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NAIC Summer 2019 National Meeting Update

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NAIC Summer 2019 National Meeting Update

The National Association of Insurance Commissioners (NAIC) recently held its Summer 2019 National Meeting (Summer Meeting). The following summarizes certain activities of the Statutory Accounting Principles (E) Working Group (SAPWG) that took place since the NAIC Spring 2019 National Meeting. Activities summarized below include both substantive and non-substantive items addressed as part of SAPWG's Hearing Agenda. These items were exposed for comment at previous NAIC National Meetings with comments received from Interested Parties as of the date of the Summer Meeting. SAPWG Meeting Agenda items exposed at the Summer Meeting for future comment and that will be deliberated at subsequent NAIC National Meetings will be addressed in future updates.

More information is available on the NAIC website at http://www.naic.org/cmte_e_app_sapwg.htm.

Related Party Transactions

SAPWG adopted revisions to SSAP No. 25 "*Affiliates and Other Related Parties*" to provide additional guidance to what constitutes a related party transaction including the necessity to assess "the substance of any agreement, and the parties, whose actions or performance materially impact the insurance reporting entity under the transaction." Revisions were also added to SSAP No. 26R "*Bonds*," SSAP No. 32 "*Preferred Stock*," SSAP No. 43R "*Loan-backed and Structured Securities*," and SSAP No. 48 "*Joint Ventures, Partnerships and Limited Liability Companies*" clarifying that any transactions pertaining to related parties that are scoped into any of these SSAP's must also follow the guidance in SSAP No. 25. Interested Parties were supportive of these changes. These revisions are effective immediately.

Mortgage Loans

SAPWG previously exposed revisions to SSAP No. 37 "*Mortgage Loans*" (SSAP No. 37) to clarify that investments in mortgage loan funds are not in scope of SSAP No. 37 and that mortgage loan participation agreements in scope of SSAP No. 37 is limited to a single mortgage loan agreement with a sole borrower. Interested Parties commented that using the language "sole borrower" is inaccurate as many participation agreements include "one or more borrowers." NAIC staff clarified its intent and adjusted its revisions to exclude the "sole borrower" language and replace it with new language to exclude bundled mortgage loans from the scope of SSAP No. 37. Interested Parties also suggested revisions to clarify that bundled mortgage loans are not to be confused with "bulk purchases" of mortgage loans where a reporting entity's interest in each mortgage loan is legally separate and divisible and the "bulk purchase" facilitates the acquisition of multiple single mortgage loan agreements. These revisions as well as some other wording edits suggested by Interested Parties (i.e., the use of the words "lender of record" versus "original lender" in footnote 2b of SSAP No. 37) were adopted at the Summer Meeting by SAPWG. These revisions are effective immediately.

Accounting Standards Updates issued by the Financial Accounting Standards Board

SAPWG rejected the following FASB ASU's recently issued by the FASB:

1. FASB ASU 2015-08 Business Combinations (Topic 805), Pushdown Accounting: "*Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115*"
2. FASB ASU 2019-02 Entertainment – Films – Other Assets – Film Costs (Subtopic 926-20) and Entertainment – Broadcasters – Intangibles – Goodwill and Other (Subtopic 920-350): "*Improvements to Accounting for Costs of Films and License Agreements for Program Materials*" a consensus of the FASB Emerging Issues Task Force

SAPWG exposed to reject the following FASB ASU's recently issued by the FASB:

1. FASB ASU 2018-12 Financial Services – Insurance (Topic 944): "*Targeted Improvements to the Accounting for Long-Duration Contracts*"

Bank Loans

SAPWG previously received a referral from the Valuation of Securities (E) Task Force with a request to review proposed guidance for bank loans to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual). The referral noted concern with identifying revolving lines of credit, borrowing base loans and debtor-in-possession (DIP) financing as bank loans in the P&P Manual and that these types of loans may be more appropriately classified as collateral loans in accordance with SSAP No. 21 "*Other Admitted Assets*" (SSAP No. 21). Interested Parties expressed the view that these loans should stay within the scope of SSAP No. 26R and that these loans should not be treated differently for statutory accounting purposes than any other fixed income investment or other type of bank loan. Upon further discussion, it was determined that a bank loan within the scope of SSAP No. 26R should not be reclassified into the scope of SSAP No. 21 simply because there is additional protection in the form of collateral. SAPWG adopted revisions to SSAP No. 21 to clarify that investments secured with collateral that are captured within the scope of SSAP No. 26R will continued to be captured as such. Interested Parties supported these revisions. These revisions are effective immediately.

Leases

SAPWG adopted a substantively revised SSAP No. 22R "*Leases*" and Issue Paper No. 161 "*Leases*" for the purpose of incorporating various U.S. GAAP concepts of FASB ASU 2016-2 Leases (Topic 842), FASB ASU 2018-10, Codification Improvements to Topic 842, Leases, FASB ASU 2018-11, Leases (Topic 842), Targeted Improvements, FASB ASU 2018-20, Leases (Topic 842), Narrow-Scope Improvements for Lessors and FASB ASU 2019-01, Leases (Topic 842), Codification Improvements into statutory accounting. The revised guidance retains the operating lease concept for statutory accounting, clarifies the application of statutory accounting guidance for leases in certain areas (i.e., sale-leaseback transactions), and identifies the types of assets allowed for lease and sale-leaseback treatment. The revised guidance is effective January 1, 2020. Interested Parties supported these changes.

Reinsurance

SAPWG previously adopted substantive revisions to SSAP No. 62R "*Property and Casualty Reinsurance*" (SSAP No. 62R) to clarify reinsurance risk transfer requirements and the proper determination of reinsurance credit for contracts that pass risk transfer. These revisions are the result of a referral from the Financial Analysis (E) Working Group (FAWG) that expressed concerns with trends regarding the use of reinsurance with risk limiting features for the purposes of providing surplus relief to troubled companies without a significant amount of risk transferred to the reinsurer.

Revisions adopted to SSAP No. 62R include substantive revisions incorporating U.S. GAAP concepts from EITF 93-6 "*Accounting for Multiple-Year Retrospectively Rated Contracts by Ceding and Assuming Enterprises*" and EITF D-035 "*FASB Staff Views on Issue No. 93-6*."

These revisions were adopted effective January 1, 2019 by SAPWG with direction to NAIC staff to draft an issue paper regarding these revisions. The Issue Paper was adopted at the Summer Meeting.

SAPWG adopted additional revisions to SSAP No. 62R at the Summer Meeting clarifying that the January 1, 2019 effective date applies to all reinsurance contracts in effect as of that date.

Interested Parties had no comments on the revisions and Issue Paper.

SCA Loss Tracking

SAPWG re-exposed revisions to SSAP No. 97 "*Investments in Subsidiary, Controlled and Affiliated Entities*" to update the accounting requirements for when an insurance reporting entity (i.e., the Parent) has a negative equity value in a subsidiary, controlled and affiliated (SCA) investment by removing the stipulations that would result in the parent double-counting the recognition of its financial commitment or guarantee of the SCA's obligations and the corresponding reduction of surplus. Conversations are ongoing with Interested Parties regarding this matter.

Reporting NAIC Designations as Weighted Averages

SAPWG previously exposed revisions to clarify accounting and reporting guidance for structured securities acquired in lots. The revisions remove the ability to report NAIC designations for structured securities acquired at different purchase prices within the same lot under a "weighted average" method. Interested Parties previously argued that as a result of the project to update the investment securities factors in the Life, Health and Property & Casualty risk based capital formulas that some of this discussion may be irrelevant as the modified filing exempt approach in SSAP No. 43R may be eliminated. This would reduce the use of "weighted average" designations. At the NAIC 2018 Fall National Meeting, the modified filing exempt approach was formally eliminated from SSAP No. 43R.

As a result of the elimination of the modified filing exempt approach, SAPWG adopted revisions to SSAP No. 43R at the Summer Meeting to report NAIC designations on structured securities as follows: 1) report the entire investment in a single reporting line at the lowest NAIC designation that would apply to a lot or 2) report the investment separately by purchase lot in the investment schedule.

Interested Parties had no comment on this item. These revisions are effective immediately.

Prepayment Penalties

SAPWG adopted revisions to SSAP No. 26R which provides clarification in distinguishing prepayment penalty or acceleration fees from realized capital gains or losses for bonds that are called. Revisions clarify that a reporting entity has a process in place to identify any explicit prepayment penalties or acceleration fees then any prepayment penalties or acceleration fees identified are reported as investment income. Any remaining difference is reported as realized capital gains or losses. Revisions further clarified that to the extent that consideration received is less than book adjusted carrying value of the bond that the entire difference is reported as investment income. Interested Parties supported these revisions. These revisions are effective immediately. The Blanks (E) Working Group concurrently adopted similar revisions to the Annual Statement Instructions.

Repurchase Disclosures

SAPWG adopted revisions to SSAP No. 103R "*Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*." The revisions eliminate the minimum and average daily balance disclosures as well as information regarding counterparties and defaults from the data-captured templates. Interested Parties supported these revisions. These revisions are effective immediately.

Bonds Received as Property Dividends or Capital Contributions

SAPWG adopted revisions to existing statutory accounting guidance and investment schedule reporting requiring bonds received as a property dividend or capital contribution to be recorded at cost value. Interested Parties supported these revisions. These revisions are effective immediately. The Blanks (E) Working Group concurrently adopted similar revisions to the Annual Statement Instructions.

Reporting Deposit-Type Contracts

SAPWG re-exposed comments to provide clarity as to why guaranteed investment contracts, or other deposit-type contracts are reported in Exhibit 5 – Aggregate Reserves for Life Contracts (Exhibit 5) or in Exhibit 6 – Aggregate Reserves for Accident and Health Contracts (Exhibit 6) instead of in Exhibit 7 – Deposit Type Contracts (Exhibit 7) in the Annual Statement. Interested Parties commented that generally guaranteed investment contracts and other types of deposit-type contracts are reported in Exhibit 7. However, there are some contracts with deposit-like characteristics that also have other characteristics that allow these contracts to be reported in either Exhibit 5 or Exhibit 6. This matter is still under consideration by SAPWG and NAIC staff whereby further evaluation is needed in order to determine if accounting revisions are necessary to ensure consistency in reporting.

Prepayments to Service and Claims Adjusting Providers

SAPWG previously exposed revisions to SSAP No. 55 "*Unpaid Claims, Losses and Loss Adjustment Expenses*" (SSAP No. 55). The revisions clarify that prepayment of unpaid losses and claims adjustment expenses to providers of claims adjustment services be recognized as a prepaid asset and non-admitted consistent with the guidance in SSAP No. 29 "*Prepaid Expenses*." Interested Parties commented that this guidance should exclude health insurance and managed care contracts since the guidance in SSAP No. 84 "*Health Care and Government Insured Plan Receivables*" already addressed the accounting for these types of contracts. SAPWG incorporated Interested Parties comments into the revisions and re-exposed for comment.

Federal Income Taxes

SAPWG previously exposed revisions to SSAP No. 101 "*Income Taxes*" Implementation Q&A (The Q&A) to clarify the application of the deferred tax admittance calculation, particularly with regards to offsetting deferred tax liabilities. Interested Parties provided comments requesting clarification regarding the need for scheduling reversal patterns of temporary differences when applying the 11c test in SSAP No. 101 "Income Taxes". SAPWG commented that a reporting entity would need to consider the reversal patterns of temporary differences only as it pertains to the determination of a statutory valuation allowance in accordance with paragraph 7e of SSAP No. 101. These revisions were adopted at the Summer Meeting effective December 31, 2019.

Additionally, SAPWG adopted transition guidance for both the above and any additional revisions implemented to The Q&A to align with SSAP No. 101 as it pertains to the Federal Tax Cuts and Jobs Act that would effect a reporting entities calculation of tax balances. The transition guidance requires the reporting entities to apply guidance in SSAP No. 3 "*Accounting Changes and Correction of Errors*" for December 31, 2019 financial reporting purposes.

Other Derivatives

SAPWG exposed revisions to SSAP No. 86 "*Derivatives*" (SSAP No. 86) to address the accounting for derivatives classified as "other" in SSAP No. 86. These types of derivatives are typically not involved in either hedging, income generation or replication transactions. SAPWG's revisions clarify that these types of "other" derivatives are recorded at fair value and non-admitted (unless allowed to be admitted under state investment law) for statutory accounting purposes. Interested Parties commented that these revisions could have unintended consequences as it pertains to structured notes held by a reporting entity and that structured notes may be inappropriately scoped into these revisions. Interested Parties proposed language to SAPWG modifying SSAP No. 86 allowing for and clarifying the admittance of structure notes as assets on a reporting entities balance sheet. SAPWG disagreed with Interested Party comments stating that the intent of the revisions was to scope in all derivative instruments classified as "other" which would include structured notes and not specifically single out the accounting for just structured notes. These revisions were re-exposed for further comment by Interested Parties.

Goodwill

SAPWG exposed revisions to SSAP No. 68 "*Business Combinations*" (SSAP No. 68) to reject FASB ASU 2014-17 Business Combinations (Topic 805), Pushdown Accounting: "a consensus of the FASB Emerging Issues Task Force." The exposed revisions also prohibit pushdown accounting in SSAP No. 97 for Subsidiary Controlled Affiliates (SCA) reported in accordance with audited U.S. GAAP. Interested Parties disagreed with these revisions and stated that if the intent is to address concerns regarding goodwill at the SCA level then there are more direct approaches to addressing those concerns and current proposed revisions will most likely be confusing and costly to reporting entities. SAPWG re-exposed for comment three options as it pertains to pushdown accounting as follows:

1. Complete rejection of pushdown accounting;
2. Permission to use pushdown accounting for all non-insurance entities with revisions to include incorporation of goodwill at the SCA level in the reporting entity's goodwill admittance test; or
3. Permit pushdown accounting if elected by SEC Registrants, excluding non-insurance entities with revisions to include incorporation of goodwill at the SCA level in the reporting entity's goodwill admittance test.

Discussion with Interested Parties regarding the above is on-going.

SAPWG disposed of previously exposed revisions to existing guidance in SSAP No. 97 which permits the application of the "look-through" approach to value investments in SCA entities when multiple downstream holding companies exist if all of the look-through entities meet the look-through criteria.

SAPWG re-exposed revisions to SSAP No. 68 and SSAP No. 97 to explicitly state that the acquisition of a holding company requires the purchase price and goodwill amount to be attributed (i.e., assigned) to the downstream entities that are directly owned by the holding company with disclosure of the allocation of goodwill and method of allocation utilized allowing the identification of the proper amount of goodwill eliminated accordingly upon sale or non-admittance of the downstream entity. Discussion with Interested Parties on this matter is on-going.

Other Working Groups

In addition to SAPWG, several other committees, working groups, and task forces met during the Summer Meeting. The following represents selected updates concerning the activities of some of these committees, working groups and task forces.

Risk Retention Group (E) Task Force

The Risk Retention Group (E) Task Force (RRG Task Force) met at the Summer Meeting to discuss the need for clarification regarding the registration of risk retention groups in non-domiciliary states. Discussion focused on revisions to the NAIC Uniform Risk Retention Group – Notice and Registration Form to assist in clarifying what information is required to be submitted by a risk retention group to a non-domiciliary state.

Additionally, the RRG Task Force exposed a frequently asked questions and best practices document for risk retention groups with the intent that this document assist non-domiciliary states in understanding state's authority as it applies to risk retention groups.

Connect With Us

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