**Attachment 11.a**

**Statement of Statutory Accounting Principles No. 109 Draft-6/5/25 Amortized Cost Method**

Asset Liability Management (ALM) Derivatives

# STATUS

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Affected by No other pronouncements

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Relevant Appendix A Guidance None

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# SCOPE OF STATEMENT

1. Current statutory accounting guidance for derivatives qualifying for hedging effectiveness is in *SSAP No. 86—Derivatives* and *SSAP No. 108-Derivatives Hedging Variable Annuity Guarantees*. This statement allows special accounting treatment for limited derivatives hedging asset/liability duration differences subject to fluctuations as a result of interest rate sensitivity [a.k.a. asset liability management (ALM) derivatives]. The provisions within this statement are separate and distinct from the guidance in SSAP No. 86 and SSAP No. 108, as the items subject to the scope of this guidance, and the provisions within, would not qualify for hedge effectiveness under SSAP No. 86 or SSAP No. 108. The provisions provided within this statement are only permitted if all of the components of the statement are met and shall not be inferred as an acceptable statutory accounting approach for derivative transactions that do not meet the stated qualifications or that are not specifically addressed within this guidance.

# SUMMARY CONCLUSION

1. This statement establishes statutory accounting principles to address derivative transactions hedging asset/liability duration differences subject to fluctuations as a result of interest rate sensitivity.

The statutory accounting guidance within this statement is considered a special accounting provision, only permitted if all the components in the standard are met and shall not be inferred as an acceptable statutory accounting approach for situations that do not meet the stated qualifications or that are not specifically addressed within this guidance.

## Terms/Concepts (for purposes of this statement)

1. The following terms reflect concepts specific to this statement. This listing only details the key concepts. Specific guidelines are reflected throughout the guidance.
   1. Derivative Instrument: An agreement, instrument or series or combination thereof: (1) To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or (2) That has a price, performance, value, or cash flow based primarily upon the actual or expected price, level, performance, value, or cash flow of one or more underlying interests. Note: derivatives with asymmetrical payoff profiles and/or derivative premiums at inception (e.g., options) are not eligible for the accounting provisions in this standard (i.e., swaps, forwards, and futures are typically eligible for the accounting treatment in this standard if they don’t contain the aforementioned).
   2. Dynamic Hedging Approach: A dynamic hedging strategy allows for the portfolio of derivatives comprising the hedging instrument to be rebalanced in accordance with changes to the hedged item in order to adhere to the specified, documented hedging strategy.
   3. Hedged Item: The hedged item is the duration difference between the designated asset portfolio and designated product liability portfolio that are both exposed to interest rate risk (with the ultimate hedged item being the interest rate sensitivity of the liability portfolio that the assets support). The hedged item may relate to the duration of an open or flexible portfolio (e.g., group of contracts with different characteristics and liability durations) that allows for addition of newly issued contracts, subtraction of surrenders and fluctuations in balances. The portfolio of product liabilities may consist of an entire book of business or declared components thereof[1.](#_bookmark5)
   4. Hedging Instrument: The hedging instrument shall reflect a specified derivative, or a portfolio of specified derivatives, that hedges the duration difference of the designated asset and liability portfolios. The hedging instrument may reflect a dynamic hedging strategy in which a portfolio of derivatives comprising the hedging instrument is rebalanced in accordance with changes to the hedged item.

## Special Accounting Provision

1. The special accounting provision within this statement permits reporting entities to utilize a form of “macro-hedging” in which a portfolio of derivatives hedges the duration difference between an asset portfolio and a portfolio of product liabilities (i.e., an ALM Hedge2), which could include the entire book of business or subsections thereof, pursuant to a Clearly Defined Hedging Strategy (throughout this issue paper also referred to as “CDHS” or “hedging strategy”). This is considered a macro-hedge, as the designated hedged item is attached to a portfolio of product liability contracts with different characteristics and liability durations. Under this special accounting provision, the portfolio of contracts giving rise to the hedged item is not required to be static but can be revised to remove assets/derivatives/policies and/or include new assets/derivatives/policies to allow for continuous risk management (hedging) of the product liabilities in accordance with the specific risks being hedged and the hedge objectives of the specified, documented hedging strategy. In designating the hedged item, reporting entities are permitted to exclude specific components of the asset, derivative, and/or liability portfolios, but such exclusions must be documented at the hedge inception.

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Product liability contracts (e.g., PRT’s) that have been signed/executed are eligible as the hedged item if highly probable of closing in the near term, include disincentives

for non-performance and have historically closed at a near 100% success rate. For example, on January 1, the company signs a PRT contract that it will assume a client’s portfolio assets and pension liabilities on March 31. The agreed upon portfolio assets have a different duration than the liabilities, so the company proceeds with hedging the difference on January 1. If the transaction meets the aforementioned probable criteria, the hedge can qualify for the treatment in this SSAP if it meets the other criteria in this SSAP, although the portfolio will not be assumed until March 31.

2 As detailed in paragraph 10, these hedges are required to be highly effective in achieving the elimination of the duration mismatch between the designated asset and liability portfolios during documented hedge period.

1. This special accounting provision permits reporting entities to utilize a specified derivative, or a portfolio of specified derivatives, as the hedging instrument within an ALM Hedge to hedge the interest rate sensitivity, or a specific percentage3 of the interest rate sensitivity, of the designated hedged item. Hedged items include various interest rate sensitive products where duration can be reliably measured using one of the metrics in paragraph 11. The hedging instrument may reflect a dynamic hedging strategy in which a portfolio of derivatives comprising the hedging instrument is rebalanced in accordance with changes to the hedged item in order to adhere to the specified, documented hedging strategy. Fair value fluctuations not attributed to the hedged risk, including fair value changes from excluded open components, shall be recognized as unrealized gains or losses.
2. With the provisions in this standard to allow for flexibility in the hedged item coupled with a dynamic hedging approach (rebalancing of derivative hedging instruments), there is a greater risk of misrepresentation of successful risk management and achievement of a highly effective hedging relationship. Although this risk cannot be eliminated, the following provisions intend to ensure governance of the program and provide sufficient tools to allow for regulator review:
   1. Prior to implementing a hedging program for application within scope of this standard, the reporting entity must obtain explicit approval from the domiciliary state commissioner allowing use of this special accounting provision. The domiciliary state commissioner may subsequently disallow use of this special accounting provision at their discretion. Although this guidance does not restrict the state domiciliary commissioner on when to prohibit future use, disallowance should be considered upon finding that the reporting entity’s documentation, controls, measurement, prior execution of strategy or historical results are not adequate to support future use.
   2. Certification by a financial officer of the company (CFO, treasurer, CIO, or designated person with authority over the actual trading of assets and derivatives) that the hedging strategy meets the definition of a Clearly Defined Hedging Strategy and that the Clearly Defined Hedging Strategy is the hedging strategy being used by the company in its actual day-to-day risk mitigation efforts. This provision does not require reporting entities to use the special accounting provision within this standard.

3 In identifying the hedged risk, reporting entities must identify whether they are hedging the full, or a portion of (e.g., 40%), the interest rate sensitivity.

1. Eligibility for the special accounting provision within this standard is strictly limited to highly effective ALM derivatives that follow a Clearly Defined Hedging Strategy, meeting all the required provisions of this SSAP allowing the reporting entity to reduce the duration differences between the designated asset and liability portfolios. In order to qualify as a Clearly Defined Hedging Strategy (which may be dynamic, static, or a combination thereof), the strategy shall at a minimum, identify:
   1. The specific risks being hedged (including a measure of hedge coverage, e.g., percentage of interest rate sensitivity being hedged),
   2. The hedging objectives,
   3. The material risks that are not hedged,
   4. The financial instruments used to hedge the risks,
   5. The hedging strategy’s trading rules, including permitted tolerances from hedging objectives,
   6. The metrics, criteria, and frequency for measuring effectiveness,
   7. The conditions under which hedging will not take place, and for how long the lack of hedging can persist,
   8. The group or area, including whether internal or external, responsible for implementing the hedging strategy,
   9. Areas where basis, gap, or assumption risk related to the hedging strategy have been identified, and
   10. The circumstances under which hedging strategy will not be effective in hedging the risks.
2. While an initially documented hedging strategy may subsequently change, any change in hedging strategy, which includes a change in hedge target, shall be documented, with notification to the domiciliary state commissioner and include an effective date of the change in strategy. Reporting entities that elect to change a documented hedging strategy prior to the end of the three-month minimum timeframe shall identify the hedging strategy, and all hedging instruments executed under the strategy, as ineffective. The three-month timeframe begins with the stated effective date of the hedging strategy. Changes in a documented hedging strategy that occur after a three-month timeframe do not necessitate an ineffective determination as long as hedged items and hedging instruments under the revised/new strategy continue to meet the requirements of a highly effective ALM hedge. Reporting entities are permitted to have more than one hedging strategy implemented, but all implemented strategies must qualify as a component of a Clearly Defined Hedging Strategy pursuant to paragraph 7.

## Assessing Hedge Effectiveness

1. The provisions within this standard require the entity to use a specific method, as detailed in paragraph 10, to assess hedge effectiveness at least quarterly (e.g., at the beginning and end of each quarter) with on-going assessment consistent with the originally documented risk management strategy.
2. Both at inception, and on an ongoing basis, the hedging relationship must be highly effective in reducing duration differences between designated asset and liability portfolios during the period that the hedge is designated. Reporting entities electing to use this special accounting provision must calculate the duration of the hedged item (liability portfolio) and compare it to the duration of the designated supporting asset portfolio with and without the designated hedging derivatives at inception and on an ongoing basis (i.e., at the beginning and end of each quarter, since asset/derivative/liability amounts may change during the normal course of business with the dynamic hedge strategy needing to remain highly effective). Only if the designated hedging derivatives are highly effective at reducing the duration difference between the asset and liability portfolios at the beginning and end of each quarter, then this special accounting provision can be utilized. This comparison is specific to the designated hedged risks and exposures; therefore, if only a portion of the duration/interest rate risk is hedged or if the designated hedge only includes specific components of the hedged liabilities, for determining hedge effectiveness, the effectiveness comparisons are limited to those designated items. If an entity’s defined risk management strategy for a particular hedging relationship excludes specific components of the hedging derivative from the assessment of hedge effectiveness, the excluded open components shall be reported at fair value with gains or losses recognized as unrealized gains or losses.
3. The term “highly effective” describes a reduction of the duration difference between the asset and liability portfolios that is accomplished by the hedging derivatives with between an 80%-125% effective rate. For example:
   1. Modified Duration is the effect that a 100-basis-point (1%) change in interest rates will have on the price of an instrument (e.g., if an instrument has a modified duration of 5, a 1% change in interest rates would be expected to cause a 5% change in the instrument's price in the opposite direction); so if an asset portfolio has a Modified Duration of 9 and a liability portfolio has a Modified Duration of 10, a highly effective derivative portfolio hedging this difference would place the Modified Duration of the assets with derivatives at between 9.8 and 10.25 (80%-125% of the modified duration difference). Alternatively, if asset portfolio duration is 9 and a liability duration is 11, an entity can elect to hedge only half the difference (in which case, a duration of the assets with derivatives of between 9.8 and 10.25 would be highly effective).
   2. Macaulay Duration is the weighted average time until cash flows are received and is measured in years; so if an asset portfolio has a Macaulay Duration of 9 years and a liability portfolio has a Macauley Duration of 10 years, a highly effective derivative portfolio hedging this difference would place the Macauley Duration of the assets with derivatives at between 9.8 years and 10.25 years (80%-125% of the Macauley Duration difference).
   3. DV01 measures the dollar change in an instrument's price for a one basis point (0.01%) change in rates; so if an asset portfolio has a DV01 of $9M and a liability portfolio has a DV01 of $10M, a highly effective derivative portfolio hedging this difference would place the DV01 of the assets with derivatives at between $9.8M and $10.25M (80%-125% of the DV01 difference).

## Measurement/Recognition of Gains and Losses of Derivative Instruments

1. All designated highly effective hedging instruments (all derivatives, including those reflected in portfolios) shall be reported in the financial statements at amortized cost.
2. Amortized cost treatment will discontinue in the following scenarios:
   1. Maturities/Terminations - Derivatives that mature or are terminated with a fair value will be recognized as deferred assets (admitted) and deferred liabilities (i.e., derivative maturity/termination fair value would initially be surplus neutral with the deferred asset/liability offset by cash received/paid at maturity/termination).
   2. De-Designation – For derivatives de-designated from a previous highly effective hedging relationship due to ineffectiveness or by election, the derivative fair value will be recognized as an asset/liability offset by a deferred asset (admitted) and deferred liability (i.e., fair value recognition is initially surplus neutral). All prospective (post de- designation) derivative fair value changes are recognized as unrealized gains/losses without deferral unless included as part of a subsequent highly effective hedge (see 13.c below). Note – a deferred asset/liability can only be recognized for the fair value change up to the last measurement date indicating high effectiveness as defined by this SSAP.
   3. Note - An amount equal to the net deferred asset and deferred liability (net amount from all hedging strategies/programs captured within this guidance) shall be allocated from unassigned funds to special surplus. Also, as detailed previously, portions of hedging instruments that are not attributable to the hedged risk, shall be recognized as unrealized gains or unrealized losses. The ability to recognize a deferred asset/liability is limited to only the portion of the hedging instruments that are attributed to the hedged risk. Lastly, as these are essentially quarterly hedges inside a clearly pre-defined program (with effectiveness tests at the beginning and end of each quarter), programs that fail effectiveness could only apply the provisions of this SSAP within the subsequent quarters that effectiveness is achieved (if program parameters did not change materially). If program parameters change materially, then this represents a new program requiring new documentation, approvals, etc.
3. Deferred assets and deferred liabilities recognized under paragraph 13 shall be amortized using a straight-line method into NGO over a finite amortization period. The amortization timeframe shall equal the weighted average life of the hedged liability portfolio but shall not exceed a period of 10 years. Amortization for a quarter’s derivative fair value recognition will begin in the following quarter regardless if the derivative fair value recognition is realized or unrealized.
   1. Reporting entities are required to separately track, with a schedule to show the initial deferred amount and amortization schedule, of the deferred assets and deferred liabilities recognized and outstanding at each reporting date.
   2. The amount reported on the financial statement at each reporting date shall reflect the net amount (net as either a deferred asset or deferred liability) for each hedging strategy captured within scope of this guidance. (Reporting entities that have more than one hedging strategy could have both deferred assets and deferred liabilities in the financial statements based on the net position of the separate hedging strategies.)
   3. Reporting entities are permitted to amortize a greater portion of the deferred assets and/or deferred liabilities into NGO at any time in advance of the scheduled amortization period.
      1. If electing to accelerate amortization, reporting entities are required to accelerate amortization equally between deferred assets and deferred liabilities within a single hedging strategy. For example, a reporting entity is not permitted to accelerate amortization of the deferred liabilities (recognizing the gains from fair value changes) and not accelerate amortization of the deferred assets (continuing to defer losses from fair value changes). If a reporting entity only has a single hedging strategy which only reflects deferred assets or deferred liabilities, the reporting entity is permitted to accelerate amortization without restrictions.
      2. If a reporting entity has more than one hedging strategy, and the strategies have offsetting net positions (both deferred assets and deferred liabilities are recognized in the financial statements), a reporting entity’s election to accelerate amortization must be applied equally to programs with offsetting net positions. (For example, a decision to accelerate amortization of a program with a net deferred liability must be applied equally to a program with a deferred asset that best corresponds to the deferred liability4.) In these situations, the guidance in paragraph 14.c.i. is also applicable, whereas the accelerated amortization must also apply equally to the deferred assets and deferred liabilities within each individual hedging program. If a reporting entity with more than one hedging strategy only has net deferred assets or net deferred liabilities recognized, the reporting entity is permitted to accelerate amortization to a single program in a manner consistent with the guidelines in paragraphs 14.c.i.

4 The intent of this guidance is to ensure that the ability to accelerate amortization does not result with elections that simply result in favorable financial statement presentation.

1. For outstanding (non-expired) derivative instruments that were removed from a highly effective hedging strategy (rebalanced), subsequent gains and losses from fair value fluctuations shall not impact previously recognized deferred assets or deferred liabilities. The deferred assets and deferred liabilities shall be “locked” and amortized under the remaining schedule unless the reporting entity elects to terminate or accelerate amortization. Subsequent to the removal from a highly effective strategy, all fair value fluctuations from the outstanding derivative instruments would be subject to the guidance in SSAP No. 86 and recognized as unrealized gains and/or unrealized losses. If the derivative is re-designated as part of a highly effective hedging strategy qualifying under this standard, subsequent fair value fluctuations (after the re-designation) may be accounted for under the special accounting provision detailed in this statement.
2. For a hedging strategy that no longer qualifies within scope of this standard or is no longer a highly effective hedge, any non-amortized deferred assets or deferred liabilities shall be amortized to NGO over the remaining amortization timeframe, not to exceed five-years. Reallocating assets/derivatives/liabilities in ALM hedging relationships does not indicate no longer qualifying within scope or no longer highly effective (as long as a significant amount of the assets/derivatives/liabilities are included in the hedging relationships before and after reallocation; and the relationship is highly effective before and after reallocation). If the deferred assets/deferred liabilities have a remaining amortization period that is less than the shortened timeframe, amortization shall continue over the remaining period. If the remaining amortization period is greater than 5-years at the time of the program no longer qualifies, or is no longer highly effective, the amortization schedule shall be revised to require full amortization within the shortened 5-year timeframe. If elected by the reporting entity, deferred assets and deferred liabilities may be immediately recognized in NGO or have accelerated amortization (less than 5-years). (An election to immediately eliminate or accelerate amortization must follow the provisions in paragraph 14.c.) All future fair value fluctuations for these derivative instruments would be subject to the guidance in SSAP No. 86 and shall be recognized as unrealized gains or unrealized losses unless the instrument is subsequently designated as part of a highly effective hedging strategy within scope of this statement. If the derivative is re-designated as part of a highly effective hedging strategy qualifying under this standard, subsequent fair value fluctuations (after the re-designation) may be accounted for under the special accounting provision detailed in this statement.
3. Reporting entities may elect to terminate use of this special accounting provision at any time. In those instances, all deferred assets and deferred liabilities shall be amortized to NGO over the remaining amortization timeframe, not to exceed five-years. If the deferred assets/deferred liabilities have an amortization period that is less than the shortened 5-year timeframe, amortization shall continue over the established period. If the remaining amortization period is greater than 5-years at the time of termination, the amortization schedule shall be revised to require full amortization within the shortened 5-year timeframe. If elected by the reporting entity, deferred assets and deferred liabilities may be immediately eliminated or have accelerated amortization (less than 5-years) with recognition in NGO. (An election to immediately eliminate or accelerate amortization must follow the provisions in paragraph 14.c.) Once the special accounting provision is terminated, unless re-designated by the reporting entity, subsequent accounting of the derivatives in a hedging strategy that would be captured within this statement shall follow the fair value accounting approach in SSAP No. 865.

5 Macro-hedges and the ability to rebalance hedging instruments are not provisions permitted within “effective” hedges in scope of SSAP No. 86. As such, hedging strategies with these components accounted for under SSAP No. 86 shall follow the fair value accounting approach detailed in that standard.

## Measurement/Recognition of Realized Gains or Losses of Expired Derivatives

1. This guidance allows for individual derivative instruments to expire and/or be removed from the portfolio of the hedging instrument (as effectiveness is tested each quarter and hedges and hedged items changing each quarter as part of dynamic hedging strategies).
2. Pursuant to the provisions in paragraph 14.c., reporting entities are permitted to amortize a greater portion of the deferred assets and/or deferred liabilities from expired derivatives into NGO in advance of the scheduled amortization period.
3. Consistent with the guidance in paragraph 17, reporting entities may elect to terminate use of this special accounting provision at any time. In those instances, all deferred assets and deferred liabilities shall be amortized to NGO over the remaining amortization timeframe, not to exceed 5-years. If the deferred assets/deferred liabilities had an amortization period that was less than the shortened timeframe, amortization shall continue over the established period. If the amortization period was greater than 5-years at the time of termination, the amortization schedule would be revised to require full amortization within the shortened timeframe. If elected by the reporting entity, the deferred assets and deferred liabilities may be immediately eliminated, or have accelerated amortization, with recognition in NGO. An election to immediate eliminate or accelerate amortization (less than 5 years) must follow the provisions in paragraph 14.c.)

## Derivative Income

1. Derivative income under this accounting provision is included in NGO pursuant to SSAP86.
2. Pursuant to the documented hedging strategy as an ALM Hedge, derivative income shall be considered as part of the overall hedging strategy and included in the assessments on whether the strategy is highly effective.

## Disclosures

1. A reporting entity that has any derivatives accounted for under this special accounting provision, or that has unamortized deferred assets and/or deferred liabilities (representing previously unrecognized qualifying fair value fluctuations) under the special accounting provision shall disclose the following within the financial statements:
   1. For each hedge program under this SSAP, discussion of hedged item, including information on the liabilities’ duration sensitivity to interest rate risk, along with similar information on the assets supporting these liabilities and the designated hedging instruments being used to hedge the duration risk. Discussion of the hedging instruments shall identify whether a hedging instrument is a single instrument or portfolio, as well as information on the hedging strategy

(including whether there have been changes in strategy from the prior reporting period, along with detailed information on the changes), and assessment of hedging effectiveness (e.g., beginning and end of quarter asset duration without derivatives, asset duration with derivatives, liability duration, percentage of difference hedged, etc.) and compliance with the “Clearly Defined Hedging Strategy”. Identification shall occur on whether the hedged item is intended to be fully hedged under the hedging strategy, or if the strategy is only focused on a portion of the asset/liability duration difference. Hedging strategies shall be identified as highly effective or not highly effective. If the strategy for a particular hedging relationship excludes a specific component of the gain or loss, or related cash flows, from the assessment of hedge effectiveness, details on the excluded components shall be disclosed.

* 1. Aggregate disclosure of the original cost and fair value of hedging instruments (including all instruments within a portfolio), including fair value changes during the reporting period. Additionally, disclose the fair value of the hedged item, the change in fair value from the prior reporting period, and the portion of the fair value change attributed to the hedged risk.
  2. Schedule showing the aggregate fair value change from the prior reporting period for the designated components for all hedging instruments, with identification of the fair value change reflected in deferred assets, and deferred liabilities. This schedule shall also show the current period amortization, including any accelerated amortization elected by the reporting entity, and the future scheduled amortization of the deferred assets and deferred liabilities. This schedule shall identify the fair value of the excluded components of the hedging instruments, and the fair value change for those components reflected in unrealized gain and unrealized loss.
  3. For hedging strategies no longer identified as highly effective previously captured within scope of this standard, information on the determination of ineffectiveness, including variations from prior assessments resulting in the change from classification as a highly effective hedge. This disclosure shall also include:
     1. Identification of outstanding hedging instruments previously captured within scope of this standard and subsequently identified as no longer part of a highly effective hedging strategy. This disclosure shall identify the date in which the domiciliary state was notified that the hedging strategy had been identified by the reporting entity as no longer highly effective.
     2. Deferred assets and deferred liabilities previously recognized when the program was highly effective, with a schedule that shows the amortization that would have occurred if the program had remained highly effective, the amount of original amortization as well as a schedule that details the amortization that will occur as the program is no longer highly effective (maximum five-year timeframe).
     3. Disclosure on whether the reporting entity is electing to accelerate amortization (in advance of the remaining scheduled amortization or the maximum five-year timeframe), along with amounts immediately recognized to unrealized gains/losses, and how the election impacts the scheduled amortization.
  4. For situations in which the reporting entity has elected to terminate the hedging strategy and/or discontinue the special accounting provisions permitted within this SSAP, the reporting entity shall disclose the key elements in the reporting’s entity’ decision to terminate, identifying changes in the reporting entity’s objectives or perspectives from initial application. This disclosure shall also include:
     1. Identification of outstanding hedging instruments previously captured within scope of this standard and the accounting impact as a result of the termination/discontinuation. (Open derivative transactions no longer captured within the special accounting provision would be subject to the accounting and reporting guidance within SSAP No. 86.) This disclosure shall identify the date in which the domiciliary state was notified that the hedging strategy or the election to use the special accounting provision in this SSAP had been terminated.
     2. Deferred assets and deferred liabilities previously recognized under the hedging strategy and/or program, with a schedule that shows the amortization that would have occurred if the strategy and/or program had remained highly effective, as well as a schedule that details the amortization that will occur with the termination of the strategy and/or program (maximum five-year timeframe).
     3. Disclosure on whether the reporting entity is electing to accelerate amortization (in advance of the remaining scheduled amortization or the maximum five-year timeframe), along with amounts immediately recognized to unrealized gains/losses, and the resulting impact to the scheduled amortization.

## Effective Date and Transition

1. This statement is effective January 1, 2026. The guidance in this SSAP is required to be applied on a prospective basis for qualifying hedge programs in place on or after the effective date. This prospective application prohibits deferred asset and deferred liability recognition from fair value fluctuations previously recognized as unrealized gains or losses that occurred prior to the effective date of the guidance.
2. Derivative gains/losses deferred in IMR prior to the effective date of this guidance shall continue to be amortized over the remaining amortization period from their original amortization schedule. Unrealized gains/losses recognized prior to the effective date of this SSAP from derivatives that utilize/qualify for the SSAP’s accounting treatment on the above effective date shall remain in unrealized gains/losses and amortize into NGO (i.e., surplus neutral) over the weighted average life of the liabilities they support (subject to the limits noted in previously in this SSAP). Reporting entities that have previously received permitted or prescribed practices for qualifying hedge programs, resulting with the recognition of deferred assets/deferred liabilities from unrecognized fair value fluctuations, shall work with their domiciliary state regulator to determine the appropriate method in transitioning from previously approved permitted practices. The reporting entity shall include disclosure of the transition approach approved by the domiciliary state in their financial statements in the first year of application. The approved transition approach is not considered a permitted practice as long as the reporting entity is fully compliant with the provisions of this statement after implementation. After the effective date of this statement, domiciliary state provisions that differ from this statement must be disclosed as a permitted or prescribed practice pursuant to *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures*.

# REFERENCES

# RELEVANT ISSUE PAPERS

* *Issue Paper No. 159—Special Accounting Treatment for Limited Derivatives*

# EXHIBIT A - EXAMPLE

Under the accounting provisions within this SSAP, all designated highly effective hedging instruments shall initially be reported in the financial statements at amortized cost. Amortized cost treatment will discontinue upon derivative maturity/termination (or de-designation due to ineffectiveness or election); at which time, the derivative fair value will be recognized as an asset or liability offset by a deferred asset (admitted) or deferred liability (i.e., fair value recognition is initially surplus neutral). Note: for derivatives de-designated due to ineffectiveness, amortized cost/deferral treatment can only be applied to fair value changes up to the date the derivatives met the highly effective criteria (after which, all prospective changes in fair value should be record in surplus-unrealized gains/losses).

Under this SSAP, the ability to recognize a derivative at amortized cost or as a deferred asset/liability is limited to only the portion of the fair value fluctuation in the hedging instruments that is attributed to the hedged risk and meets the highly effective criteria. As detailed in this standard, the hedged risk may be designated as a specific component of the hedged item. For example, an entity may designate the duration difference between a portfolio of fixed income investments and a group of future annuity payments in a pension risk transfer (PRT) and/or structured settlements block of liabilities.

Unless a different method has been approved by the domiciliary state commissioner, reporting entities shall utilize the calculations detailed in paragraph 11 to determine if the hedging relationship meets the highly effective criteria. For example:

* Clearly Defined Hedging Strategy (CDHS) characteristics:
  + Hedged item – Structured settlement liability net cash flows
  + Hedged risk – Duration difference between hedged item and designated fixed income asset portfolio supporting the hedged item
* On July 1, 202x, the company’s documented/defined hedged liability item had a Modified Duration of 10 (i.e., a 1% change in interest rates will cause a 10% change in fair value in the opposite direction), while the documented/defined supporting asset portfolio had a Modified Duration of 9.
  + The company designates a portfolio of derivatives to eliminate 100% of this duration difference (i.e., a highly effective derivative portfolio hedging this difference would place the Modified Duration of the fixed income assets with derivatives at between 9.8 and 10.25, which is 80%-125% of the modified duration difference). The company measures the effectiveness on July 1, 202x, and determines the hedge is highly effective (Modified Duration of supporting fixed income asset portfolio with derivatives = 10; Modified Duration of hedged liability = 10).
* On September 30, 202x, the company measures the effectiveness of the hedge program. Note: throughout the 3-month period, the company may have added various supporting fixed income assets, derivatives, and liability cash flows to this hedging relationship (all of which were clearly identified and classified as part of this linked portfolio at each inception). The hedge effectiveness is determined to be highly effective (e.g., Modified Duration of supporting fixed income asset portfolio with derivatives = 10; Modified Duration of hedged liability = 10).
* Example journal entries related to the above are as follows:

