement reporting revisions submitted to the Blanks (E) Working Group.

INT 24-02T Discussion

Statutory Accounting and Reporting Considerations for MP3

11. The Working Group reached the following tentative consensus for MP3 statutory accounting and reporting guidance. In addition, Appendix 1 illustrates some basic journal entries which help to show the intended financial statement results.

MP3 Recoverables

12. MP3 recoverables from enrollees shall be accrued and reported on asset line 24 Health care and other amounts receivable when the related pharmacy out-of-pocket payment is incurred.

13. Current MP3 recoverables, meaning those that are less than and up to 90 days overdue, are admitted assets to the extent that they comply with the guidance in this Interpretation. Repayment by MP3 enrollees represents a probable future economic benefit to the Part D plan sponsor resulting from past transactions or events (i.e., paying the MP3 enrollee's out-of-pocket costs to the pharmacy). MP3 recoverables are also subject to impairment analysis.

14. Uncollected MP3 recoverables more than 90 days overdue are nonadmitted. The due date for aging of the MP3 recoverables shall follow the program billing guidelines.

15. If an MP3 recoverable is fully collected, it will equal the corresponding out-of-pocket payment for pharmaceutical claim payment. In those cases, there will not be an income statement impact regarding claims (or claims adjusting expenses) if the MP3 recoverable is fully collected.

Impairments

16. Uncollected MP3 recoverables from enrollees are subject to impairment analysis which shall be assessed using the evaluation guidelines in *SSAP No. 5—Liabilities, Contingencies, and Impairment of Assets.* However, when impairments for uncollectible MP3 recoverables are recorded, the expense for the impairment shall be reflected in as incurred Medicare Part D prescription drug claims in the statutory income statement.

Out-of-Pocket MP3 Pharmacy Payments

17. When the Part D plan pays out-of-pocket drug claims to the pharmacy a claims expense, a contra claims expense, and a contra claims expense account recoverable are recorded. The contra claims expense, or some similar mechanism, is recorded to prevent initial claims expense recognition in the income statement so that there is zero initial impact to the income statement. This is because there is an amount recoverable from the enrollee and to the extent that the enrollee pays in full there should not be any claims recognition. This is analogous to the handling of anticipated pharmaceutical rebates or anticipated subrogation recoveries.

18. If the enrollee pays the amount due in full there will be no income statement impact in claims expenses from the MP3 pharmacy payment and subsequent enrollee payments. In such cases the MP3 recoverable will be reduced as payments are collected and there would be no income statement impact.

19. If the enrollee recoverable is not repaid in whole or in part, there will be an income statement impact to reflect paid claims for the amount of the MP3 recoverable that are impaired and written off. Since there is an MP3 recoverable from the enrollee, there should be no income statement amount for an incurred claim until the related MP3 recoverable is written off for impairment.

20. When the MP3 recoverable is impaired, the contra claims expense is decreased by the amount of the MP3 recoverable that is written off. This results in the incurred Medicare prescription claim reported reflecting the uncollectible MP3 recoverable for statutory reporting. The premium to offset these claims is included in Medicare premium bids, so reporting the incurred uncollectible MP3 amounts as losses allows the statutory accounting loss ratio to reflect incurred Medicare Part D prescription costs which include MP3 uncollectible amounts.

21. Reporting uncollectible and impaired MP3 recoverables in statutory filings as claims incurred is different than the CMS treatment of which reports such amounts as administrative expense for MLR purposes.

Administrative Costs

22. Costs of implementing the MP3 program and program collections are included in the administrative expenses of the Part D plan and are not included in the claim expenses or claim adjustment expenses.

MLR Reporting Difference

23. Note that the reporting of the uncollectible (impaired) MP3 recoverable in Medicare prescription claims, is a difference from CMS treatment of such amounts in the MLR. The CMS treatment of uncollectible MP3 recoverables reports such amounts as administrative amounts. These administrative amounts are included in the denominator of the MLR by CMS.

INT 24-02T Status

24. This INT is tentatively planned to be effective March 30, 2025.

25. Further discussion is planned.

Appendix 1 - Illustrative Journal Entries

Medicare Prescription Payment Plan Scenarios			
	Claims	**Receivable**	**Cash**
Initial entries for all scenarios *Assumed to have been recorded by the insurance company prior to Scenarios 1 – 3.*			
DR Claims Expense *To represent claims expense incurred on behalf of the enrollee.*	$ 2,000		
CR Cash *To represent the $2,000 paid by the insurance company to the pharmacy on behalf of the enrollee.*			$ (2,000)
DR Healthcare Receivable *To represent the amount due to the insurance company from the enrollee, which the enrollee must pay over the policy term.*		$ 2,000	
CR Claims A/R (contra-claims expense) *To be reported within the claims expense line, essentially a contra-claims expense, and represents the amount due to the insurance company from the enrollee which the enrollee must pay over the policy term. This offsets the claims expense amount, so results in a current net $0 impact to the income statement, but both the DR and CR on the income statement are in claims expense.*	$ (2,000)		
Scenario 1 - The enrollee pays their full amount of $2,000 to the insurance company.			
DR Cash To *record receipt of the enrollee's payment in full.*			$ 2,000
CR Healthcare Receivable *The net income statement impact remains at $0, because the original claims expense was offset by the contra-claims expense (Claims A/R), and since the full $2,000 was received from the enrollee, there are no further income statement journal entry impacts.*		$ (2,000)	
Scenario 1 Net result on Financial Statements	**$ -**	**$ -**	**$ -**
Scenario 2 - The enrollee pays $1,500 out of the $2,000 to the insurance company and doesn't pay the remaining $500.			
DR Cash To *record receipt of enrollee partial payment of outstanding balance.*			$ 1,500
CR Healthcare receivable *To reduce enrollee receivable for amounts paid.*		$ (1,500)	

DR Claims A/R (contra-claims expense) *To represent the write-off of the receivable. This results in the insurance company having a total income statement impact debit to claims expense of $500, represented as the initial $2,000 claims expense for the out-of-pocket paid to the pharmacy by the insurance company, offset by the $1,500 received from the enrollee.*	$ (500)		
CR Healthcare receivable *To write-off the remaining uncollectible amount as impaired*		$ (500)	
Scenario 2 Net result on Financial Statements	**$ 500**	**$**	**$ (500)**
Scenario 3 - The enrollee does not pay any of the $2,000 owed to the insurance company.			
DR Claims A/R (contra-claims expense) *To represent the write-off of the amount anticipated to be paid by the enrollee. This results in the income statement impact to the insurance company being a debit of $2,000, for the amount paid to the pharmacy by the insurance company and not reimbursed by the enrollee.*	$ 2,000		
CR Healthcare receivable *To represent the write-off of the $2000 receivable.*		$ (2,000)	
Scenario 3 Net result on Financial Statements	**$ 2,000**	**$ -**	**$ (2,000)**

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

Issue: SSAP No. 16 Clarifications

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☒	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue: NAIC staff were contacted about a question related to *SSAP No. 16—Electronic Data Processing Equipment and Software*. While working on the issue, staff noted several instances in the SSAP where the FASB ASC Topic has been referenced directly instead of the ASU. When guidance is adopted by FASB, it is issued through an accounting standards update which formally adopts the guidance into the FASB Accounting Codification. The Working Group will then address the guidance in the ASU, which is the guidance at a moment in time instead of the actual ASC, which represents guidance that will change over time as other ASUs are adopted. As the guidance stands now, a new ASU could be issues that impacts the ASC sections that are referenced in the SSAP, thereby changing statutory accounting guidance without the Working Group addressing and considering the issue.

Existing Authoritative Literature: There are multiple instances that need to be addressed in SSAP No. 16, which are detailed below in the Staff Recommendation.

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, categorized as a SAP clarification, and expose revisions to *SSAP No. 16—Electronic Data Processing Equipment and Software*, to include proper references to the specific FASB ASU or SOP when not specifically referenced in the SSAP, as illustrated below.

8. This statement adopts with modification FASB Codification 985-20, Software - Costs of Software to be Sold, Leased or Marketed (ASC 985-20), as revised by *ASU 2009-14, Certain Revenue Arrangements That Include Software Elements*, to preclude the capitalization of software development costs and to reject guidance regarding the treatment of capitalized costs. Additionally, this statement rejects FASB Codification 985-330, Software - Inventory (ASC 985-330). Statutory modifications to ASC 985-20 and rejection of ASC 985-330 precludes capitalization of costs, and requires such costs to be expensed, for:

10. This statement adopts with modification *FASB Accounting Standards Codification (ASC) 350-40, Internal Use Software* (ASC 350-40), as originally adopted as part of SOP 98-1, as described in this statement. (This adoption reflects adjustments to ASC 350-40 from *ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*.) This statement also adopts *FASB Accounting Standards Codification 350-50, Website Development Costs* (ASC 350-50) in its entirety.

13. For hosting arrangements that are service contracts, reporting entities shall account for the contract as follows:

a. The reporting entity shall capitalize implementation costs of the hosting arrangement (the costs incurred to implement the cloud hosting service contract), as nonoperating system software. The capitalized costs shall be consistent with the costs which are permitted to be capitalized for internal use software and shall be reported as a nonadmitted asset. These implementation costs shall be recognized as each module or component of the hosting arrangement is ready for its intended use.

b. The implementation costs shall be amortized over the lesser of the term of the hosting arrangement, or five years. (This statement adopts the provisions in ASC 350-40-35-13 through ASC 350-40-35-17, as originally adopted with modification as part of SOP 98-1, for determining the term of the hosting arrangement and for when amortization shall begin.) The amortization cost shall be recognized as depreciation of the nonoperating system software. (This is a modification from U.S. GAAP as the amortization is not recognized in the same expense line as the service contract lease.)

Staff Review Completed by: Jake Stultz—NAIC Staff

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Meeting/G - 24-25 - SSAP 16 Cleanup.docx

NAIC Accounting Practices and Procedures Manual
Editorial and Maintenance Update
November 17, 2024

Maintenance updates provide revisions to the *Accounting Practices and Procedures Manual* (Manual) such as editorial corrections, reference changes and formatting.

SSAP/Appendix	Description/Revision
SSAP No. 26—Bonds	Editorial change to reinstate disclosure language and reporting category provision.

SSAP No. 26—Bonds:

Overview: The disclosure in paragraph 39e is an existing disclosure (pre-bond-definition revisions) in SSAP No. 26. However, the pre-bond-definition version of the disclosure included direction for disclosure by Schedule D broad reporting categories, with categories listed in the SSAP. These reporting categories were removed from the adopted revised SSAP No. 26 disclosure effective Jan. 1, 2025. Although this disclosure is satisfied by the completion of Schedule D-1-1 and D-1-2 for statutory accounting purposes, comments have been made that the adopted revised language could require a listing of all bonds in the audited financial statements. As such, editorial revisions have been proposed to reinstate the prior language for "receiving bond treatment" (as adopted, revised SSAP No. 43, paragraph 44m points to this SSAP No. 26 disclosure for ABS items), and to include reference to reporting categories. A listing of the reporting categories is not deemed necessary within the SSAP.

Proposed Edits to SSAP No. 26 (effective Jan. 1, 2025):

39e. For each annual balance sheet presented, the book/adjusted carrying values, fair values, excess of book/carrying value over fair value or fair value over book/adjusted carrying values for each pertinent bond or assets ~~in scope of this statement~~receiving bond treatment, by category and subcategory as reported in Annual Statement Schedule D – Part 1, Section 1 (Issuer Credit Obligations) and Section 2 (Asset-Backed Securities).

Staff Recommendation:
NAIC staff recommend that the Statutory Accounting Principles (E) Working Group move this agenda item to the active listing, categorize as a SAP Clarification, and expose editorial revisions as illustrated within.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Meeting/H - 24-26EP Fall 2024.docx

Fall National Meeting - Review of GAAP Exposures for Statutory Accounting:

Pursuant to a 2014 direction from the SAPWG chair, there is a desire for the Statutory Accounting Principles (E) Working Group to be more proactive in considering FASB exposures that may be significant to statutory accounting and reporting. Historically, the SAPWG has commented on limited, key FASB exposures – mostly pertaining to insurance contracts and financial instruments. To ensure consideration of all FASB exposures, staff prepared this memorandum to highlight the current exposures, comment deadlines, and to provide a high-level summary of the exposed item's potential impact to statutory accounting. It is anticipated that this information would assist the Working Group in determining whether a comment letter should be submitted to the FASB on the issues. Regardless of the Working Group's election to submit comments to the FASB on proposed accounting standards, under the NAIC Policy Statement on Statutory Accounting Principles Maintenance Agenda Process, issued US GAAP guidance noted in the hierarchy within Section V of the Preamble to the *Accounting Practices and Procedures Manual* must be considered by the Statutory Accounting Principles (E) Working Group.

FASB Exposures: [Exposure Documents and Public Comment Documents (fasb.org)]

Exposed FASB Guidance	Comment Deadline & Initial Staff Comments
Proposed Accounting Standards Update—*Derivatives and Hedging (Topic 815): Hedge Accounting Improvements*	November 25, 2024

The FASB is issuing this proposed Update to clarify certain aspects of the guidance on hedge accounting and to address several incremental hedge accounting issues arising from the global reference rate reform initiative.

In 2017, the FASB issued Accounting Standards Update No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities, to better portray the economic results of an entity's risk management activities in its financial statements and to make certain targeted improvements to simplify the application of the hedge accounting guidance. After the issuance of Update 2017-12, stakeholders asked the Board to clarify certain aspects of the guidance in the amendments of that Update. In 2019, the Board issued a proposed Accounting Standards Update, Derivatives and Hedging (Topic 815): Codification Improvements to Hedge Accounting, to clarify certain areas of the guidance to better align with the objective articulated in Update 2017-12.

Stakeholders indicated that the amendments in the 2019 proposed Update would not sufficiently resolve certain issues and that additional clarity was needed. In addition, in response to the 2021 Invitation to Comment, Agenda Consultation, stakeholders expressed concerns that current guidance increases the prevalence of missed forecasted transactions for otherwise highly effective hedging relationships, thus resulting in less decision-useful information for investors. Stakeholders also identified several areas of hedge accounting guidance requiring further updates to address the effects of reference rate reform on hedge accounting.

Consistent with the original objective of Update 2017-12, the objective of this proposed Update is to more closely align hedge accounting with the economics of an entity's risk management activities. The amendments included in the five issues addressed in this proposed Update are intended to better reflect those strategies in financial reporting by enabling entities to achieve and maintain hedge accounting for a greater number of highly effective economic hedges. The proposed amendments would limit the occurrence of unintuitive de-designation events and missed forecasted transactions for those hedging relationships. The amendments in this proposed Update would apply to any entity that elects to apply hedge accounting in accordance with Topic 815.

Issue 1: Similar Risk Assessment for Cash Flow Hedges

The amendments in this proposed Update would expand the hedged risks permitted to be aggregated in a group of individual forecasted transactions in a cash flow hedge by changing the requirement to designate a group of individual forecasted transactions from having a shared risk exposure to having a similar risk exposure. Entities would be required to assess risk similarity both at hedge inception and on an ongoing basis. The proposed amendments also would clarify that a group of individual forecasted transactions would be considered to have a similar risk exposure if the derivative used as the hedging instrument is highly effective against each risk in the group. In addition, in some cases, entities would be permitted to perform an ongoing qualitative assessment of whether a group of individual forecasted transactions has a similar risk exposure on a hedge-by-hedge basis.

The amendments in this proposed Update would improve GAAP by expanding the hedged risks permitted to be aggregated in a group of individual forecasted transactions, thereby enabling entities to apply hedge accounting to broader portfolios of forecasted transactions. Entities would be able to apply hedge accounting in a more efficient, cost-effective manner while reducing the risk of missed forecasts for highly effective economic hedges. Furthermore, clarifying the application of the similar risk assessment would improve operability and help entities apply the guidance more consistently. Therefore, investors would have more relevant information about entities' risk management activities related to cash flow hedges of groups of forecasted transactions.

Issue 2: Hedging Forecasted Interest Payments on Choose-Your-Rate Debt Instruments

The amendments in this proposed Update would facilitate the application of the change in hedged risk guidance to cash flow hedges of forecasted interest payments on variable-rate debt instruments with contractual terms that permit the borrower to change the interest rate index and interest rate tenor (that is, reset frequency) upon which interest is accrued (commonly referred to as "choose-your-rate" debt instruments). The contractual terms of the debt agreement would determine the alternative interest rate indexes and interest rate tenors that an entity may select during the hedging relationship without needing to discontinue hedge accounting. In addition, the proposed amendments would permit entities to use simplified assumptions when assessing hedge effectiveness and the probability of forecasted transactions occurring. Entities would be prohibited from applying this simplified guidance by analogy to other circumstances.

The amendments in this proposed Update would improve GAAP by establishing an operable model to address a pervasive hedging strategy for which stakeholders highlighted that diversity in practice exists. Furthermore, the amendments would enable entities to reduce the risk of hedge de-designation events and missed forecasts, while broadening the application of hedge accounting. As a result, entities would be able to more consistently reflect risk management strategies in the financial information provided to investors.

Issue 3: Cash Flow Hedges of Nonfinancial Forecasted Transactions

The amendments in this proposed Update would expand hedge accounting for forecasted purchases and sales of nonfinancial assets. Entities would be permitted to designate variable price components of the forecasted purchase or sale of a nonfinancial asset that meet the clearly-and-closely-related criteria would permit hedge accounting for eligible components of forecasted spot-market transactions and subcomponents of explicitly referenced components in an agreement's pricing formula.

The amendments in this proposed Update would improve GAAP because the application of hedge accounting would not necessarily be limited by whether the nonfinancial purchase or sale transaction is executed in the spot or forward market. Furthermore, the proposed amendments also may enable entities to reduce the risk of missed forecasts for highly effective economic hedges, more closely aligning entities' risk management strategies with hedge accounting to better reflect those strategies in financial reporting. The amendments in this proposed Update also would clarify that entities may designate a variable price component in a contract that is accounted for as a derivative as the hedged risk if the associated forecasted purchase or sale of the nonfinancial asset qualifies to be a hedged forecasted transaction. That clarification would improve GAAP because it would resolve diversity in practice about whether hedge accounting may be applied in those situations and would allow hedge accounting to be applied to highly effective economic hedges.

Issue 4: Net Written Options as Hedging Instruments

The amendments in this proposed Update would permit compound derivatives composed of a written option and a non-option derivative (for example, an interest rate swap with a written cap or floor) to qualify for designation as a hedging instrument in a cash flow hedge by adjusting the eligibility criteria for when a net written option may be designated as a hedging instrument. The proposed amendments would permit an entity to assume that certain terms of the hedged forecasted transactions match those of the hedging instrument for purposes of applying the net written option test.

The amendments in this proposed Update would improve GAAP by making the net written option test more operable for hedging relationships involving a variable-rate loan with an interest rate floor hedged by an interest rate swap that contains a mirror-image interest rate floor. The proposed amendments would accomplish that by allowing simplifying assumptions to be made that would accommodate differences in the loan and swap markets that exist after the cessation of the London Interbank Offered Rate (LIBOR). Making those simplifying assumptions would allow entities to continue to apply hedge accounting for strategies involving compound derivatives composed of a written option and a non-option derivative after LIBOR cessation.

Issue 5: Foreign-Currency-Denominated Debt Instrument as Hedging Instrument and Hedged Item (Dual Hedge)

The amendments in this proposed Update would eliminate the recognition and presentation mismatch related to a dual hedge strategy (that is, a hedge for which a foreign-currency-denominated debt instrument is both designated as the hedging instrument in a net investment hedge and designated as the hedged item in a fair value hedge of interest rate risk). The proposed amendments would require that an entity exclude the debt instrument's fair value hedge basis adjustment from the net investment hedge effectiveness assessment. As a result, an entity would immediately recognize in earnings the gains and losses from the remeasurement of the debt instrument's fair value hedge basis adjustment at the spot exchange rate. Entities would be prohibited from applying this guidance by analogy to other circumstances.

The amendments in this proposed Update would improve GAAP by enabling entities that utilize dual hedging strategies to reflect the economic offset of changes attributable to both interest rate risk and foreign exchange risk. The effective date for the amendments in this proposed Update will be determined after the Board considers stakeholders' feedback on the proposed amendments. The amendments in this proposed Update would require that an entity apply the guidance on a prospective basis for existing hedging relationships as of the date of adoption. Early adoption would be permitted for all entities on any date on or after issuance of a final Update. Upon adoption of the amendments in this proposed Update, entities may either be required or permitted to modify critical terms of certain existing hedging relationships, without de-designating the hedge.

Staff Review and Commentary:

Comment deadline is November 25, 2024

NAIC staff recommend that ASU be reviewed under the SAP Maintenance Process as detailed in *Appendix F—Policy Statements.*

Exposed FASB Guidance	**Comment Deadline & Initial Staff Comments**
Proposed Accounting Standards Update—*Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Clarifications to Share-Based Consideration Payable to a Customer*	November 14, 2024

The Board is issuing this guidance to reduce diversity in practice and improve the decision usefulness and operability of the guidance for share-based consideration payable to a customer in conjunction with selling goods or services.

Some entities offer to provide consideration to a customer (or to other parties that purchase the entity's goods or services from the customer) to incentivize the customer (or its customers) to purchase goods and services. Although consideration payable to a customer often takes the form of cash or credit that can be applied against amounts owed to the entity, it also can take the form of equity instruments (or other types of share-based consideration) such as warrants. When share-based consideration is granted to a customer (a grantee), it often vests upon the grantee purchasing a specified volume or monetary amount of goods and services from the grantor.

The guidance in Topic 606, Revenue from Contracts with Customers, requires that an entity account for consideration payable to a customer as a reduction of the transaction price and, therefore, as a reduction of revenue unless the payment to the customer is in exchange for a distinct good or service.

The amendments in Accounting Standards Update No. 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer, require that a grantor apply the guidance in Topic 718, Compensation—Stock Compensation, to measure and classify share-based consideration payable to a customer (the "Topic 718 approach"). Those amendments also require that if share-based consideration payable to a customer contains vesting conditions, the grantor must determine whether the vesting conditions represent service conditions or performance conditions. That determination can affect when the grantor recognizes revenue because it is required to estimate the probable outcome of a performance condition (and, therefore, whether the share-based consideration is expected to vest or is expected to be forfeited). By contrast, for service conditions, instead of estimating forfeitures, a grantor can elect to account for forfeitures as they occur. When the grantor elects to account for forfeitures as they occur, revenue recognition may be delayed for awards that are not probable of vesting.

Stakeholders indicated that this delay in revenue recognition can diminish the decision usefulness of a grantor's revenue information. For example, revenue may be recognized upon the forfeiture of warrants that were not expected to vest. Therefore, revenue may be recognized several reporting periods after the grantor has satisfied the related performance obligation(s), even if in that time there has been no change in the likelihood that the award will vest. Stakeholders also noted that the current guidance for forfeitures can increase the differences in financial reporting outcomes between share-based consideration payable to a customer and other forms of consideration payable to a customer (including cash consideration).

Under current guidance, there is diversity in practice in determining whether certain conditions (for example, those based on customer purchases) are service conditions or performance conditions. Therefore, stakeholders asked that the Board clarify how to distinguish between service conditions and performance conditions. Stakeholders also asked the Board to more closely align how forfeitures of share-based consideration with service conditions and forfeitures of share-based consideration with performance conditions affect the measurement of the transaction price (which affects revenue recognition timing) to improve the operability of the guidance and the decision usefulness of the resulting financial reporting information.

The amendments in this proposed Update would affect all entities that issue share-based consideration to a customer that is within the scope of Topic 606.

Under current GAAP, the definitions of performance condition and service condition do not explicitly discuss purchases made by a customer or parties that purchase a grantor's goods or services from the grantor's customers. For share-based consideration payable to a customer (including share-based consideration payable to other parties that purchase the grantor's goods or services from the grantor's customers) with a service condition, current GAAP permits the grantor to elect to account for the effect of forfeitures as they occur, which may result in a delay in revenue recognition for awards that are not probable of vesting. In addition, current GAAP also does not explicitly state whether the guidance in Topic 606 on constraining estimates of variable consideration applies to share-based consideration payable to a customer that is measured and classified under the Topic 718 approach.

The amendments in this proposed Update would revise the Master Glossary definition of the term performance condition for share-based consideration payable to a customer. The revised definition would incorporate conditions (including vesting conditions) that are based on the volume, monetary amount, or timing of a customer's purchases of goods or services from the grantor. The revised definition also would incorporate performance targets based on the volume of purchases made by other parties that purchase the grantor's goods or services from the grantor's customers.

Although proportionally fewer customer awards would be expected to have service conditions, for those that do have service conditions, the amendments in this proposed Update would eliminate the policy election permitting a grantor to account for forfeitures as they occur. Therefore, when measuring share-based consideration payable to a customer that has a service condition, the grantor would be required to estimate the number of forfeitures expected to occur. Separate policy elections for forfeitures would remain available for share-based payment awards with service conditions granted to employees and non-employees in exchange for goods or services to be used or consumed in the grantor's own operations.

The amendments in this proposed Update would clarify that share-based consideration encompasses the same instruments as share-based payment arrangements but the grantee would not need to be a supplier of goods or services to the grantor.

Finally, the amendments in this proposed Update would clarify that, under the Topic 718 approach, a grantor should not apply the guidance in Topic 606 on constraining estimates of variable consideration to share-based consideration payable to a customer. Therefore, a grantor would be required to assess the probability that an award will vest using only the guidance in Topic 718.

Collectively, these changes would improve the decision usefulness of a grantor's financial statements, improve the operability of the guidance, and reduce diversity in practice for accounting for share-based consideration payable to a customer. Under the proposed amendments, revenue recognition would no longer be delayed when an entity grants awards that are not expected to vest. This is expected to result in estimates of the transaction price that better reflect the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer and, therefore, more decision-useful financial reporting.

The amendments in this proposed Update would permit a grantor to apply the new guidance on either a modified retrospective or a retrospective basis. When applying the amendments in this proposed Update on a modified retrospective basis, a grantor would be required to recognize a cumulative effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the period of adoption and would not recast any financial statement information before the period of adoption. A grantor would apply the proposed amendments as of the date of initial application to all share-based consideration payable to a customer. When applying the amendments in this proposed Update on a retrospective basis, a grantor would be required to recast comparative periods and recognize a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the earliest period presented.

The effective date and whether early application should be permitted will be determined after the Board considers stakeholders' feedback on this proposed Update.

Staff Review and Commentary:

Comment deadline is November 14, 2024

NAIC staff recommend that ASU be reviewed under the SAP Maintenance Process as detailed in *Appendix F—Policy Statements.*

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/11-17-24 Fall National Meeting/Meeting/H - Review of GAAP Exposures.docx

