Appendix A
Excerpts of NAIC Model Laws

Introduction

The following appendices are an integral part of the NAIC *Accounting Practices and Procedures Manual*. The guidance herein is referred to by specific statements of statutory accounting principles (SSAPs).

Some appendices define certain terms. Such definitions are not intended to change the meaning of any terms used elsewhere in the NAIC *Accounting Practices and Procedures Manual* and should only be used in the context of the appendix in which it appears and the SSAP that refers to that appendix.

Certain appendices contain requirements regarding reserves, which are effective with new business written after the effective date of the related SSAP. Transition guidance is provided in the related SSAPs.

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Appendix A-001

Investments of Reporting Entities

Relevant SSAPs:
SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures
SSAP No. 21—Other Admitted Assets
SSAP No. 83—Mezzanine Real Estate Loans

Introduction

A reporting entity may acquire, hold or invest in investments or engage in investment practices as set forth in the laws and regulations of its domiciliary state. The disclosure required by this appendix is not intended to preempt such state authority. The financial information disclosed herein is intended solely for the use of state regulators for solvency analysis and should not be used for any other purpose.

Section 1. Reporting Requirements

The following reporting requirements apply to the provisions of this appendix:

1. Annual Statement – Section 3
2. Supplement to Annual Statement filed by April 1 – Section 2
3. Audited Statutory Financial Statements – Sections 2 and 3

Section 2. Investment Risks Interrogatories

Of The.. Insurance Company
Address (City, State, Zip Code) ....
NAIC Group Code.. NAIC Company Code.. Employer's ID Number...............................

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements.

Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement: $____________

2. Ten largest exposures to a single issuer/borrower/investment:

	1 Issuer		2 Description of Exposure	3 Amount	4 Percentage of Total Admitted Assets
2.01	....	a.	....	$..........................	.................................%
2.02	....	b.	....	$..........................	.................................%
2.03	....	c.	....	$..........................	.................................%
2.04	....	d.	....	$..........................	.................................%
2.05	....	e.	....	$..........................	.................................%
2.06	....	f.	....	$..........................	.................................%
2.07	....	g.	....	$..........................	.................................%
2.08	....	h.	....	$..........................	.................................%
2.09	....	i.	....	$..........................	.................................%
2.10	....	j.	....	$..........................	.................................%

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC designation:

	Bonds	1	2		**Preferred Stocks**	3	4
3.01	NAIC – 1	$...............	................%	3.07	NAIC – 1	$................	................%
3.02	NAIC – 2	$...............	................%	3.08	NAIC – 2	$................	................%
3.03	NAIC – 3	$...............	................%	3.09	NAIC – 3	$................	................%
3.04	NAIC – 4	$...............	................%	3.10	NAIC – 4	$................	................%
3.05	NAIC – 5	$...............	................%	3.11	NAIC – 5	$................	................%
3.06	NAIC – 6	$...............	................%	3.12	NAIC – 6	$................	................%

4. Assets held in foreign investments:

4.01 Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response, to 4.01 above is yes, responses are not required for interrogatories 5 – 10.

4.02	Total admitted assets held in foreign investments	$	.... %
4.03	Foreign-currency-denominated investments	$	.... %
4.04	Insurance liabilities denominated in that same foreign currency	$	.... %

5. Aggregate foreign investment exposure categorized by NAIC sovereign designation:

		1	2
5.01	Countries designated NAIC – 1	$	.... %
5.02	Countries designated NAIC – 2	$	.... %
5.03	Countries designated NAIC – 3 or below	$	.... %

6. Two largest foreign investment exposures to a single country, categorized by the country's NAIC sovereign designation:

		1	2
	Countries designated NAIC – 1:		
6.01	Country:	$	.... %
6.02	Country:	$	.... %
	Countries designated NAIC – 2:		
6.03	Country:	$	.... %
6.04	Country:	$	.... %
	Countries designated NAIC – 3 or below:		
6.05	Country:	$	.... %
6.06	Country:	$	.... %

7. Aggregate unhedged foreign currency exposure: $........................... .... %

8. Aggregate unhedged foreign currency exposure categorized by NAIC sovereign designation:

		1	2
8.01	Countries designated NAIC – 1	$	.... %
8.02	Countries designated NAIC – 2	$	.... %
8.03	Countries designated NAIC – 3 or below	$	.... %

9. Two largest unhedged foreign currency exposures to a single country, categorized by the country's NAIC sovereign designation:

		1	2
	Countries designated NAIC – 1:		
9.01	Country:	$	.... %
9.02	Country:	$	.... %
	Countries designated NAIC – 2:		
9.03	Country:	$	.... %
9.04	Country:	$	.... %
	Countries designated NAIC – 3 or below:		
9.05	Country:	$	.... %
9.06	Country:	$	.... %

10. Ten largest non-sovereign (i.e., non-governmental) foreign issues:

	1 Issuer	2 NAIC Designation	3	4
10.01	....	....	$	.... %
10.02	....	....	$	.... %
10.03	....	....	$	.... %
10.04	....	....	$	.... %
10.05	....	....	$	.... %
10.06	....	....	$	.... %
10.07	....	....	$	.... %
10.08	....	....	$	.... %
10.09	....	....	$	.... %
10.10	....	....	$	.... %

11. Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure:

11.01 Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11.

		1	2
11.02	Total admitted assets held in Canadian Investments	$............................	.............................%
11.03	Canadian-currency-denominated investments	$............................	.............................%
11.04	Canadian-denominated insurance liabilities	$............................	.............................%
11.05	Unhedged Canadian currency exposure	$............................	.............................%

12. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions:

12.01 Are assets held in investments with contractual sales restrictions less than 2.5% of the Reporting entity's total admitted assets. Yes [ ] No [ ]

If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12.

	1	2	3
12.02	Aggregate statement value of investments with contractual sales restrictions:	$	.... %
	Largest 3 investments with contractual sales restrictions:		
12.03	....	$	.... %
12.04	....	$	.... %
12.05	....	$	.... %

13. Amounts and percentages of admitted assets held in the ten largest equity interests:

13.01 Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 13.01 is yes, responses are not required for the remainder of Interrogatory 13.

	1 Issuer	2	3
13.02	....	$	.... %
13.03	....	$	.... %
13.04	....	$	.... %
13.05	....	$	.... %
13.06	....	$	.... %
13.07	....	$	.... %
13.08	....	$	.... %
13.09	....	$..........................	.... %
13.10	....	$..........................	.... %
13.11	....	$	.... %

14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:

14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14.

	1	2	3
14.02	Aggregate statement value of investments held in nonaffiliated, privately placed equities:	$	.... %
	Largest 3 investments held in nonaffiliated, privately placed equities:		
14.03	....	$	.... %
14.04	....	$	.... %
14.05	....	$	.... %

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

	1	2	3
15.02	Aggregate statement value of investments held in general partnership interests:	$	.... %
	Largest 3 investments in general partnership interests:		
15.03	....	$	.... %
15.04	....	$	.... %
15.05	....	$	.... %

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

	1 (Type (Residential, Commercial, Agricultural)	2	3
16.02	....	$	.... %
16.03	....	$	.... %
16.04	....	$	.... %
16.05	....	$	.... %
16.06	....	$	.... %
16.07	....	$	.... %
16.08	....	$	.... %
16.09	....	$	.... %
16.10	....	$	.... %
16.11	....	$	.... %

Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

		Loans	
16.12	Construction loans	$	..............................%
16.13	Mortgage loans over 90 days past due	$	..............................%
16.14	Mortgage loans in the process of foreclosure	$	..............................%
16.15	Mortgage loans foreclosed	$	..............................%
16.16	Restructured mortgage loans	$	..............................%

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

	Loan-to-Value	Residential		Commercial		Agricultural	
		1	2	3	4	5	6
17.01	above 95%	$...................	.... %	$	.... %	$	.... %
17.02	91% to 95%	$...................	.... %	$	.... %	$	.... %
17.03	81% to 90%	$...................	.... %	$	.... %	$	.... %
17.04	71% to 80%	$...................	.... %	$	.... %	$	.... %
17.05	below 70%	$...................	.... %	$	.... %	$	.... %

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate:

18.01 Are assets held in real estate reported in less than 2.5% of the reporting entity's total admitted assets? Yes [ ] No [ ]

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate:

	Description 1	2	3
18.02	....	$	.... %
18.03	....	$	.... %
18.04	....	$	.... %
18.05	....	$	.... %
18.06	....	$	.... %

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments held in mezzanine real estate loans:

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the Reporting entity's total admitted assets. Yes [ ] No [ ]

If response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

	1	2	3
19.02	Aggregate statement value of investments held in mezzanine real estate loans:	$	.... %
	Largest 3 investments held in mezzanine real estate loans:		
19.03	....	$	.... %
19.04	....	$	.... %
19.05	....	$	.... %

20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

	At Year-end		At End of Each Quarter		
			1st Qtr	2nd Qtr	3rd Qtr
	1	2	3	4	5
20.01 Securities lending agreements (do not include assets held as collateral for such transactions)	$	.... %	$...............	$..............	$..............
20.02 Repurchase agreements	$	.... %	$...............	$..............	$..............
20.03 Reverse repurchase agreements	$	.... %	$...............	$..............	$..............
20.04 Dollar repurchase agreements	$	.... %	$...............	$..............	$..............
20.05 Dollar reverse repurchase agreements	$	.... %	$...............	$..............	$..............

21. Amounts and percentages of the reporting entity's total admitted assets for warrants not attached to other financial instruments, options, caps, and floors:

		Owned		Written	
		1	2	3	4
21.01	Hedging	$	.... %	$	..............................%
21.02	Income generation	$	.... %	$	..............................%
21.03	Other	$	.... %	$	..............................%

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

		At Year-end		At End of Each Quarter		
				1st Qtr	2nd Qtr	3rd Qtr
		1	2	3	4	5
22.01	Hedging	$	.... %	$	$.................	$ ....
22.02	Income generation	$	.... %	$	$.................	$ ....
22.03	Replications	$	.... %	$	$.................	$ ....
22.04	Other	$	.... %	$	$.................	$ ....

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

		At Year-end		At End of Each Quarter		
				1st Qtr	2nd Qtr	3rd Qtr
		1	2	3	4	5
23.01	Hedging	$......................	.... %	$	$	$ ....
23.02	Income generation	$......................	.... %	$	$	$ ....
23.03	Replications	$......................	.... %	$	$	$ ....
23.04	Other	$......................	.... %	$	$	$ ....

Section 3. Summary Investment Schedule (Revised for reporting periods effective January 1, 2019)

Investment Categories	Gross Investment Holdings		Admitted Assets as Reported in the Annual Statement			
	1	2	3	4	5	6
	Amount	Percentage	Amount	Securities Lending Reinvested Collateral Amount	Total (Col. 3+4) Amount	Percentage
1. Bonds (Schedule D, Part 1)						
1.1 U.S. Governments	....	....	....	....	....	....
1.2 All Other Government	....	....	....	....	....	....
1.3 U.S. States, Territories and Possessions, etc., Guaranteed	....	....	....	....	....	....
1.4 U.S. Political Subdivisions of States, Territories and Possessions, Guaranteed	....	....	....	....	....	....
1.5 U.S. Special Revenue & Special Assessment Obligations, etc., Non-Guaranteed	....	....	....	....	....	....
1.6 Industrial and Miscellaneous	....	....	....	....	....	....
1.7 Hybrid Securities	....	....	....	....	....	....
1.8 Parent, Subsidiaries and Affiliates	....	....	....	....	....	....
1.9 SVO Identified Funds	....	....	....	....	....	....
1.10 Bank Loans	....	....	....	....	....	....
1.11 Total Long-Term Bonds	....	....	....	....	....	....
2. Preferred Stock (Schedule D, Part 2, Section 1)						
2.1 Industrial and Miscellaneous (Unaffiliated)	....	....	....	....	....	....
2.2 Parent Subsidiaries and Affiliates	....	....	....	....	....	....
3. Common Stocks (Schedule D, Part 2, Section 2)						
3.1 Industrial and Miscellaneous (Unaffiliated) Publicly Traded	....	....	....	....	....	....
3.2 Industrial and Miscellaneous (Unaffiliated) Other	....	....	....	....	....	....
3.3 Parent, Subsidiaries and Affiliates Publicly Traded	....	....	....	....	....	....
3.4 Parent, Subsidiaries and Affiliates Other	....	....	....	....	....	....
3.5 Mutual Funds	....	....	....	....	....	....
3.6 Total Common Stocks	....	....	....	....	....	....
4. Mortgage Loans (Schedule B)						
4.1 Farm Mortgages	....	....	....	....	....	....
4.2 Residential Mortgages	....	....	....	....	....	....
4.3 Commercial Loans	....	....	....	....	....	....
4.4 Mezzanine Real Estate Loans	....	....	....	....	....	....
4.5 Total Valuation Allowance	....	....	....	....	....	....
4.6 Total Mortgages	....	....	....	....	....	....
5. Real Estate Investments (Schedule A)						
5.1 Property occupied by company	....	....	....	....	....	....
5.2 Property held for production of income	....	....	....	....	....	....
5.3 Property held for sale	....	....	....	....	....	....

Investment Categories	Gross Investment Holdings 1 Amount	2 Percentage	Admitted Assets as Reported in the Annual Statement 3 Amount	4 Securities Lending Reinvested Collateral Amount	5 Total (Col. 3+4) Amount	6 Percen-tage
6. Cash, Cash Equivalents and Short-Term Investments						
6.1 Cash (Schedule E, Part 1)	....	....	....	....	....	....
6.2 Cash Equivalents (Schedule E, Part 2)	....	....	....	....	....	....
6.3 Short-Term Investments (Schedule DA)	....	....	....	....	....	....
6.4 Total Cash, Cash Equivalents and Short-Term Investments	....	....	....	....	....	....
7. Contract Loans	....	....	....	....	....	....
8. Derivatives (Schedule DB)	....	....	....	....	....	....
9. Other Invested Assets (Schedule BA)	....	....	....	....	....	....
10. Receivables for Securities	....	....	....	....	....	....
11. Securities Lending (Schedule DL, Part1)	....	....	....	....	....	....
12. Aggregate Write-Ins for Invested Assets	....	....	....	....	....	....
13. **Total Invested Assets**	....	....	....	....	....	....

Appendix A-010

Minimum Reserve Standards for Individual and Group Health Insurance Contracts

Relevant SSAPs:
SSAP No. 35—Guaranty Fund and Other Assessments
SSAP No. 54—Individual and Group Accident and Health Contracts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. “Annual claim cost” is the net annual cost per unit of benefit before the addition of expenses, including claim settlement expenses, and a margin for profit or contingencies. For example, the annual claim cost for a $100 monthly disability benefit, for a maximum disability benefit period of one year, with an elimination period of one week, with respect to a male at age 35, in a certain occupation might be $12, while the gross premium for this benefit might be $18. The additional $6 would cover expenses and profit or contingencies.

2. “Claims accrued” is that portion of claims incurred on or prior to the valuation date that result in liability of the insurer for the payment of benefits for medical services that have been rendered on or prior to the valuation date, and for the payment of benefits for days of hospitalization and days of disability that have occurred on or prior to the valuation date, that the insurer has not paid as of the valuation date, but for which it is liable and will have to pay after the valuation date. This liability is sometimes referred to as a liability for “accrued” benefits. A claim reserve, which represents an estimate of this accrued claim liability, must be established. *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses defines this as a Claim Liability and not a Claim Reserve.*

3. “Claims reported” are considered as a reported claim for annual statement purposes when an insurer has been informed that a claim has been incurred, if the date reported is on or prior to the valuation date.

4. “Claims unaccrued” represent that portion of claims incurred on or prior to the valuation date which result in liability of the insurer for the payment of benefits for medical services expected to be rendered after the valuation date, and for benefits expected to be payable for days of hospitalization and days of disability occurring after the valuation date. This liability is sometimes referred to as a liability for unaccrued benefits. A claim reserve, which represents an estimate of the unaccrued claim payments expected to be made (which may or may not be discounted with interest), must be established. *SSAP No. 54~~R~~—Individual and Group Accident and Health Contracts defines this as a Claim Reserve differentiated from the Claim Liability in paragraph 2 above.*

5. When an insurer has not been informed, on or before the valuation date, concerning a claim that has been incurred on or prior to the valuation date, the claim is considered an “unreported claim” for annual statement purposes.

6. “Date of disablement” is the earliest date the insured is considered as being disabled under the definition of disability in the contract, based on a doctor’s evaluation or other evidence. Normally this date will coincide with the start of any elimination period.

7. “Elimination period” is a specified number of days, weeks, or months starting at the beginning of each period of loss, during which no benefits are payable.

8. “Gross premium” is the amount of premium charged by the insurer. It includes the net premium (based on claim-cost) for the risk, together with any loading for expenses, profit or contingencies.

9. The term “group long-term disability income” includes group contracts providing group disability income coverage with a maximum benefit duration longer than two years. Group long-term disability income contracts are based on a group pricing structure. The term “group long-term disability” does not include group short-term disability (coverage with benefit periods of two years or less in maximum duration). It also does not include voluntary group disability income coverage that is priced on an individual risk structure and generally sold in the workplace.

10. The term “group insurance” includes blanket insurance and franchise insurance and any other forms of group insurance.

11. “Level premium” is a premium calculated to remain unchanged throughout either the lifetime of the policy or for some shorter projected period of years. The premium need not be guaranteed; in which case, although it is calculated to remain level, it may be changed if any of the assumptions on which it was based are revised at a later time. Generally, the annual claim costs are expected to increase each year and the insurer, instead of charging premiums that correspondingly increase each year, charges a premium calculated to remain level for a period of years or for the lifetime of the contract. In this case the benefit portion of the premium is more than needed to provide for the cost of benefits during the earlier years of the policy and less than the actual cost in the later years. The building of a prospective contract reserve is a natural result of level premiums.

12. “Long-term care insurance” is any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than twelve (12) consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis; for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital. Such term also includes a policy or rider which provides for payment of benefits based upon cognitive impairment or the loss of functional capacity. Long-term care insurance may be issued by insurers; fraternal benefit societies; nonprofit health, hospital, and medical service corporations; prepaid health plans; health maintenance organizations or any similar organization to the extent they are otherwise authorized to issue life or health insurance. Long-term care insurance shall not include any insurance policy which is offered primarily to provide basic Medicare supplement coverage, basic hospital expense coverage, basic medical-surgical expense coverage, hospital confinement indemnity coverage, major medical expense coverage, disability income or related asset-protection coverage, accident only coverage, specified disease or specified accident coverage, or limited benefit health coverage.

13. “Modal Premium” refers to the premium paid on a contract based on a premium term which could be annual, semi-annual, quarterly, monthly, or weekly. Thus if the annual premium is $100 and if, instead, monthly premiums of $9 are paid then the modal premium is $9.

14. Normally the terminal reserve is a positive value. However, if the values of the benefits are decreasing with advancing age or duration it could be a negative value, called a “negative reserve.”

15. “Preliminary Term Reserve Method” is a method of valuation whereby the valuation net premium for each year falling within the preliminary term period is exactly sufficient to cover the expected incurred claims of that year, so that the terminal reserves will be zero at the end of the year. As of the end of the preliminary term period, a new constant valuation net premium (or stream of changing valuation premiums) becomes applicable such that the present value of all such premiums is equal to the present value of all claims expected to be incurred following the end of the preliminary term period.

16. “Present value of amounts not yet due on claims” represents the reserve for “claims unaccrued” (see definition), which may be discounted at interest.

17. “Rating block” means a grouping of contracts determined by the valuation actuary based on common characteristics, such as a policy form or forms having similar benefit designs.

18. The term “reserve” is used to include all items of benefit liability, whether in the nature of incurred claim liability or in the nature of contract liability relating to future periods of coverage, and whether the liability is accrued or unaccrued. An insurer under its contracts promises benefits which result in:

   a. Claims that have been incurred, that is, for which the insurer has become obligated to make payment, on or prior to the valuation date. On these claims, payments expected to be made after the valuation date for accrued and unaccrued benefits are liabilities of the insurer which shall be provided for by establishing claim reserves; or

   b. Claims that are expected to be incurred after the valuation date. Any present liability of the insurer for these future claims shall be provided for by the establishment of contract reserves and unearned premium reserves.

19. “Terminal reserve” is the reserve at the end of a contract year and is defined as the present value of benefits expected to be incurred after that contract year minus the present value of future valuation net premiums.

20. “Unearned premium reserve” values that portion of the premium paid or due to the insurer which is applicable to the period of coverage extending beyond the valuation date. Thus if an annual premium of $120 was paid on November 1, $20 would be earned as of December 31 and the remaining $100 would be unearned. The unearned premium reserve could be on a gross basis as in this example or on a valuation net premium basis.

21. “Valuation net modal premium” is the modal fraction of the valuation net annual premium that corresponds to the gross modal premium in effect on any contract to which contract reserves apply. Thus if the mode of payment in effect is quarterly, the valuation net modal premium is the quarterly equivalent of the valuation net annual premium.

22. “Worksite Disability Policies” refers to individual short-term disability policies that are sold at the worksite through employer-sponsored enrollment, cover normal pregnancy, and that have benefit periods up to 24 months. Worksite disability policies do not include personal disability policies sold to an individual and not associated with employer-sponsored enrollment. They also do not include business overhead expense, disability buyout or key person policies, in whatever manner those policies are sold.

Scope

23. These standards apply to all individual and group health and accident and sickness insurance coverages, including single premium credit disability insurance. All other credit insurance is not subject to Appendix A-010.

24. When an insurer determines that adequacy of its health insurance reserves requires reserves in excess of the minimum standards specified herein, such increased reserves shall be held and shall be considered the minimum reserves for that insurer.

25. With respect to any block of contracts, or with respect to an insurer’s health business as a whole, a prospective gross premium valuation is the ultimate test of reserve adequacy as of a given valuation date. Such a gross premium valuation will take into account, for contracts in force, in a claims status, or in a continuation of benefits status on the valuation date, the present value as of the valuation date of: all expected benefits unpaid, all expected expenses unpaid, and all unearned or expected premiums, adjusted for future premium increases reasonably expected to be put into effect.

26. Such a gross premium valuation is to be performed whenever a significant doubt exists as to reserve adequacy with respect to any major block of contracts, or with respect to the insurer's health business as a whole. In the event inadequacy is found to exist, immediate loss recognition shall be made and the reserves restored to adequacy. Adequate reserves (inclusive of claim, premium and contract reserves, if any) shall be held with respect to all contracts, regardless of whether contract reserves are required for such contracts under these standards.

27. Whenever minimum reserves, as defined in this Appendix, exceed reserve requirements as determined by a prospective gross premium valuation, such minimum reserves remain the minimum requirement under these standards.

28. The following paragraphs set forth minimum standards for three categories of health insurance reserves:

a. Claim Reserves;

b. Premium Reserves;

c. Contract Reserves.

29. Adequacy of an insurer's health insurance reserves is to be determined on the basis of all three categories combined. However, these standards emphasize the importance of determining appropriate reserves for each of the three categories separately.

Claim Reserves

30. General:

a. Claim reserves are required for all incurred but unpaid claims on all health insurance policies. For contracts with an elimination period, the duration of disablement shall be measured as dating from the time that benefits would have begun to accrue had there been no elimination period.

b. Appropriate claim expense reserves are required with respect to the estimated expense of settlement of all incurred but unpaid claims.

c. All such reserves for prior valuation years are to be tested for adequacy and reasonableness along the lines of claim runoff schedules in accordance with the statutory financial statement including consideration of any residual unpaid liability.

d. For claim reserves on policies that require contract reserves, the claim incurral date is to be considered the "issue date" for determining the table and interest rate to be used for claim reserves.

e. The maximum interest rate for claim reserves is specified in Exhibit 1.

f. With respect to claim reserves for policies issued before the operative date[1] of the Valuation Manual, the requirements for claim reserves on claims incurred after that date shall be as described in this Appendix A-010 based on the incurred date of the claim.

[1] The historical application of new requirements for claim reserves has been the incurred date of the claim. The 2009 changes to the Standard Valuation Law apply new requirements provided through the *Valuation Manual* only to policies issued after the effective date of the changes and the *Valuation Manual*. This addition makes new requirements for claim reserves applicable based on the incurred date irrespective of the policy issue date – i.e. consistent with historical practice.

Minimum Morbidity Standards for Individual Disability Income Claim Reserves:

31. For individual disability income claims incurred January 1, 2001, to January 1, 2007, each insurer may elect which of the following to use as the minimum morbidity standard for claim reserves:

a. The minimum morbidity standard in effect for claim reserves as of the date the claim was incurred, or

b. The standards as defined in paragraph 32, which applies on or after January 1, 2017, shall be applied to all open claims unless the company chooses on or after January 1, 2017, to apply the standards in paragraph 31.c. Once an insurer elects to calculate reserves for all open claims on the newer standards defined in paragraph 32 or paragraph 31.c., all future valuations must be on that basis.

c. The standards as defined in paragraph 33 through paragraph 36, which apply on or after January 1, 2017, shall be applied to all open claims. Once an insurer elects to calculate reserves for all open claims on the standards defined in paragraph 33 through paragraph 36, all future valuations must be on that basis.

32. For individual disability income claims incurred on or after January 1, 2007, and prior to the effective date for the company as determined in paragraph 35, the minimum standards with respect to morbidity are those specified in Exhibit 1, except that, at the option of the insurer, assumptions regarding claim termination rates for the period less than two (2) years from the date of disablement may be based on the insurer's experience, if such experience is considered credible, or upon other assumptions designed to place a sound value on the liabilities.

33. For claims incurred on or after January 1, 2020, the minimum standards are those specified in Exhibit 1, including (as derived in accordance with *Actuarial Guideline L—2013 Individual Disability Income Valuation Table Actuarial Guideline*):

a. The use of the insurer's own experience;

b. An adjustment to include an own experience measurement margin; and

c. The application of a credibility factor.

34. In determining the minimum reserves in accordance with paragraph 33, the provisions in paragraph 33.a., 33.b. and 33.c. are not required if:

a. The insurer meets the Own Experience Measurement Exemption provided in Actuarial Guideline L; or

b. For worksite disability policies with benefit periods of up to two years, at the option of the insurer, disabled life reserves may be based on the insurer's experience, if such experience is considered credible, or upon other assumptions and methods designed to place a sound value on the liabilities.

35. An insurer may begin to use the minimum reserve standards in paragraph 33 at a date earlier than January 1, 2020, but not prior to January 1, 2017.

36. An insurer may, within three years[2] of January 1, 2020 (or such earlier date it elects under paragraph 35), apply the new standards in paragraph 33 to all open claims incurred prior to the effective date of paragraph 33 for the insurer. Once an insurer elects to calculate reserves for all open claims based on paragraph 33, all future valuations must be on that basis.

Minimum Morbidity Standards for Group Disability Income Claim Reserves

37. For group disability income claims incurred from January 1, 2001, through December 31, 2006, with a duration from date of disablement of more than two (2) years but less than five (5) years, reserves may be based on the insurer's experience if such experience is considered credible and for which the insurer maintains underwriting and claim administration control.

38. For group disability income claims incurred prior to January 1, 2007, each insurer may elect to use as the minimum morbidity standard for claim reserves:

a. The group disability income claims minimum morbidity standard in effect for claim reserves as of the date the claim was incurred; or

b. After the effective date selected by the company in paragraphs 41 and 42, the standards as defined in paragraphs 41 and 42 applied to all open group long-term disability income claims, or

c. The standards as defined in paragraphs 41 and 42 applied to all open group disability income claims.

Once an insurer elects to calculate reserves for all open claims on a more recent standard, then all future valuations must be on that basis.

39. For group long-term disability income claims incurred on or after January 1, 2007, but before the effective date selected by the company in paragraph 42, and group disability income claims incurred on or after January 1, 2007, that are not group long-term disability income, the minimum standards with respect to morbidity are those specified in Exhibit 1, except that, at the option of the insurer:

a. Assumptions regarding claim termination rates for the period less than two (2) years from the date of disablement may be based on the insurer's experience, if the experience is considered credible, or upon other assumptions designed to place a sound value on the liabilities.

b. Assumptions regarding claim termination rates for the period two (2) or more years but less than five (5) years from the date of disablement may, with the approval of the commissioner, be based on the insurer's experience if such experience is considered credible and for which the insurer maintains underwriting and claim administration control.

c. With respect to claims termination standards in paragraphs 37 and 39.b., for experience to be considered credible for purposes of this appendix, the company should be able to provide claim termination patterns over no more than six (6) years reflecting at least

[2] The 2013 Table requires additional information that was not required to determine claim reserves under prior tables. The three year period is a period after the date a company starts using the 2013 Table for new claims to allow the company to update its claims data to use the 2013 Table for claims incurred prior to that date. For example, if a company begins to use the 2013 Table on January 1, 2020, for claims incurred after that date, it does not need to immediately convert all existing claims. This provision allows for the run-off of existing claims until December 31, 2022. As of that date (or an earlier date), the company must either continue use of the existing tables applicable to these claims or may convert all still open claims to the 2013 Table (adding the necessary data only for the remaining open claims).

5,000 claims terminations during the third through fifth claims durations on reasonably similar applicable policy forms. The request for such approval of a plan of modification to the reserve basis must be in writing and must include:

i. An analysis of the credibility of the experience;

ii. A description of how all of the insurer's experience is proposed to be used in setting reserves;

iii. A description and quantification of the margins to be included;

iv. A summary of the financial impact that the proposed plan of modification would have had on the insurer's last filed annual statement;

v. A copy of the approval of the proposed plan of modification by the commissioner of the state of domicile; and

vi. Any other information deemed necessary by the commissioner.

d. For claim reserves to reflect "sound values" and/or reasonable margins, reserve tables based on credible experience should be adjusted regularly to maintain reasonable margins.

40. On or after October 1, 2014, with respect to incurred claims subject to paragraph 39, each insurer may elect which of the following to use as the minimum morbidity standard for group long-term disability income claim reserves:

a. The minimum morbidity standard in effect for claim reserves as of the date the claim was incurred, or

b. The standards as defined in paragraph 41, applied to all open claims.

Once an insurer elects to calculate reserves for all open claims on a more recent standard, then all future valuations must be on that basis.

41. For group long-term disability income claims incurred on or after January 1, 2017, or the earlier date that is chosen for optional early adoption, but not before October 1, 2014, the minimum standards with respect to morbidity shall be based on the 2012 GLTD termination table with considerations of:

a. The insurer's own experience computed in accordance with Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*,

b. An adjustment to include an own experience measurement margin derived in accordance with Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*, and

c. A credibility factor derived in accordance with Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*.

42. An insurer may begin to use the minimum reserve standards in paragraph 41 at a date earlier than January 1, 2017, but not prior to October 1, 2014. An insurer may apply the standards in paragraph 41 to all open claims incurred prior to the effective date of paragraph 41 for the insurer. Once an insurer elects to calculate reserves for all open claims based on paragraph 41, all future valuations must be on that basis. This option with respect to Exhibit 1, paragraph 1.a.iii.(a) and paragraph 1.a.iii.(b) may be selected only if

the insurer maintains adequate claim records for claims incurred to use the 2013 Individual Disability Income (IDI) Valuation Table appropriately.

Minimum Morbidity Standards for Other Health Insurance Claim Reserves

43. The reserve shall be based on the insurer's experience, if such experience is considered credible, or upon other assumptions designed to place a sound value on the liabilities.

44. Claim Reserve Methods Generally – A generally accepted actuarial reserving method or other reasonable method, or a combination of methods may be used to estimate all claim liabilities. The methods used for estimating liabilities generally may be aggregate methods, or various reserve items may be separately valued. Approximations based on groupings and averages may also be employed. Adequacy of the claim reserves, however, shall be determined in the aggregate.

Premium Reserves

45. General:

  a. Except as noted in paragraph 46.b., unearned premium reserves are required for all contracts with respect to the period of coverage for which premiums, other than premiums paid in advance, have been paid beyond the date of valuation.

  b. Single premium credit disability insurance individual policies and group certificates are excluded from unearned premium reserve requirements of paragraphs 45-47.

  c. If premiums due and unpaid are carried as an asset, such premiums must be treated as premiums in force, subject to unearned premium reserve determination. The value of unpaid commissions, premium taxes, and the cost of collection associated with due and unpaid premiums must be carried as an offsetting liability.

  d. The gross premiums paid in advance for a period of coverage commencing after the next premium due date which follows the date of valuation may be appropriately discounted to the valuation date and shall be held as a separate liability.

46. Minimum Standards for Unearned Premium Reserves:

  a. The minimum unearned premium reserve with respect to any contract is the pro rata unearned modal premium that applies to the premium period beyond the valuation date, with such premium determined on the basis of:

    i. The valuation net modal premium on the contract reserve basis applying to the contract; or;

    ii. The gross modal premium for the contract if no contract reserve applies.

  b. However, in no event may the sum of the unearned premium and contract reserves for all contracts of the insurer subject to contract reserve requirements be less than the gross modal unearned premium reserve on all such contracts, as of the date of valuation. Such reserve shall never be less than the expected claims for the period beyond the valuation date represented by such unearned premium reserve, to the extent not provided for elsewhere.

47. Premium Reserve Methods Generally – The insurer may employ suitable approximations and estimates; including, but not limited to, groupings, averages and aggregate estimation; in computing premium reserves. Such approximations or estimates shall be tested periodically to determine their continuing adequacy and reliability.

Contract Reserves

48. General:

a. Contract reserves are required, unless otherwise specified in paragraph 48.b. for:

i. All individual and group contracts with which level premiums are used; or

ii. All individual and group contracts with respect to which, due to the gross premium pricing structure at issue, the value of the future benefits at any time exceeds the value of any appropriate future valuation net premiums at that time. This evaluation may be applied on a rating block basis if the total premiums for the block were developed to support the total risk assumed and expected expenses for the block each year, and a qualified actuary certifies the premium development. The actuary should state in the certification that premiums for the rating block were developed such that each year's premium was intended to cover that year's costs without any prefunding. If the premium is also intended to recover costs for any prior years, the actuary should also disclose the reasons for and magnitude of such recovery. The values specified in this paragraph shall be determined on the basis specified in paragraph 49.

iii. If rates are determined such that each year's premium is intended to cover that year's cost, the rating block approach results in no contract reserves unless required by paragraph 51. If rates are designed to prefund future years' costs, contract reserves will be required.

b. Contracts not requiring a contract reserve are contracts which cannot be continued after one year from issue and contracts already in force on January 1, 2001, for which no contract reserve was required under SSAP No. 54~~R~~, paragraph 42.

c. The contract reserve is in addition to claim reserves and premium reserves.

d. The methods and procedures for contract reserves shall be consistent with those for claim reserves for any contract, or else appropriate adjustment must be made when necessary to assure provision for the aggregate liability. The definition of the date of incurral must be the same in both determinations.

e. The total contract reserve established shall incorporate provisions for moderately adverse deviations.

49. Minimum Standards for Contract Reserves:

a. Basis:

i. Morbidity or other Contingency. Minimum standards with respect to morbidity are those set forth in Exhibit 1.

(a) Valuation net premiums used under each contract must have a structure consistent with the gross premium structure at issue of the contract as this relates to advancing age of insured, contract duration and period for which gross premiums have been calculated.

(b) Except as provided in paragraph 48.a.ii., if for a policy form there is no gross premium variation by age, the valuation net premiums will nonetheless vary based on age at issue for each contract since at issue the present value of valuation net premiums for a contract must equal the present value of tabular claim costs.

(c) Contracts for which tabular morbidity standards are not specified in Exhibit 1 shall be valued using tables established for reserve purposes by a qualified actuary. The morbidity tables shall contain a pattern of incurred claims cost that reflects the underlying morbidity and shall not be constructed for the primary purpose of minimizing reserves.

(d) Effective January 1, 2007, when determining the morbidity assumptions, the actuary shall use assumptions that represent the best estimate of anticipated future experience, but shall not incorporate any expectation of future morbidity improvement. Morbidity improvement is a change, in the combined effect of claim frequency and the present value of future expected claim payments given that a claim has occurred, from the current morbidity tables or experience that will result in a reduction to reserves. It is not the intent of this provision to restrict the ability of the actuary to reflect the morbidity impact for a specific known event that has occurred and that is able to be evaluated and quantified.

(e) Business in force prior to January 1, 2007, may be permitted to retain the original reserve basis, which may not meet the provisions of (d) above.

ii. Interest. The maximum interest rate is specified in Exhibit 1.

iii. Termination rates. Termination rates used in the computation of reserves shall be on the basis of a mortality table as specified in Exhibit 1 except as noted in the following paragraphs.

(a) Under contracts for which premium rates are not guaranteed, and where the effects of insurer underwriting are specifically used by policy duration in the valuation morbidity standard or for return of premium or other deferred cash benefits, total termination rates may be used at ages and durations where these exceed specified mortality table rates, but not in excess of the lesser of:

(1) Eighty percent of the total termination rate used in the calculation of the gross premiums, or

(2) Eight percent.

(b) For long-term care individual policies or group certificates, issued within the period January 1, 2001, to December 31, 2006, the contract reserve may be established on a basis of separate:

(1) Mortality (as specified in Exhibit 1) and

(2) Terminations other than mortality, where the terminations are not to exceed:

(i) For policy years one through four (4), the lesser of eighty percent (80%) of the voluntary lapse rate used in the calculation of gross premiums and eight percent (8%);

(ii) For policy years five (5) and later, the lesser of one hundred percent (100%) of the voluntary lapse rate used in the calculation of gross premiums and four percent (4%).

(c) For long-term care individual policies or group certificates issued on or after January 1, 2007, the contract reserve shall be established on the basis of:

(1) Mortality (as specified in Exhibit 1); and

(2) Terminations other than mortality, where the terminations are not to exceed:

(i) For policy year one, the lesser of eighty percent (80%) of the voluntary lapse rate used in the calculation of gross premiums and six percent (6%).

(ii) For policy years two (2) through four (4), the lesser of eighty percent (80%) of the voluntary lapse rate used in the calculation of gross premiums and four percent (4%).

(iii) For policy years five (5) and later, the lesser of one hundred percent (100%) of the voluntary lapse rate used in the calculation of gross premiums and two percent (2%), except certificates under policies issued to one or more employers or labor organizations, or to a trust or to the trustees of a fund established by one or more employers or labor organizations, or a combination thereof, for employees or former employees or a combination thereof, or for members or former members or a combination thereof, of a labor organization where the 2% shall be three percent (3%).

(d) Where a morbidity standard specified in Exhibit 1 is on an aggregate basis, such morbidity standard may be adjusted to reflect the effect of insurer underwriting by policy duration. The adjustments must be appropriate to the underwriting.

b. Reserve Method:

i. For insurance except long-term care and return of premium or other deferred cash benefits, the minimum reserve is the reserve calculated on the two-year full preliminary term method; that is, under which the terminal reserve is zero at the first and also the second contract anniversary.

ii. For long-term care insurance, the minimum reserve is the reserve calculated on the one-year full preliminary term method.

iii. (a) For return of premium or other deferred cash benefits, the minimum reserve is the reserve calculated as follows:

(1) On the one-year preliminary term method if the benefits are provided at any time before the twentieth anniversary;

(2) On the two-year preliminary term method if the benefits are only provided on or after the twentieth anniversary.

(b) The preliminary term method may be applied only in relation to the date of issue of a contract. Reserve adjustments introduced later, as a result of rate increases, revisions in assumptions (e.g., projected inflation rates) or for other reasons, are to be applied immediately as of the effective date of adoption of the adjusted basis.

c. Negative Reserves. Negative reserves on any benefit may be offset against positive reserves for other benefits in the same contract, but the total contract reserve with respect to all benefits combined may not be less than zero.

d. Nonforfeiture Benefits for Long-Term Care Insurance. The contract reserve on a policy basis shall not be less than the net single premium for the nonforfeiture benefits at the appropriate policy duration, where the net single premium is computed according to the above specifications.

50. Alternative Valuation Methods and Assumptions Generally – Provided the contract reserve on all contracts to which an alternative method or basis is applied is not less in the aggregate than the amount determined according to the applicable standards specified above; an insurer may use any reasonable assumptions as to interest rates, termination and/or mortality rates, and rates of morbidity or other contingency. Also, subject to the preceding condition, the insurer may employ methods other than the methods stated above in determining a sound value of its liabilities under such contracts, including but not limited to the following: the net level premium method; the one-year full preliminary term method; prospective valuation on the basis of actual gross premiums with reasonable allowance for future expenses; the use of approximations such as those involving age groupings, groupings of several years of issue, average amounts of indemnity, grouping of similar contract forms; the computation of the reserve for one contract benefit as a percentage of, or by other relation to, the aggregate contract reserves exclusive of the benefit or benefits so valued; and the use of a composite annual claim cost for all or any combination of the benefits included in the contracts valued.

51. Tests For Adequacy and Reasonableness of Contract Reserves:

a. Annually, an appropriate review shall be made of the insurer's prospective contract liabilities on contracts valued by tabular reserves, to determine the continuing adequacy and reasonableness of the tabular reserves giving consideration to future gross premiums. The insurer shall make appropriate increments to such tabular reserves if such tests indicate that the basis of such reserves is no longer adequate subject, however, to the minimum standards in paragraph 49.

b. In the event a company has a contract or a group of related similar contracts, for which future gross premiums will be restricted by contract, insurance department regulations, or for other reasons, such that the future gross premiums reduced by expenses for administration, commissions, and taxes will be insufficient to cover future claims, the company shall establish contract reserves for such shortfall in the aggregate.

Reinsurance

52. Increases to, or credits against reserves carried, arising because of reinsurance assumed or reinsurance ceded, must be determined in a manner consistent with these minimum reserve standards and with all applicable provisions of the reinsurance contracts which affect the insurer's liabilities.

Exhibit 1 Specific Standards For Morbidity, Interest And Mortality

Morbidity

1. Minimum morbidity standards for valuation of specified individual contract health insurance benefits are as follows:

a. Disability Income Benefits Due to Accident or Sickness

i. Contract Reserves for Contracts issued before January 1, 2020:

(a) The 1985 Commissioners Individual Disability Tables A (85CIDA); or

(b) The 1985 Commissioners Individual Disability Tables B (85CIDB).

(c) Each insurer shall elect, with respect to all individual contracts issued in any one statement year, whether it will use Tables A or Tables B as the minimum standard.

ii. Contract Reserves for Contracts issued on or after January 1, 2020:

The 2013 IDI Valuation Table with modifiers as described in Actuarial Guideline L. An insurer may begin to use the 2013 IDI Valuation Table with modifiers at a date earlier than January 1, 2020, but not prior to January 1, 2017.

Within three years of 2020, or the earlier date that an insurer begins to use the 2013 IDI Valuation Table, the insurer may elect to apply that morbidity standard for all policies issued subject to other valuation tables. This may be done if the following conditions are met:

(a) The insurer must apply the morbidity standard to all inforce policies and incurred claims;

(b) The insurer elects or has elected to apply the 2013 IDI Valuation Table to all claims incurred, regardless of incurred date;

(c) The insurer maintains adequate policy records on policies issued prior to 2020 that allow the insurer to apply the 2013 IDI Valuation Table appropriately; and

(d) Once an insurer elects to calculate reserves for all inforce policies based on the 2013 IDI Valuation Table morbidity standard, all future valuations must be on that basis

iii. Claim Reserves:

(a) For claims incurred from January 1, 2001, through December 31, 2001:

Each insurer may elect which of the following to use as the minimum standard for claims incurred prior to January 1, 2002:

(1) The minimum morbidity standard in effect for contract reserves on currently issued contracts, as of the date the claim is incurred, or

(2) The standard as defined in Exhibit 1, paragraph 1.a.iii.(b) on or after January 1, 2002, applied to all open claims, or

(3) The standard as defined in Exhibit 1, paragraph 1.a.iii.(c) on or after January 1, 2017, applied to all open non-worksite claims, provided the insurer maintains adequate claim records to allow the insurer to apply the standard defined in Exhibit 1, paragraph 1.a.iii.(c). This option is available whether claims incurred prior to January 1, 2002, were determined under Exhibit 1, paragraph 1.a.iii.(a) or paragraph 1.a.iii.(b).

(4) Once an insurer elects to calculate reserves for all open claims on the standard defined in Exhibit 1, in either paragraph 1.a.iii.(b) or paragraph 1.a.iii.(c), all future valuations must be on that basis.

(b) For claims incurred on or after January 1, 2002, and prior to January 1, 2020:

The 1985 Commissioners Individual Disability Table A (85CIDA) with claim termination rates multiplied by the following adjustment factors:

Duration	Adjustment Factor	Adjusted Termination Rates*
Week 1	0.366	0.04831
2	0.366	0.04172
3	0.366	0.04063
4	0.366	0.04355
5	0.365	0.04088
6	0.365	0.04271
7	0.365	0.04380
8	0.365	0.04344
9	0.370	0.04292
10	0.370	0.04107
11	0.370	0.03848
12	0.370	0.03478
13	0.370	0.03034
Month 4	0.391	0.08758
5	0.371	0.07346
6	0.435	0.07531
7	0.500	0.07245
8	0.564	0.06655
9	0.613	0.05520
10	0.663	0.04705
11	0.712	0.04486
12	0.756	0.04309
13	0.800	0.04080
14	0.844	0.03882
15	0.888	0.03730

Duration	Adjustment Factor	Adjusted Termination Rates*
16	0.932	0.03448
17	0.976	0.03026
18	1.020	0.02856
19	1.049	0.02518
20	1.078	0.02264
21	1.107	0.02104
22	1.136	0.01932
23	1.165	0.01865
24	1.195	0.01792
Year 3	1.369	0.16839
4	1.204	0.10114
5	1.199	0.07434
6 and later	1.000	**

* The adjusted termination rates derived from the application of the adjustment factors to the DTS Valuation Table termination rates shown in exhibits 3a, 3b, 3c, 4, and 5 (*Transactions of the Society of Actuaries* (TSA) XXXVII, pp. 457-463) is displayed. The adjustment factors for age, elimination period, class, sex, and cause displayed in exhibits 3a, 3b, 3c, and 4 should be applied to the adjusted termination rates shown in this table.

** Applicable DTS Valuation Table duration rate from exhibits 3c and 4 (TSA XXXVII, pp. 462-463).

The 85CIDA table so adjusted for the computation of claim reserves shall be known as 85CIDC (The 1985 Commissioners Individual Disability Table C).

(c) For claims incurred on or after 2020, the 2013 IDI Valuation Table with modifiers and adjustments for company experience as prescribed in Actuarial Guideline L, except for worksite disability policies with benefit periods of 24 months or less.

(d) For worksite disability policies, claim reserves may be calculated using claim run-out analysis or claim triangles, or other methods that place a sound value on the reserves that are appropriate for the business and risks involved.

b. Hospital Benefits, Surgical Benefits and Maternity Benefits (Scheduled benefits or fixed time period benefits only)

i. Contract Reserves:

The 1974 Medical Expense Tables, Table A, Transactions of the Society of Actuaries, Volume XXX, pg. 63. Refer to the paper (in the same volume, pg. 9) to which this table is appended, including its discussions, for methods of adjustment for benefits not directly valued in Table A: "Development of the 1974 Medical Expense Benefits," Houghton and Wolf.

ii. Claim Reserves:

No specific standard. See paragraph 1.f. of this Exhibit.

c. Cancer Expense Benefits

i. Contract Reserves:

(a) Contracts issued on or after January 1, 1986, and before January 1, 2019: The 1985 NAIC Cancer Claim Cost Tables (1985 CCCT).

(b) Contracts issued on or after January 1, 2019:

(i) For first occurrence and hospitalization benefits: The 2016 Cancer Claim Cost Valuation Tables (2016 CCCVT): *https://content.naic.org/sites/default/files/actuary-01-naic-2017-cancer-claim-cost-valuation-table.xlsx*.

(ii) For all other benefits: Assumptions based on company experience, relevant industry experience and actuarial judgement. Such assumptions should be appropriate for valuation which considers margin for adverse experience.

(iii) For contracts issued on or after January 1, 2018, and before January 1, 2019, a company may elect to use morbidity basis described in paragraphs (i.) and (ii). Once a company begins use of the 2016 CCCVT for new issues, it may not revert to the 1985 CCCT.

ii. Claim Reserves:

No specific standard. See paragraph 1.f. of this Exhibit.

d. Accidental Death Benefits

i. Contract Reserves:

The 1959 Accidental Death Benefits Table.

ii. Claim Reserves:

Actual amount incurred.

e. Single Premium Credit Disability

i. Contract Reserves:

(a) For contracts issued on or after January 1, 2002:

(i) For plans having less than a thirty-day elimination period, the 1985 Commissioners Individual Disability Table A (85CIDA) with claim incidence rates increased by twelve percent (12%).

(ii) For plans having a thirty-day and greater elimination period, the 85CIDA for a fourteen-day elimination period with the adjustment in Item (i).

(b) For contracts issued prior to January 1, 2002, each insurer may elect either Item (i) or (ii) to use as the minimum standard. Once an insurer elects to calculate reserves for all contracts on the standard defined in Item (a), all future valuations must be on that basis.

(i) The minimum morbidity standard in effect for contract reserves on currently issued contracts, as of the date the contract was issued, or

(ii) The standard as defined in Item (a), applied to all contracts.

ii. Claim Reserves:

Claim reserves are to be determined as provided in paragraph 44.

f. Other Individual Contract Benefits

i. Contract Reserves:

For all other individual contract benefits, morbidity assumptions are to be determined as provided in the reserve standards.

ii. Claim Reserves:

For all benefits other than disability, claim reserves are to be determined as provided in the standards.

2. Minimum morbidity standards for valuation of specified group contract health insurance benefits are as follows:

a. Disability Income Benefits Due to Accident or Sickness where this Appendix references this Exhibit; otherwise, Actuarial Guideline XLVII, as included in the most current version of the NAIC *Accounting Practices and Procedures Manual*.

i. Contract Reserves:

The 1987 Commissioners Group Disability Income Table (87CGDT).

ii. Claim Reserves:

The 1987 Commissioners Group Disability Income Table (87CGDT);

b. Single Premium Credit Disability

i. Contract Reserves:

(a) For contracts issued on or after January 1, 2002:

(i) For plans having less than a thirty-day elimination period, the 1985 Commissioners Individual Disability Table A (85CIDA) with claim incidence rates increased by twelve percent (12%).

(ii) For plans having a thirty-day and greater elimination period, the 85CIDA for a fourteen-day elimination period with the adjustment in item (i).

ii. For contracts issued prior to January 1, 2002, each insurer may elect either Item (a) or (b) to use as the minimum standard. Once an insurer elects to calculate reserves for all contracts on the standard defined in Item (a), all future valuations must be on that basis.

(a) The minimum morbidity standard in effect for contract reserves on currently issued contracts, as of the date the contract was issued, or

(b) The standard as defined in Item (a), applied to all contracts.

iii. Claim Reserves:

Claim reserves are to be determined as provided in paragraph 44.

c. Other Group Contract Benefits

i. Contract Reserves:

For all other group contract benefits, morbidity assumptions are to be determined as provided in the reserve standards.

ii. Claim Reserves:

For all benefits other than disability, claim reserves are to be determined as provided in the standards.

Interest

3. For contract reserves the maximum interest rate is the maximum rate allowed by Appendix A-820 in the valuation of whole life insurance issued on the same date as the health insurance contract.

4. For claim reserves on policies that require contract reserves, the maximum interest rate is the maximum rate allowed by Appendix A-820 in the valuation of whole life insurance issued on the same date as the claim incurral date.

5. For claim reserves on policies not requiring contract reserves, the maximum interest rate is the maximum rate allowed by Appendix A-820 in the valuation of single premium immediate annuities issued on the same date as the claim incurral date, reduced by 100 basis points.

Mortality

6. a. Unless paragraph 7 or paragraph 8 of this Exhibit 1 applies, the mortality basis used for all policies except long-term care individual policies and group certificates issued before January 1, 2001, shall be according to a table (but without use of selection factors) permitted by law for the valuation of whole life insurance issued on the same date as the health insurance contract.

b. For long-term care insurance individual policies or group certificates issued from January 1, 2001, through December 31, 2006, the mortality basis used shall be the 1983 Group Annuity Mortality Table without projection. For long-term care insurance individual policies or group certificates issued on or after January 1, 2007, the mortality basis used shall be the 1994 Group Annuity Mortality Static Table.

7. Other mortality tables adopted by the NAIC and promulgated by the commissioner may be used in the calculation of the minimum reserves if appropriate for the type of benefits and if approved by the commissioner. The request for approval shall include the proposed mortality table and the reason that the standard specified in paragraph 6.a. of this Exhibit 1 is inappropriate.

8. For single premium credit insurance using the 85CIDA table, no separate mortality shall be assumed.

Exhibit 2 Reserves for Waiver of Premium (Supplementary explanatory material)

1. Waiver of premium reserves involve several special considerations. First, the disability valuation tables promulgated by the NAIC are based on exposures that include contracts on premium waiver as in-force contracts. Hence, contract reserves based on these tables are NOT reserves on "active lives" but rather reserves on contracts "in force." This is true for the 1964 CDT and for both the 1985 CIDA and CIDB tables.

2. Accordingly, tabular reserves using any of these tables should value reserves on the following basis:

   a. Claim reserves should include reserves for premiums expected to be waived, valuing as a minimum the valuation net premium being waived.

   b. Premium reserves should include contracts on premium waiver as in-force contracts, valuing as a minimum the unearned modal valuation net premium being waived.

   c. Contract reserves should include recognition of the waiver of premium benefit in addition to other contract benefits provided for, valuing as a minimum the valuation net premium to be waived.

If an insurer is, instead, valuing reserves on what is truly an active life table, or if a specific valuation table is not being used but the insurer's gross premiums are calculated on a basis that includes in the projected exposure only those contracts for which premiums are being paid, then it may not be necessary to provide specifically for waiver of premium reserves. Any insurer using such a true "active life" basis should carefully consider, however, whether or not additional liability should be recognized on account of premiums waived during periods of disability or during claim continuation.

Appendix A-200

Separate Accounts Funding Guaranteed Minimum Benefits Under Group Contracts

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Actuarial Opinion and Memorandum Regulation (#822)

Scope

1. This appendix applies to a group life insurance contract providing survivor income benefits, a group annuity contract, or a funding agreement if the contract is a group contract that utilizes a separate account and provides guaranteed minimum benefits. This appendix shall not apply to modified guaranteed annuities or modified guaranteed life insurance or variable annuity or variable life insurance subject to appendices A-255, A-588, A-250, and A-270 or equity index products but this appendix shall apply to index contracts as defined in paragraph 18.

Definitions

2. "Account assets" means separate account assets plus any assets held in the general account or a supplemental account to meet the asset maintenance requirements.

3. "Account contracts" means the contracts providing guaranteed minimum benefits or other benefits and funded by a separate account and, if applicable, funded in part by the general account or a supplemental account to meet the asset maintenance requirements.

4. "Actuarial opinion" means the valuation actuary's opinion covering reserves for contract liabilities under account contracts that is required to be submitted to the commissioner.

5. "Actuarial memorandum" means the memorandum of the valuation actuary that supports the actuarial opinion covering reserves for contract liabilities under account contracts.

6. "Appointed actuary" means the qualified actuary appointed or retained either directly by or by the authority of the board of directors through an executive officer of the company to prepare the annual statement of actuarial opinion for the company as a whole.

7. "Asset maintenance requirements" means the requirement to maintain assets to fund contract benefits in accordance with paragraphs 30-45.

8. "Book value contract" means a fixed accumulation contract (GIC), purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer, that does not participate in the investment experience of a separate account, with a fixed interest rate guarantee, including a guarantee based on an external index, and that is supported by a separate account, the plan of operations of which provides that the separate account's assets are valued as if the assets were held in the insurance company's general account.

9. "Class of contracts" means the set of all contracts to which a given plan of operations pertains.

10. “Contract” means a group life insurance policy, group annuity contract, or funding agreement that is within the scope of this appendix as set forth in paragraph 1.

11. “Contract benefits” means the amounts obligated to be paid by the insurance company under an account contract.

12. “Contract liabilities” means the liabilities of the insurance company under account contracts, including liabilities with respect to which guarantees as to amount are provided by the insurance company and liabilities with respect to which guarantees as to amount are not provided by the insurance company.

13. a. “Derivative instrument” means an agreement, option, instrument or a series or combination of them:

i. 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

ii. 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.

b. Derivative instruments include options, warrants used in a hedging transaction and not attached to another financial instrument, caps, floors, collars, swaps, forwards, futures and any other agreements, options or substantially similar instruments or any series or combination of them.

14. “Duration” means, with respect to separate account or supplemental account assets or guaranteed contract liabilities, a measure of the price sensitivity of a stream of cash flows to interest rate movements, including, but not limited to, modified duration or option adjusted duration.

15. “General account” means the assets of the insurance company other than separate account and supplemental account assets, and associated reserves.

16. “Guaranteed minimum benefits” means benefits payable under the terms of the contract that are based on either (1) the greater of paragraph 16.a. or 16.b., or (2) paragraph 16.c. where:

a. Is that part of the market value of account assets that determines the contractholder’s benefits, i.e., to the extent the assets are beneficially “client” assets; provided, that if asset performance does not determine the contractholder’s benefit, this subparagraph equals zero;

b. Is a fixed minimum guarantee related to all or part of the considerations received under the contract; and

c. Is an amount based upon a publicly available interest rates series or an index of the aggregate market value of a group of publicly traded financial instruments, either of which is specified in the contract.

17. “Hedging transaction” means a derivative transaction, involving use of one or more derivative instruments, that is entered into and maintained to reduce:

a. The risk of a change in the value, yield, price, cash flow or quantity of assets or liabilities that the insurer has acquired or incurred or anticipates acquiring or incurring; or

b. The currency exchange risk or the degree of exposure as to assets or liabilities that an insurer has acquired or incurred or anticipates acquiring or incurring.

18. "Index contract" means a contract under which contract benefits shall be based upon a publicly available interest rate series or an index of the aggregate market value of a group of publicly traded financial instruments, either of which is specified in the contract, and that does not provide a guarantee of some or all of the consideration received plus earnings at a fixed rate specified in advance and that does not provide any secondary guarantees on elective benefits or maturity values.

19. "Market value separate account" means a separate account in which the separate account assets are valued at their market value.

20. "Nationally Recognized Statistical Rating Organization (NRSRO)" means a rating organization so designated by the Securities and Exchange Commission of the United States of America (SEC) which has applied to, and whose NRSRO status has been confirmed by, the NAIC Securities Valuation Office.

21. "Plan of operations" means a written plan meeting the requirements of paragraph 29.

22. "Prudent estimate" assumption means an assumption developed by applying a margin to the best estimate assumption for that risk.

23. "Qualified actuary" means an individual who is qualified to sign statements of actuarial opinion in accordance with the qualification standards set forth in Appendix A-820.

24. "Spot rate"

a. "Treasury-based spot rate corresponding to a given time of benefit payment means the yield on a zero-coupon non-callable and non-prepayable United States government obligation maturing at that time, or the zero-coupon yield implied by the price of a representative sampling of coupon-bearing, non-callable and non-prepayable United States government obligations in accordance with a formula set forth in the plan of operation.

b. "Index spot rate" corresponding to a given time of benefit payment means the zero-coupon yield implied by (x) the Barclays Short Term Corporate Index (for a given time of benefit payment under one year) or (y) the zero-coupon yield implied by the Barclays U.S. Corporate Investment Grade Bond Index (for a given time of benefit payment greater than or equal to one year).

c. "Blended spot rate" corresponding to a given time of benefit payment means a blend of 50% of each of (i) the Treasury-based spot rate, and (ii) the index spot rate. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country rates, in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the commissioner and which are supported by investments denominated in the currency of the foreign country, the Treasury-based spot rate component of the blended spot rate may be determined by reference to substantially similar obligations of the government of the foreign country. For liabilities other than those described above, the blended spot rate shall be determined on a basis mutually agreed upon by the insurer and the commissioner.

25. "Supplemental account" means a separate account to which assets may be contributed by the insurance company for the purpose of complying, in whole or in part, with the asset maintenance requirement and with respect to which neither the account contracts nor applicable law shall provide that the assets of the supplemental account are not chargeable with liabilities arising out of any other business of the insurance company.

26. "United States government obligation" means a direct obligation issued, assumed, guaranteed or insured by the United States of America or by an agency or instrumentality of the United States.

27. "Valuation actuary" means the appointed actuary or, alternatively, a qualified actuary designated by the appointed actuary to render the actuarial opinion. Written documentation of any such designation shall be on file at the company and available for review upon request.

Plan of Operations

28. The plan of operations for a class of contracts shall describe the financial implications for the insurer of the issuance of contracts in the class, and shall include at least the following:

a. A description of the class of contracts to which the plan of operations pertains. This should include a description of the products, the markets to which the products will be sold, the benefits that are being offered (including whether those benefits will be paid on a market or book value basis);

b. A statement of the investment policy for the separate account and any supplemental account, including requirements for diversification, maturity, type and quality of assets, and as applicable, target duration for matching guaranteed contract liabilities or the degree to which the investment policy is likely to match the performance of an interest rate series or index on which contract benefits are based;

c. A description of how the value of the separate account assets and any supplemental account is to be determined, including but not limited to, a statement of procedures and rules for valuing securities and other assets that are not publicly traded;

d. A description of how the guaranteed contract liabilities are to be valued, including, if applicable, with respect to guaranteed minimum benefits or other benefits, a description of the methodology for calculating spot rates and the rates proposed to be used to discount guaranteed contract liabilities if higher than the applicable spot rates, but the rate or rates used shall not exceed the blended spot rate, except that if the expected time of payment of a contract benefit is more than thirty (30) years, it shall be discounted from the expected time of payment to year thirty (30) at a rate of no more than eighty percent (80%) of the thirty-year blended spot rate and from year thirty (30) to the date of valuation at a rate not greater than the thirty-year blended spot rate, and shall conservatively reflect expected investment returns (taking into account foreign exchange risks);

e. A statement of how the separate account's operations are designed to provide for payment of contract benefits as they become due, including but not limited to:

i. A description of the method for estimating the amount and timing of benefit payments;

ii. The arrangements necessary to provide liquidity to cover contingencies;

iii. The method to be used to comply with the asset maintenance requirement;

iv. The manner in which account assets will be allocated between the separate account, any supplemental account, and the general account;

v. If applicable, the deductions to be used in determining the market value of an asset when determining the asset maintenance requirement when the investment policy of the separate account and any supplemental accounts is not likely to match the performance of an interest rate series or index on which contract benefits are based; and

vi. For index contracts, the deductions to be used for replicated (synthetic) asset transactions in determining the market value of the separate account.

vii. For market value separate accounts supporting contracts other than index contracts:

(a) A description of the criteria used by the insurer in approving for contract issuance a pooled fund representing multiple employer-sponsored plans;

(b) A description of risk-mitigation techniques used by the insurer in connection with contracts issued to pooled funds representing multiple employer-sponsored plans

f. If hedging transactions are to be utilized in managing separate account or any supplemental account assets, a description of the instruments and techniques and an explanation of how they are intended to reduce risk of loss;

g. If the amount of the asset maintenance requirement depends on the separate account, any supplemental account or a subportfolio of either being duration matched, a description of the method used to determine the durations of separate account and any supplemental account assets and guaranteed contract liabilities;

h. If a part of the asset maintenance requirement is to be met by maintaining a reserve liability in the general account, a description of:

i. The circumstances under which increases and decreases in the general account portion of the reserve liability will be made;

ii. The circumstances under which transfers will be made between the separate account and the general account; and

iii. Any arrangements needed to provide sufficient liquidity in the general account to enable the insurance company to make transfers to the separate account when due.

i. A statement as to the extent to which the contracts in the class will provide or applicable law does provide that the separate account assets shall not be chargeable with liabilities arising out of any other business of the insurance company; and

j. If any person other than the insurance company may authorize, approve or review the acquisition and disposition of investments for the separate account or any supplemental account, a statement of the safeguards adopted by the insurance company to assure that the actions to be taken by these persons are appropriate, including a description of the criteria used by the insurance company in selecting the person.

29. Notwithstanding the descriptions in the plan of operations, the insurance company may change the rate used pursuant to paragraph 35 to discount guaranteed contract liabilities and other items applicable to the separate account or any supplemental accounts, such as if the investment portfolio is different from that anticipated by the plan of operations, provided that the rates used shall not exceed the blended spot rates as prescribed in paragraph 28.d.

Asset Maintenance Requirements for Market Value Separate Accounts Supporting Contracts other than Index Contracts

30. At all times an insurer shall hold sufficient assets as a reserve in the general account, the separate account or supplemental accounts, as appropriate, such that the:

a. Market value of the assets held in the separate account, plus

b. The market value of any supplemental account, plus

c. Any assets held in the general account as a reserve for guaranteed contract liabilities, less

d. The deductions provided for in paragraph 31, equals or exceeds the value of guaranteed contract liabilities determined in accordance with paragraphs 35 and 36.

31. In determining compliance with the asset maintenance requirement and the reserve for guaranteed contract liabilities in accordance with paragraph 30, the insurance company shall deduct a percentage of the market value of the separate account or supplemental account asset or an amount attributable to a replicated (synthetic) asset transaction as follows:

a. For debt instruments, the percentage shall be the NAIC asset valuation reserve "reserve objective factor," but the factor shall be increased fifty percent (50%) for the purpose of this calculation if the difference in durations of the assets and liabilities is more than one-half year;

b. For assets that are not debt instruments, the percentage shall be the NAIC asset valuation reserve "maximum reserve factor"; and

c. For replicated (synthetic) asset transactions, the market value of the separate account or supplemental account assets shall be decreased by an amount equal to the asset valuation reserve for the transaction as if the transaction were occurring in the general account, determined in accordance with SSAP No. 7; but to the extent that the NAIC asset valuation reserve maximum reserve factor was not used in determining the amount of the deduction, the amount of the deduction shall be increased fifty percent (50%) for purposes of this calculation.

32. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by separate account or supplemental account assets denominated in the currency of the foreign country, the percentage deduction for these assets under paragraph 31 shall be that for a substantially similar investment denominated in the currency of the United States.

33. To the extent that guaranteed contract liabilities are denominated in the currency of the United States and are supported by separate account or supplemental account assets denominated in the currency of a foreign country, and to the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by separate account or supplemental account assets denominated in the currency of the United States, the deduction for debt instruments and replicated (synthetic) assets transactions under paragraph 31 shall be increased by fifteen percent (15%) of its market value unless the currency exchange risk has been adequately hedged, in which case the percentage deduction under paragraph 31 shall be increased by one-half percent (0.5%). No guaranteed contract liabilities denominated in the currency of a foreign country shall be supported by separate account or supplemental account assets denominated in the currency of another foreign country. For purposes of this paragraph, the currency exchange rate on an asset is deemed to be adequately hedged if:

a. It is an obligation of a jurisdiction that is rated in one of two (2) highest rating categories by an NRSRO or a political subdivision or other governmental unit of the jurisdiction, or is organized under the laws of the jurisdiction; and

b. At all times the principal amount and scheduled interest payments on the principal are hedged against the United States dollar pursuant to contracts or agreements that are:

i. Issued by or traded on a securities exchange or board of trade regulated under the laws of the United States or Canada or a province of Canada;

ii. Entered into with a United States banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations, that are rated in one of the two (2) highest rating categories by an NRSRO, or with a broker-dealer registered with the Securities and Exchange Commission that has net capital in excess of $250 million; or

iii. Entered into with any other banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an NRSRO and that is organized under the laws of a jurisdiction that is rated in one of the two (2) highest rating categories by an NRSRO.

34. All or a portion of the amount needed to comply with the asset maintenance requirement may be allocated to one or more supplemental accounts. If the account contract or applicable law provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurance company, the insurance company shall maintain in a supplemental account or the general account the amount of any account assets in excess of the sum of (i) the amounts contributed (net of withdrawals) by the contractholder, and (ii) the earnings attributable to the amounts contributed (net of withdrawals) by the contractholder.

35. For purposes of paragraphs 30-36, the minimum value of guaranteed contract liabilities is defined to be the sum of the expected guaranteed contract benefits, each discounted at a rate corresponding to the expected time of payment of the contract benefit that is not greater than the rate supportable by the expected return from the separate account and any supplemental account assets provided that the rate used shall not exceed the blended spot rates as prescribed in paragraph 28.d. or as described in the actuarial opinion. In calculating the minimum value of contract benefits, all guaranteed contract benefits potentially available to the contractholder shall be considered in the valuation process and analysis, and the reserve held shall be sufficient to fund the greatest present value of each independent guaranteed benefit stream, including guaranteed annuitization options available.

36. To the extent that future cash flows are dependent upon the benefit responsiveness features of an employer-sponsored plan, a best estimate or an estimate based on the insurance company's experience shall be used in the projections of the future cash flows. In addition, the valuation actuary shall periodically review the actual experience under the contract to validate the assumptions used. In projecting cash flows for contingent benefits involving mortality, the mortality tables for these benefits prescribed in Appendix A-820 shall be used.

37. The minimum value of guaranteed contract benefits under a contract issued to a pooled fund representing multiple employer-sponsored plans shall be determined so as to reflect projected plan sponsor contract value withdrawals available to the member plans in the pooled fund. Projections of such future cash flows shall take into account (i) known plan sponsor withdrawals, and (ii) a prudent estimate of future plan sponsor withdrawals. The prudent estimate shall be based on company experience and other relevant criteria.

38. A single valuation rate shall be determined equal to the lesser of:

a. The expected return from the separate account, or

b. The blended spot rate based on the duration of the separate account.

39. This single valuation rate shall be used to model future market values of the separate account. Future credited interest rates shall be modeled according to the contractually defined crediting rate formula. Modeled future contract values shall reflect modeled future market values, modeled future credited interest rates, known future plan sponsor withdrawals, the prudent estimate of future plan sponsor withdrawals, future withdrawals consistent with paragraph 37, and any remaining final payment at the modeled contract termination date.

40. All such modeled withdrawals and termination payments shall be discounted using the single valuation rate and the modeled times of those withdrawals and payments. The sum of these present values shall be deemed the minimum value of the guaranteed contract liabilities for a pooled fund contract.

Asset Maintenance Requirements for Market Value Separate Accounts Supporting Index Contracts

41. At all times an insurance company shall hold sufficient assets as a reserve in the general account, the separate account or supplemental accounts, as appropriate, such that the:

a. Market value of the assets held in the separate account, plus

b. The market value of any supplemental account, plus

c. Any assets held in the general account as a reserve for guaranteed contract liabilities, less

d. Any deduction provided for in paragraph 42, equals or exceeds the value of guaranteed contract liabilities determined in the manner set forth in the plan of operations.

42. In determining compliance with the asset maintenance requirement and the reserves for guaranteed contract liabilities in accordance with paragraph 41, the insurance company shall deduct a percentage of the market value of a separate account or supplemental account asset as set forth in the plan of operations, and for replication (synthetic asset) transactions, the value of the separate account or supplemental account assets shall be decreased in the manner set forth in the plan of operations.

43. All or a portion of the amount needed to comply with the asset maintenance requirement may be allocated to one or more supplemental accounts. If the account contract or applicable law provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurance company, the insurance company shall maintain in a supplemental account or the general account the amount of any account assets in excess of the sum of (i) the amounts contributed (net of withdrawals) by the contractholder, and (ii) the earnings attributable to the amounts contributed (net of withdrawals) by the contractholder.

Asset Maintenance Requirements for Separate Accounts Supporting Book Value Contracts

44. At all times an insurance company shall hold sufficient assets in the general account, the separate account or supplemental accounts, as appropriate, such that the value of the account assets, valued as if the assets were held in the insurance company's general account, equals or exceeds the reserve required for contracts supported by the separate account, determined as if the contracts were held in the general account.

45. All or any portion of the amount needed to comply with the asset maintenance requirement may be allocated to one or more supplemental accounts. If the account contract or applicable law provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurance company, the insurance company shall maintain in a supplemental account or the general account the amount of any account assets in excess of the sum of (i) the amounts contributed (net of withdrawals) by the contractholder, and (ii) the earnings attributable to the amounts contributed (net of withdrawals) by the contractholder.

Asset Valuation Reserve

46. When the insurance company values separate account or supplemental account assets at market and complies with the asset maintenance requirements of the section entitled Asset Maintenance Requirements for Market Value Separate Accounts Supporting Contracts other than Index Contracts or the section entitled Asset Maintenance Requirements for Market Value Separate Accounts Supporting Index Contracts, it need not maintain an asset valuation reserve with respect to these assets.

Reserve Valuation and Documentation

47. Reserves for contracts funded by a market value separate account supporting contracts other than index contracts shall be an amount equal to the following:

a. The total reserve required to be maintained on the valuation date under paragraphs 30-36;

b. Plus the excess, if any, of the market value of separate account assets (to the extent that the market value of the assets determines the contractholder's benefits, i.e., to the extent the assets are beneficially "client" assets) over the amount determined in accordance with paragraph 47.a.;

c. Plus any additional amount determined by the valuation actuary as necessary to make adequate provision for all of the contract liabilities.

48. Reserves for index contracts funded by a market value separate account shall be an amount equal to the following:

a. The total reserve required to be maintained on the valuation date under paragraphs 41-43;

b. Plus the excess, if any, of the market value of separate account assets (to the extent that the market value of the assets determines the contractholder's benefits, i.e., to the extent the assets are beneficially "client" assets) over the amount determined in accordance with paragraph 48.a.;

c. Plus any additional amounts determined by the valuation actuary as necessary to make adequate provision for all of the contract liabilities.

49. Reserves for book value contracts shall be determined as if the contracts were held in the general account.

50. The amount of any reserves required by paragraph 47.c. or paragraph 48.c. may be established by either:

a. Allocating sufficient assets to the separate account or a supplemental account to satisfy the requirement; or

b. Setting up the additional reserves in the general account.

51. Account assets shall make adequate provision for contract liabilities, taking into account any risk charge payable from the separate account assets and the amount of any reserve liability of the general account and amounts held in any supplemental account with respect to the asset maintenance requirement.

52. The level of risk charges, if any, payable to the general account shall be appropriate in view of such factors as the nature of the guaranteed contract liabilities and losses experienced in connection with account contracts and other pricing factors.

53. The fixed-income asset portfolio shall conform to and justify the rates used to discount contract liabilities for valuation pursuant to paragraph 35 if applicable.

54. The company shall document whether any rates used pursuant to paragraph 35 to discount guaranteed contract liabilities and other items applicable to the separate account or any supplemental account were modified from the rate or rates described in the plan of operations.

55. The company shall substantially conform with Appendix A-822 and maintain internal documentation to either:

a. Demonstrate the adequacy of account assets based upon cash flow analysis; or

b. Explain why cash flow analysis is not appropriate, describe the alternative methodology of asset adequacy testing used, and demonstrate the adequacy of account assets under such methodology.

56. The company's internal documentation pertaining to reserves for contract liabilities under account contracts shall also:

a. Clearly describe the assumptions used in projecting cash flows under each class of assets, and any dynamic portfolio hedging techniques utilized and the tests performed on the utilization of the techniques;

b. Clearly describe how the company reflected the risk of default on obligations and mortgage loans, including obligations and mortgage loans that are not investment grade;

c. Clearly describe how the company has reflected withdrawal risks, if applicable, including a discussion of the positioning of the contracts within the benefit withdrawal priority order pertaining to the contracts, the impact of any dynamic lapse assumption and the results of sensitivity testing the prudent estimate of future plan sponsor withdrawals pursuant to paragraphs 37-40;

d. If the plan of operations provides for investments in separate account or supplemental account assets other than United States government obligations, demonstrate that the rates used to discount contract liabilities pursuant to paragraph 35 conservatively reflect expected investment returns (taking into account any foreign exchange risks);

e. If the contracts provide that in certain circumstances they would cease to be funded by a separate account and, instead, would become contracts funded by the general account, clearly describe how any increased reserves would be provided for if and to the extent these circumstances occurred;

f. Document the amount of separate account assets that are not chargeable with liabilities arising out of any other business of the insurance company;

g. Document the amount of reserves and supporting assets as of December 31 and where the reserves and assets are shown in the annual statement;

h. Document the amount of any contingency reserve carried as part of surplus;

i. For book value contracts, document the market value of supporting assets; and

j. Where separate account assets are not chargeable with liabilities arising out of any other business of the insurance company, describe how the level of risk charges payable to the general account provider are appropriate compensation for the risk taken by the general account.

Appendix A-205

Illustrative Disclosure of Differences Between NAIC Statutory Accounting Practices and Procedures and Accounting Practices Prescribed or Permitted by the State of Domicile

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

XYZ Insurance Company
Footnotes to Financial Statements
December 31, 2002, and 2001

Note 1–Organization

The XYZ Company is a mutual life insurance company domiciled in the state of ABC and licensed to do business in all 50 states. The company markets traditional whole life, term and disability income insurance policies to individuals through its career agency force.

Notes 2–Basis of Presentation

The financial statements of XYZ Company are presented on the basis of accounting practices prescribed or permitted by the ABC Insurance Department.

The ABC Insurance Department recognizes only statutory accounting practices prescribed or permitted by the state of ABC for determining and reporting the financial condition and results of operations of an insurance company, for determining its solvency under the ABC Insurance Law. The National Association of Insurance Commissioners' (the "NAIC") *Accounting Practices and Procedures Manual* version effective January 1, 2001 ("NAIC SAP") has been adopted as a component of prescribed or permitted practices by the state of ABC. The state has adopted certain prescribed accounting practices which differ from those found in NAIC SAP. Specifically, 1) goodwill arising from the purchase of a subsidiary, controlled or affiliated entity is written off directly to surplus in the year it originates by ABC domiciled companies; in NAIC SAP, goodwill in amounts not to exceed 10% of an insurer's capital and surplus may be capitalized and all amounts of goodwill are amortized to unrealized gains and losses on investments over periods not to exceed 10 years, and 2) 100% of all fixed assets may be admitted by ABC domiciled companies; in NAIC SAP, fixed assets are not admitted. The Commissioner of Insurance has the right to permit other specific practices which deviate from prescribed practices.

The Company, with the explicit permission of the Commissioner of Insurance of the state of ABC, records the value of its home office building at fair market value instead of at the depreciated cost method required by NAIC SAP. If the home office building were carried at depreciated cost, home office property and statutory surplus would be decreased by $2,500,000 and $2,300,000 as of December 31, 2002 and 2001, respectively. Additionally, net income would be increased by $120,000 and $103,000 respectively, for the years then ended.

Illustration to use if prescribed or permitted statutory accounting practices (individually or in the aggregate), which differ from the NAIC basis of accounting, prevent the triggering of a regulatory event:

> If the reporting entity had not used the above prescribed and permitted practices that differ from the NAIC basis of accounting a risk based capital regulatory event would have been triggered. The company would have moved to a risk based capital company action level and the total adjusted capital would have been decreased by $300,000.

Illustration to use if prescribed or permitted practices statutory accounting practices, which differ from the NAIC basis of accounting, have no impact on regulatory events:

> If the reporting entity has not used the above prescribed and permitted practices that differ from the NAIC basis of accounting a risk based capital regulatory event would not have been triggered. The impact on net income and capital is shown in the following paragraphs.

A reconciliation of the Company's net income and capital and surplus between NAIC SAP and practices prescribed and permitted by the state of ABC is shown below.

	2002	**2001**
Net Income, ABC state basis	$3,200,000	$2,900,000
State Prescribed Practices:		
Depreciation of fixed assets	100,000	110,000
State Permitted Practices:		
Depreciation, home office property	120,000	103,000
Net Income, NAIC SAP	$3,420,000	$3,113,000
Statutory Surplus, ABC state basis	$30,000,000	$27,900,000
State Prescribed Practices:		
Goodwill, net	3,000,000	2,700,000
Fixed Assets, net	(850,000)	(950,000)
State Permitted Practices:		
Home Office Property	(2,500,000)	(2,300,000)
Statutory Surplus, NAIC SAP	$29,650,000	$27,350,000

Appendix A-225

Managing General Agents

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 53—Property and Casualty Contracts–Premiums
SSAP No. 54—Individual and Group Accident and Health Contracts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Definitions

1. "Managing General Agent" (MGA) means any person, firm, association or corporation who:

    a. Manages all or part of the insurance business of an insurer (including the management of a separate division, department or underwriting office); and

    b. Acts as an agent for such insurer whether known as a Managing General Agent, manager or other similar term, who, with or without the authority, either separately or together with affiliates, produces, directly or indirectly, and underwrites an amount of gross direct written premium equal to or more than five percent (5%) of the policyholder surplus as reported in the last annual statement of the insurer in any one quarter or year together with one or more of the following activities related to the business produced:

        i. Adjusts or pays claims in a material amount;

        ii. Negotiates reinsurance on behalf of the insurer.

    c. Notwithstanding the above, the following persons shall not be considered MGAs for the purposes of this Appendix:

        i. An employee of the insurer;

        ii. A U.S. Manager of the United States branch of an alien insurer;

        iii. An underwriting manager which, pursuant to contract, manages all or part of the insurance operations of the insurer, is under common control with the insurer, subject to a regulatory holding company act, if any, and whose compensation is not based on the volume of premiums written;

        iv. The attorney-in-fact authorized by and acting for the subscribers of a reciprocal insurer or inter-insurance exchange under powers of attorney.

2. "Underwrite" means the authority to accept or reject risk on behalf of the insurer.

Appendix A-235

Interest-Indexed Annuity Contracts

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definition

1. “Interest-indexed annuity contract” means any annuity contract where the interest credits are linked to an external reference.

Valuation Requirements

2. In developing life insurance reserves for interest-indexed annuity contracts, the insurer must be in compliance with the minimum requirements of Appendix A-820.

3. In the calculation of reserves for interest-indexed annuity contracts, future guarantees will be determined by assuming that future interest crediting rates will be equal to the statutory valuation interest rate for such contracts as defined in Appendix A-820.

Appendix A-250

Variable Annuities

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. “Variable annuity” means a policy or contract, individual or group, that provides for annuity benefits that vary according to the investment experience of a separate account or accounts maintained by the insurer as to the policy or contract.

2. The company shall maintain in each such separate account assets with a value at least equal to the reserves and other contract liabilities with respect to the account.

3. The reserve liability for variable annuities shall be established pursuant to the requirements of Appendix A-820 in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees.

Appendix A-255

Modified Guaranteed Annuities

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. A "Modified Guaranteed Annuity" is a deferred annuity contract, individual or group, the underlying assets of which are held in a separate account, and the values of which are guaranteed if held for specified periods. The contract contains nonforfeiture values that are based upon a market-value adjustment formula if held for shorter periods. This formula may or may not reflect the value of assets held in the separate account. The assets underlying the contract must be in a separate account during the period or periods when the contract holder can surrender the contract.

2. "Interest credits" means all interest that is credited to the contract.

3. "Separate account" means a separate account established pursuant to the insurance laws pertaining to the insurer.

Valuation Requirements

4. Reserve liabilities for modified guaranteed annuities shall be established as provided in Appendix A-820 in accordance with actuarial procedures that recognize:

   a. That assets of the separate account are based on market values;

   b. The variable nature of benefits provided; and

   c. Any mortality guarantees.

5. As a minimum, the separate account liability will equal the surrender value based upon the market-value adjustment formula contained in the contract. If that liability is greater than the market value of the assets, a transfer of assets will be made into the separate account so that the market value of the assets at least equals that of the liabilities. Any additional reserve that is needed to cover future guaranteed benefits shall be established.

6. The market-value adjustment formula, the interest guarantees, and the degree to which projected cash flow of assets and liabilities are matched must also be considered. The company shall determine whether the assets in the separate account are adequate to provide all future benefits that are guaranteed.

Separate Accounts

7. The insurer shall maintain in each separate account assets with a value at least equal to the valuation reserves and other contract liabilities respecting such account.

Appendix A-270

Variable Life Insurance

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. “Variable life insurance policy” means an individual or group policy that provides for life insurance the amount or duration of which varies according to the investment experience of any separate account or accounts established and maintained by the insurer as to the policy.

2. “Affiliate” of an insurer means a person, directly or indirectly, controlling, controlled by, or under common control with the insurer; a person who regularly furnishes investment advice to the insurer with respect to its separate accounts for which a specific fee or commission is charged; or any director, officer, partner or employee of the insurer, controlling or controlled person, or person providing investment advice or any member of the immediate family of such person.

3. “Assumed investment rate” means the rate of investment return that would be required to be credited to a variable life insurance policy, after deduction of charges for taxes, investment expenses and mortality and expense guarantees to maintain the variable death benefit equal at all times to the amount of death benefit, other than incidental insurance benefits, which would be payable under the plan of insurance if the death benefit did not vary according to the investment experience of the separate account.

4. “Benefit base” means the amount to which the net investment return is applied.

5. “Control” (including the terms “controlling,” “controlled by” and “under common control with”) means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or non-management services, or otherwise, unless the power is the result of an official position with or corporate office held by the person. Control shall be presumed to exist if a person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing more than ten percent (10%) of the voting securities of any other person. This presumption can be overcome by predominant evidence to the contrary, however, it shall stand until overcome by such predominant contradictory evidence.

6. “Flexible premium policy” means any variable life insurance policy other than a “scheduled premium policy” as defined in paragraph 13.

7. “General account” means all assets of the insurer other than assets in separate accounts.

8. “Incidental insurance benefit” means all insurance benefits in a variable life insurance policy, other than the variable death benefit and the minimum death benefit, including but not limited to, accidental death and dismemberment benefits, disability benefits, guaranteed insurability options, family income or term riders.

9. “Minimum death benefit” means the amount of the guaranteed death benefit, other than incidental insurance benefits, payable under a variable life insurance policy regardless of the investment performance of the separate account.

10. "Net investment return" means the rate of investment return in a separate account to be applied to the benefit base.

11. "Person" means an individual, corporation, partnership, association, trust or fund.

12. "Policy processing day" means the day on which charges authorized in the policy are deducted from the policy's cash value.

13. "Scheduled premium policy" means a variable life insurance policy under which both the amount and timing of premium payments are fixed by the insurer.

14. "Variable death benefit" means the amount of the death benefit, other than incidental insurance benefits, payable under a variable life insurance policy dependent on the investment performance of the separate account, which the insurer would have to pay in the absence of any minimum death benefit.

Valuation Requirements

15. Reserve liabilities for variable life insurance policies shall be established as provided in Appendix A-820 in accordance with actuarial procedures that recognize the variable nature of the benefits provided and any mortality guarantees.

16. Reserve liabilities for the guaranteed minimum death benefit shall be the reserve needed to provide for the contingency of death occurring when the guaranteed minimum death benefit exceeds the death benefit that would be paid in the absence of the guarantee, and shall be maintained in the general account of the insurer and shall not be less than the greater of the following minimum reserves:

a. The aggregate total of the term costs, if any, covering a period of one full year from the valuation date or, if less, covering the period provided for in the guarantee not otherwise provided for by the reserves held in the separate account, on each variable life insurance contract, assuming an immediate one-third depreciation in the current value of the assets in the separate account followed by a net investment return equal to the assumed investment rate; or

b. The aggregate total of the "attained age level" reserves on each variable life insurance contract. The "attained age level" reserve on each variable life insurance contract shall not be less than zero and shall equal the "residue," as described in paragraph 16.b.i. below, of the prior year's "attained age level" reserve on the contract, with any such "residue," increased or decreased by a payment computed on an attained age basis as described in paragraph 16.b.ii. below.

i. The "residue" of the prior year's "attained age level" reserve on each variable life insurance contract shall not be less than zero and shall be determined by adding interest at the valuation interest rate to the prior year's reserve, deducting the tabular claims based on the "excess," if any, of the guaranteed minimum death benefit over the death benefit that would be payable in the absence of a guarantee, and dividing the net result by the tabular probability of survival. The "excess" referred to in the preceding sentence shall be based on the actual level of death benefits that would have been in effect during the preceding year in the absence of the guarantee, taking appropriate account of the reserve assumptions regarding the distribution of death claim payments over the year.

ii. The payment referred to in this paragraph shall be computed so that the present value of a level payment of that amount each year over the future period for which charges for this risk will be collected under the contract, is equal to (A) minus (B) minus (C), where (A) is the present value of the future guaranteed minimum death benefits, (B) is the present value of the future death benefits that would be payable in the absence of such guarantee, and (C) is any “residue,” as described in paragraph 16.b.i. of the prior year’s “attained age level” reserve on such variable life insurance contract. This result shall be divided by the present value, at the valuation date, of a temporary life annuity of one per annum at the current attained age payable over the period in which future charges for this risk will be collected under the contract. If no future charges for this risk will be collected under the contract, the payment shall equal (A) minus (B) minus (C). The amounts of the future death benefits referred to in (B) shall be computed assuming a net investment return of the separate account which may differ from the assumed investment rate or the valuation interest but in no event may exceed the maximum interest rate permitted for the valuation of life contracts.

c. The valuation interest rate and mortality table used in computing the two minimum reserves described in 16 a. and 16 b. above shall conform to acceptable standards for the valuation of life insurance contracts. In determining the minimum reserves, the company may employ suitable approximations and estimates, including but not limited to groupings and averages.

17. Incidental Insurance Benefit. Reserve liabilities for all fixed incidental insurance benefits and any guarantees associated with variable accidental insurance benefits shall be maintained in the general account and reserve liabilities for all variable aspects of the variable incidental insurance benefits shall be maintained in a separate account, in amounts determined in accordance with the actuarial procedures appropriate to the benefit.

Separate Accounts

18. The assets of separate accounts shall be valued at least as often as variable benefits are determined but, in any event, at least monthly.

19. The insurer shall maintain in each separate account assets with a value at least equal to the valuation reserves and other contract liabilities respecting such account.

Appendix A-440

Insurance Holding Companies

Relevant SSAPs:
SSAP No. 25—Affiliates and Other Related Parties
SSAP No. 62—Property and Casualty Reinsurance

Definitions

1. “Affiliate.” An “affiliate” of, or person “affiliated” with, a specific person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.

2. “Control.” The term “control” (including the terms “controlling,” “controlled by” and “under common control with”) means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position with or corporate office held by the person. Control shall be presumed to exist if any person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent (10%) or more of the voting securities of any other person. This presumption can be overcome by predominant evidence to the contrary, however, it shall stand until overcome by such predominant contradictory evidence.

3. “Insurance Holding Company System.” An “insurance holding company system” consists of two (2) or more affiliated persons, one or more of which is an insurer.

4. “Person.” A “person” is an individual, a corporation, a limited liability company, a partnership, an association, a joint stock company, a trust, an unincorporated organization, any similar entity or any combination of the foregoing acting in concert, but shall not include any joint venture partnership exclusively engaged in owning, managing, leasing or developing real or tangible personal property.

5. “Securityholder.” A “securityholder” of a specified person is one who owns any security of such person, including common stock, preferred stock, debt obligations and any other security convertible into or evidencing the right to acquire any of the foregoing.

6. “Subsidiary.” A “subsidiary” of a specified person is an affiliate controlled by such person directly or indirectly through one or more intermediaries.

7. “Voting Security.” The term “voting security” shall include any security convertible into or evidencing a right to acquire a voting security.

Standards and Management of an Insurer Within a Holding Company System

8. Transactions Within a Holding Company System

9. Transactions within a holding company system to which an insurer subject to registration is a party shall be subject to the following standards:

a. The terms shall be fair and reasonable;

b. Charges or fees for services performed shall be reasonable;

c. Expenses incurred and payment received shall be allocated to the insurer in conformity with statutory accounting practices consistently applied;

d. The books, accounts and records of each party to all such transactions shall be so maintained as to clearly and accurately disclose the nature and details of the transactions including such accounting information as is necessary to support the reasonableness of the charges or fees to the respective parties; and

e. The insurer's surplus as regards policyholders following any dividends or distributions to shareholder affiliates shall be reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs. In determining whether an insurer's surplus as regards policyholders is reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs, the following factors, among others, shall be considered:

i. The size of the insurer as measured by its assets, capital and surplus, reserves, premium writings, insurance in force and other appropriate criteria;

ii. The extent to which the insurer's business is diversified among several lines of insurance;

iii. The number and size of risks insured in each line of business;

iv. The extent of the geographical dispersion of the insurer's insured risks;

v. The nature and extent of the insurer's reinsurance program;

vi. The quality, diversification and liquidity of the insurer's investment portfolio;

vii. The recent past and projected future trend in the size of the insurer's investment portfolio;

viii. The surplus as regards policyholders maintained by other comparable insurers;

ix. The adequacy of the insurer's reserves; and

x. The quality and liquidity of investments in affiliates.

Appendix A-585

Universal Life Insurance

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. “Cash surrender value” means the net cash surrender value plus any amounts outstanding as policy loans.

2. “Fixed premium universal life insurance policy” means a universal life insurance policy other than a flexible premium universal life insurance policy.

3. “Flexible premium universal life insurance policy” means a universal life insurance policy which permits the policyowner to vary, independently of each other, the amount or timing of one or more premium payments or the amount of insurance.

4. “Interest-indexed universal life insurance policy” means any universal life insurance policy where the interest credits are linked to an external referent.

5. “Net cash surrender value” means the maximum amount payable to the policyowner upon surrender.

6. “Policy value” means the amount to which separately identified interest credits and mortality, expense, or other charges are made under a universal life insurance policy.

7. “Universal life insurance policy” means a life insurance policy where separately identified interest credits (other than in connection with dividend accumulations, premium deposit funds, or other supplementary accounts) and mortality and expense charges are made to the policy. A universal life insurance policy may provide for other credits and charges, such as charges for the cost of benefits provided by rider.

Valuation Requirements

8. The minimum valuation standard for universal life insurance policies shall be the Commissioners Reserve Valuation Method, as described below for such policies, and the tables and interest rates specified below. The terminal reserve for the basic policy and any benefits and/or riders for which premiums are not paid separately as of any policy anniversary shall be equal to the net level premium reserves less (C) and less (D), where:

   a. Reserves by the net level premium method shall be equal to ((A)-(B))r where (A), (B) and “r” are as defined below:

      i. (A) is the present value of all future guaranteed benefits at the date of valuation.

      ii. (B) is the quantity $\frac{PVFB}{\ddot{a}_x}\ddot{a}_{x+t}$ where PVFB is the present value of all benefits guaranteed at issue assuming future guaranteed maturity premiums are paid by the policyowner and taking into account all guarantees contained in the policy or declared by the insurer.

b. $\ddot{a}_x$ and $\ddot{a}_{x+t}$ are present values of an annuity of one per year payable on policy anniversaries beginning at ages x and x+t, respectively, and continuing until the highest attained age at which a premium may be paid under the policy. The letter “x” is defined as the issue age and the letter “t” is defined as the duration of the policy.

c. The guaranteed maturity premium for flexible premium universal life insurance policies shall be that level gross premium, paid at issue and periodically thereafter over the period during which premiums are allowed to be paid, which will mature the policy on the latest maturity date, if any, permitted under the policy (otherwise at the highest age in the valuation mortality table), for an amount which is in accordance with the policy structure.[1] The guaranteed maturity premium is calculated at issue based on all policy guarantees at issue (excluding guarantees linked to an external referent). The guaranteed maturity premium for fixed premium universal life insurance policies shall be the premium defined in the policy which at issue provides the minimum policy guarantees.[2]

d. The letter “r” is equal to one, unless the policy is a flexible premium policy and the policy value is less than the guaranteed maturity fund, in which case “r” is the ratio of the policy value to the guaranteed maturity fund.

e. The guaranteed maturity fund at any duration is that amount which, together with future guaranteed maturity premiums, will mature the policy based on all policy guarantees at issue.

f. (C) is the quantity $((a)-(b))\frac{\ddot{a}_{x+t}}{\ddot{a}_x} r$ where (a)-(b) is as described in paragraph 9 of Appendix A-820 for the plan of insurance defined at issue by the guaranteed maturity premiums and all guarantees contained in the policy or declared by the insurer.

g. (D) is the sum of any additional quantities analogous to (C) which arise because of structural changes[3] in the policy, with each such quantity being determined on a basis consistent with that of (C) using the maturity date in effect at the time of the change.

[1] The maturity amount shall be the initial death benefit where the death benefit is level over the lifetime of the policy except for the existence of a minimum-death-benefit corridor, or shall be the specified amount where the death benefit equals a specified amount plus the policy value or cash surrender value except for the existence of a minimum-death-benefit corridor.

[2] The Guaranteed Maturity Premium for both flexible and fixed premium policies shall be adjusted for death benefit corridors provided by the policy. The Guaranteed Maturity Premium may be less than the premium necessary to pay all charges. This can especially happen in the first year for policies with large first year expense charges.

[3] Structural changes are those changes which are separate from the automatic workings of the policy. Such changes usually would be initiated by the policyholder and include changes in the guaranteed benefits, changes in latest maturity date, or changes in allowable premium payment period. For fixed premium universal life policies with redetermination of all credits and charges no more frequently than annually, on policy anniversaries, structural changes also include changes in guaranteed benefits, or in fixed premiums, unanticipated by the guaranteed maturity premium for such policies at the date of issue, even if such changes arise from automatic workings of the policy. The recomputation of (B) in paragraph 8.a.ii. above, for fixed premium universal life structural changes, shall exclude from PVFB, the present value of future guaranteed benefits, those guaranteed benefits which are funded by the excess of the insurer’s declared guarantees of interest, mortality and expenses, over the guarantees contained in the policy at the date of issue.

h. The guaranteed maturity premium, the guaranteed maturity fund and (B) above shall be recalculated to reflect any structural changes in the policy. This recalculation shall be done in a manner consistent with the descriptions above.

i. Future guaranteed benefits are determined by (1) projecting the greater of the guaranteed maturity fund and the policy value, taking into account future guaranteed maturity premiums, if any, and using all guarantees of interest, mortality, expense deductions, etc., contained in the policy or declared by the insurer; and (2) taking into account any benefits guaranteed in the policy or by declaration which do not depend on the policy value.

j. All present values shall be determined using (i) an interest rate (or rates) specified by Appendix A-820 for policies issued in the same year; (ii) the mortality rates specified by Appendix A-820 for policies issued in the same year; and (iii) any other tables needed to value supplementary benefits provided by a rider which is being valued together with the policy.

9. To the extent that the insurer declares guarantees more favorable than those in the policy (contractual guarantees), such declared guarantees shall be applicable to the determination of future guaranteed benefits.

10. The mortality and interest bases for calculating present values are the minimum standards in Appendix A-820.

11. In effecting structural changes, consistent methods are prescribed when calculating reserves. Several such methods are possible, but perhaps the simplest such method would be that of maintaining proportionality between the Guaranteed Maturity Fund and Guaranteed Maturity Premium values and the current face amount. In applying this method, Guaranteed Maturity Fund and Guaranteed Maturity Premium values could be calculated per dollar of face amount and simply multiplied by the new face amount. This would eliminate much of the complexity involved in other methods.

Alternative Minimum Reserves

12. If, in any policy year, the guaranteed maturity premium on any universal life insurance policy is less than the valuation net premium for such policy, calculated by the valuation method actually used in calculating the reserve thereon but using the minimum valuation standards of mortality and rate of interest, the minimum reserve required for such contract shall be the greater of a. or b.

a. The reserve calculated according to the method, the mortality table, and the rate of interest actually used.

b. The reserve calculated according to the method actually used but using the minimum valuation standards of mortality and rate of interest and replacing the valuation net premium by the Guaranteed Maturity Premium in each policy year for which the valuation net premium exceeds the Guaranteed Maturity Premium.

13. For universal life insurance reserves on a net level premium basis, the valuation net premium is:

$$\frac{PVFB}{\ddot{a}x}$$

and for reserves on a Commissioners Reserve Valuation Method, the valuation net premium is:

$$\frac{PVFB}{\ddot{a}x} + \frac{(a)-(b)}{\ddot{a}x}$$

Appendix A-588

Modified Guaranteed Life Insurance

The NAIC no longer maintains Model Law 588 as an NAIC sponsored model law; however, as this appendix is referenced in *SSAP No. 56—Separate Accounts*, the Statutory Accounting Principles (E) Working Group has chosen to retain this appendix as a valid NAIC standard.

Relevant SSAPs:
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. “Interest Credits” means all interest that is credited to the policy.

2. “Modified Guaranteed Life Insurance Policy” means an individual or group policy of life insurance, the underlying assets which are held in a separate account, and the values of which are guaranteed if held for specified periods. It contains cash-surrender values that are based upon a market value adjustment formula if held for shorter periods. The formula may, or may not, reflect the value of assets held in the separate account. The assets underlying the policy must be in a separate account during the period or periods when the policyholder can surrender the policy.

3. “Policy processing day” means the day on which charges authorized in the policy are deducted from the policy’s cash value.

4. “Separate account” means a separate account established pursuant to the insurance laws pertaining to the insurer.

Valuation Requirements

5. Reserve liabilities for modified guaranteed life insurance policies shall be established pursuant to the requirements of Appendix A-820 in accordance with actuarial procedures that recognize:

   a. That assets of the separate account are based on market value;

   b. The variable nature of the benefits provided; and

   c. Any mortality guarantees.

6. As a minimum, the separate account liability will equal the surrender value based upon the market value adjustment formula contained in the policy. If that liability is greater than the market value of the assets, a transfer of assets will be made into the separate account so that the market value of the assets at least equals that of the liabilities. Any additional reserve that is needed to cover future guaranteed benefits shall be established.

7. The market value adjustment formula, the interest guarantees and the degree to which projected cash flow of assets and liabilities are matched must also be considered. The company shall determine whether the assets in the separate account are adequate to provide all future guaranteed benefits.

8. Reserve liabilities for all fixed incidental insurance benefits and any guarantees associated with variable incidental insurance benefits shall be maintained in the general account.

Separate Accounts

9. The insurer shall maintain in each separate account assets with a value at least equal to the valuation reserves and other contract liabilities respecting such account.

Appendix A-620

Accelerated Benefits

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Purpose

The purpose of this Appendix is to provide guidance with respect to accelerated benefit related to individual and group life insurance policies. This Appendix shall apply to all accelerated benefits provisions of individual and group life insurance policies except those subject to Appendix A-641.

Definitions

1. “Accelerated benefits” covered under this Appendix are benefits payable under a life insurance contract:

    a. To a policyowner or certificateholder, during the lifetime of the insured, in anticipation of death or upon the occurrence of specified life-threatening or catastrophic conditions as defined by the policy or rider; and

    b. Which reduce the death benefit otherwise payable under the life insurance contract; and

    c. Which are payable upon the occurrence of a single qualifying event which results in the payment of a benefit amount fixed at the time of acceleration.

2. “Qualifying event” shall mean one or more of the following:

    a. A medical condition which would result in a drastically limited life span as specified in the contract, for example, twenty-four (24) months or less; or

    b. A medical condition which has required or requires extraordinary medical intervention, such as, but not limited to, major organ transplant or continuous artificial life support, without which the insured would die; or

    c. Any condition which usually requires continuous confinement in an eligible institution as defined in the contract if the insured is expected to remain there for the rest of his or her life; or

    d. A medical condition which would, in the absence of extensive or extraordinary medical treatment, result in a drastically limited life span. Such conditions may include, but are not limited to, one or more of the following:

        i. Coronary artery disease resulting in an acute infarction or requiring surgery;

        ii. Permanent neurological deficit resulting from cerebral vascular accident;

iii. End stage renal failure; or

iv. Acquired Immune Deficiency Syndrome.

Valuation Requirements

3. When benefits are provided through the acceleration of benefits under group or individual life policies or riders to such policies, policy reserves shall be determined in accordance with Appendix A-820. Mortality tables and interest for life insurance reserves as specified in Appendix A-820 shall be used as well as appropriate assumptions for the other provisions incorporated in the policy form. Reserves in the aggregate should be sufficient to cover:

a. Policies upon which no claim has yet arisen.

b. Policies upon which an accelerated claim has arisen.

4. For policies and certificates which provide actuarially equivalent benefits, no additional reserves need to be established.

5. Policy liens and policy loans, including accrued interest, represent assets of the company for statutory reporting purposes. For any policy on which the policy lien exceeds the policy's statutory reserve liability such excess must be held as a nonadmitted asset.

Appendix A-628

Title Insurance

Relevant SSAPs:
SSAP No. 57—Title Insurance

Definitions

1. “Abstract of title” or “abstract” means a written history, synopsis or summary of the recorded instruments affecting the title to real property.

2. “Affiliate” means a specific person that directly, or indirectly through one or more intermediaries, controls, or is controlled by or is under common control with the person specified.

3. “Bona fide employee” of the title insurer or title insurance agent means an individual who devotes substantially all of his or her time to performing services on behalf of a title insurer or title insurance agent and whose compensation for those services is in the form of salary or its equivalent paid by the title insurer or title insurance agent.

4. “Control” (including the terms “controlling,” “controlled by” and “under common control with”) means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position or corporate office held by the person. Control shall be presumed to exist if a person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent (10%) or more of the voting securities of another person. This presumption can be overcome by predominant evidence to the contrary; however, it shall stand until overcome by such predominant contradictory evidence.

5. “Escrow” means written instruments, money or other items deposited by one party with a depository, escrow agent or escrowee for delivery to another party upon the performance of a specified condition or the happening of a certain event.

6. “Escrow, settlement or closing fee” means the consideration for supervising or handling the actual execution, delivery or recording of transfer and lien documents and for disbursing funds.

7. “Net retained liability” means the total liability retained by a title insurer for a single risk, after taking into account any ceded liability and collateral, acceptable to the commissioner, maintained by the insurer.

8. “Person” means any natural person, partnership, association, cooperative, corporation, trust or other legal entity.

9. “Security” or “security deposit” means funds or other property received by the title insurer as collateral to secure an indemnitor’s obligation under an indemnity agreement pursuant to which the insurer is granted a perfected security interest in the collateral in exchange for agreeing to provide coverage in a title insurance policy for a specific title exception to coverage.

10. “Title insurance agent” or “agent” means an authorized person, other than a bona fide employee of the title insurer who, on behalf of the title insurer, performs the following acts, in conjunction with the issuance of a title insurance report or policy:

a. Determines insurability and issues title insurance reports or policies, or both, based upon the performance or review of a search or abstract of title; and

b. Performs one or more of the following functions:

i. Collects or disburses premiums, escrow or security deposits or other funds;

ii. Handles escrows, settlements or closings;

iii. Solicits or negotiates title insurance business; or

iv. Records closing documents.

11. "Title insurance business" or "business of title insurance" means:

a. Issuing as insurer or offering to issue as insurer a title insurance policy;

b. Transacting or proposing to transact by a title insurer any of the following activities when conducted or performed in contemplation of or in conjunction with the issuance of a title insurance policy:

i. Soliciting or negotiating the issuance of a title insurance policy;

ii. Guaranteeing, warranting or otherwise insuring the correctness of title searches for all instruments affecting titles to real property, any interest in real property, cooperative units and proprietary leases and for all liens or charges affecting the same;

iii. Handling of escrows, settlements or closings;

iv. Executing title insurance policies;

v. Effecting contracts of reinsurance; or

vi. Abstracting, searching or examining titles;

c. Guaranteeing, warranting or insuring searches or examinations of title to real property or any interest in real property; or

d. Guaranteeing or warranting the status of title as to ownership of or liens on real property and personal property by any person other than the principals to the transaction; or

e. Doing or proposing to do any business substantially equivalent to any of the activities listed in this paragraph in a manner designed to evade the provisions of this Appendix.

12. "Title insurance policy" or "policy" means a contract insuring or indemnifying owners of, or other persons lawfully interested in, real or personal property or any interest in real property, against loss or damage arising from any or all of the following conditions existing on or before the policy date and not excepted or excluded:

a. Defects in or liens or encumbrances on the insured title;

b. Unmarketability of the insured title;

c. Invalidity, lack of priority or unenforceability of liens or encumbrances on the stated property;

d. Lack of legal right of access to the land; or

e. Unenforceability of rights in title to the land.

13. "Title insurance report" or "report" means a preliminary report, commitment or binder issued prior to the issuance of a title insurance policy containing the terms, conditions, exceptions and any other matters incorporated by reference under which the title insurer is willing to issue its title insurance policy.

14. "Title insurer" or "insurer" means a company organized for the purpose of transacting the business of title insurance.

15. "Title plant" means a set of records consisting of documents, maps, surveys or entries affecting title to real property or any interest in or encumbrance on the property, which have been filed or recorded in the jurisdiction for which the title plant is established or maintained.

Admitted Asset Standards

16. An investment in a title plant or plants in an amount equal to the actual cost shall be allowed as an admitted asset for title insurers. The aggregate amount of the investment shall not exceed the lesser of twenty percent (20%) of admitted assets or forty percent (40%) of surplus to policyholders, both as required to be shown on the statutory balance sheet of the insurer for its most recently filed statement with the domiciliary state commissioner; if the amount of the investment exceeds the above limits, the excess amount shall be recorded as a nonadmitted asset.

Reserves

17. A title insurer shall establish and maintain:

a. A known claim reserve in an amount estimated to be sufficient to cover all unpaid losses, claims and allocated loss adjustment expenses arising under title insurance policies, guaranteed certificates of title, guaranteed searches and guaranteed abstracts of title, and all unpaid losses, claims and allocated loss adjustment expenses for which the title insurer may be liable, and for which the insurer has received notice by or on behalf of the insured, holder of a guarantee or escrow or security depositor.

b. A Statutory or Unearned Premium Reserve consisting of:

i. The amount of the statutory or unearned premium or reinsurance reserve legally held at December 31, 2000. The balance of this reserve shall be released in accordance with the state laws in effect prior to January 1, 2001; and

ii. For those title insurance policies and guarantees written after January 1, 2001, reserves shall be established that are equal to the sum of the following items, as set forth in the title insurer's most recent annual statement:

(a) For each title insurance policy on a single risk written or assumed, an amount, as determined by the insurer's state of domicile, per $1,000 of net retained liability for policies under $500,000 and for policies of $500,000 or greater, or any other reasonable method as required by the insurer's state of domicile; and

(b) An amount as determined by the insurer's state of domicile for the escrow, settlement and closing fees collected in contemplation of the issuance of title insurance policies or guarantees.

iii. The aggregate of the amounts set aside in this reserve in any calendar year pursuant to paragraph 17.b.ii. shall be released from the reserve and restored to net profits over a period of twenty (20) years pursuant to the following formula: thirty-five percent (35%) of the aggregate sum on July 1 of the year next succeeding the year of addition; fifteen percent (15%) of the aggregate sum on July 1 of each of the succeeding two (2) years; ten percent (10%) of the aggregate sum on July 1 of the next succeeding year; three percent (3%) of the aggregate sum on July 1 of each of the next three (3) succeeding years; two percent (2%) of the aggregate sum on July 1 of each of the next three (3) succeeding years; and one percent (1%) of the aggregate sum on July 1 of each of the next succeeding ten (10) years.

iv. The insurer shall calculate a retroactive adjusted statutory or unearned premium reserve on an aggregate basis at January 1, 2001. The adjusted aggregate reserve shall be calculated as if Subsection b. ii. had been in effect for all years beginning twenty (20) years prior to January 1, 2001. If the adjusted aggregate reserve exceeds the aggregate amount set aside for statutory or unearned premiums in the insurer's December 31, 2000 annual statement, the insurer shall–increase its statutory or unearned premium reserve by an amount equal to one-sixth of that excess in each of the succeeding six years, commencing with the 2001 calendar year.

v. The aggregate of the amounts set aside in this reserve in any calendar year as adjustments to the insurer's statutory or unearned premium reserve pursuant to Subsection b. iv. shall be released from the reserve and restored to net profits, or equity if the additions required by paragraph 17.b.iv. of this section reduced equity directly, over a period not exceeding ten (10) years pursuant to the following table:

Year of Addition	Release
2001	Equally over 10 years
2002	Equally over 9 years
2003	Equally over 8 years
2004	Equally over 7 years
2005	Equally over 6 years
2006	Equally over 5 years

c. A supplemental reserve shall be established consisting of any other reserves necessary, when taken in combination with the reserves required by paragraphs 17.a. and 17.b. to cover the company's liabilities with respect to all losses, claims and loss adjustment expenses.

Appendix A-630

Mortgage Guaranty Insurance

Relevant SSAPs:
SSAP No. 58—Mortgage Guaranty Insurance

Definitions

1. “Mortgage guaranty insurance” is:

   a. Insurance against financial loss by reason of nonpayment of principal, interest or other sums agreed to be paid under the terms of any note or bond or other evidence of indebtedness secured by a mortgage, deed of trust, or other instrument constituting a lien or charge on real estate, provided the improvement on such real estate is a residential building or a condominium unit or buildings designed for occupancy by not more than four families.

   b. Insurance against financial loss by reason of nonpayment of principal, interest or other sums agreed to be paid under the terms of any note or bond or other evidence of indebtedness secured by a mortgage, deed of trust, or other instrument constituting a lien or charge on real estate, providing the improvement on such real estate is a building or buildings designed for occupancy by five (5) or more families or designed to be occupied for industrial or commercial purposes.

   c. Insurance against financial loss by reason of nonpayment of rent or other sums agreed to be paid under the terms of a written lease for the possession, use or occupancy of real estate, provided the improvement on such real estate is a building or buildings designed to be occupied for industrial or commercial purposes.

2. “Authorized real estate security” for the purpose of this Appendix means an amortized note, bond or other evidence of indebtedness, not exceeding ninety-five percent (95%) of the fair market value of the real estate, secured by a mortgage, deed of trust, or other instrument which constitutes, or is equivalent to, a first lien or charge on real estate; provided:

   a. The real estate loan secured in such manner is one of a type which a bank, savings and loan association, or an insurance company, which is supervised and regulated by a state department or the federal government, is authorized to make, or would be authorized to make, disregarding any requirement applicable to such an institution that the amount of the loan not exceed a certain percentage of the value of the real estate.

   b. The improvement on such real estate is a building or buildings designed for occupancy as specified by paragraphs 1.a. and 1.b. of this Appendix.

   c. The lien on such real estate may be subject to and subordinate to the following:

      i. The lien of any public bond, assessment or tax, when no installment, call or payment of or under such bond, assessment or tax is delinquent.

      ii. Outstanding mineral, oil, water or timber rights, rights-of-way, easements or rights-of-way of support, sewer rights, building restrictions or other restrictions or covenants, conditions or regulations of use, or outstanding leases upon such real property under which rents or profits are reserved to the owner thereof.

3. “Contingency reserve” means an additional premium reserve established to protect policyholders against the effect of adverse economic cycles.

Investment Limitation

4. A mortgage guaranty insurance company shall not report as an admitted asset notes or other evidences of indebtedness secured by mortgage or other lien upon real property. This provision shall not apply to obligations secured by real property, or contracts for the sale of real property, which obligations or contracts of sale are acquired in the course of the good faith settlement of claims under policies of insurance issued by the mortgage guaranty insurance company, or in the good faith disposition of real property so acquired.

Reserves

5. Unearned Premium Reserves – A mortgage guaranty insurance company shall compute and maintain an unearned premium reserve.

6. Loss Reserve – A mortgage guaranty insurance company shall compute and maintain adequate case basis and other loss reserves which accurately reflect loss frequency and loss severity and shall include components for claims reported and for claims incurred but not reported, including estimated losses on:

a. Insured loans which have resulted in the conveyance of property which remains unsold;

b. Insured loans in the process of foreclosure;

c. Insured loans in default for four (4) months or for any lesser period which is defined as default for such purposes in the policy provisions; and

d. Insured leases in default for four (4) months or for any lesser period which is defined as default for such purposes in policy provisions.

7. Contingency Reserve – Each mortgage guaranty insurance company shall compute and maintain a contingency reserve.

8. Reinsurance – Whenever a mortgage guaranty insurance company obtains reinsurance from an insurance company which is properly licensed to provide such reinsurance or from an appropriate governmental agency, the mortgage guaranty insurer and the reinsurer shall establish and maintain the reserves required in this Appendix in appropriate proportions in relation to the risk retained by the original insurer and ceded to the assuming reinsurer so that the total reserves established shall not be less than the reserves required by this Appendix.

Appendix A-641

Long-Term Care Insurance

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 54—Individual and Group Accident and Health Contracts

Relevant NAIC Model Laws/Regulations:
Health Insurance Reserves Model Regulation (#010)
Standard Valuation Law (#820)

Definitions

1. "Long-term care insurance" means any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than twelve (12) consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis; for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital. Such term includes group and individual annuities and life insurance policies or riders which provide directly or which supplement long-term care insurance. Such term also includes a policy or rider which provides for payment of benefits based upon cognitive impairment or the loss of functional capacity. The term shall also include qualified long-term care insurance contracts. Long-term care insurance may be issued by insurers; fraternal benefit societies; nonprofit health, hospital, and medical service corporations; prepaid health plans; health maintenance organizations or any similar organization to the extent they are otherwise authorized to issue life or health insurance. Long-term care insurance shall not include any insurance policy which is offered primarily to provide basic Medicare supplement coverage, basic hospital expense coverage, basic medical-surgical expense coverage, hospital confinement indemnity coverage, major medical expense coverage, disability income or related asset-protection coverage, accident only coverage, specified disease or specified accident coverage, or limited benefit health coverage. With regard to life insurance, this term does not include life insurance policies which accelerate the death benefit specifically for one or more of the qualifying events of terminal illness, medical conditions requiring extraordinary medical intervention, or permanent institutional confinement, and which provide the option of a lump-sum payment for those benefits and in which neither the benefits nor the eligibility for the benefits is conditioned upon the receipt of long-term care. Notwithstanding any other provision contained herein, any product advertised, marketed or offered as long-term care insurance shall be subject to the provisions of this Appendix.

2. "Applicant" means:

   a. In the case of an individual long-term care insurance policy, the person who seeks to contract for benefits, and

   b. In the case of a group long-term care insurance policy, the proposed certificate holder.

3. "Certificate" means, for the purposes of this Appendix, any certificate issued under a group long-term care insurance policy, which policy has been delivered or issued for delivery.

4. "Group long-term care insurance" means a long-term care insurance policy which is delivered or issued for delivery to:

   a. One or more employers or labor organizations, or to a trust or to the trustees of a fund established by one or more employers or labor organizations, or a combination thereof, for employees or former employees or a combination thereof or for members or former members or a combination thereof, of the labor organizations; or

b. Any professional, trade or occupational association for its members or former or retired members, or combination thereof, if such association:

i. Is composed of individuals all of whom are or were actively engaged in the same profession, trade or occupation; and

ii. Has been maintained in good faith for purposes other than obtaining insurance; or

c. An association or a trust or the trustee(s) of a fund established, created or maintained for the benefit of members of one or more associations. Prior to advertising, marketing or offering such policy, the association or associations, or the insurer of the association or associations, shall evidence that the association or associations have at the outset a minimum of 100 persons and have been organized and maintained in good faith for purposes other than that of obtaining insurance; have been in active existence for at least one year; and have a constitution and bylaws which provide that:

i. The association or associations hold regular meetings not less than annually to further purposes of the members;

ii. Except for credit unions, the association or associations collect dues or solicit contributions from members; and

iii. The members have voting privileges and representation on the governing board and committees.

5. "Policy" means, for the purposes of this Appendix, any policy, contract, subscriber agreement, rider or endorsement delivered or issued for delivery by an insurer; fraternal benefit society; nonprofit health, hospital, or medical service corporation; prepaid health plan; health maintenance organization or any similar organization.

6. a. "Qualified long-term care insurance contract" or "federally tax-qualified long-term care insurance contract" means an individual or group insurance contract that meets the requirements of Section 7702B(b) of the Internal Revenue Code of 1986, as amended, as follows:

i. The only insurance protection provided under the contract is coverage of qualified long-term care services. A contract shall not fail to satisfy the requirements of this subparagraph by reason of payments being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate;

ii. The contract does not pay or reimburse expenses incurred for services or items to the extent that the expenses are reimbursable under Title XVIII of the Social Security Act, as amended, or would be so reimbursable but for the application of a deductible or coinsurance amount. The requirements of this subparagraph do not apply to expenses that are reimbursable under Title XVIII of the Social Security Act only as a secondary payor. A contract shall not fail to satisfy the requirements of this subparagraph by reason of payments being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate;

iii. The contract is guaranteed renewable, within the meaning of section 7702B(b)(1)(C) of the Internal Revenue Code of 1986, as amended;

iv. The contract does not provide for a cash surrender value or other money that can be paid, assigned, pledged as collateral for a loan, or borrowed except as provided in subparagraph 6.a.v. below;

v. All refunds of premiums, and all policyholder dividends or similar amounts, under the contract are to be applied as a reduction in future premiums or to increase future benefits, except that a refund on the event of death of the insured or a complete surrender or cancellation of the contract cannot exceed the aggregate premiums paid under the contract; and

vi. The contract meets the consumer protection provisions set forth in Section 7702B(g) of the Internal Revenue Code of 1986, as amended.

b. "Qualified long-term care insurance contract" or "federally tax-qualified long term care insurance contract" also means the portion of a life insurance contract that provides long-term care insurance coverage by rider or as part of the contract and that satisfies the requirements of Sections 7702B(b) and (e) of the Internal Revenue Code of 1986, as amended.

Valuation Requirements

7. When long-term care benefits are provided through the acceleration of benefits under group or individual life policies or riders to such policies, policy reserves for the benefits shall be determined in accordance with Appendix A-820. Claim reserves shall also be established in the case when the policy or rider is in claim status.

8. Reserves for policies and riders subject to this Appendix should be based on the multiple decrement model utilizing all relevant decrements except for voluntary termination rates. Single decrement approximations are acceptable if the calculation produces essentially similar reserves, if the reserve is clearly more conservative, or if the reserve is immaterial. The calculations may consider the reduction in life insurance benefits due to the payment of long-term care benefits. However, in no event shall the reserves for the long-term care benefit and the life insurance benefit be less than the reserves for the life insurance benefit assuming no long-term care benefit.

9. In the development and calculation of reserves for policies and riders subject to this Appendix, due regard shall be given to the applicable policy provisions, marketing methods, administrative procedures and all other considerations which have an impact on projected claim costs, including, but not limited to, the following:

a. Definition of insured events;

b. Covered long-term care facilities;

c. Existence of home convalescence care coverage;

d. Definition of facilities;

e. Existence or absence of barriers to eligibility;

f. Premium waiver provision;

g. Renewability;

h. Ability to raise premiums;

i. Marketing method;

j. Underwriting procedures;

k. Claims adjustment procedures;

l. Waiting period;

m. Maximum benefit;

n. Availability of eligible facilities;

o. Margins in claim costs;

p. Optional nature of benefit;

q. Delay in eligibility for benefit;

r. Inflation protection provisions; and

s. Guaranteed insurability option.

10. When long-term care benefits are provided other than as in the above, reserves shall be determined in accordance with Appendix A-010.

Appendix A-695

Synthetic Guaranteed Investment Contracts

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Actuarial Opinion and Memorandum Regulation (#822)

Scope and Application

1. This appendix applies to that portion of a group annuity contract or other agreement described in paragraph 25 and issued by a life insurer:

   a. That functions as an accounting record for an accumulation fund; and

   b. That has benefit guarantees relating to a principal amount and levels of interest at a fixed rate of return specified in advance.

2. The fixed rates of return:

   a. Shall be constant over the applicable rate periods;

   b. May reflect prior and current market conditions with respect to the segregated portfolio; and

   c. Shall not reference future changes in market conditions.

3. The updates to the appendix related to interest rates, including revisions to the method for determining the discount rate applied to the calculation of the minimum value of guaranteed contract liabilities, as primarily reflected in paragraph 29, and the definition of the blended spot rate are effective on or after January 1, 2016, for all[1] contracts inforce and contracts issued on or after the effective date.

Definitions

4. "Account assets" means the assets in the segregated portfolio plus any assets held in the general account or a separate account to meet the asset maintenance requirements.

5. "Actuarial opinion and memorandum" means the valuation actuary's opinion and memorandum covering synthetic guaranteed investment contract liabilities that is required to be submitted to the commissioner.

[1] This appendix is not intended to apply to contingent deferred annuities (CDAs), defined in the Contingent Deferred Annuity (A) Working Group recommendation on CDAs adopted by the Life Insurance and Annuities (A) Committee on April 7, 2013, (NAIC Proceedings, Spring 2013, Volume 1, pdf page 416) as "an annuity contract that establishes a life insurer's obligation to make periodic payments for the annuitant's lifetime at the time designated investments, which are not owned or held by the insurer, are depleted to a contractually defined amount due to contractually permitted withdrawals, market performance, fees and/or other charges."

6. “Appointed actuary” means the qualified actuary appointed or retained either directly by or by the authority of the board of directors through an executive officer of the company to prepare the annual statement of actuarial opinion for the company as a whole.

7. “Asset maintenance requirement” means the requirement to maintain assets to fund contract benefits in accordance with paragraph 29 of this appendix.

8. “Class of contracts” means the set of all contracts to which a given plan of operation pertains.

9. “Contract value record” means an accounting record, provided by the contract in relation to a segregated portfolio of assets, that is credited with a fixed rate of return over regular periods, and that is used to measure the extent of the insurer’s obligation to the contractholder. The fixed rate of return credited to the contract value record is determined by means of a crediting rate formula or declared at the inception of the contract and valid for the entire term of the contract.

10. “Crediting rate formula” means a mathematical formula used to calculate the fixed rate of return credited to the contract value record during any rate period and based in part upon the difference between the contract value record and the market value record amortized over an appropriate period. The fixed rate of return calculated by means of this formula may reflect prior and current market conditions with respect to the segregated portfolio, but may not reference future changes in market conditions.

11. “Duration” means, with respect to the segregated portfolio assets or guaranteed contract liabilities, a measure of price sensitivity to changes in interest rates, such as the Macaulay duration or option-adjusted duration.

12. “Fair market value” means a reasonable estimate of the amount that a knowledgeable buyer of an asset would be willing to pay, and a knowledgeable seller of an asset would be willing to accept, for the asset without duress in an arm's length transaction. In the case of a publicly traded security, the fair market value is the price at which the security is traded or, if no price is available, a price that appropriately reflects the latest bid and asked prices for the security. In the case of a debt instrument that is not publicly traded, the fair market value is the discounted present value of the asset calculated at a reasonable discount rate. For all other non-publicly traded assets, fair market value will be determined in accordance with valuation practices customarily used within the financial industry.

13. “Guaranteed minimum benefits” means contract benefits on a specified date that may be either:

a. A principal guarantee, with or without a fixed minimum interest rate guarantee, related to the segregated portfolio;

b. An assurance as to the future investment return or performance of the segregated portfolio; or

c. The fair market value of the segregated portfolio, to the extent that the fair market value of the assets determines the contractholder’s benefits.

14. a. “Hedging instrument” means:

i. An interest rate futures agreement or foreign currency futures agreement, an option to purchase or sell an interest rate futures agreement or foreign currency futures agreement, or any option to purchase or sell a security or foreign currency, used in a bona fide hedging transaction; or

ii. A financial agreement or arrangement entered into with a broker, dealer or bank, qualified under applicable federal and state securities or banking law and regulation, in connection with investment in one or more securities in order to reduce the risk of changes in market valuation or to create a synthetic investment that, when added to the portfolio, reduces the risk of changes in market valuation.

b. An instrument shall not be considered a hedging instrument or a part of a bona fide hedging transaction if it is purchased in conjunction with another instrument where the effect of the combined transaction is an increase in the portfolio's exposure to market risk.

15. "Investment guidelines" means a set of written guidelines, established in advance by the person with investment authority over the segregated portfolio, to be followed by the investment manager. The guidelines shall include a description of:

a. The segregated portfolio's investment objectives and limitations;

b. The investment manager's degree of discretion;

c. The duration, asset class, quality, diversification, and other requirements of the segregated portfolio; and

d. The manner in which derivative instruments may be used, if at all, in the segregated portfolio.

16. "Investment manager" means the person (including the contractholder) responsible for managing the assets in the segregated portfolio in accordance with the investment guidelines in a fiduciary capacity to the owner of the assets.

17. "Market value record" means an accounting record provided by the contract to reflect the fair market value of the segregated portfolio.

18. "Nationally Recognized Statistical Rating Organization (NRSRO)" means a rating organization so designated by the Securities and Exchange Commission of the United States of America (SEC) which has applied to, and whose NRSRO status has been confirmed by, the NAIC Securities Valuation Office.

19. "Permitted custodial institution" means a bank, trust company or other licensed fiduciary services provider.

20. "Plan of operation" means a written plan meeting the requirements of paragraph 28 of this appendix.

21. "Qualified actuary" means an individual who meets the qualification standards set forth in Appendix A-820.

22. "Rate period" means the period of time during which the fixed rate of return credited to the contract value record is applicable between crediting rate formula adjustments.

23. "Segregated portfolio" means:

a. A portfolio or sub-portfolio of assets to which the contract pertains that is held in a custody or trust account by the permitted custodial institution and identified on the records of the permitted custodial institution as special custody assets held for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract; and

b. Any related cash or currency received by the permitted custodial institution for the account of the contractholder and held in a deposit account for the exclusive benefit of the retirement plans or other entities on whose behalf the contractholder holds the contract.

24. "Spot rate"

a. "Treasury-based spot rate" corresponding to a given time of benefit payment means the yield on a zero-coupon non-callable and non-prepayable United States government obligation maturing at that time, or the zero-coupon yield implied by the price of a representative sampling of coupon-bearing, non-callable and non-prepayable United States government obligations in accordance with a formula set forth in the plan of operation.

b. "Index spot rate" corresponding to a given time of benefit payment means the zero-coupon yield implied by (x) the Barclays Short-Term Corporate Index (for a given time of benefit payment under one year) or (y) the zero-coupon yield implied by the Barclays U.S. Corporate Investment Grade Bond Index (for a given time of benefit payment greater than or equal to one year).

c. "Blended spot rate" corresponding to a given time of benefit payment means a blend of 50% each of (i) the treasury-based spot rate, and (ii) the index spot rate. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country rated in one of the two (2) highest rating categories by an independent nationally recognized United States rating agency acceptable to the NAIC Securities Valuation Office and are supported by investments denominated in the currency of the foreign country, the treasury-based spot rate component of the blended spot rate may be determined by reference to substantially similar obligations of the government of the foreign country.

25. "Synthetic guaranteed investment contract" or "contract" means a group annuity contract or other agreement that establishes the insurer's obligations by reference to a segregated portfolio of assets that is not owned by the insurer. The contract functions as an accounting record for an accumulation fund and the fixed rate of return credited to the fund reflects an amortization of the segregated portfolio's market gains and losses based on the period specified in the crediting formula, subject to any minimum interest rate guarantee.

26. "United States government obligation" means a direct obligation issued, assumed, guaranteed or insured by the United States of America or by an agency or instrumentality of the United States government.

27. "Valuation actuary" means the appointed actuary or, alternatively, a qualified actuary designated by the appointed actuary to render the actuarial opinion. Written documentation of any such designation shall be on file at the company and available for review upon request.

Plan of Operation

28. The plan of operation for a class of contracts shall describe the financial implications for the insurer of the issuance of contracts in the class, and shall include at least the following:

a. A statement describing the methods and procedures used to value statutory liabilities for purposes of paragraph 29;

b. A description of the allowable investment parameters (such as objectives, derivative strategies, asset classes, quality, duration and diversification requirements applied to the assets held within the segregated portfolio) to be reflected in the investment guidelines applicable to each contract issued in the class to which the submitted plan of operation applies; and a description of the procedures that will be followed by the insurer in evaluating the appropriateness of any specific investment guidelines submitted by the contractholder;

c. A description of the criteria used by the insurer in approving for contract issuance a pooled fund representing multiple employer-sponsored plans and in approving the investment manager for the segregated portfolio of assets associated with such pooled fund contract;

d. A description of risk-mitigation techniques used by the insurer in connection with contracts issued to pooled funds representing multiple employer-sponsored plans.

Reserves and Documentation

29. Asset maintenance requirements for segregated portfolios covered by this appendix.

a. At all times an insurer shall hold minimum reserves in the general account or one or more separate accounts, as appropriate, equal to the excess, if any, of the value of the guaranteed contract liabilities, determined in accordance with paragraphs 29.f. and 29.g., over the market value of the assets in the segregated portfolio less the deductions provided for in paragraph 29.b. These reserve requirements shall be applied on a contract-by-contract basis.

b. In determining compliance with the asset maintenance requirement and the reserve for guaranteed contract liabilities specified in paragraph 29.a., the insurer shall deduct a percentage of the market value of an asset as follows:

i. For debt instruments, the percentage shall be the NAIC asset valuation reserve "reserve objective factor," but the factor shall be increased by fifty percent (50%) for the purpose of this calculation if the difference in durations of the assets and liabilities is more than one-half year. The above notwithstanding, in the event that under the terms of the synthetic guaranteed investment contract, the asset default risk for debt instruments is borne solely by the contractholder, there shall be no asset valuation reserve percentage deduction from the market value of an asset, for purposes of complying with the asset maintenance requirement and the reserve for guaranteed contract liabilities specified in paragraph 29.a.

ii. For assets that are not debt instruments, the percentage shall be the NAIC asset valuation reserve “maximum reserve factor.”

c. To the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by segregated portfolio assets denominated in the currency of the foreign country, the percentage deduction for these assets under paragraph 29.b. shall be that for a substantially similar investment denominated in the currency of the United States.

d. To the extent that guaranteed contract liabilities are denominated in the currency of the United States and are supported by segregated portfolio assets denominated in the currency of a foreign country, and to the extent that guaranteed contract liabilities are denominated in the currency of a foreign country and are supported by segregated portfolio assets denominated in the currency of the United States, the deduction for debt instruments under paragraph 29.b. shall be increased by fifteen percent (15%) of the market value of the assets unless the currency exchange risk on the assets has been adequately hedged, in which case the percentage deduction under paragraph 29.b. shall be increased by one-half percent (.5%). No guaranteed contract liabilities denominated in the currency of a foreign country shall be supported by segregated portfolio assets denominated in the currency of another foreign country. For purposes of this paragraph, the currency exchange risk on an asset is deemed to be adequately hedged if:

i. It is an obligation of

(a) A jurisdiction that is rated in one of the two (2) highest rating categories by an NRSRO;

(b) Any political subdivision or other governmental unit of such a jurisdiction, or any agency or instrumentality of jurisdiction, political subdivision or other governmental unit; or

(c) An institution that is organized under the laws of any such jurisdiction; and

ii. At all times the principal amount of the obligation and scheduled interest payments on the obligation are hedged against the United States dollar pursuant to contracts or agreements that are:

(a) Issued by or traded on a securities exchange or board of trade regulated under the laws of the United States or Canada or a province of Canada;

(b) Entered into with a United States banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an NRSRO, or with a broker-dealer registered with the Securities and Exchange Commission that has net capital in excess of $250 million; or

(c) Entered into with any other banking institution that has assets in excess of $5 billion and that has obligations outstanding, or has a parent corporation that has obligations outstanding, that are rated in one of the two (2) highest rating categories by an NRSRO and that is organized under the laws of a jurisdiction that is rated in one of the two (2) highest rating categories by an NRSRO.

e. These contracts may provide for the allocation to one or more separate accounts of all or any portion of the amount needed to meet the asset maintenance requirement. If the contract provides that the assets in the separate account shall not be chargeable with liabilities arising out of any other business of the insurer, the insurer shall maintain in a distinct separate account that is so chargeable:

i. That portion of the amount needed to meet the asset maintenance requirement that has been allocated to separate accounts; less

ii. The amounts contributed to separate accounts by the contractholder in accordance with the contract and the earnings on the contract.

f. For purposes of this paragraph, the minimum value of guaranteed contract liabilities is defined to be the sum of the expected guaranteed contract benefits, each discounted at a rate corresponding to the expected time of payment of the contract benefit that is not greater than the spot rate supportable by the expected return from the segregated portfolio assets, and in no event greater than the blended spot rate as described in the plan of operation or the actuary's opinion and memorandum, except that if the expected time of payment of a contract benefit is more than thirty (30) years, it shall be discounted from the expected date of payment to year thirty (30) at a rate of no more than eighty percent (80%) of the thirty-year spot rate and from year thirty (30) to the date of valuation at a rate not greater than the thirty-year blended spot rate.

g. In calculating the minimum value of guaranteed contract benefits:

i. All guaranteed benefits potentially available to the contractholder on an ongoing basis shall be considered in the valuation process and analysis, and the reserve held must be sufficient to fund the greatest present value of each independent guaranteed contract benefit. For purposes of this subparagraph, the right granted to the contractholder to exit the contract by discharging the insurer of its guarantee obligation under the contract and taking control of the assets in the segregated portfolio shall not be considered a guaranteed benefit.

ii. To the extent that future guaranteed cash flows are dependent upon the benefit responsiveness of an employer-sponsored plan, a best estimate based on company experience, or other reasonable criteria if company experience is not available, shall be used in the projections of future cash flows.

iii. The minimum value of guaranteed contract benefits under a contract issued to a pooled fund representing multiple employer-sponsored plans shall be determined so as to reflect projected plan sponsor contract value withdrawals available to the member plans in the pooled fund.

Projections of such future cash flows shall take into account (i) known plan sponsor withdrawals, and (ii) a prudent estimate of future plan sponsor withdrawals. The prudent estimate shall be based on company experience and other relevant criteria.

A single valuation rate shall be determined, consistent with paragraph 29.f., equal to the lesser of:

(a) The expected return from the segregated portfolio of assets, or

(b) The blended spot rate based on the duration of the segregated portfolio of assets.

This single valuation rate shall be used to model future market values of the segregated portfolio of assets. Future credited interest rates shall be modeled according to the contractually defined crediting rate formula. Modeled future contract values shall reflect modeled future market values, modeled future credited interest rates, known future plan sponsor withdrawals, the prudent estimate of future plan sponsor withdrawals, future withdrawals consistent with paragraph 29.g.ii. of this subsection and any remaining final payment at the modeled contract termination date.

All such modeled withdrawals and termination payments shall be discounted using the single valuation rate and the modeled times of those withdrawals and payments. The sum of these present values shall be deemed the minimum value of the guaranteed contract liabilities for a pooled fund contract.

30. Account assets shall make adequate provision for contract liabilities, taking into account any risk charge payable, the segregated portfolio assets, and the amount of any reserve liability with respect to the asset maintenance requirement.

31. The fixed-income segregated portfolio shall conform to and justify the rates used to discount contract liabilities for valuation pursuant to paragraph 29.f.

32. The company shall document whether any rates used pursuant to paragraph 29.f. to discount guaranteed contract liabilities and other items applicable to the segregated portfolio were modified from the rate or rates described in the plan of operation.

33. The level of risk charges, if any, retained in the general account shall be appropriate in view of such factors as the nature of the guaranteed contract liabilities and losses experienced in connection with account contracts and other pricing factors.

34. The company shall substantially conform with Appendix A-822 and maintain internal documentation to either:

a. Demonstrate the adequacy of account assets based upon cash flow analysis, or

b. Explain why cash flow testing analysis is not appropriate, describe the alternative methodology of asset adequacy testing used, and demonstrate the adequacy of account assets under that methodology;

35. The company's internal documentation pertaining to reserves for synthetic guaranteed investment contract liabilities shall also:

a. Clearly describe the assumptions used in projecting cash flows under each class of assets, and any dynamic portfolio hedging techniques utilized and the tests performed on the utilization of the techniques;

b. Clearly describe how the company has reflected the cost of capital;

c. Clearly describe how the company has reflected the risk of default on obligations and mortgage loans, including obligations and mortgage loans that are not investment grade;

d. Clearly describe how the company has reflected withdrawal risks, if applicable, including a discussion of the positioning of the contracts within the benefit withdrawal priority order pertaining to the contracts, the impact of any dynamic lapse assumption and the results of sensitivity testing the prudent estimate of future plan sponsor withdrawals pursuant to paragraph 29.g.iii.;

e. If the plan of operation provides for investments in segregated portfolio assets other than United States government obligations, demonstrate that the rates used to discount contract liabilities pursuant to paragraph 29.f. conservatively reflect expected investment returns, taking into account any foreign exchange risks;

f. If the contracts provide that in certain circumstances they would cease to be funded by a segregated portfolio and, instead would become contracts funded by the general account, clearly describe how any increased reserves would be provided for if and to the extent these circumstances occurred;

g. Document the amount of account assets maintained in a separate account that are not chargeable with liabilities arising out of any other business of the insurance company;

h. Document the amount of reserves and supporting assets as of December 31 and where the reserves are shown in the annual statement;

i. Document the amount of any contingency reserve carried as part of surplus;

j. Document the market value of the segregated asset portfolio; and

k. Where separate account assets are not chargeable with liabilities arising out of any other business of the insurance company, describe how the level of risk charges payable to the general account provides an appropriate compensation for the risk taken by the general account.

36. When the insurer issues a synthetic guaranteed investment contract and complies with the asset maintenance requirements of paragraph 29, it need not maintain an asset valuation reserve with respect to those account assets.

37. This paragraph describes the reserve valuation requirements for contracts subject to this appendix.

a. Reserves for synthetic investment contracts subject to this appendix shall be an amount equal to the sum of the following:

i. The amounts determined as the minimum reserve as required under paragraph 29; and

ii. Any additional amount determined by the insurer's valuation actuary as necessary to make adequate provision for all contract liabilities.

b. The amount of any reserves required by paragraph 37.a. may be established by either:

i. Allocating sufficient assets to one or more separate accounts; or

ii. Setting up the additional reserves in the general account.

Appendix A-785

Credit for Reinsurance

Relevant SSAPs:
SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance
SSAP No. 62—Property and Casualty Reinsurance
SSAP No. 66—Retrospectively Rated Contracts

Definitions

1. “Commissioner” refers to the commissioner of insurance in the state where credit or a reduction from liability is taken.

2. “Jurisdiction” refers to any state, district or territory of the United States and also to territories, provinces or jurisdictions other than the United States.

3. “Liabilities” shall mean the assuming insurer’s gross liabilities attributable to reinsurance ceded by U. S. domiciled insurers that are not otherwise secured by acceptable means.

4. “Beneficiary” means the entity for whose sole benefit the trust has been established and any successor of the beneficiary by operation of law. If a court of law appoints a successor in interest to the named beneficiary, then the named beneficiary includes and is limited to the court appointed domiciliary receiver (including conservator, rehabilitator or liquidator).

5. “Grantor” means the entity that has established a trust for the sole benefit of the beneficiary. When established in conjunction with a reinsurance agreement, the grantor is the unlicensed, unaccredited assuming insurer.

6. “Obligations,” as used in paragraph 30 of this appendix means:

   a. Reinsured losses and allocated loss expenses paid by the ceding company, but not recovered from the assuming insurer;

   b. Reserves for reinsured losses reported and outstanding;

   c. Reserves for reinsured losses incurred but not reported; and

   d. Reserves for allocated reinsured loss expenses and unearned premiums.

Credit Allowed a Domestic Ceding Insurer

7. Credit for reinsurance shall be allowed a domestic ceding insurer as either an asset or a reduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of paragraphs 8, 9, 10, 11, 12, 13 or 14 of this appendix. Credit shall be allowed under paragraphs 8, 9, or 10 of this appendix only as respects cessions of those kinds or classes of business which the assuming insurer is licensed or otherwise allowed to write or assume in its state of domicile or, in the case of a U.S. branch of an alien assuming insurer, in the state through which it is entered and licensed to transact insurance or reinsurance. Credit shall be allowed under paragraphs 10 or 11 of this appendix only if the applicable requirements of paragraph 15 have been satisfied.

8. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is licensed to transact insurance or reinsurance in the domiciliary state of the ceding insurer.

9. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is accredited as a reinsurer by the domiciliary state of the ceding insurer. In order to be eligible for accreditation, a reinsurer must:

a. File with the commissioner evidence of its submission to the domiciliary state's jurisdiction;

b. Submit to the domiciliary state's authority to examine its books and records;

c. Be licensed to transact insurance or reinsurance in at least one state, or in the case of a U.S. branch of an alien assuming insurer, is entered through and licensed to transact insurance or reinsurance in at least one state;

d. File annually with the commissioner a copy of its annual statement filed with the insurance department of its state of domicile and a copy of its most recent audited financial statement; and

e. Demonstrate to the satisfaction of the commissioner that it has adequate financial capacity to meet its reinsurance obligations and is otherwise qualified to assume reinsurance from domestic insurers. An assuming insurer is deemed to meet this requirement as of the time of its application if it maintains a surplus as regards policyholders in an amount not less than $20,000,000 and its accreditation has not been denied by the commissioner within ninety (90) days after submission of its application.

10. a. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is domiciled in, or in the case of a U.S. branch of an alien assuming insurer is entered through, a state that employs standards regarding credit for reinsurance substantially similar to those of the domiciliary state of the ceding insurer and the assuming insurer or U.S. branch of an alien assuming insurer:

i. Maintains a surplus as regards policyholders in an amount not less than $20,000,000; and

ii. Submits to the authority of the domiciliary state to examine its books and records.

b. The requirement of paragraph 10.a.i. does not apply to reinsurance ceded and assumed pursuant to pooling arrangements among insurers in the same holding company system.

11. a. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that maintains a trust fund in a qualified U.S. financial institution, as defined in paragraph 54, for the payment of the valid claims of its U.S. ceding insurers, their assigns and successors in interest. The assuming insurer shall report annually information substantially the same as that required to be reported on the NAIC Annual Statement form by licensed insurers. The assuming insurer shall submit to examination of its books and records by the commissioner and bear the expense of examination.

b. i. Credit for reinsurance shall not be granted under this paragraph 11 unless the form of the trust and any amendments to the trust have been approved by:

(a) The commissioner of the state where the trust is domiciled; or

(b) The commissioner of another state who, pursuant to the terms of the trust instrument, has accepted principal regulatory oversight of the trust.

ii. The trust instrument shall provide that:

(a) Contested claims shall be valid and enforceable out of funds in trust to the extent remaining unsatisfied thirty (30) days after entry of the final order of any court of competent jurisdiction in the United States;

(b) Legal title to the assets of the trust shall be vested in the trustee for the benefit of the grantor's U.S. ceding insurers, their assigns and successors in interest;

(c) The trust shall be subject to examination as determined by the commissioner;

(d) The trust shall remain in effect for as long as the assuming insurer, or any member or former member of a group of insurers, shall have outstanding obligations under reinsurance agreements subject to the trust; and

(e) No later than February 28 of each year the trustee of the trust shall report to the commissioner in writing setting forth the balance in the trust and listing the trust's investments at the preceding year-end, and shall certify the date of termination of the trust, if so planned, or certify that the trust shall not expire prior to the following December 31.

c. The following requirements apply to the following categories of assuming insurer:

i. The trust fund for a single assuming insurer shall consist of funds in trust in an amount not less than the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers, and, in addition, the assuming insurer shall maintain a trusteed surplus of not less than $20,000,000, except as provided in paragraph 11.c.ii. of this appendix.

ii. At any time after the assuming insurer has permanently discontinued underwriting new business secured by the trust for at least three full years, the commissioner with principal regulatory oversight of the trust may authorize a reduction in the required trusteed surplus, but only after a finding, based on an assessment of the risk, that the new required surplus level is adequate for the protection of U.S. ceding insurers, policyholders and claimants in light of reasonably foreseeable adverse loss development. The risk assessment may involve an actuarial review, including an independent analysis of reserves and cash flows, and shall consider all material risk factors, including when applicable the lines of business involved, the stability of the incurred loss estimates and the effect of the surplus requirements on the assuming insurer's liquidity or solvency. The minimum required trusteed surplus may not be reduced to an amount less than thirty percent (30%) of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers covered by the trust.

iii. (a) In the case of a group including incorporated and individual unincorporated underwriters:

(1) For reinsurance ceded under reinsurance agreements with an inception, amendment or renewal date on or after January 1, 1993, the trust shall consist of a trusteed account in an amount not less than the respective underwriters' several liabilities

attributable to business ceded by U.S. domiciled ceding insurers to any underwriter of the group;

(2) For reinsurance ceded under reinsurance agreements with an inception date on or before December 31, 1992, and not amended or renewed after that date, not-withstanding the other provisions contained herein, the trust shall consist of a trusteed account in an amount not less than the respective underwriters' several insurance and reinsurance liabilities attributable to business written in the United States; and

(3) In addition to these trusts, the group shall maintain in trust a trusteed surplus of which $100,000,000 shall be held jointly for the benefit of the U.S. domiciled ceding insurers of any member of the group for all years of account; and

(b) The incorporated members of the group shall not be engaged in any business other than underwriting as a member of the group and shall be subject to the same level of regulation and solvency control by the group's domiciliary regulator as are the unincorporated members.

(c) Within ninety (90) days after its financial statements are due to be filed with the group's domiciliary regulator, the group shall provide to the commissioner an annual certification by the group's domiciliary regulator of the solvency of each underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the group.

iv. In the case of a group of incorporated underwriters under common administration, the group shall:

(a) Have continuously transacted an insurance business outside the United States for at least three (3) years immediately prior to making application for accreditation;

(b) Maintain aggregate policyholders' surplus of at least $10,000,000,000;

(c) Maintain a trust fund in an amount not less than the group's several liabilities attributable to business ceded by U.S. domiciled ceding insurers to any member of the group pursuant to reinsurance contracts issued in the name of the group;

(d) In addition, maintain a joint trusteed surplus of which $100,000,000 shall be held jointly for the benefit of U.S. domiciled ceding insurers of any member of the group as additional security for these liabilities; and

(e) Within ninety (90) days after its financial statements are due to be filed with the group's domiciliary regulator, make available to the commissioner an annual certification of each underwriter member's solvency by the member's domiciliary regulator and financial statements of each underwriter member of the group prepared by its independent public accountant.

d. For the purposes of this paragraph 11., the term "liabilities" shall mean the assuming insurer's gross liabilities attributable to reinsurance ceded by U.S. domiciled insurers excluding liabilities that are otherwise secured by acceptable means, and shall include:

i. For business ceded by domestic insurers authorized to write accident and health, and property and casualty insurance:

(a) Losses and allocated loss expenses paid by the ceding insurer, recoverable from the assuming insurer;

(b) Reserves for losses reported and outstanding;

(c) Reserves for losses incurred but not reported;

(d) Reserves for allocated loss expenses; and

(e) Unearned premiums.

ii. For business ceded by domestic insurers authorized to write life, health and annuity insurance:

(a) Aggregate reserves for life policies and contracts net of policy loans and net due and deferred premiums;

(b) Aggregate reserves for accident and health policies;

(c) Deposit funds and other liabilities without life or disability contingencies; and

(d) Liabilities for policy and contract claims.

12. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that has been certified as a reinsurer in the domestic state of the ceding insurer and secures its obligations in accordance with the requirements of this paragraph 12.

a. In order to be eligible for certification, the assuming insurer shall meet the following requirements:

i. The assuming insurer must be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction, as determined by the domestic state of the ceding insurer pursuant to paragraphs 12.c. and 12.k. of this subsection;

ii. The assuming insurer must maintain minimum capital and surplus, or its equivalent, in an amount as provided in paragraph 12.i.iii.(b) of this appendix;

iii. The assuming insurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the domestic state of the ceding insurer, as provided in paragraph 12.i.iii.(c) of this appendix;

iv. The assuming insurer must agree to submit to the jurisdiction of the domestic state of the ceding insurer, appoint the commissioner of the domestic state of the ceding insurer as its agent for service of process in that state, and agree to provide security for 100 percent of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers if it resists enforcement of a final U.S. judgment;

v. The assuming insurer must agree to meet applicable information filing requirements as determined by the domestic state of the ceding insurer, both with respect to an initial application for certification and on an ongoing basis; and

vi. The assuming insurer must satisfy any other requirements for certification deemed relevant by the domestic state of the ceding insurer.

b. An association including incorporated and individual unincorporated underwriters may be a certified reinsurer. In order to be eligible for certification, in addition to satisfying requirements of paragraph 12.a. of this appendix:

i. The association shall satisfy its minimum capital and surplus requirements through the capital and surplus equivalents (net of liabilities) of the association and its members, which shall include a joint central fund that may be applied to any unsatisfied obligation of the association or any of its members, in an amount determined by the domestic state of the ceding insurer to provide adequate protection;

ii. The incorporated members of the association shall not be engaged in any business other than underwriting as a member of the association and shall be subject to the same level of regulation and solvency control by the association's domiciliary regulator as are the unincorporated members; and

iii. Within ninety (90) days after its financial statements are due to be filed with the association's domiciliary regulator, the association shall provide to the domestic state of the ceding insurer an annual certification by the association's domiciliary regulator of the solvency of each underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the association.

c. The domestic state of the ceding insurer shall create and publish a list of qualified jurisdictions, under which an assuming insurer licensed and domiciled in such jurisdiction is eligible to be considered for certification by the domestic state of the ceding insurer as a certified reinsurer.

i. In order to determine whether the domiciliary jurisdiction of a non-U.S. assuming insurer is eligible to be recognized as a qualified jurisdiction, the domestic state of the ceding insurer shall evaluate the appropriateness and effectiveness of the reinsurance supervisory system of the jurisdiction, both initially and on an ongoing basis, and consider the rights, benefits and the extent of reciprocal recognition afforded by the non-U.S. jurisdiction to reinsurers licensed and domiciled in the U.S. A qualified jurisdiction must agree to share information and cooperate with the domestic state of the ceding insurer with respect to all certified reinsurers domiciled within that jurisdiction. A jurisdiction may not be recognized as a qualified jurisdiction if the domestic state of the ceding insurer has determined that the jurisdiction does not adequately and promptly enforce final U.S. judgments and arbitration awards. Additional factors may be considered in the discretion of the domestic state of the ceding insurer.

ii. A list of qualified jurisdictions shall be published through the NAIC Committee Process. The domestic state of the ceding insurer shall consider this list in determining qualified jurisdictions. If the domestic state of the ceding insurer approves a jurisdiction as qualified that does not appear on the list of qualified jurisdictions, the state shall provide thoroughly documented justification in accordance with criteria to be developed under regulations.

iii. U.S. jurisdictions that meet the requirement for accreditation under the NAIC financial standards and accreditation program shall be recognized as qualified jurisdictions.

iv. If a certified reinsurer's domiciliary jurisdiction ceases to be a qualified jurisdiction, the domestic state of the ceding insurer has the discretion to suspend the reinsurer's certification indefinitely, in lieu of revocation.

d. The domestic state of the ceding insurer shall assign a rating to each certified reinsurer, giving due consideration to the financial strength ratings that have been assigned by rating agencies deemed acceptable to the commissioner pursuant to regulation. The domestic state of the ceding insurer shall publish a list of all certified reinsurers and their ratings.

e. A certified reinsurer shall secure obligations assumed from U.S. ceding insurers under this subsection at a level consistent with its rating, as specified in paragraph 12.h.i. of this appendix.

i. In order for a domestic ceding insurer to qualify for full financial statement credit for reinsurance ceded to a certified reinsurer, the certified reinsurer shall maintain security in a form acceptable to the domestic state of the ceding insurer and consistent with the provisions of paragraph 19 of this appendix, or in a multibeneficiary trust in accordance with paragraph 11 of this appendix, except as otherwise provided in paragraph 12.e.ii. through 12.e.v. of this appendix.

ii. If a certified reinsurer maintains a trust to fully secure its obligations subject to paragraph 11 of this appendix, and chooses to secure its obligations incurred as a certified reinsurer in the form of a multibeneficiary trust, the certified reinsurer shall maintain separate trust accounts for its obligations incurred under reinsurance agreements issued or renewed as a certified reinsurer with reduced security as permitted by paragraph 12, or comparable laws of other U.S. jurisdictions, and for its obligations subject to paragraph 11 of this appendix. It shall be a condition to the grant of certification under paragraph 12 of this appendix that the certified reinsurer shall have bound itself, by the language of the trust and agreement with the commissioner with principal regulatory oversight of each such trust account, to fund, upon termination of any such trust account, out of the remaining surplus of such trust any deficiency of any other such trust account.

iii. The minimum trusteed surplus requirements provided in paragraph 11 of this appendix are not applicable with respect to a multibeneficiary trust maintained by a certified reinsurer for the purpose of securing obligations incurred under this subsection, except that such trust shall maintain a minimum trusteed surplus of $10,000,000.

iv. With respect to obligations incurred by a certified reinsurer under paragraph 12 of this appendix, if the security is insufficient, the allowable reinsurance credit shall be reduced by an amount proportionate to the deficiency, and the domestic state of the ceding insurer has the discretion to impose further reductions in allowable credit upon finding that there is a material risk that the certified reinsurer's obligations will not be paid in full when due.

v. For purposes of paragraph 12, a certified reinsurer whose certification has been terminated for any reason shall be treated as a certified reinsurer required to secure 100 percent of its obligations.

(a) As used in paragraph 12.e.v., the term "terminated" refers to revocation, suspension, voluntary surrender and inactive status.

(b) If the domestic state of the ceding insurer continues to assign a higher rating as permitted by other provisions of paragraph 12, this requirement does not apply to a certified reinsurer in inactive status or to a reinsurer whose certification has been suspended.

f. If an applicant for certification has been certified as a reinsurer in an NAIC accredited jurisdiction, the domestic state of the ceding insurer has the discretion to defer to that jurisdiction's certification, and has the discretion to defer to the rating assigned by that jurisdiction, and such assuming insurer shall be considered to be a certified reinsurer in the domestic state of the ceding insurer.

g. A certified reinsurer that ceases to assume new business in this state may request to maintain its certification in inactive status in order to continue to qualify for a reduction in security for its in-force business. An inactive certified reinsurer shall continue to comply with all applicable requirements of paragraph 12, and the domestic state of the ceding insurer shall assign a rating that takes into account, if relevant, the reasons why the reinsurer is not assuming new business.

h. The credit allowed under paragraph 12 shall be based upon the security held by or on behalf of the ceding insurer in accordance with a rating assigned to the certified reinsurer by the commissioner. The security shall be in a form consistent with the provisions of paragraph 12 and paragraph 19 of this appendix, and paragraphs 20-51 of this appendix, as applicable. The amount of security required in order for full credit to be allowed shall correspond with the following requirements:

i.

Ratings	**Security Required**
Secure – 1	0%
Secure – 2	10%
Secure – 3	20%
Secure – 4	50%
Secure – 5	75%
Vulnerable – 6	100%

ii. Affiliated reinsurance transactions shall receive the same opportunity for reduced security requirements as all other reinsurance transactions.

iii. The commissioner shall require the certified reinsurer to post one hundred percent (100%), for the benefit of the ceding insurer or its estate, security upon the entry of an order of rehabilitation, liquidation or conservation against the ceding insurer.

iv. In order to facilitate the prompt payment of claims, a certified reinsurer shall not be required to post security for catastrophe recoverables for a period of one year from the date of the first instance of a liability reserve entry by the ceding company as a result of a loss from a catastrophic occurrence as recognized by the commissioner. The one year deferral period is contingent upon the certified reinsurer continuing to pay claims in a timely manner. Reinsurance recoverables for only the following lines of business as reported on the NAIC annual financial statement related specifically to the catastrophic occurrence will be included in the deferral:

(a) Line 1: Fire

(b) Line 2: Allied Lines

(c) Line 3: Farmowners multiple peril

(d) Line 4: Homeowners multiple peril

(e) Line 5: Commercial multiple peril

(f) Line 9: Inland Marine

(g) Line 12: Earthquake

(h) Line 21: Auto physical damage

v. Credit for reinsurance under paragraph 12 of this appendix shall apply only to reinsurance contracts entered into or renewed on or after the effective date of the certification of the assuming insurer. Any reinsurance contract entered into prior to the effective date of the certification of the assuming insurer that is subsequently amended after the effective date of the certification of the assuming insurer, or a new reinsurance contract, covering any risk for which collateral was provided previously, shall only be subject to this section with respect to losses incurred and reserves reported from and after the effective date of the amendment or new contract.

vi. Nothing in paragraph 12 of this appendix shall prohibit the parties to a reinsurance agreement from agreeing to provisions establishing security requirements that exceed the minimum security requirements established for certified reinsurers under this section.

i. Certification Procedure

i. The commissioner of the domestic state of the ceding insurer shall post notice on the insurance department's website promptly upon receipt of any application for certification, including instructions on how members of the public may respond to the application. The commissioner may not take final action on the application until at least thirty (30) days after posting the notice required by this paragraph.

ii. The commissioner of the domestic state of the ceding insurer shall issue written notice to an assuming insurer that has made application and been approved as a certified reinsurer. Included in such notice shall be the rating assigned the certified reinsurer in accordance with paragraph 12.h. of this appendix. The commissioner shall publish a list of all certified reinsurers and their ratings.

iii. In order to be eligible for certification, the assuming insurer shall meet the following requirements:

(a) The assuming insurer must be domiciled and licensed to transact insurance or reinsurance in a Qualified Jurisdiction, as determined by the commissioner pursuant to paragraph 12.c. and 12.k. of this appendix.

(b) The assuming insurer must maintain capital and surplus, or its equivalent, of no less than $250,000,000 calculated in accordance with paragraph 12.i.iv.(h) of this appendix. This requirement may also be satisfied by an association including incorporated and individual unincorporated underwriters having minimum capital and surplus equivalents (net of liabilities) of at least $250,000,000 and a central fund containing a balance of at least $250,000,000.

(c) The assuming insurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the commissioner. These ratings shall be based on interactive communication between the rating agency and the assuming insurer and shall not be based solely on publicly available information. These financial strength ratings will be one factor used by the commissioner in determining the rating that is assigned to the assuming insurer. Acceptable rating agencies include the following:

(1) Standard & Poor's;

(2) Moody's Investors Service;

(3) Fitch Ratings;

(4) A.M. Best Company; or

(5) Any other Nationally Recognized Statistical Rating Organization.

(d) The certified reinsurer must comply with any other requirements reasonably imposed by the commissioner of the domestic state of the ceding insurer.

iv. Each certified reinsurer shall be rated on a legal entity basis, with due consideration being given to the group rating where appropriate, except that an association including incorporated and individual unincorporated underwriters that has been approved to do business as a single certified reinsurer may be evaluated on the basis of its group rating. Factors that may be considered as part of the evaluation process include, but are not limited to, the following:

(a) The certified reinsurer's financial strength rating from an acceptable rating agency. The maximum rating that a certified reinsurer may be assigned will correspond to its financial strength rating as outlined in the table below. The commissioner shall use the lowest financial strength rating received from an approved rating agency in establishing the maximum rating of a certified reinsurer. A failure to obtain or maintain at least two financial strength ratings from acceptable rating agencies will result in loss of eligibility for certification:

Ratings	Best	S&P	Moody's	Fitch
Secure – 1	A++	AAA	Aaa	AAA
Secure – 2	A+	AA+, AA, AA-	Aa1, Aa2, Aa3	AA+, AA, AA-
Secure – 3	A	A+, A	A1, A2	A+, A
Secure – 4	A-	A-	A3	A-
Secure – 5	B++, B+	BBB+, BBB, BBB-	Baa1, Baa2, Baa3	BBB+, BBB, BBB-
Vulnerable – 6	B, B-C++, C+, C, C-, D, E, F	BB+, BB, BB-, B+, B, B-, CCC, CC, C, D, R	Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, C	BB+, BB, BB-, B+, B, B-, CCC+, CC, CCC-, DD

(b) The business practices of the certified reinsurer in dealing with its ceding insurers, including its record of compliance with reinsurance contractual terms and obligations;

(c) For certified reinsurers domiciled in the U.S., a review of the most recent applicable NAIC annual statement blank, either Schedule F (for property/casualty reinsurers) or Schedule S (for life and health reinsurers);

(d) For certified reinsurers not domiciled in the U.S., a review annually of Form CR-F (for property/casualty reinsurers) or Form CR-S (for life and health reinsurers);

(e) The reputation of the certified reinsurer for prompt payment of claims under reinsurance agreements, based on an analysis of ceding insurers' Schedule F reporting of overdue reinsurance recoverables, including the proportion of obligations that are more than ninety (90) days past due or are in dispute, with specific attention given to obligations payable to companies that are in administrative supervision or receivership;

(f) Regulatory actions against the certified reinsurer;

(g) The report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in paragraph (h) below;

(h) For certified reinsurers not domiciled in the U.S., audited financial statements, regulatory filings, and actuarial opinion (as filed with the non-U.S. jurisdiction supervisor, with a translation into English). Upon the initial application for certification, the commissioner will consider audited financial statements for the last two (2) years filed with its non-U.S. jurisdiction supervisor;

(i) The liquidation priority of obligations to a ceding insurer in the certified reinsurer's domiciliary jurisdiction in the context of an insolvency proceeding;

(j) A certified reinsurer's participation in any solvent scheme of arrangement, or similar procedure, which involves U.S. ceding insurers. The commissioner shall receive prior notice from a certified reinsurer that proposes participation by the certified reinsurer in a solvent scheme of arrangement; and

(k) Any other information deemed relevant by the commissioner.

v. Based on the analysis conducted under paragraph 12.i.iv.(e) of a certified reinsurer's reputation for prompt payment of claims, the commissioner may make appropriate adjustments in the security the certified reinsurer is required to post to protect its liabilities to U.S. ceding insurers, provided that the commissioner shall, at a minimum, increase the security the certified reinsurer is required to post by one rating level under paragraph 12.h. if the commissioner finds that:

(a) more than fifteen percent (15%) of the certified reinsurer's ceding insurance clients have overdue reinsurance recoverables on paid losses of ninety (90) days or more which are not in dispute and which exceed $100,000 for each cedent; or

(b) the aggregate amount of reinsurance recoverables on paid losses which are not in dispute that are overdue by ninety (90) days or more exceeds $50,000,000.

vi. The assuming insurer must submit a properly executed Form CR-1 as evidence of its submission to the jurisdiction of this state, appointment of the commissioner as an agent for service of process in this state, and agreement to provide security for one hundred percent (100%) of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers if it resists enforcement of a final U.S. judgment. The commissioner shall not certify any assuming insurer that is domiciled in a jurisdiction that the commissioner has determined does not adequately and promptly enforce final U.S. judgments or arbitration awards.

vii. The certified reinsurer must agree to meet applicable information filing requirements as determined by the commissioner, both with respect to an initial application for certification and on an ongoing basis. All information submitted by certified reinsurers which are not otherwise public information subject to disclosure shall be exempted from disclosure under [cite state law equivalent of Freedom of Information Act] and shall be withheld from public disclosure. The applicable information filing requirements are, as follows:

(a) Notification within ten (10) days of any regulatory actions taken against the certified reinsurer, any change in the provisions of its domiciliary license or any change in rating by an approved rating agency, including a statement describing such changes and the reasons therefore;

(b) Annually, Form CR-F or CR-S, as applicable;

(c) Annually, the report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in paragraph 12.i.vii.(d) below;

(d) Annually, the most recent audited financial statements, regulatory filings, and actuarial opinion (as filed with the certified reinsurer's supervisor, with a translation into English). Upon the initial certification, audited financial statements for the last two (2) years filed with the certified reinsurer's supervisor;

(e) At least annually, an updated list of all disputed and overdue reinsurance claims regarding reinsurance assumed from U.S. domestic ceding insurers;

(f) A certification from the certified reinsurer's domestic regulator that the certified reinsurer is in good standing and maintains capital in excess of the jurisdiction's highest regulatory action level; and

(g) Any other information that the commissioner may reasonably require.

j. Change in Rating or Revocation of Certification

i. In the case of a downgrade by a rating agency or other disqualifying circumstance, the commissioner shall upon written notice assign a new rating to the certified reinsurer in accordance with the requirements of paragraph 12.i.

ii. The commissioner shall have the authority to suspend, revoke, or otherwise modify a certified reinsurer's certification at any time if the certified reinsurer fails to meet its obligations or security requirements under this section, or if other financial or operating results of the certified reinsurer, or documented significant delays in payment by the certified reinsurer, lead the commissioner to reconsider the certified reinsurer's ability or willingness to meet its contractual obligations.

iii. If the rating of a certified reinsurer is upgraded by the commissioner, the certified reinsurer may meet the security requirements applicable to its new rating on a prospective basis, but the commissioner shall require the certified reinsurer to post security under the previously applicable security requirements as to all contracts in force on or before the effective date of the upgraded rating. If the rating of a certified reinsurer is downgraded by the commissioner, the commissioner shall require the certified reinsurer to meet the security requirements applicable to its new rating for all business it has assumed as a certified reinsurer.

iv. Upon revocation of the certification of a certified reinsurer by the commissioner, the assuming insurer shall be required to post security in accordance with paragraph 19 in order for the ceding insurer to continue to take credit for reinsurance ceded to the assuming insurer. If funds continue to be held in trust in accordance with paragraph 11, the commissioner may allow additional credit equal to the ceding insurer's *pro rata* share of such funds, discounted to reflect the risk of uncollectibility and anticipated expenses of trust administration. Notwithstanding the change of a certified reinsurer's rating or revocation of its certification, a domestic insurer that has ceded reinsurance to that certified reinsurer may not be denied credit for reinsurance for a period of three (3) months for all reinsurance ceded to that certified reinsurer, unless the reinsurance is found by the commissioner to be at high risk of uncollectibility.

k. Qualified Jurisdictions

i. If, upon conducting an evaluation with respect to the reinsurance supervisory system of any non-U.S. assuming insurer, the commissioner of the domestic state of the ceding insurer determines that the jurisdiction qualifies to be recognized as a qualified jurisdiction, the commissioner shall publish notice and evidence of such recognition in an appropriate manner. The commissioner may establish a procedure to withdraw recognition of those jurisdictions that are no longer qualified.

ii. In order to determine whether the domiciliary jurisdiction of a non-U.S. assuming insurer is eligible to be recognized as a qualified jurisdiction, the commissioner shall evaluate the reinsurance supervisory system of the non-U.S. jurisdiction, both initially and on an ongoing basis, and consider the rights, benefits and the extent of reciprocal recognition afforded by the non-U.S. jurisdiction to reinsurers licensed and domiciled in the U.S. The commissioner shall determine the appropriate approach for evaluating the qualifications of such jurisdictions, and create and publish a list of jurisdictions whose reinsurers may be approved by the commissioner as eligible for certification. A qualified jurisdiction must agree to share information and cooperate with the commissioner with respect to all certified reinsurers domiciled within that jurisdiction. Additional factors to be considered in determining whether to recognize a qualified jurisdiction, in the discretion of the commissioner, include but are not limited to the following:

(a) The framework under which the assuming insurer is regulated.

(b) The structure and authority of the domiciliary regulator with regard to solvency regulation requirements and financial surveillance.

(c) The substance of financial and operating standards for assuming insurers in the domiciliary jurisdiction.

(d) The form and substance of financial reports required to be filed or made publicly available by reinsurers in the domiciliary jurisdiction and the accounting principles used.

(e) The domiciliary regulator's willingness to cooperate with U.S. regulators in general and the commissioner in particular.

(f) The history of performance by assuming insurers in the domiciliary jurisdiction.

(g) Any documented evidence of substantial problems with the enforcement of final U.S. judgments in the domiciliary jurisdiction. A jurisdiction will not be considered to be a qualified jurisdiction if the commissioner has determined that it does not adequately and promptly enforce final U.S. judgments or arbitration awards.

(h) Any relevant international standards or guidance with respect to mutual recognition of reinsurance supervision adopted by the International Association of Insurance Supervisors or successor organization.

(i) Any other matters deemed relevant by the commissioner.

iii. A list of qualified jurisdictions shall be published through the NAIC Committee Process. The commissioner shall consider this list in determining qualified jurisdictions. If the commissioner approves a jurisdiction as qualified that does not appear on the list of qualified jurisdictions, the commissioner shall provide thoroughly documented justification with respect to the criteria provided under paragraphs 12.k.ii.(a) to (i).

iv. U.S. jurisdictions that meet the requirements for accreditation under the NAIC financial standards and accreditation program shall be recognized as qualified jurisdictions.

l. Recognition of Certification Issued by an NAIC Accredited Jurisdiction

i. If an applicant for certification has been certified as a reinsurer in an NAIC accredited jurisdiction, the commissioner has the discretion to defer to that jurisdiction's certification, and to defer to the rating assigned by that jurisdiction, if the assuming insurer submits a properly executed Form CR-1 and such additional information as the commissioner requires. The assuming insurer shall be considered to be a certified reinsurer in this State.

ii. Any change in the certified reinsurer's status or rating in the other jurisdiction shall apply automatically in this State as of the date it takes effect in the other jurisdiction. The certified reinsurer shall notify the commissioner of any change in its status or rating within 10 days after receiving notice of the change.

iii. The commissioner may withdraw recognition of the other jurisdiction's rating at any time and assign a new rating in accordance with paragraph 12.j. of this appendix.

iv. The commissioner may withdraw recognition of the other jurisdiction's certification at any time, with written notice to the certified reinsurer. Unless the commissioner suspends or revokes the certified reinsurer's certification in accordance with paragraph 12.j. of this appendix, the certified reinsurer's certification shall remain in good standing in the domestic state of the ceding insurer for a period of three (3) months, which shall be extended if additional time is necessary to consider the assuming insurer's application for certification in this State.

m. Mandatory Funding Clause. In addition to the clauses required under *SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance* and *SSAP No. 62—Property and Casualty Reinsurance*, reinsurance contracts entered into or renewed under paragraph 12 of this appendix shall include a proper funding clause, which requires the certified reinsurer to provide and maintain security in an amount sufficient to avoid the imposition of any financial statement penalty on the ceding insurer under this section for reinsurance ceded to the certified reinsurer.

n. The commissioner shall comply with all reporting and notification requirements that may be established by the NAIC with respect to certified reinsurers and qualified jurisdictions.

13. Credit shall be allowed when the reinsurance is ceded to an assuming insurer meeting each of the conditions set forth in paragraphs 13.a. through 13.h. Credit shall be allowed for reinsurance ceded by a domestic insurer to an assuming insurer that is licensed to write reinsurance by, and has its head office or is domiciled in, a Reciprocal Jurisdiction, and which meets the other requirements of paragraph 13.

a. The assuming insurer must have its head office or be domiciled in, as applicable, and be licensed in a Reciprocal Jurisdiction. A "Reciprocal Jurisdiction" is a jurisdiction that meets one of the following:

i. A non-U.S. jurisdiction that is subject to an in-force covered agreement with the United States, each within its legal authority or, in the case of a covered agreement between the United States and European Union, is a member state of the European Union. For purposes of this subsection, a "covered agreement" is an agreement entered into pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act, 31 U.S.C. §§ 313 and 314, that is currently in effect or in a period of provisional application and addresses the elimination, under specified conditions, of collateral requirements as a condition for entering into any reinsurance agreement with a ceding insurer domiciled in this state or for allowing the ceding insurer to recognize credit for reinsurance;

ii. A U.S. jurisdiction that meets the requirements for accreditation under the NAIC financial standards and accreditation program; or

iii. A qualified jurisdiction, as determined by the commissioner, which is not otherwise described in paragraphs 13.a.i. or 13.a.ii. and which the commissioner determines meets all of the following additional requirements:

(a) Provides that an insurer which has its head office or is domiciled in such qualified jurisdiction shall receive credit for reinsurance ceded to a U.S.-domiciled assuming insurer in the same manner as credit for reinsurance is received for reinsurance assumed by insurers domiciled in such qualified jurisdiction;

(b) Does not require a U.S.-domiciled assuming insurer to establish or maintain a local presence as a condition for entering into a reinsurance agreement with any ceding insurer subject to regulation by the non-U.S. jurisdiction or as a condition to allow the ceding insurer to recognize credit for such reinsurance;

(c) Recognizes the U.S. state regulatory approach to group supervision and group capital, by providing written confirmation by a competent regulatory authority, in such qualified jurisdiction, that insurers and insurance groups that are domiciled or maintain their headquarters in this state or another jurisdiction accredited by the NAIC shall be subject only to worldwide prudential insurance group supervision including worldwide group governance, solvency and capital, and reporting, as applicable, by the commissioner or the commissioner of the domiciliary state and will not be subject to group supervision at the level of the worldwide parent undertaking of the insurance or reinsurance group by the qualified jurisdiction; and

(d) Provides written confirmation by a competent regulatory authority in such qualified jurisdiction that information regarding insurers and their parent, subsidiary, or affiliated entities, if applicable, shall be provided to the commissioner in accordance with a memorandum of understanding or similar document between the commissioner and such qualified jurisdiction, including but not limited to the International Association of Insurance Supervisors Multilateral Memorandum of Understanding or other multilateral memoranda of understanding coordinated by the NAIC.

b. The assuming insurer must have and maintain on an ongoing basis minimum capital and surplus, or its equivalent, calculated on at least an annual basis as of the preceding December 31 or at the annual date otherwise statutorily reported to the Reciprocal Jurisdiction, and confirmed as set forth in paragraph 13.g. according to the methodology of its domiciliary jurisdiction, in the following amounts:

i. No less than $250,000,000; or

ii. If the assuming insurer is an association, including incorporated and individual unincorporated underwriters:

(a) Minimum capital and surplus equivalents (net of liabilities) or own funds of the equivalent of at least $250,000,000; and

(b) A central fund containing a balance of the equivalent of at least $250,000,000.

c. The assuming insurer must have and maintain on an ongoing basis a minimum solvency or capital ratio, as applicable, as follows:

i. If the assuming insurer has its head office or is domiciled in a Reciprocal Jurisdiction as defined in paragraph 13.a.i., the ratio specified in the applicable covered agreement;

ii. If the assuming insurer is domiciled in a Reciprocal Jurisdiction as defined in paragraph 13.a.ii., a risk-based capital (RBC) ratio of three hundred percent (300%) of the authorized control level, calculated in accordance with the formula developed by the NAIC; or

iii. If the assuming insurer is domiciled in a Reciprocal Jurisdiction as defined in paragraph 13.a.iii., after consultation with the Reciprocal Jurisdiction and considering any recommendations published through the NAIC Committee Process, such solvency or capital ratio as the commissioner determines to be an effective measure of solvency.

d. The assuming insurer must agree and provide adequate assurance to the commissioner, in a form of a properly executed Form RJ-1, as follows:

i. The assuming insurer must provide prompt written notice and explanation to the commissioner if it falls below the minimum requirements set forth in paragraphs 13.b. or 13.c., or if any regulatory action is taken against it for serious noncompliance with applicable law;

ii. The assuming insurer must consent in writing to the jurisdiction of the courts of this state and to the appointment of the commissioner as agent for service of process. The commissioner may require that consent for service of process be provided to the commissioner and included in each reinsurance agreement. Nothing in this provision shall limit, or in any way alter, the capacity of parties to a reinsurance agreement to agree to alternative dispute resolution mechanisms, except to the extent such agreements are unenforceable under applicable insolvency or delinquency laws;

iii. The assuming insurer must consent in writing to pay all final judgments, wherever enforcement is sought, obtained by a ceding insurer or its legal successor, that have been declared enforceable in the jurisdiction where the judgment was obtained;

iv. Each reinsurance agreement must include a provision requiring the assuming insurer to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities attributable to reinsurance ceded pursuant to that agreement if the assuming insurer resists enforcement of a final judgment that is enforceable under the law of the jurisdiction in which it was obtained or a properly enforceable arbitration award, whether obtained by the ceding insurer or by its legal successor on behalf of its resolution estate; and

v. The assuming insurer must confirm that it is not presently participating in any solvent scheme of arrangement which involves this state's ceding insurers, and agree to notify the ceding insurer and the commissioner and to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities to the ceding insurer, should the assuming insurer enter into such a solvent scheme of arrangement. Such security shall be in a form consistent with the provisions of paragraph 12 and paragraph 19. The term "solvent scheme of arrangement" means a foreign or alien statutory or regulatory compromise procedure subject to requisite majority creditor approval and judicial sanction in the assuming insurer's home jurisdiction either to finally commute liabilities of duly noticed classed members or creditors of a solvent debtor, or to reorganize or restructure the debts and obligations of a solvent debtor on a final basis, and which may be subject to judicial recognition and enforcement of the arrangement by a governing authority outside the ceding insurer's home jurisdiction.

vi. The assuming insurer must agree in writing to meet the applicable information filing requirements as set forth in paragraph 13.e.

e. The assuming insurer or its legal successor must provide, if requested by the commissioner, on behalf of itself and any legal predecessors, the following documentation to the commissioner:

i. For the two years preceding entry into the reinsurance agreement and on an annual basis thereafter, the assuming insurer's annual audited financial statements, in accordance with the applicable law of the jurisdiction of its head office or domiciliary jurisdiction, as applicable, including the external audit report;

ii. For the two years preceding entry into the reinsurance agreement, the solvency and financial condition report or actuarial opinion, if filed with the assuming insurer's supervisor;

iii. Prior to entry into the reinsurance agreement and not more than semi-annually thereafter, an updated list of all disputed and overdue reinsurance claims outstanding for 90 days or more, regarding reinsurance assumed from ceding insurers domiciled in the United States; and

iv. Prior to entry into the reinsurance agreement and not more than semi-annually thereafter, information regarding the assuming insurer's assumed reinsurance by ceding insurer, ceded reinsurance by the assuming insurer, and reinsurance recoverable on paid and unpaid losses by the assuming insurer to allow for the evaluation of the criteria set forth in paragraph 13.f.

f. The assuming insurer must maintain a practice of prompt payment of claims under reinsurance agreements. The lack of prompt payment will be evidenced if any of the following criteria is met:

i. More than fifteen percent (15%) of the reinsurance recoverables from the assuming insurer are overdue and in dispute as reported to the commissioner;

ii. More than fifteen percent (15%) of the assuming insurer's ceding insurers or reinsurers have overdue reinsurance recoverable on paid losses of 90 days or more which are not in dispute and which exceed for each ceding insurer $100,000, or as otherwise specified in a covered agreement; or

iii. The aggregate amount of reinsurance recoverable on paid losses which are not in dispute, but are overdue by 90 days or more, exceeds $50,000,000, or as otherwise specified in a covered agreement.

g. The assuming insurer's supervisory authority must confirm to the commissioner on an annual basis, as of the preceding December 31 or at the annual date otherwise statutorily reported to the Reciprocal Jurisdiction, that the assuming insurer complies with the requirements set forth in paragraphs 13.b. and 13.c.

h. Nothing in this provision precludes an assuming insurer from providing the commissioner with information on a voluntary basis.

i. The commissioner shall timely create and publish a list of Reciprocal Jurisdictions.

i. A list of Reciprocal Jurisdictions is published through the NAIC Committee Process. The commissioner's list shall include any Reciprocal Jurisdiction as defined under paragraphs 13.a.i. and 13.a.ii., and shall consider any other Reciprocal Jurisdiction included on the NAIC list. The commissioner may approve a jurisdiction that does not appear on the NAIC list of Reciprocal Jurisdictions.

ii. The commissioner may remove a jurisdiction from the list of Reciprocal Jurisdictions upon a determination that the jurisdiction no longer meets one or more of the requirements of a Reciprocal Jurisdiction, except that the commissioner shall not remove from the list a Reciprocal Jurisdiction as defined under paragraphs 13.a.i. and 13.a.ii. Upon removal of a Reciprocal Jurisdiction from this list credit for reinsurance ceded to an assuming insurer domiciled in that jurisdiction shall be allowed, if otherwise allowed pursuant to this appendix.

j. The commissioner shall timely create and publish a list of assuming insurers that have satisfied the conditions set forth in paragraph 13 and to which cessions shall be granted credit in accordance with paragraph 13.

i. If an NAIC accredited jurisdiction has determined that the conditions set forth in paragraph 13 have been met, the commissioner has the discretion to defer to that jurisdiction's determination, and add such assuming insurer to the list of assuming insurers to which cessions shall be granted credit in accordance with this subsection. The commissioner may accept financial documentation filed with another NAIC accredited jurisdiction or with the NAIC in satisfaction of the requirements of paragraph 13.b., 13.c. and 13.d.

ii. When requesting that the commissioner defer to another NAIC accredited jurisdiction's determination, an assuming insurer must submit a properly executed Form RJ-1 and additional information as the commissioner may require. A state that has received such a request will notify other states through the NAIC Committee Process and provide relevant information with respect to the determination of eligibility.

k. If the commissioner determines that an assuming insurer no longer meets one or more of the requirements under this section, the commissioner may revoke or suspend the eligibility of the assuming insurer for recognition under this section.

i. While an assuming insurer's eligibility is suspended, no reinsurance agreement issued, amended or renewed after the effective date of the suspension qualifies for credit except to the extent that the assuming insurer's obligations under the contract are secured in accordance with paragraph 19.

ii. If an assuming insurer's eligibility is revoked, no credit for reinsurance may be granted after the effective date of the revocation with respect to any reinsurance agreements entered into by the assuming insurer, including reinsurance agreements entered into prior to the date of revocation, except to the extent that the assuming insurer's obligations under the contract are secured in a form acceptable to the commissioner and consistent with the provisions of paragraph 19.

l. Before denying statement credit or imposing a requirement to post security with respect to paragraph 13.k. or adopting any similar requirement that will have substantially the same regulatory impact as security, the commissioner shall:

i. Communicate with the ceding insurer, the assuming insurer, and the assuming insurer's supervisory authority that the assuming insurer no longer satisfies one of the conditions listed in paragraphs 13.a., 13.b. and 13.c.;

ii. Provide the assuming insurer with 30 days from the initial communication to submit a plan to remedy the defect, and 90 days from the initial communication to remedy the defect, except in exceptional circumstances in which a shorter period is necessary for policyholder and other consumer protection;

iii. After the expiration of 90 days or less, as set out in paragraph 13.l.ii., if the commissioner determines that no or insufficient action was taken by the assuming insurer, the commissioner may impose any of the requirements as set out in this subsection; and

iv. Provide a written explanation to the assuming insurer of any of the requirements set out in paragraph 13.l.

m. If subject to a legal process of rehabilitation, liquidation or conservation, as applicable, the ceding insurer, or its representative, may seek and, if determined appropriate by the court in which the proceedings are pending, may obtain an order requiring that the assuming insurer post security for all outstanding liabilities.

n. Nothing in this subsection shall limit or in any way alter the capacity of parties to a reinsurance agreement to agree on requirements for security or other terms in that reinsurance agreement, except as expressly prohibited by this appendix.

o. Credit may be taken under this subsection only for reinsurance agreements entered into, amended, or renewed on or after the effective date of the statute adding this subsection, and only with respect to losses incurred and reserves reported on or after the later of (i) the date on which the assuming insurer has met all eligibility requirements pursuant to paragraphs 13.a. through 13.h., and (ii) the effective date of the new reinsurance agreement, amendment, or renewal.

i. This paragraph does not alter or impair a ceding insurer's right to take credit for reinsurance, to the extent that credit is not available under this subsection, as long as the reinsurance qualifies for credit under any other applicable provision of this appendix.

ii. Nothing in this subsection shall authorize an assuming insurer to withdraw or reduce the security provided under any reinsurance agreement except as permitted by the terms of the agreement.

iii. Nothing in this subsection shall limit, or in any way alter, the capacity of parties to any reinsurance agreement to renegotiate the agreement.

14. Credit shall be allowed when the reinsurance is ceded to an assuming insurer not meeting the requirements of paragraphs 8, 9, 10, 11, 12 or 13 of this appendix, but only as to the insurance of risks located in jurisdictions where the reinsurance is required by applicable law or regulation of that jurisdiction.

15. If the assuming insurer is not licensed, accredited or certified to transact insurance or reinsurance in the domiciliary state of the ceding insurer, the credit allowed by paragraphs 10 and 11 of this appendix shall not be allowed unless the assuming insurer agrees in the reinsurance agreements:

a. i. That in the event of the failure of the assuming insurer to perform its obligations under the terms of the reinsurance agreement, the assuming insurer, at the request of the ceding insurer, shall submit to the jurisdiction of any court of competent jurisdiction in any state of the United States, will comply with all requirements necessary to give the court jurisdiction, and will abide by the final decision of the court or of any appellate court in the event of an appeal.

ii. To designate the commissioner or a designated attorney as its true and lawful attorney upon whom may be served any lawful process in any action, suit or proceeding instituted by or on behalf of the ceding insurer.

b. This paragraph 15 is not intended to conflict with or override the obligation of the parties to a reinsurance agreement to arbitrate their disputes, if this obligation is created in the agreement.

16. If the assuming insurer does not meet the requirements of paragraphs 8, 9 or 10, the credit allowed by paragraph 11 or 12 of this appendix shall not be allowed unless the assuming insurer agrees in the trust agreements to the following conditions:

a. Notwithstanding any other provisions in the trust instrument, if the trust fund is inadequate because it contains an amount less than the amount required by paragraph 11 c. of this appendix, or if the grantor of the trust has been declared insolvent or placed into receivership, rehabilitation, liquidation or similar proceedings under the laws of its state or country of domicile, the trustee shall comply with an order of the commissioner with regulatory oversight over the trust or with an order of a court of competent jurisdiction directing the trustee to transfer to the commissioner with regulatory oversight all of the assets of the trust fund.

b. The assets shall be distributed by and claims shall be filed with and valued by the commissioner with regulatory oversight in accordance with the laws of the state in which the trust is domiciled that are applicable to the liquidation of domestic insurance companies.

c. If the commissioner with regulatory oversight determines that the assets of the trust fund or any part thereof are not necessary to satisfy the claims of the U.S. ceding insurers of the grantor of the trust, the assets or part thereof shall be returned by the commissioner with regulatory oversight to the trustee for distribution in accordance with the trust agreement.

d. The grantor shall waive any right otherwise available to it under U.S. law that is inconsistent with this provision.

17. If an accredited or certified reinsurer ceases to meet the requirements for accreditation or certification, the domestic state of the ceding insurer may suspend or revoke the reinsurer's accreditation or certification.

a. The domestic state of the ceding insurer must give the reinsurer notice an opportunity for hearing. The suspension or revocation may not take effect until after the state's order on hearing, unless:

i. The reinsurer waives its right to hearing;

ii. The state's order is based on regulatory action by the reinsurer's domiciliary jurisdiction or the voluntary surrender or termination of the reinsurer's eligibility to transact insurance or reinsurance business in its domiciliary jurisdiction or in the primary certifying state of the reinsurer under paragraph 12.f. of this appendix; or

iii. The domestic state of the ceding insurer finds that an emergency requires immediate action and a court of competent jurisdiction has not stayed the state's action.

b. While a reinsurer's accreditation or certification is suspended, no reinsurance contract issued or renewed after the effective date of the suspension qualifies for credit except to the extent that the reinsurer's obligations under the contract are secured in accordance with paragraph 19. If a reinsurer's accreditation or certification is revoked, no credit for reinsurance may be granted after the effective date of the revocation except to the extent that the reinsurer's obligations under the contract are secured in accordance with paragraph 12.e. or paragraph 19.

Valuation of and Requirements for Trust Assets

18. Assets deposited in the trust shall be valued according to their current fair market value and shall consist only of cash in U.S. dollars, certificates of deposit issued by a U.S. financial institution as defined in paragraph 53, clean, irrevocable, unconditional and "evergreen" letters of credit issued or confirmed by a qualified U.S. financial institution, as defined in paragraph 53, and investments of the type specified in this paragraph, but investments in or issued by an entity controlling, controlled by or under common

control with either the grantor or beneficiary of the trust shall not exceed five percent (5%) of total investments. No more than twenty percent (20%) of the total of the investments in the trust may be foreign investments authorized under paragraphs 18.a.v., 18.c., 18.f.ii. or 18.g., and no more than ten percent (10%) of the total of the investments in the trust may be securities denominated in foreign currencies. For purposes of applying the preceding sentence, a depository receipt denominated in U.S. dollars and representing rights conferred by a foreign security shall be classified as a foreign investment denominated in a foreign currency. The assets of a trust shall be invested only as follows:

a. Government obligations that are not in default as to principal or interest, that are valid and legally authorized and that are issued, assumed or guaranteed by:

i. The United States or by any agency or instrumentality of the United States;

ii. A state of the United States;

iii. A territory, possession or other governmental unit of the United States;

iv. An agency or instrumentality of a governmental unit referred to in paragraphs 18.a.i. and 18.a.ii. if the obligations shall be by law (statutory of otherwise) payable, as to both principal and interest, from taxes levied or by law required to be levied or from adequate special revenues pledged or otherwise appropriated or by law required to be provided for making these payments, but shall not be obligations eligible for investment under this paragraph if payable solely out of special assessments on properties benefited by local improvements; or

v. The government of any other country that is a member of the Organization for Economic Cooperation and Development and whose government obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC;

b. Obligations that are issued in the United States, or that are dollar denominated and issued in a non-U.S. market, by a solvent U.S. institution (other than an insurance company) or that are assumed or guaranteed by a solvent U.S. institution (other than an insurance company) and that are not in default as to principal or interest if the obligations:

i. Are rated A or higher (or the equivalent) by a securities rating agency recognized by the Securities Valuation Office of the NAIC, or if not so rated, are similar in structure and other material respects to other obligations of the same institution that are so rated;

ii. Are insured by at least one authorized insurer (other than the investing insurer or a parent, subsidiary or affiliate of the investing insurer) licensed to insure obligations in this state and, after considering the insurance, are rated AAA (or the equivalent) by a securities rating agency recognized by the Securities Valuation Office of the NAIC; or

iii. Have been designated as Class One or Class Two by the Securities Valuation Office of the NAIC;

c. Obligations issued, assumed or guaranteed by a solvent non U.S. institution chartered in a country that is a member of the Organization for Economic Cooperation and Development or obligations of U.S. corporations issued in a non-U.S. currency, provided that in either case the obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC;

d. An investment made pursuant to the provisions of paragraphs 18.a., 18.b. or 18.c. shall be subject to the following additional limitations:

i. An investment in or loan upon the obligations of an institution other than an institution that issues mortgage-related securities shall not exceed five percent (5%) of the assets of the trust;

ii. An investment in any one mortgage-related security shall not exceed five percent (5%) of the assets of the trust;

iii. The aggregate total investment in mortgage-related securities shall not exceed twenty-five percent (25%) of the assets of the trust; and

iv. Preferred or guaranteed shares issued or guaranteed by a solvent U.S. institution are permissible investments if all of the institution's obligations are eligible as investments under paragraphs 18.b.i. and 18.b.iii., but shall not exceed two percent (2%) of the assets of the trust.

e. As used in this appendix:

i. "Mortgage-related security" means an obligation that is rated AA or higher (or the equivalent) by a securities rating agency recognized by the Securities Valuation Office of the NAIC and that either:

(a) Represents ownership of one or more promissory notes or certificates of interest or participation in the notes (including any rights designed to assure servicing of, or the receipt or timeliness of receipt by the holders of the notes, certificates, or participation of amounts payable under, the notes, certificates or participation), that:

(1) Are directly secured by a first lien on a single parcel of real estate, including stock allocated to a dwelling unit in a residential cooperative housing corporation, upon which is located a dwelling or mixed residential and commercial structure, or on a residential manufactured home as defined in 42 U.S.C.A. Section 5402(6), whether the manufactured home is considered real or personal property under the laws of the state in which it is located; and

(2) Were originated by a savings and loan association, savings bank, commercial bank, credit union, insurance company, or similar institution that is supervised and examined by a federal or state housing authority, or by a mortgagee approved by the Secretary of Housing and Urban Development pursuant to 12 U.S.C.A. Sections 1709 and 1715-b, or, where the notes involve a lien on the manufactured home, by an institution or by a financial institution approved for insurance by the Secretary of Housing and Urban Development pursuant to 12 U.S.C.A. Section 1703; or

(b) Is secured by one or more promissory notes or certificates of deposit or participations in the notes (with or without recourse to the insurer of the notes) and, by its terms, provides for payments of principal in relation to payments, or reasonable projections of payments, or notes meeting the requirements of paragraphs 18.e.i.(a)(1) and 18.e.i.(a)(2);

ii. "Promissory note," when used in connection with a manufactured home, shall also include a loan, advance or credit sale as evidenced by a retail installment sales contract or other instrument.

f. Equity interests

i. Investments in common shares or partnership interests of a solvent U.S. institution are permissible if:

(a) Its obligations and preferred shares, if any, are eligible as investments under this paragraph; and

(b) The equity interests of the institution (except an insurance company) are registered on a national securities exchange as provided in the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a to 78kk or otherwise registered pursuant to that Act, and if otherwise registered, price quotations for them are furnished through a nationwide automated quotations system approved by the Financial Industry Regulatory Authority, or successor organization. A trust shall not invest in equity interests under this paragraph an amount exceeding one percent (1%) of the assets of the trust even though the equity interests are not so registered and are not issued by an insurance company.

ii. Investments in common shares of a solvent institution organized under the laws of a country that is a member of the Organization for Economic Cooperation and Development, if:

(a) All its obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC; and

(b) The equity interests of the institution are registered on a securities exchange regulated by the government of a country that is a member of the Organization for Economic Cooperation and Development.

iii. An investment in or loan upon any one institution's outstanding equity interests shall not exceed one percent (1%) of the assets of the trust. The cost of an investment in equity interests made pursuant to this paragraph, when added to the aggregate cost of other investments in equity interests then held pursuant to this paragraph, shall not exceed ten percent (10%) of the assets in the trust;

g. Obligations issued, assumed or guaranteed by a multinational development bank, provided the obligations are rated A or higher, or the equivalent, by a rating agency recognized by the Securities Valuation Office of the NAIC.

h. Investment companies:

i. Securities of an investment company registered pursuant to the Investment Company Act of 1940, 15 U.S.C. § 802, are allowable investments if the investment company:

(a) Invests at least ninety percent (90%) of its assets in the types of securities that qualify as an investment under paragraphs 18.a., 18.b., or 18.c., or invests in securities that are determined to be substantively similar to the types of securities set forth in paragraphs 18.a., 18.b., or 18.c.; or

(b) Invests at least ninety percent (90%) of its assets in the types of equity interests that qualify as an investment under paragraph 18.f.i.;

ii. Investments made by a trust in investment companies under this paragraph shall not exceed the following limitations:

(a) An investment in an investment company qualifying under paragraph 18.h.i.(a) shall not exceed ten percent (10%) of the assets in the trust and the aggregate amount of investment in qualifying investment companies shall not exceed twenty-five percent (25%) of the assets in the trust; and

(b) Investments in an investment company qualifying under paragraph 18.h.i.(b) of this paragraph shall not exceed five percent (5%) of the assets in the trust and the aggregate amount of investment in qualifying investment companies shall be included when calculating the permissible aggregate value of equity interests pursuant to paragraph 18.f.i.

i. Letters of Credit

i. In order for a letter of credit to qualify as an asset of the trust, the trustee shall have the right and the obligation pursuant to the deed of trust or some other binding agreement (as duly approved by the commissioner), to immediately draw down the full amount of the letter of credit and hold the proceeds in trust for the beneficiaries of the trust if the letter of credit will otherwise expire without being renewed or replaced.

ii. The trust agreement shall provide that the trustee shall be liable for its negligence, willful misconduct or lack of good faith. The failure of the trustee to draw against the letter of credit in circumstances where such draw would be required shall be deemed to be negligence and/or willful misconduct.

Asset or Reduction from Liability for Reinsurance Ceded by a Domestic Insurer to an Assuming Insurer not Meeting the Requirements detailed above under "Credit Allowed a Domestic Ceding Insurer" (paragraphs 7-18)

19. An asset or a reduction from liability for the reinsurance ceded by a domestic insurer to an assuming insurer not meeting the requirements under "Credit Allowed a Domestic Ceding Insurer" (paragraphs 7-18) shall be allowed in an amount not exceeding the liabilities carried by the ceding insurer. The reduction shall be in the amount of funds held by or on behalf of the ceding insurer, including funds held in trust for the ceding insurer, under a reinsurance contract with the assuming insurer as security for the payment of obligations thereunder, if the security is held in the United States subject to withdrawal solely by, and under the exclusive control of, the ceding insurer; or, in the case of a trust, held in a qualified U.S. financial institution, as defined under "Qualified U.S. Financial Institutions" at paragraph 54. This security may be in the form of:

a. Cash;

b. Securities listed by the Securities Valuation Office of the National Association of Insurance Commissioners, including those deemed exempt from filing as defined by the *Purposes and Procedures Manual of the NAIC Securities Valuation Office*, and qualifying as admitted assets;

Drafting Note: The Purposes and Procedures Manual of the NAIC Securities Valuation Office has been renamed the Purposes and Procedures Manual of the NAIC Investment Analysis Office; however, the Model law refers to the previous name.

c. i. Clean, irrevocable, unconditional and evergreen letters of credit, issued or confirmed by a qualified U.S. financial institution, as defined in paragraph 53, effective no later than December 31 of the year for which the filing is being made, and in the possession of, or in trust for, the ceding insurer on or before the filing date of its annual statement;

ii. Letters of credit meeting applicable standards of issuer acceptability as of the dates of their issuance (or confirmation) shall, notwithstanding the issuing (or confirming) institution's subsequent failure to meet applicable standards of issuer acceptability, continue to be acceptable as security until their expiration, extension, renewal, modification or amendment, whichever first occurs.

d. An admitted asset or a reduction from liability for reinsurance ceded to an unauthorized assuming insurer pursuant to this appendix shall be allowed only when the requirements of paragraph 15 and the applicable portions under the sections below titled "Trust Agreements Qualified under Paragraph 19", "Letters of Credit Qualified under Paragraph 19", and "Other Security" at paragraph 51.

Trust Agreements Qualified under Paragraph 19

20. The trust agreement shall be entered into between the beneficiary, the grantor and a trustee, which shall be a qualified U.S. financial institution as defined in paragraph 54.

21. The trust agreement shall create a trust account into which assets shall be deposited.

22. All assets in the trust account shall be held by the trustee at the trustee's office in the United States.

23. The trust agreement shall provide that:

a. The beneficiary shall have the right to withdraw assets from the trust account at any time, without notice to the grantor, subject only to written notice from the beneficiary to the trustee;

b. No other statement or document is required to be presented to withdraw assets, except that the beneficiary may be required to acknowledge receipt of withdrawn assets;

c. It is not subject to any conditions or qualifications outside of the trust agreement; and

d. It shall not contain references to any other agreements or documents except as provided for in paragraph 30.

24. The trust agreement shall be established for the sole benefit of the beneficiary.

25. The trust agreement shall require the trustee to:

a. Receive assets and hold all assets in a safe place;

b. Determine that all assets are in such form that the beneficiary, or the trustee upon direction by the beneficiary, may whenever necessary negotiate any such assets, without consent or signature from the grantor or any other person or entity;

c. Furnish to the grantor and the beneficiary a statement of all assets in the trust account upon its inception and at intervals no less frequent than the end of each calendar quarter;

d. Notify the grantor and the beneficiary within ten (10) days, of any deposits to or withdrawals from the trust account;

e. Upon written demand of the beneficiary, immediately take any and all steps necessary to transfer absolutely and unequivocally all right, title and interest in the assets held in the trust account to the beneficiary and deliver physical custody of the assets to the beneficiary; and

f. Allow no substitutions or withdrawals of assets from the trust account, except on written instructions from the beneficiary, except that the trustee may, without the consent of but with notice to the beneficiary, upon call or maturity of any trust asset, withdraw such asset upon condition that the proceeds are paid into the trust account.

26. The trust agreement shall provide that at least thirty (30) days, but not more than forty-five (45) days, prior to termination of the trust account, written notification of termination shall be delivered by the trustee to the beneficiary.

27. The trust agreement shall be made subject to and governed by the laws of the state in which the trust is domiciled.

28. The trust agreement shall prohibit invasion of the trust corpus for the purpose of paying compensation to, or reimbursing the expenses of, the trustee. In order for a letter of credit to qualify as an asset of the trust, the trustee shall have the right and the obligation pursuant to the deed of trust or some other binding agreement, as duly approved by the commissioner, to immediately draw down the full amount of the letter of credit and hold the proceeds in trust for the beneficiaries of the trust if the letter of credit will otherwise expire without being renewed or replaced.

29. The trust agreement shall provide that the trustee shall be liable for its negligence, willful misconduct or lack of good faith. The failure of the trustee to draw against the letter of credit in circumstances where such draw would be required shall be deemed to be negligence and/or willful misconduct.

30. Notwithstanding other provisions of this appendix, when a trust agreement is established in conjunction with a reinsurance agreement covering risks other than life, annuities and accident and health, where it is customary practice to provide a trust agreement for a specific purpose, the trust agreement may provide that the ceding insurer shall undertake to use and apply amounts drawn upon the trust account, without diminution because of the insolvency of the ceding insurer or the assuming insurer, only for the following purposes:

a. To pay or reimburse the ceding insurer for the assuming insurer's share under the specific reinsurance agreement regarding any losses and allocated loss expenses paid by the ceding insurer, but not recovered from the assuming insurer, or for unearned premiums due to the ceding insurer if not otherwise paid by the assuming insurer;

b. To make payment to the assuming insurer of any amounts held in the trust account that exceed 102 percent of the actual amount required to fund the assuming insurer's obligations under the specific reinsurance agreement; or

c. Where the ceding insurer has received notification of termination of the trust account and where the assuming insurer's entire obligations under the specific reinsurance agreement remain unliquidated and undischarged ten (10) days prior to the termination date, to withdraw amounts equal to the obligations and deposit those amounts in a separate account, in the name of the ceding insurer in any qualified U.S. financial institution as defined in paragraph 54 apart from its general assets, in trust for such uses and purposes specified in paragraphs 30.a. and 30.b. as may remain executory after such withdrawal and for any period after the termination date.

31. Notwithstanding other provisions of this appendix, when a trust agreement is established to meet the requirements of paragraph 19 in conjunction with a reinsurance agreement covering life, annuities or accident and health risks, where it is customary to provide a trust agreement for a specific purpose, the trust agreement may provide that the ceding insurer shall undertake to use and apply amounts drawn upon the trust account, without diminution because of the insolvency of the ceding insurer or the assuming insurer, only for the following purposes:

a. To pay or reimburse the ceding insurer for:

i. The assuming insurer's share under the specific reinsurance agreement of premiums returned, but not yet recovered from the assuming insurer, to the owners of policies reinsured under the reinsurance agreement on account of cancellations of the policies; and

ii. The assuming insurer's share under the specific reinsurance agreement of surrenders and benefits or losses paid by the ceding insurer, but not yet recovered from the assuming insurer, under the terms and provisions of the policies reinsured under the reinsurance agreement;

b. To pay to the assuming insurer amounts held in the trust account in excess of the amount necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer; or

c. Where the ceding insurer has received notification of termination of the trust and where the assuming insurer's entire obligations under the specific reinsurance agreement remain unliquidated and undischarged ten (10) days prior to the termination date, to withdraw amounts equal to the assuming insurer's share of liabilities, to the extent that the liabilities have not yet been funded by the assuming insurer, and deposit those amounts in a separate account, in the name of the ceding insurer in any qualified U. S. financial institution apart from its general assets, in trust for the uses and purposes specified in paragraphs 31.a. and 31.b. as may remain executory after withdrawal and for any period after the termination date.

32. Either the reinsurance agreement or the trust agreement must stipulate that assets deposited in the trust account shall be valued according to their current fair market value and shall consist only of cash in United States dollars, certificates of deposit issued by a United States bank and payable in United States dollars, and investments permitted by the Insurance Code or any combination of the above, provided investments in or issued by an entity controlling, controlled by or under common control with either the grantor or the beneficiary of the trust shall not exceed five percent (5%) of total investments. The agreement may further specify the types of investments to be deposited. If the reinsurance agreement covers life, annuities or accident and health risks, then the provisions required by this paragraph must be included in the reinsurance agreement.

33. Notwithstanding any other provisions in the trust instrument, if the grantor of the trust has been declared insolvent or placed into receivership, rehabilitation, liquidation or similar proceedings under the laws of its state or country of domicile, the trustee shall comply with an order of the commissioner with regulatory oversight over the trust or court of competent jurisdiction directing the trustee to transfer to the commissioner with regulatory oversight or other designated receiver all of the assets of the trust fund. The assets shall be applied in accordance with the priority statutes and laws of the state in which the trust is domiciled applicable to the assets of insurance companies in liquidation. If the commissioner with regulatory oversight determines that the assets of the trust fund or any part thereof are not necessary to

satisfy claims of the U.S. beneficiaries of the trust, the assets or any part of them shall be returned to the trustee for distribution in accordance with the trust agreement.

34. The trust agreement may provide that the trustee may resign upon delivery of a written notice of resignation, effective not less than ninety (90) days after the beneficiary and grantor receive the notice and that the trustee may be removed by the grantor by delivery to the trustee and the beneficiary of a written notice of removal, effective not less than ninety (90) days after the trustee and the beneficiary receive the notice, provided that no such resignation or removal shall be effective until a successor trustee has been duly appointed and approved by the beneficiary and the grantor and all assets in the trust have been duly transferred to the new trustee.

35. The grantor may have the full and unqualified right to vote any shares of stock in the trust account and to receive from time to time payments of any dividends or interest upon any shares of stock or obligations included in the trust account. Any interest or dividends shall be either forwarded promptly upon receipt to the grantor or deposited in a separate account established in the grantor's name.

36. The trustee may be given authority to invest, and accept substitutions of, any funds in the account, provided that no investment or substitution shall be made without prior approval of the beneficiary, unless the trust agreement specifies categories of investments acceptable to the beneficiary and authorizes the trustee to invest funds and to accept substitutions that the trustee determines are at least equal in market value to the assets withdrawn and that are consistent with the restrictions in paragraph 39.b.

37. The trust agreement may provide that the beneficiary may at any time designate a party to which all or part of the trust assets are to be transferred. Transfer may be conditioned upon the trustee receiving, prior to or simultaneously, other specified assets.

38. The trust agreement may provide that, upon termination of the trust account, all assets not previously withdrawn by the beneficiary shall, with written approval by the beneficiary, be delivered over to the grantor.

39. A reinsurance agreement may contain provisions that:

a. Require the assuming insurer to enter into a trust agreement and to establish a trust account for the benefit of the ceding insurer, and specifying what the agreement is to cover;

b. Require the assuming insurer, prior to depositing assets with the trustee, to execute assignments or endorsements in blank, or to transfer legal title to the trustee of all shares, obligations or any other assets requiring assignments, in order that the ceding insurer, or the trustee upon the direction of the ceding insurer, may whenever necessary negotiate these assets without consent or signature from the assuming insurer or any other entity;

c. Require that all settlements of account between the ceding insurer and the assuming insurer be made in cash or its equivalent; and

d. Stipulate that the assuming insurer and the ceding insurer agree that the assets in the trust account, established pursuant to the provisions of the reinsurance agreement, may be withdrawn by the ceding insurer at any time, notwithstanding any other provisions in the reinsurance agreement, and shall be utilized and applied by the ceding insurer or its successors in interest by operation of law, including without limitation any liquidator, rehabilitator, receiver or conservator of such company, without diminution because of insolvency on the part of the ceding insurer or the assuming insurer, only for the following purposes:

i. To pay or reimburse the ceding insurer for:

(a) The assuming insurer's share under the specific reinsurance agreement of premiums returned, but not yet recovered from the assuming insurer, to the owners of policies reinsured under the reinsurance agreement because of cancellations of such policies;

(b) The assuming insurer's share of surrenders and benefits or losses paid by the ceding insurer pursuant to the provisions of the policies reinsured under the reinsurance agreement; and

(c) Any other amounts necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer;

ii. To make payment to the assuming insurer of amounts held in the trust account in excess of the amount necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer.

40. The reinsurance agreement also may contain provisions that:

a. Give the assuming insurer the right to seek approval from the ceding insurer, which shall not be unreasonably or arbitrarily withheld, to withdraw from the trust account all or any part of the trust assets and transfer those assets to the assuming insurer, provided:

i. The assuming insurer shall, at the time of withdrawal, replace the withdrawn assets with other qualified assets having a current fair market value equal to the market value of the assets withdrawn so as to maintain at all times the deposit in the required amount; or

ii. After withdrawal and transfer, the current fair market value of the trust account is no less than 102 percent of the required amount.

b. Provide for the return of any amount withdrawn in excess of the actual amounts required for paragraph 39.d., and for interest payments at a rate not in excess of the prime rate of interest on such amounts;

c. Allow the award by any arbitration panel or court of competent jurisdiction of:

i. Interest at a rate different from that provided in paragraph 40.b.;

ii. Court or arbitration costs;

iii. Attorney's fees; and

iv. Any other reasonable expenses.

41. Financial Reporting - A trust agreement may be used to reduce any liability for reinsurance ceded to an unauthorized assuming insurer in statutory financial statements when established on or before the date of filing of the statutory financial statement of the ceding insurer. Further, the reduction for the existence of an acceptable trust account may be up to the current fair market value of acceptable assets available to be withdrawn from the trust account at that time, but such reduction shall be no greater than the specific obligations under the reinsurance agreement that the trust account was established to secure.

42. The failure of any trust agreement to specifically identify the beneficiary as defined in paragraph 4 shall not be construed to affect any actions or rights that the commissioner may take or possess pursuant to the provisions of the laws of the domiciliary state.

Letters of Credit Qualified under Paragraph 19

43. The letter of credit must be clean, irrevocable, unconditional and issued or confirmed by a qualified U.S. financial institution as defined in paragraph 53. The letter of credit shall contain an issue date and expiration date and shall stipulate that the beneficiary need only draw a sight draft under the letter of credit and present it to obtain funds and that no other document need be presented. The letter of credit also shall indicate that it is not subject to any condition or qualifications outside of the letter of credit. In addition, the letter of credit itself shall not contain reference to any other agreements, documents or entities, except as provided in paragraph 50.a. If a court of law appoints a successor in interest to the named beneficiary, then the named beneficiary includes and is limited to the court appointed domiciliary receiver (including conservator, rehabilitator or liquidator).

44. The heading of the letter of credit may include a boxed section containing the name of the applicant and other appropriate notations to provide a reference for the letter of credit. The boxed section shall be clearly marked to indicate that such information is for internal identification purposes only.

45. The letter of credit shall contain a statement to the effect that the obligation of the qualified U.S. financial institution under the letter of credit is in no way contingent upon reimbursement with respect thereto.

46. The term of the letter of credit shall be for at least one year and shall contain an "evergreen clause" that prevents the expiration of the letter of credit without due notice from the issuer. The "evergreen clause" shall provide for a period of no less than thirty (30) days prior to the expiration date or nonrenewal.

47. The letter of credit shall state whether it is subject to and governed by the laws of the ceding insurers state or the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce (Publication 600) or International Standby Practices of the International Chamber of Commerce Publication 590 (ISP98), or any successor publication, and all drafts drawn thereunder shall be presentable at an office in the United States of a qualified U.S. financial institution.

48. If the letter of credit is made subject to the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce Publication 600 (UCP 600) or International Standby Practices of the International Chamber of Commerce Publication 590 (ISP98), or any successor publication, then the letter of credit shall specifically address and provide for an extension of time to draw against the letter of credit in the event that one or more of the occurrences specified in Article 36 of Publication 600 or any other successor publication, occur.

49. If the letter of credit is issued by a financial institution authorized to issue letters of credit, other than a qualified U.S. financial institution as described in paragraph 43, then the following additional requirements shall be met:

a. The issuing financial institution shall formally designate the confirming qualified U.S. financial institution as its agent for the receipt and payment of the drafts; and

b. The "evergreen clause" shall provide for thirty (30) days notice prior to expiration date for nonrenewal.

50. Reinsurance agreement provisions:

a. The reinsurance agreement in conjunction with which the letter of credit is obtained may contain provisions that:

i. Require the assuming insurer to provide letters of credit to the ceding insurer and specify what they are to cover;

ii. Stipulate that the assuming insurer and ceding insurer agree that the letter of credit provided by the assuming insurer pursuant to the provisions of the reinsurance agreement may be drawn upon at any time, notwithstanding any other provisions in the agreement, and shall be utilized by the ceding insurer or its successors in interest only for one or more of the following reasons:

(a) To pay or reimburse the ceding insurer for:

(1) The assuming insurer's share under the specific reinsurance agreement of premiums returned, but not yet recovered from the assuming insurers, to the owners of policies reinsured under the reinsurance agreement on account of cancellations of such policies;

(2) The assuming insurer's share, under the specific reinsurance agreement, of surrenders and benefits or losses paid by the ceding insurer, but not yet recovered from the assuming insurers, under the terms and provisions of the policies reinsured under the reinsurance agreement; and

(3) Any other amounts necessary to secure the credit or reduction from liability for reinsurance taken by the ceding insurer;

(b) Where the letter of credit will expire without renewal or be reduced or replaced by a letter of credit for a reduced amount and where the assuming insurer's entire obligations under the reinsurance agreement remain unliquidated and undischarged ten (10) days prior to the termination date, to withdraw amounts equal to the assuming insurer's share of the liabilities, to the extent that the liabilities have not yet been funded by the assuming insurer and exceed the amount of any reduced or replacement letter of credit, and deposit those amounts in a separate account in the name of the ceding insurer in a qualified U.S. financial institution apart from its general assets, in trust for such uses and purposes specified in paragraph 50.a.ii.(a) as may remain after withdrawal and for any period after the termination date.

iii. All of the provisions of paragraph 50.a. shall be applied without diminution because of insolvency on the part of the ceding insurer or assuming insurer.

b. Nothing contained in paragraph 50.a. shall preclude the ceding insurer and assuming insurer from providing for:

i. An interest payment, at a rate not in excess of the prime rate of interest, on the amounts held pursuant to paragraph 50.a.ii.; or

ii. The return of any amounts drawn down on the letters of credit in excess of the actual amounts required for the above or any amounts that are subsequently determined not to be due.

Other Security

51. A ceding insurer may take credit for unencumbered funds withheld by the ceding insurer in the United States subject to withdrawal solely by the ceding insurer and under its exclusive control.

52. Credit will not be granted, nor an asset or reduction from liability allowed, to a ceding insurer for reinsurance effected with assuming insurers meeting the requirements of this appendix or otherwise in compliance with this appendix unless the reinsurance agreement:

a. Includes a proper insolvency clause, which stipulates that reinsurance is payable directly to the liquidator or successor without diminution regardless of the status of the ceding company;

b. Includes a provision pursuant to Section [cite state law equivalent to Section 2 of the Credit for Reinsurance Model Law] whereby the assuming insurer, if an unauthorized assuming insurer, has submitted to the jurisdiction of an alternative dispute resolution panel or court of competent jurisdiction within the United States, has agreed to comply with all requirements necessary to give the court or panel jurisdiction, has designated an agent upon whom service of process may be effected, and has agreed to abide by the final decision of the court or panel; and

c. Includes a proper reinsurance intermediary clause, if applicable, which stipulates that the credit risk for the intermediary is carried by the assuming insurer.

Qualified U.S. Financial Institutions

53. For purposes of paragraphs 18, 19.c., 43 and 49, a "qualified U.S. financial institution" means an institution that:

a. Is organized or (in the case of a U.S. office of a foreign banking organization) licensed, under the laws of the United States or any state thereof;

b. Is regulated, supervised and examined by U.S. federal or state authorities having regulatory authority over banks and trust companies; and

c. Has been determined by either the commissioner or the Securities Valuation Office of the National Association of Insurance Commissioners to meet such standards of financial condition and standing as are considered necessary and appropriate to regulate the quality of financial institutions whose letters of credit will be acceptable to the commissioner.

54. A "qualified U.S. financial institution" means, for purposes of those provisions of this appendix specifying those institutions that are eligible to act as a fiduciary of a trust, an institution that:

a. Is organized, or in the case of a U.S. branch or agency office of a foreign banking organization, licensed, under the laws of the United States or any state thereof and has been granted authority to operate with fiduciary powers; and

b. Is regulated, supervised and examined by federal or state authorities having regulatory authority over banks and trust companies.

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Life and Health Reinsurance Agreements

Relevant SSAPs:
SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance
SSAP No. 72—Surplus and Quasi-Reorganizations
SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act

Relevant NAIC Model Laws/Regulations:
Credit for Reinsurance Model Law (#785)

Accounting Requirements

1. This Appendix shall not apply to assumption reinsurance, yearly renewable term reinsurance or certain nonproportional reinsurance such as stop loss or catastrophe reinsurance.

Q – Aside from assumption reinsurance, what other types of reinsurance are exempt from the accounting requirements?

A – Yearly renewable term (YRT) and certain nonproportional reinsurance arrangements, such as stop loss and catastrophe reinsurance are exempt because these do not normally provide significant surplus relief and therefore are outside the scope of this Appendix. If a catastrophe arrangement takes a reserve credit for actual losses beyond the attachment point or the unearned premium reserve (UPR) of the current year's premium, there will most likely be no regulatory concern.

Similarly, if a YRT treaty provides incidental reserve credits for the ceding insurer's net amount at risk for the year with no other allowance to enhance surplus, there will most likely be no regulatory concern. For purposes of this exemption, a treaty labeled as YRT does not meet the intended definition of YRT if the surplus relief in the first year is greater than that provided by a YRT treaty with zero first year reinsurance premium and no additional allowance from the reinsurer.

Additional pertinent information applicable to all YRT treaties and to non-proportional reinsurance arrangements is contained in paragraphs 19 and 20 of SSAP No. 61.

2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:

   a. Renewal expense allowances provided or to be provided to the ceding insurer by the reinsurer in any accounting period are not sufficient to cover anticipated allocable renewal expenses of the ceding insurer on the portion of the business reinsured, unless a liability is established for the present value of the shortfall (using assumptions equal to the applicable statutory reserve basis on the business reinsured). Those expenses include commissions, premium taxes and direct expenses including, but not limited to, billing, valuation, claims and maintenance expected by the company at the time the business is reinsured;

Q – What should be included in the renewal expense allowances with regard to direct expenses? An allocation of salaries? Computer usage? Or just marginal expenses directly related to the business reinsured such as claim payment expenses, postage, etc.?

A – The primary purpose of the accounting requirements is to prohibit credit for reinsurance under financial arrangements where the ceding company enters into an agreement for the principal purpose of producing significant surplus aid for the ceding insurer on a temporary basis, while not transferring all of the significant risks inherent in the business being reinsured.

Paragraph 2.a. implements that purpose by prohibiting credit for reinsurance in certain instances where the ceding insurer is afforded a large ceding commission at the inception of the agreement resulting in a significant increase in surplus only to have such surplus increase be drained away in subsequent periods because renewal expense allowances provided under the agreement are insufficient to cover the direct allocable costs estimated at the time the business is reinsured, which are anticipated to be incurred by the ceding insurer in maintaining the business reinsured.

An exception to complete disallowance of credit for reinsurance is allowed in situations where the ceding insurer reflects a liability for the present value of the shortage between renewal expense allowances provided under the agreement and the direct allocable costs expected in the future by the insurer in maintaining the business reinsured. This liability must be calculated using actuarial assumptions that are consistent with those utilized in the statutory reserve calculation. The expenses to be accounted for in establishing this liability should represent all costs of the ceding insurer in servicing the business that is subject to the agreement.

In determining what the ceding insurer should include in the renewal expenses with regard to direct expenses, there should be an allocation of all renewal expenses anticipated at the time the business is reinsured including salaries, computer usage, postage, etc. This comprehensive calculation should recognize that the anticipated expense levels may be estimated; a comparison with pricing assumptions may be considered in determining the reasonableness of such assumptions.

When an agreement does not comply with paragraph 2.a., this area of non-compliance should be addressed by the posting of a reserve for the present value of the deficiency rather than denial for credit for reinsurance, assuming that no other area of non-compliance is encountered with the agreement and that the assets received corresponding to the ceding commission are in compliance with the Codification, including Appendix A-785. For example, the assets received corresponding to the ceding commission must be admissible and not subject to repayment to the reinsurer.

b. The ceding insurer can be deprived of surplus or assets at the reinsurer's option or automatically upon the occurrence of some event, such as the insolvency of the ceding insurer, except that termination of the reinsurance agreement by the reinsurer for nonpayment of reinsurance premiums or other amounts due, such as modified coinsurance reserve adjustments, interest and adjustments on funds withheld, and tax reimbursements, shall not be considered to be such a deprivation of surplus or assets;

Q – With regard to existing business, should the coinsurance reserve percentage or the coinsurance reserve amount not be allowed to increase in a combination coinsurance/modified coinsurance treaty? How would the rule be applicable to the difference between the total reserve and the amount of funds withheld in a coinsurance with funds withheld treaty?

A – Under a combination coinsurance/modified coinsurance (co/modco) arrangement the ceding company and the reinsurer both establish reserves for future claim payments. Treaty provisions which adjust the reserves each party holds in lieu of transferring funds owed to the reinsurer are acceptable. However, adjustment of reserves in lieu of payment when funds are due to the ceding company is a violation of the accounting requirements since it is a depletion of the ceding company's assets. In other words, statutory gains can be used to increase the modified coinsurance reserve but statutory losses cannot be used to reduce the modified coinsurance reserve. This is the case even if the agreement provides for this adjustment at inception and never requires a payment to be owed by the reinsurer.

Under a coinsurance with funds withheld treaty the reinsurer establishes the entire amount of reserve liability on its share of reinsured policies, but the ceding company withholds a portion of the reinsurer’s assets typically in an amount less than the reserves, to offset future obligations. Provided the withheld assets are not withheld for any purpose other than the payment of future claims, it is not a violation of the accounting requirements for the reinsurer to require full use of such withheld assets for the payment of claims prior to using any other assets owned by the reinsurer.

Paragraph 2.b. disallows reinsurance credit if the ceding company can be deprived of assets at the reinsurer's option or automatically upon the occurrence of some event. Thus, a provision in a coinsurance with funds withheld or modified coinsurance treaty which unilaterally or automatically allows the reinsurer to convert the treaty to coinsurance at some later date would be of concern. Although the parties could have entered a coinsurance agreement at inception, regulators are concerned that the reinsurer would take invested assets from the ceding company at a time which would be to the detriment of the ceding company's policyholders. Therefore, a conversion provision will not violate paragraph 2.b. only if all of the following are met:

i) the triggers for conversion are limited to ceding company violations of treaty provisions, including complying representations and warranties; the occurrence of a violation has been determined; and the ceding company has been given an opportunity and refuses to promptly remedy the violation;

ii) the conversion is structured so that the surplus of the ceding company will remain unchanged immediately following the conversion;

iii) the invested assets to be transferred upon conversion are less than or equal to the modco reserve, in the case of modco or co/modco, or to the Funds Withheld, in the case of coinsurance funds withheld, and have been maintained in a Trust or Escrow Account since inception of the agreement; and

iv) the reinsurance complies with Credit for Reinsurance requirements (see Appendix A-785) immediately upon conversion.

c. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement, except that neither offsetting experience refunds against current and prior years’ losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years’ losses under the agreement upon voluntary termination of in force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience. Voluntary termination does not include situations where termination occurs because of unreasonable provisions which allow the reinsurer to reduce its risk under the agreement. An example of such a provision is the right of the reinsurer to increase reinsurance premiums or risk and expense charges to excessive levels forcing the ceding company to prematurely terminate the reinsurance treaty;

Q – If group term life business is reinsured under a YRT reinsurance agreement (which includes risk-limiting features such as with an experience refund provision which offsets refunds against current and/or prior years' losses (i.e., a "loss carryforward" provision), under what circumstances would any provisions of the reinsurance agreement be considered "unreasonable provisions which allow the reinsurer to reduce its risk under the agreement" thereby violating subsection 2.c.?

A – Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide. So long as the reinsurer cannot charge premiums in excess of the premium received by the ceding insurer under the provisions of the YRT reinsurance agreement, such provisions would not be considered unreasonable. Any provision in the YRT reinsurance agreement which allows the reinsurer to charge reinsurance premiums in excess of the proportionate premium received by the ceding insurer would be considered unreasonable. The revisions to this QA regarding group term life yearly renewable term agreements is effective for contracts in effect as of January 1, 2021.

d. The ceding insurer must, at specific points in time scheduled in the agreement, terminate or automatically recapture all or part of the reinsurance ceded;

e. The reinsurance agreement involves the possible payment by the ceding insurer to the reinsurer of amounts other than from income realized from the reinsured policies. For example, it is improper for a ceding company to pay reinsurance premiums, or other fees or charges to a reinsurer which are greater than the direct premiums collected by the ceding company;

Q – Should a reinsurer have a unilateral right to establish underlying cost of insurance rates or credited interest rates for policies which are wholly or partially reinsured?

A – No, only the ceding company has the right to set the cost of insurance rates charged policyholders and to set the rates of interest credited to them. However, a representation (but not a warranty) that the ceding company shall vary nonguaranteed elements reinsured in a manner consistent with the ceding company's documented procedures, in effect at the time the agreement was entered into, does not violate the accounting requirements.

Q – May a reinsurance contract allow the reinsurer to change the cost of insurance that the ceding company must pay under the treaty?

A – So long as the aggregate amounts payable by the ceding company in any settlement period do not exceed the income of the reinsured policies during that period, the treaty's structure would not be in violation of paragraph 2.e. There is not compliance if any changes could cause payments made by the ceding company to exceed income from the reinsured business, unless the change is necessary to conform to the documented procedures represented to the reinsurer at the time the treaty was entered into and as long as the ceding company has the ability to change the insurance rates it charges policyholders by at least as much as was included in the original representation.

Q – If a reinsured policy allows the ceding company to guarantee rates of interest to be credited to the policyholder which are greater than those guaranteed by the policy, may a reinsurance contract allow the reinsurer to limit its participation in such credited rate as long as it at least provides for the amount based on the rate guaranteed in the contract?

A – So long as the aggregate amounts payable by the ceding company in any settlement period do not exceed the income of the reinsured policies during that period, the treaty's structure would not be in violation of paragraph 2.e. There is not compliance if any changes could cause payments made by the ceding company to exceed income from the reinsured business, unless the limited participation reflects a change in declared interest rates which is necessary to conform to the documented procedures represented to the reinsurer at the time the treaty was entered into and as long as the ceding company has the ability to change the declared interest rates to be credited to policyholders by at least as much as was included in the original representation.

f. The treaty does not transfer all of the significant risk inherent in the business being reinsured. The following table identifies for a representative sampling of products or type of business, the risks which are considered to be significant. For products not specifically included, the risks determined to be significant shall be consistent with this table.

Risk categories:

i. Morbidity

ii. Mortality

iii. Lapse

This is the risk that a policy will voluntarily terminate prior to the recoupment of a statutory surplus strain experienced at issue of the policy.

iv. Credit Quality

This is the risk that invested assets supporting the reinsured business will decrease in value. The main hazards are that assets will default or that there will be a decrease in earning power. It excludes market value declines due to changes in interest rate.

v. Reinvestment

This is the risk that interest rates will fall and funds reinvested (coupon payments or monies received upon asset maturity or call) will therefore earn less than expected. If asset durations are less than liability durations, the mismatch will increase.

vi. Disintermediation

This is the risk that interest rates rise and policy loans and surrenders increase or maturing contracts do not renew at anticipated rates of renewal. If asset durations are greater than the liability durations, the mismatch will increase. Policyholders will move their funds into new products offering higher rates. The company may have to sell assets at a loss to provide for these withdrawals.

+ - Significant 0 - Insignificant

RISK CATEGORY

	i.	ii.	iii.	iv.	v.	vi.
Health Insurance - other than LTC/LTD*	+	0	+	0	0	0
Health Insurance - LTC/LTD*	+	0	+	+	+	0

Immediate Annuities	0	+	0	+	+	0
Single Premium Deferred Annuities	0	0	+	+	+	+
Flexible Premium Deferred Annuities	0	0	+	+	+	+
Guaranteed Interest Contracts	0	0	0	+	+	+
Other Annuity Deposit Business	0	0	+	+	+	+
Single Premium Whole Life	0	+	+	+	+	+
Traditional Non-Par Permanent	0	+	+	+	+	+
Traditional Non-Par Term	0	+	+	0	0	0
Traditional Par Permanent	0	+	+	+	+	+
Traditional Par Term	0	+	+	0	0	0
Adjustable Premium Permanent	0	+	+	+	+	+
Indeterminate Premium Permanent	0	+	+	+	+	+
Universal Life Flexible Premium	0	+	+	+	+	+
Universal Life Fixed Premium	0	+	+	+	+	+
Universal Life Fixed Premium dump-in premiums allowed	0	+	+	+	+	+

*LTC = Long Term Care Insurance

LTD = Long Term Disability Insurance

Q – If a company cedes health insurance business that is subject to a Medical Loss Ratio (MLR), or similar statutorily required refunds / rebates, must the reinsurer participate in the payment of any refunds / rebates?

A – The reinsurer needs to participate in the payment of its share of any statutorily required MLR or similar refund or rebate based on loss ratio calculations to the extent that the experience of the health business reinsured, during the period that it is reinsured, contributes to the calculation of the refund. Although the payment of such a refund based on the experience of business that is currently reinsured could result in a reduction of surplus on the part of the ceding insurer, if the reduction in surplus of the ceding insurer is entirely attributable to the experience prior to the effective date of the reinsurance, then it is outside of the contract requirements. Accordingly, such a provision should not cause a reinsurance agreement to be out of compliance with Appendix A-791 of the Accounting Practices and Procedure Manual. It is recognized that some refund calculations may involve multiple years.

Furthermore, just as an experience refund is not considered in the determination as to whether a reinsurance agreement is proportional, the requirement for the payment of a refund to policyholders based on a Medical Loss Ratio requirement should also not be considered.

Note: This Q&A only applies to refunds related to a statutory MLR or similar refund or rebate requirement for health insurance and should not be applied to any other situation.

g. i. The credit quality, reinvestment, or disintermediation risk is significant for the business reinsured and the ceding company does not (other than for the classes of business excepted in paragraph g.ii.) either transfer the underlying assets to the reinsurer or legally segregate such assets in a trust or escrow account or otherwise establish a satisfactory mechanism which legally segregates, by contract or contract provision, the underlying assets.

Q – Is asset segmentation an acceptable mechanism for legal segregation of assets?

A – Generally no. Segmentation involves the allocation of a company's general account investment earnings over several lines of business, or various groups of policies within those lines, such that the performance of one corporate bond, for example, may affect the earnings of several segments within a company. The accounting for the segmentation is largely internal, and the detail of the record keeping varies from company to company.

The fundamental purpose of the requirement for a reinsurance treaty to employ the use of a segregated asset portfolio ("SAP") is that all payments (interest, benefits, allowances, etc.) must be made from the SAP, so as to eliminate any problems that could arise in determining what asset or assets should be sold, and to avoid disputes in the event of insolvency. Any sale of assets that could affect policies not subject to reinsurance, or policies subject to reinsurance with other reinsurers is problematic.

In addition, auditing the performance of a treaty using traditional segmentation methods would be extremely difficult and prone to disagreement, which could provide a reinsurer with broad leverage to contest amounts due that reinsurer, especially in the event of insolvency or rehabilitation of the ceding company.

It is important to determine that the arrangement in place does in fact transfer all of the risks of the underlying assets supporting the reinsured business to the reinsurer.

Q – If a percentage of all policies in a block of business is reinsured, must the company segregate that percentage of the assets supporting the business, or can it segregate all the assets?

A – The company may segregate only assets supporting the reinsured portion or the segregated asset portfolio may represent the entire block of business if the reinsured portion is the same for all policies. In the latter case, the reinsurer would take its proportionate share of the SAP performance.

Q – If the ceding company cedes a portion of each policy in a block of business to one reinsurer and a portion to another, while retaining some itself, does it have to segregate assets separately for each reinsurer, or is it acceptable to have all the assets segregated together with each reinsurer responsible for its portion of the investment risk?

A – The ceding company does not need to segregate assets separately for each reinsurer if the treaties are virtually identical.

Q – At the time assets are legally segregated under a coinsurance with funds withheld treaty, should they be valued at market value, statutory value, or some combination?

A – The assets should be valued at their statutory admitted value.

Q – When the assets are legally segregated, how are the funds withheld payables and receivables reported?

A – The payables and receivables are recorded in the same manner as in a funds withheld treaty where the assets are not legally segregated and will usually mirror the value of the funds withheld account. However, the funds withheld account, which reflects the statutory admitted value of the assets in the SAP, will fluctuate, and thus may differ from the reserves on the reinsured business.

ii. Notwithstanding the requirements of paragraph g.i., the assets supporting the reserves for the following classes of business and any classes of business which do not have a significant credit quality, reinvestment or disintermediation risk may be held by the ceding company without segregation of such assets:

(a) Health Insurance - LTC/LTD

(b) Traditional Non-Par Permanent

(c) Traditional Par Permanent

(d) Adjustable Premium Permanent

(e) Indeterminate Premium Permanent

(f) Universal Life Fixed Premium

(no dump-in premiums allowed)

The associated formula for determining the reserve interest rate adjustment must use a formula which reflects the ceding company's investment earnings and incorporates all realized and unrealized gains and losses reflected in the statutory statement. The following is an acceptable formula:

$$\text{Rate} = \frac{2\,(I + CG)}{X + Y - I - CG}$$

Where:

I	is the net investment income
CG	is capital gains less capital losses
X	is the current year cash and invested assets plus investment income due and accrued less borrowed money
Y	is the same as X but for the prior year

h. Settlements are made less frequently than quarterly or payments due from the reinsurer are not made in cash within ninety (90) days of the settlement date.

i. The ceding insurer is required to make representations or warranties not reasonably related to the business being reinsured.

j. The ceding insurer is required to make representations or warranties about future performance of the business being reinsured.

k. The reinsurance agreement is entered into for the principal purpose of producing significant surplus aid for the ceding insurer, typically on a temporary basis, while not transferring all of the significant risks inherent in the business reinsured and, in substance or effect, the expected potential liability to the ceding insurer remains basically unchanged.

3. Any increase in surplus net of federal income tax resulting from reinsurance agreements entered into or amended after the effective date of the Codification which involve the reinsurance of business issued prior to the effective date of the agreements shall be identified separately on the insurer's statutory financial statement as a surplus item and recognition of the surplus increase as income shall be reflected on a net of tax basis as earnings emerge from the business reinsured.

> {For example, on the last day of calendar year N, company XYZ pays a $20 million initial commission and expense allowance to company ABC for reinsuring an existing block of business. Assuming a 34% tax rate, the net increase in surplus at inception is $13.2 million ($20 million - $6.8 million) which is reported on the "Aggregate write-ins for gains and losses in surplus" line in the Capital and Surplus account. $6.8 million (34% of $20 million) is reported as income on the "Commissions and expense allowances on reinsurance ceded" line of the Summary of Operations.
>
> At the end of year N+1 the business has earned $4 million. ABC has paid $.5 million in profit and risk charges in arrears for the year and has received a $1 million experience refund. Company ABC's annual statement would report $1.65 million (66% of ($4 million - $1 million - $.5 million) up to a maximum of $13.2 million) on the "Commissions and expense allowance on reinsurance ceded" line of the Summary of Operations, and -$1.65 million on the "Aggregate write-ins for gains and losses in surplus" line of the Capital and Surplus account. The experience refund would be reported separately as a miscellaneous income item in the Summary of Operations.}

Written Agreements

4. No reinsurance agreement or amendment to any agreement may be used to reduce any liability or to establish any asset in any financial statement, unless the agreement, amendment or a binding letter of intent has been duly executed by both parties no later than the "as of date" of the financial statement.

5. In the case of a letter of intent, a reinsurance agreement or an amendment to a reinsurance agreement must be executed within a reasonable period of time, not exceeding ninety (90) days from the execution date of the letter of intent, in order for credit to be granted for the reinsurance ceded.

6. The reinsurance agreement shall contain provisions which provide that:

   a. The agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder and that there are no understandings between the parties other than as expressed in the agreement; and

   b. Any change or modification to the agreement shall be null and void unless made by amendment to the agreement and signed by both parties.

Appendix A-812

Smoker/Nonsmoker Mortality Tables for Use in Determining Minimum Reserve Liabilities

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 56—Separate Accounts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Purpose

1. The purpose of this Appendix is to permit the use of mortality tables that reflect differences in mortality between smokers and nonsmokers in determining minimum reserve liabilities for plans of insurance with separate premium rates for smokers and nonsmokers.

Definitions

2. As used in this Appendix, "1980 CSO Table, with or without Ten-Year Select Mortality Factor" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the Society of Actuaries Committee to Recommend New Mortality Tables for Valuation of Standard Individual Ordinary Life Insurance, referred to as the Commissioners 1980 Standard Ordinary Mortality Table. The same select factors will be used for both smokers and nonsmokers tables.

3. As used in this Appendix, "1980 CET Table" means that mortality table consisting of separate rates of mortality for male and female lives, developed by the Society of Actuaries Committee to Recommend New Mortality Tables for Valuation of Standard Individual Ordinary Life Insurance, and referred to as the Commissioners 1980 Extended Term Insurance Table.

4. As used in this Appendix, the phrase "smoker and nonsmoker mortality tables" refers to the mortality tables with separate rates of mortality for smokers and nonsmokers derived from the tables defined in paragraphs 2-3 which were developed by the Society of Actuaries Task Force on Smoker/Nonsmoker Mortality and the California Insurance Department staff and recommended by the NAIC Technical Staff Actuarial Group.

5. As used in this Appendix, the phrase "composite mortality tables" refers to the mortality tables defined in paragraphs 2-3 as they were originally published with rates of mortality that do not distinguish between smokers and nonsmokers.

Alternate Tables

6. For any policy of insurance delivered or issued for delivery after the effective date of Codification, at the option of the company and subject to the conditions stated in paragraph 7 of this Appendix;

   a. The 1980 CSO Smoker and Nonsmoker Mortality Tables, with or without Ten-Year Select Mortality Factors, may be substituted for the 1980 CSO Table, with or without Ten-Year Select Mortality Factors, and

   b. The 1980 CET Smoker and Nonsmoker Mortality Tables may be substituted for the 1980 CET Table for use in determining minimum reserve liabilities.

Conditions

7. For each plan of insurance with separate rates for smokers and nonsmokers an insurer may

   a. Use composite mortality tables to determine minimum reserve liabilities,

   b. Use smoker and nonsmoker mortality tables to determine the valuation net premiums and additional minimum reserves, if any, required by Appendix A-820 and use composite mortality tables to determine the basic minimum reserves, or

   c. Use smoker and nonsmoker mortality to determine minimum reserve liabilities.

Appendix A-815

Model Regulation Permitting the Recognition of Preferred Mortality Tables for Use in Determining Minimum Reserve Liabilities

Relevant SSAPs:
SSAP No. 51—Life Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Valuation of Life Insurance Policies Model Regulation (#830)

Purpose

1. The purpose of this regulation is to recognize, permit and prescribe the use of mortality tables that reflect differences in mortality between preferred and standard lives in determining minimum reserve liabilities in accordance with paragraph 3.a.iii. of Appendix A-820 Standard Valuation Law and paragraphs 16 and 17 of Appendix A-830 Valuation of Life Insurance Model Regulation.

2. **Definitions**

a. "2001 CSO Mortality Table" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the American Academy of Actuaries CSO Task Force from the Valuation Basic Mortality Table developed by the Society of Actuaries Individual Life Insurance Valuation Mortality Task Force, and adopted by the NAIC in December 2002. The 2001 CSO Mortality Table is included in the *Proceedings of the NAIC (2nd Quarter 2002)* and supplemented by the 2001 CSO Preferred Class Structure Mortality Table defined below in Subsection B. Unless the context indicates otherwise, the "2001 CSO Mortality Table" includes both the ultimate form of that table and the select and ultimate form of that table and includes both the smoker and nonsmoker mortality tables and the composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality tables. Mortality tables in the 2001 CSO Mortality Table include the following:

i. "2001 CSO Mortality Table (F)" means that mortality table consisting of the rates of mortality for female lives from the 2001 CSO Mortality Table.

ii. "2001 CSO Mortality Table (M)" means that mortality table consisting of the rates of mortality for male lives from the 2001 CSO Mortality Table.

iii. "Composite mortality tables" means mortality tables with rates of mortality that do not distinguish between smokers and nonsmokers.

iv. "Smoker and nonsmoker mortality tables" means mortality tables with separate rates of mortality for smokers and nonsmokers.

b. "2001 CSO Preferred Class Structure Mortality Table" means mortality tables with separate rates of mortality for super preferred nonsmokers, preferred nonsmokers, residual standard nonsmokers, preferred smokers, and residual standard smoker splits of the 2001 CSO Nonsmoker and Smoker Tables, as adopted by the NAIC at the September, 2006 national meeting and published in the *NAIC Proceedings {3rd Quarter 2006}*. Unless the context indicates otherwise, the "2001 CSO Preferred Class Structure Mortality Table" includes both the ultimate form of that table and the select and ultimate form of that table. It includes both the smoker and nonsmoker mortality tables. It includes both the male and female mortality tables and the gender composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality table.

c. "Statistical agent" means an entity with proven systems for protecting the confidentiality of individual insured and insurer information; demonstrated resources for and history of ongoing electronic communications and data transfer ensuring data integrity with insurers, which are its members or subscribers; and a history of and means for aggregation of data and accurate promulgation of the experience modifications in a timely manner.

2001 CSO Preferred Class Structure Table

3. At the election of the company, for each calendar year of issue, for any one or more specified plans of insurance and subject to satisfying the conditions stated in this regulation, the 2001 CSO Preferred Class Structure Mortality Table may be substituted in place of the 2001 CSO Smoker or Nonsmoker Mortality Table as the minimum valuation standard for policies issued on or after January 1, 2007. For policies issued on or after January 1, 2004 (effective date of adoption of the 2001 CSO Mortality Table for Use in Determining Minimum Reserve Liabilities and Nonforfeiture Benefits), and prior to January 1, 2007, these tables may be substituted with the consent of the commissioner and subject to the conditions of paragraph 4. In determining such consent, the commissioner may rely on the consent of the commissioner of the company's state of domicile. No such election shall be made until the company demonstrates at least 20% of the business to be valued on this table is in one or more of the preferred classes. A table from the 2001 CSO Preferred Class Structure Mortality Table used in place of a 2001 CSO Mortality Table, pursuant to the requirements of this rule, will be treated as part of the 2001 CSO Mortality Table only for purposes of reserve valuation pursuant to the requirements of the NAIC model regulation, "Recognition of the 2001 CSO Mortality Table For Use In Determining Minimum Reserve Liabilities And Nonforfeiture Benefits Model Regulation."

4. **Conditions**

a. For each plan of insurance with separate rates for preferred and standard nonsmoker lives, an insurer may use the super preferred nonsmoker, preferred nonsmoker, and residual standard nonsmoker tables to substitute for the nonsmoker mortality table found in the 2001 CSO Mortality Table to determine minimum reserves. At the time of election and annually thereafter, except for business valued under the residual standard nonsmoker table, the appointed actuary shall certify that:

i. The present value of death benefits over the next ten years after the valuation date, using the anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the valuation basic table corresponding to the valuation table being used for that class.

ii. The present value of death benefits over the future life of the contracts, using anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the valuation basic table corresponding to the valuation table being used for that class.

b. For each plan of insurance with separate rates for preferred and standard smoker lives, an insurer may use the preferred smoker and residual standard smoker tables to substitute for the smoker mortality table found in the 2001 CSO Mortality Table to determine minimum reserves. At the time of election and annually thereafter, for business valued under the preferred smoker table, the appointed actuary shall certify that:

i. The present value of death benefits over the next ten years after the valuation date, using the anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the preferred smoker valuation basic table corresponding to the valuation table being used for that class.

ii. The present value of death benefits over the future life of the contracts, using anticipated mortality experience without recognition of mortality improvement beyond the valuation date for each class, is less than the present value of death benefits using the preferred smoker valuation basic table.

c. Unless exempted by the commissioner, every authorized insurer using the 2001 CSO Preferred Class Structure Table shall annually file with the commissioner, with the NAIC, or with a statistical agent designated by the NAIC and acceptable to the commissioner, statistical reports showing mortality and such other information as the commissioner may deem necessary or expedient for the administration of the provisions of this regulation. The form of the reports shall be established by the commissioner or the commissioner may require the use of a form established by the NAIC or by a statistical agent designated by the NAIC and acceptable to the commissioner.

d. The use of the 2001 CSO Preferred Class Structure Table for the valuation of policies issued prior to January 1, 2007 shall not be permitted in any statutory financial statement in which a company reports, with respect to any policy or portion of a policy coinsured, either of the following:

i. In cases where the mode of payment of the reinsurance premium is less frequent than the mode of payment of the policy premium, a reserve credit that exceeds, by more than the amount specified in this paragraph as Y, the gross reserve calculated before reinsurance. Y is the amount of the gross reinsurance premium that (a) provides coverage for the period from the next policy premium due date to the earlier of the end of the policy year and the next reinsurance premium due date, and (b) would be refunded to the ceding entity upon the termination of the policy.

ii. In cases where the mode of payment of the reinsurance premium is more frequent than the mode of payment of the policy premium, a reserve credit that is less than the gross reserve, calculated before reinsurance, by an amount that is less than the amount specified in this paragraph as Z. Z is the amount of the gross reinsurance premium that the ceding entity would need to pay the assuming company to provide reinsurance coverage from the period of the next reinsurance premium due date to the next policy premium due date minus any liability established for the proportionate amount not remitted to the reinsurer.

For purposes of this condition, both the reserve credit and the gross reserve before reinsurance (i) for the mean reserve method shall be defined as the mean reserve minus the deferred premium asset, and (ii) for the mid-terminal reserve method shall include the unearned premium reserve. A company may estimate and adjust its accounting on an aggregate basis in order to meet the conditions to use the 2001 CSO Preferred Class Structure Table.

Effective Date

5. The effective date of this regulation is after January 1, 2007.

Appendix A-817

Preneed Life Insurance Minimum Standards for Determining Reserve Liabilities and Nonforfeiture Values

Relevant SSAPs:
SSAP No. 51—Life Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Scope

1. This rule applies to preneed insurance contracts, as defined in paragraph 5 and to similar policies and certificates.

Purpose

2. The purpose of this appendix is to establish for preneed insurance products minimum mortality standards for reserves and nonforfeiture values, and to require the use of the 1980 Commissioners Standard Ordinary (CSO) Life Valuation Mortality Table for use in determining the minimum standard of valuation of reserves and the minimum standard nonforfeiture values for preneed insurance products.

Definitions

3. The term "**2001 CSO Mortality Table**" means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the American Academy of Actuaries CSO Task Force from the Valuation Basic Mortality Table developed by the Society of Actuaries Individual Life Insurance Valuation Mortality Task Force, and adopted by the NAIC in December 2002. The 2001 CSO Mortality Table is included in the *Proceedings of the NAIC (2nd Quarter 2002)*. Unless the context indicates otherwise, the "2001 CSO Mortality Table" includes both the ultimate form of that table and the select and ultimate form of that table and includes both the smoker and nonsmoker mortality tables and the composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality tables.

4. The term "**Ultimate 1980 CSO**" means the Commissioners' 1980 Standard Ordinary Life Valuation Mortality Tables (1980 CSO) without ten-year (10-year) selection factors, incorporated into the 1980 amendments to the NAIC Standard Valuation Law approved in December 1983.

5. For the purposes of this guidance, preneed insurance is any life insurance policy or certificate that is issued in combination with, in support of, with an assignment to, or as a guarantee for a prearrangement agreement for goods and services to be provided at the time of and immediately following the death of the insured. Goods and services may include, but are not limited to embalming, cremation, body preparation, viewing or visitation, coffin or urn, memorial stone, and transportation of the deceased. The status of the policy or contract as preneed insurance is determined at the time of issue in accordance with the policy form filing.

Minimum Valuation Mortality Standards

6. For preneed insurance contracts, as defined in paragraph 5, and similar policies and contracts, the minimum mortality standard for determining reserve liabilities and nonforfeiture values for both male and female insureds shall be the Ultimate 1980 CSO.

Minimum Valuation Interest Rate Standards

7. The interest rates used in determining the minimum standard for valuation of preneed insurance shall be the calendar year statutory valuation interest rates as defined in *Appendix A-820—Minimum Life and Annuity Reserve Standards*, paragraphs 5-8.

8. The interest rates used in determining the minimum standard for nonforfeiture values for preneed insurance shall be the calendar year statutory nonforfeiture interest rates.

Minimum Valuation Method Standards

9. The method used in determining the standard for the minimum valuation of reserves of preneed insurance shall be the method defined in *Appendix A-820—Minimum Life and Annuity Reserve Standards*, paragraphs 9-11.

Transition Rules

10. For preneed insurance policies issued on or after the effective date of this appendix and before January 1, 2012, the 2001 CSO may be used as the minimum standard for reserves and minimum standard for nonforfeiture benefits for both male and female insureds.

11. If an insurer elects to use the 2001 CSO as a minimum standard for any policy issued on or after the effective date of this appendix and before January 1, 2012, the insurer shall provide, as a part of the actuarial opinion memorandum submitted in support of the company's asset adequacy testing, an annual written notification to the domiciliary commissioner. The notification shall include:

a. A complete list of all preneed policy forms that use the 2001 CSO as a minimum standard;

b. A certification signed by the appointed actuary stating that the reserve methodology employed by the company in determining reserves for the preneed policies issued after the effective date and using the 2001 CSO as a minimum standard, develops adequate reserves (For the purposes of this certification, the preneed insurance policies using the 2001 CSO as a minimum standard cannot be aggregated with any other policies.); and

c. Supporting information regarding the adequacy of reserves for preneed insurance policies issued after the effective date of this guidance and using the 2001 CSO as a minimum standard for reserves.

12. Preneed insurance policies issued on or after January 1, 2012, must use the Ultimate 1980 CSO in the calculation of minimum nonforfeiture values and minimum reserves.

Effective Date

13. This rule is applicable to preneed insurance policies and certificates and similar contracts and certificates, as specified in paragraph 5, issued on or after January 1, 2011.

Appendix A-818

Determining Reserve Liabilities for Credit Life Insurance Model Regulation

Relevant SSAPs:
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Definitions

1. “2001 CSO Mortality Table” means that mortality table, consisting of separate rates of mortality for male and female lives, developed by the American Academy of Actuaries CSO Task Force from the Valuation Basic Mortality Table developed by the Society of Actuaries Individual Life Insurance Valuation Mortality Task Force, and adopted by the NAIC in December 2002. The 2001 CSO Mortality Table is included in the *Proceedings of the NAIC (2nd Quarter 2002)*. Unless the context indicates otherwise, the “2001 CSO Mortality Table” includes both the ultimate form of that table and the select and ultimate form of that table and includes both the smoker and nonsmoker mortality tables and the composite mortality tables. It also includes both the age-nearest-birthday and age-last-birthday bases of the mortality tables.

2. “Composite mortality tables” means mortality tables with rates of mortality that do not distinguish between smokers and nonsmokers.

3. “Credit life insurance” means insurance on a debtor or debtors, pursuant to or in connection with a specific loan or other credit transaction, to provide for satisfaction of a debt, in whole or in part, upon the death of an insured debtor.

4. Credit life insurance does NOT include:

   a. Insurance written in connection with a credit transaction that is:

      i. Secured by a first mortgage or deed of trust; and

      ii. Made to finance the purchase of real property or the construction of a dwelling thereon, or to refinance a prior credit transaction made for such a purpose;

   b. Insurance sold as an isolated transaction on the part of the insurer and not related to an agreement or a plan for insuring debtors of the creditor.

   c. Insurance for which no identifiable charge is made to the debtor.

   d. Insurance on accounts receivable.

5. This rule applies to credit life insurance policies and certificates, and those similar policies and certificates where there is no identifiable charge made to the debtor.

2001 CSO Male Composite Ultimate Mortality Table

6. The minimum standard for both male and female insureds shall be 2001 CSO Male Composite Ultimate Mortality Table.

7. Where the credit life insurance policy or certificate insures two lives, the minimum standard shall be twice the mortality in the 2001 CSO Male Composite Ultimate Mortality Table based on the age of the older insured.

Minimum Standards

8. Appendix A-830 shall not apply to credit life insurance.

9. The interest rates used in determining the minimum standard for valuation shall be the calendar year statutory valuation interest rates as defined in Appendix A-820, paragraphs 7-10.

10. The method used in determining the minimum standard for valuation shall be the commissioners reserve valuation method as defined in Appendix A-820, paragraphs 11-13.

Appendix A-820

Minimum Life and Annuity Reserve Standards

Relevant SSAPs:
SSAP No. 35—Guaranty Fund and Other Assessments
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 54—Individual and Group Accident and Health Contracts
SSAP No. 56—Separate Accounts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts
SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities

Relevant NAIC Model Laws/Regulations:
Preneed Life Insurance Minimum Standards for Determining Reserve Liabilities and Nonforfeiture Values Model Regulation (#817)
NAIC Model Rule for Recognizing a New Annuity Mortality Table for Use in Determining Reserve Liabilities for Annuities (#821)

Definitions

1. For the purposes of this Appendix, the following definitions shall apply on or after the operative date of the *Valuation Manual*:

a. The term "accident and health insurance" means contracts that incorporate morbidity risk and provide protection against economic loss resulting from accident, sickness, or medical conditions and as may be specified in the *Valuation Manual*.

b. The term "appointed actuary" means a qualified actuary who is appointed in accordance with the *Valuation Manual* to prepare the actuarial opinion.

c. The term "company" means an entity, which (a) has written, issued, or reinsured life insurance contracts, accident and health insurance contracts, or deposit-type contracts in a U.S. State, district or territory and has at least one such policy in force or on claim or (b) has written, issued, or reinsured life insurance contracts, accident and health insurance contracts, or deposit-type contracts in any U.S. State, district or territory and is required to hold a certificate of authority to write life insurance, accident and health insurance, or deposit-type contracts in a U.S. State, district or territory.

d. The term "deposit-type contract" means contracts that do not incorporate mortality or morbidity risks and as may be specified in the *Valuation Manual*.

e. The term "life insurance" means contracts that incorporate mortality risk, including annuity and pure endowment contracts, and as may be specified in the *Valuation Manual*.

f. The term "NAIC" means the National Association of Insurance Commissioners.

g. The term "policyholder behavior" means any action a policyholder, contract holder or any other person with the right to elect options, such as a certificate holder, may take under a policy or contract subject to this Appendix including, but not limited to, lapse, withdrawal, transfer, deposit, premium payment, loan, annuitization, or benefit elections prescribed by the policy or contract but excluding events of mortality or morbidity that result in benefits prescribed in their essential aspects by the terms of the policy or contract.

h. The term "principle-based valuation" means a reserve valuation that uses one or more methods or one or more assumptions determined by the insurer and is required to comply with paragraphs 25-27 of this Appendix as specified in the *Valuation Manual*.

i. The term "qualified actuary" means an individual who is qualified to sign the applicable statement of actuarial opinion in accordance with the American Academy of Actuaries qualification standards for actuaries signing such statements and who meets the requirements specified in the *Valuation Manual*.

j. The term "tail risk" means a risk that occurs either where the frequency of low probability events is higher than expected under a normal probability distribution or where there are observed events of very significant size or magnitude.

k. The term "*Valuation Manual*" means the manual of valuation instructions adopted by the NAIC as specified in this Appendix or as subsequently amended.

Valuation Requirements

2. Reserves reported in the financial statements shall:

a. Be computed in accordance with presently accepted actuarial standards;

b. Be based on actuarial assumptions that produce reserves at least as great as those called for in any contract provision as to reserve basis and method, and are in accordance with all other contract provisions. The reported reserves and related actuarial items held in support of the policies and contracts when considered in light of the assets held by the company with respect to the reserves and related actuarial items, including but not limited to the investment earnings on the assets and the considerations anticipated to be received and retained under the policies and contracts, make adequate provision for the company's obligations under the policies and contracts, including but not limited to the benefits under and expenses associated with the policies and contracts;

c. Be computed on the basis of assumptions consistent with those used in computing the corresponding items in the annual statement of the preceding year-end with any exceptions disclosed in the notes to the financial statements; and

d. Include provision for all actuarial reserves and related statement items which ought to be established.

Policies and Contracts Issued On or After the Operative Date of the Valuation Manual

3. The provisions set forth in paragraphs 23-27 of this Appendix shall apply to all policies and contracts issued on or after the January 1, 2017, operative date of the *Valuation Manual*.

Policies and Contracts Issued Prior to the Operative Date of the Valuation Manual

4. The provisions set forth in paragraphs 5-22 of this Appendix shall apply to all policies and contracts, as appropriate, subject to this Appendix prior to the January 1, 2017, operative date of the *Valuation Manual* and the provisions set forth in paragraphs 23-27 of this Appendix shall not apply to any such policies and contracts.

Computation of Minimum Standard for Life Insurance and Endowment Benefits – Policies and Contracts Issued Prior to the Operative Date of the Valuation Manual

5. The minimum standard for the valuation of all life insurance and endowment policies and contracts shall be the commissioners reserve valuation methods defined in paragraphs 11-13, valuation interest rates provided in paragraphs 7-10, and the following tables:

a. For ordinary policies of life insurance issued on the standard basis on or after January 1, 2004, excluding preneed policies (which follow Appendix A-817) any disability and accidental death benefits in the policies:

i. The Commissioners 2001 Standard Ordinary Mortality Table;

ii. At the election of the company for any one or more specified plans of life insurance, the Commissioners 2001 Standard Ordinary Mortality Table with 25-Year Select Mortality Factors; or

iii. Any ordinary mortality table adopted subsequently by the NAIC for use in determining the minimum standard for valuation for such policies;

b. For ordinary policies of life insurance issued on the standard basis, prior to January 1, 2004, excluding any disability and accidental death benefits in the policies and including preneed policies issued on or after January 1, 2012 (see A-817):

i. The Commissioners 1980 Standard Ordinary Mortality Table;

ii. At the election of the company for any one or more specified plans of life insurance, the Commissioners 1980 Standard Ordinary Mortality Table with Ten-Year Select Mortality Factors;

c. For industrial life insurance policies issued on the standard basis, excluding any disability and accidental death benefits in the policies, the Commissioners 1961 Standard Industrial Mortality Table or any industrial mortality table adopted after 1980 by the NAIC for use in determining the minimum standard of valuation for the policies;

d. For total and permanent disability benefits in or supplementary to ordinary policies or contracts, the tables of Period 2 disablement rates and the 1930 to 1950 termination rates of the 1952 Disability Study of the Society of Actuaries, with due regard to the type of benefit or any tables of disablement rates and termination rates adopted after 1980 by the NAIC, for use in determining the minimum standard of valuation for those policies. Any such table shall, for active lives, be combined with a mortality table permitted for calculating the reserves for life insurance policies;

e. For accidental death benefits in or supplementary to policies, the 1959 Accidental Death Benefits Table or any accidental death benefits table adopted after 1980 by the NAIC for use in determining the minimum standard of valuation for those policies. The table shall be combined with a mortality table for calculating the reserves for life insurance policies; and

f. For group life insurance, life insurance issued on the substandard basis and other special benefits: tables which provide for an adequate reserve.

Computation of Minimum Standard for Annuities

6. The minimum standard of valuation for individual annuity and pure endowment contracts and for annuities and pure endowments purchased under group annuity and pure endowment contracts, shall be the commissioners annuity reserve valuation methods defined in paragraphs 14 and 15, valuation interest rates provided in paragraphs 7-10, and the tables defined in Appendix A-821.

Computation of Minimum Standard Valuation Interest Rates by Calendar Year of Issue - All Business

7. The interest rates used in determining the minimum standard for the valuation of policies issued on or after the effective date of the Codification shall be the calendar year statutory valuation interest rates as defined below:

a. Calendar Year Statutory Valuation Interest Rates

i. The calendar year statutory valuation interest rates, I, shall be determined as follows and the results rounded to the nearer one-quarter of one percent (1/4 of 1%):

(a) For life insurance:

$$I = .03 + W(R_1 - .03) + \frac{W}{2}(R_2 - .09);$$

(b) For single premium immediate annuities and for annuity benefits involving life contingencies arising from other annuities with cash settlement options and from guaranteed interest contracts with cash settlement options:

$$I = .03 + W(R - .03)$$

Where R_1 is the lesser of R and .09,

R_2 is the greater of R and .09,

R is the reference interest rate defined in paragraph 9,

and W is the weighting factor defined in paragraph 8;

(c) For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on an issue year basis, except as stated in subparagraph (b) above, the formula for life insurance stated in subparagraph (a) above shall apply to annuities and guaranteed interest contracts with guarantee durations in excess of ten (10) years and the formula for single premium immediate annuities stated in subparagraph (b) above shall apply to annuities and guaranteed interest contracts with guarantee duration of ten (10) years or less;

(d) For other annuities with no cash settlement options and for guaranteed interest contracts with no cash settlement options, the formula for single premium immediate annuities stated in subparagraph (b) above shall apply.

(e) For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a change in fund basis, the formula for single premium immediate annuities stated in subparagraph (b) above shall apply.

ii. However, if the calendar year statutory valuation interest rate for a life insurance policy issued in any calendar year determined without reference to this sentence differs from the corresponding actual rate for similar policies issued in the immediately preceding calendar year by less than one-half of one percent (1/2 of 1%), the calendar year statutory valuation interest rate for the life insurance policies shall be equal to the corresponding actual rate for the immediately preceding calendar year.

Weighting Factors

8. The weighting factors referred to in the formulas stated above are given in the following tables:

a. Weighting Factors for Life Insurance:

Guarantee Duration (Years)	Weighting Factors
10 or less	.50
More than 10, but not more than 20	.45
More than 20	.35

For life insurance, the guarantee duration is the maximum number of years the life insurance can remain in force on a basis guaranteed in the policy or under options to convert to plans of life insurance with premium rates or nonforfeiture values or both which are guaranteed in the original policy;

b. Weighting factor for single premium immediate annuities and for annuity benefits involving life contingencies arising from other annuities with cash settlement options and guaranteed interest contracts with cash settlement options:

.80

c. Weighting factors for other annuities and for guaranteed interest contracts, except as stated in subparagraph (b) above, shall be as specified in items i., ii. and iii. below, according to the rules and definitions in items iv., v. and vi. below:

i. For annuities and guaranteed interest contracts valued on an issue year basis:

Guarantee Duration (Years)	Weighting Factor for Plan Type		
	A	B	C
5 or less:	.80	.60	.50
More than 5, but not more than 10:	.75	.60	.50
More than 10, but not more than 20:	.65	.50	.45
More than 20:	.45	.35	.35

		Plan Type	
	A	B	C
ii. For annuities and guaranteed interest contracts valued on a change in fund basis, the factors shown in item i. above increased by:	.15	.25	.05

		Plan Type	
	A	B	C
iii. For annuities and guaranteed interest contracts valued on an issue year basis (other than those with no cash settlement options) that do not guarantee interest on considerations received more than one year after issue or purchase and for annuities and guaranteed interest contracts valued on a change in fund basis that do not guarantee interest rates on considerations received more than twelve (12) months beyond the valuation date, the factors shown in item i. or derived in item ii. increased by:	.05	.05	.05

iv. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, the guarantee duration is the number of years for which the contract guarantees interest rates in excess of the calendar year statutory valuation interest rate for life insurance policies with guarantee duration in excess of twenty (20) years. For other annuities with no cash settlement options and for guaranteed interest contracts with no cash settlement options, the guaranteed duration is the number of years from the date of issue or date of purchase to the date annuity benefits are scheduled to commence.

v. Plan type as used in the above tables is defined as follows:

(a) Plan Type A: At any time policyholder may withdraw funds only (l) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) without an adjustment but installments over five years or more, or (3) as an immediate life annuity, or (4) no withdrawal permitted.

(b) Plan Type B: Before expiration of the interest rate guarantee, policyholder may withdraw funds only (1) with an adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) without an adjustment but in installments over five years or more, or (3) no withdrawal permitted. At the end of interest rate guarantee, funds may be withdrawn without an adjustment in a single sum or installments over less than five years.

(c) Plan Type C: Policyholder may withdraw funds before expiration of interest rate guarantee in a single sum or installments over less than five years either (1) without adjustment to reflect changes in interest rates or asset values since receipt of the funds by the insurance company, or (2) subject only to a fixed surrender charge stipulated in the contract as a percentage of the fund.

vi. A company may elect to value guaranteed interest contracts with cash settlement options and annuities with cash settlement options on either an issue year basis or on a change in fund basis. Guaranteed interest contracts with no cash settlement options and other annuities with no cash settlement options must be valued on an issue year basis. An issue year basis of valuation refers to a valuation basis under which the interest rate used to determine the minimum valuation standard for the entire duration of the annuity or guaranteed interest contract is the calendar year valuation interest rate for the year of issue or year of purchase of the annuity or guaranteed interest contract, and the change in fund basis of valuation refers to a valuation basis under which the interest rate used to determine the minimum valuation standard applicable to each change in the fund held under the annuity or guaranteed interest contract is the calendar year valuation interest rate for the year of the change in the fund.

Reference Interest Rate

9. The reference interest rate referred to in paragraph 7 of this Appendix shall be defined as follows:

a. For life insurance, the lesser of the average over a period of thirty-six (36) months and the average over a period of twelve (l2) months, ending on June 30 of the calendar year preceding the year of issue, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

b. For single premium immediate annuities and for annuity benefits involving life contingencies arising from other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or year of purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

c. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a year of issue basis, except as stated in subparagraph (b) above, with guarantee duration in excess of ten (10) years, the lesser of the average over a period of thirty-six (36) months and the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

d. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a year of issue basis, except as stated in subparagraph (b) above, with guarantee duration of ten (10) years or less, the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

e. For other annuities with no cash settlement options and for guaranteed interest contracts with no cash settlement options, the average over a period of twelve (12) months, ending on June 30 of the calendar year of issue or purchase, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.;

f. For other annuities with cash settlement options and guaranteed interest contracts with cash settlement options, valued on a change in fund basis, except as stated in subparagraph b. above, the average over a period of twelve (12) months, ending on June 30 of the calendar year of the change in the fund, of the monthly average of the composite yield on seasoned corporate bonds, as published by Moody's Investors Service, Inc.

10. Alternative Method for Determining Reference Interest Rates – In the event that the monthly average of the composite yield on seasoned corporate bonds is no longer published by Moody's Investors Service, Inc. or in the event that the NAIC determines that the monthly average of the composite yield on seasoned corporate bonds as published by Moody's Investors Service, Inc. is no longer appropriate for the determination of the reference interest rate, then an alternative method for determination of the reference interest rate adopted by the NAIC may be substituted.

Reserve Valuation Method—Life Insurance and Endowment Benefits

11. Except as otherwise provided in this Appendix, reserves according to the commissioners reserve valuation method, for the life insurance and endowment benefits of policies providing for a uniform amount of insurance and requiring the payment of uniform premiums shall be the excess, if any, of the present value, at the date of valuation, of the future guaranteed benefits provided for by those policies, over the then present value of any future modified net premiums therefore. The modified net premiums for a policy shall be the uniform percentage of the respective contract premiums for the benefits such that the present value, at the date of issue of the policy, of all modified net premiums shall be equal to the sum of the then present value of the benefits provided for by the policy and the excess of a. over b., as follows:

a. A net level annual premium equal to the present value, at the date of issue, of the benefits provided for after the first policy year, divided by the present value, at the date of issue, of an annuity of one per annum payable on the first and each subsequent anniversary of the policy on which a premium falls due. However, the net level annual premium shall not exceed the net level annual premium on the nineteen-year premium whole life plan for insurance of the same amount at an age one year higher than the age at issue of the policy.

b. A net one-year term premium for the benefits provided for in the first policy year.

12. For a life insurance policy for which the contract premium in the first policy year exceeds that of the second year and for which no comparable additional benefit is provided in the first year for the excess and which provides an endowment benefit or a cash surrender value or a combination in an amount greater than the excess premium, the reserve according to the commissioners reserve valuation method as of any policy anniversary occurring on or before the assumed ending date defined herein as the first policy anniversary on which the sum of any endowment benefit and any cash surrender value then available is greater than the excess premium shall, except as otherwise provided in paragraphs 19 and 20, be the greater of the reserve as of the policy anniversary calculated as described in the preceding paragraph and the reserve as of the policy anniversary calculated as described in those paragraphs, but with (i) the value defined in that paragraph being reduced by fifteen percent (15%) of the amount of such excess first year premium, (ii) all present values of benefits and premiums being determined without reference to premiums or benefits provided for by the policy after the assumed ending date, (iii) the policy being assumed to mature on that date as an endowment, and (iv) the cash surrender value provided on that date being considered as an endowment benefit. In making the above comparison the mortality stated in paragraph 5 and interest bases stated in paragraphs 7-10 shall be used.

13. Reserves according to the commissioners reserve valuation method shall be calculated by a method consistent with the principles of paragraphs 11 and 12 for:

a. Life insurance policies providing for a varying amount of insurance or requiring the payment of varying premiums;

b. Group annuity and pure endowment contracts purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer (including a partnership or sole proprietorship) or by an employee organization, or by both, other than a plan providing individual retirement accounts or individual retirement annuities under Section 408 of the Internal Revenue Code, as now or hereafter amended;

c. Disability and accidental death benefits in all policies and contracts; and

d. All other benefits, except life insurance and endowment benefits in life insurance policies and benefits provided by all other annuity and pure endowment contracts.

Reserve Valuation Method—Annuity and Pure Endowment Benefits

14. Paragraph 15 shall apply to all annuity and pure endowment contracts other than group annuity and pure endowment contracts purchased under a retirement plan or plan of deferred compensation, established or maintained by an employer (including a partnership or sole proprietorship) or by an employee organization, or by both, other than a plan providing individual retirement accounts or individual retirement annuities under Section 408 of the Internal Revenue Code, as now or hereafter amended.

15. Reserves according to the commissioners annuity reserve method for benefits under annuity or pure endowment contracts, excluding any disability and accidental death benefits in the contracts, shall be the greatest of the respective excesses of the present values, at the date of valuation, of the future guaranteed benefits, including guaranteed nonforfeiture benefits, provided for by the contracts at the end of each respective contract year, over the present value, at the date of valuation, of any future valuation considerations derived from future gross considerations, required by the terms of the contract, that become payable prior to the end of the respective contract year. The future guaranteed benefits shall be determined by using the mortality table, if any, and the interest rate, or rates, specified in the contracts for determining guaranteed benefits. The valuation considerations are the portions of the respective gross considerations applied under the terms of the contracts to determine nonforfeiture values.

Minimum Reserves

16. In no event shall a company's aggregate reserves for all life insurance policies, excluding disability and accidental death benefits be less than the aggregate reserves calculated in accordance with the methods set forth in paragraphs 11-15, paragraphs 19-21, and the mortality table or tables and rate or rates of interest used in calculating nonforfeiture benefits for the policies.

Optional Reserve Calculation

17. Reserves for any category of policies, contracts or benefits, may be calculated, at the option of the company, according to any standards that produce greater aggregate reserves for the category than those calculated according to the minimum standard provided herein, but the rate or rates of interest used for policies and contracts, other than annuity and pure endowment contracts, shall not be greater than the corresponding rate or rates of interest used in calculating any nonforfeiture benefits provided in the policies or contracts.

18. A company which adopts at any time a standard of valuation producing greater aggregate reserves than those calculated according to the minimum standard provided herein may, adopt a lower standard of

valuation, but not lower than the minimum provided herein; provided that the holding of additional reserves previously determined by the appointed actuary shall not be deemed to be the adoption of a higher standard of valuation.

Reserve Calculation—Valuation Net Premium Exceeding the Gross Premium Charged

19. If in any contract year the gross premium charged by a company on a policy or contract is less than the valuation net premium for the policy or contract calculated by the method used in calculating the reserve but using the minimum valuation standards of mortality and rate of interest, the minimum reserve required for the policy or contract shall be the greater of either the reserve calculated according to the mortality table, rate of interest, and method actually used for the policy or contract, or the reserve calculated by the method actually used for the policy or contract but using the minimum valuation standards of mortality and rate of interest and replacing the valuation net premium by the actual gross premium in each contract year for which the valuation net premium exceeds the actual gross premium. The minimum valuation standards of mortality and rate of interest to be used are those standards stated in paragraph 5 and paragraphs 7-10 of this Appendix.

20. For a life insurance policy for which the gross premium in the first policy year exceeds that of the second year and for which no comparable additional benefit is provided in the first year for the excess and which provides an endowment benefit or a cash surrender value or a combination in an amount greater than the excess premium, the provisions of paragraphs 19 and 20 shall be applied as if the method actually used in calculating the reserve for the policy were the method described in paragraph 11. The minimum reserve at each policy anniversary of such a policy shall be the greater of the minimum reserve calculated in accordance with paragraphs 11 and 12 and the minimum reserve calculated in accordance with paragraphs 19 and 20.

Reserve Calculation—Indeterminate Premium Plans

21. In the case of a plan of life insurance that provides for future premium determination, the amounts of which are to be determined by the insurance company based on then estimates of future experience, or in the case of a plan of life insurance or annuity that is of such a nature that the minimum reserves cannot be determined by the methods described above, the reserves that are held under the plan shall:

a. Be appropriate in relation to the benefits and the pattern of premiums for that plan; and

b. Be computed by a method that is consistent with the principles of this Appendix.

Minimum Standard for Accident and Health Insurance Contracts On or After the Operative Date of the Valuation Manual

22. For accident and health insurance contracts issued on or after the operative date of the *Valuation Manual*, the standard prescribed in the *Valuation Manual* is the minimum standard of valuation required under paragraph 3. For [disability, accident and sickness, accident and health] insurance contracts issued on or after January 1, 2017, and prior to the operative date of the *Valuation Manual* the minimum standard of valuation is the standard adopted by the commissioner by regulation.

Valuation Manual for Policies Issued On or After the Operative Date of the Valuation Manual

23. For policies issued on or after the operative date of the *Valuation Manual*, the standard prescribed in the *Valuation Manual* is the minimum standard of valuation required under paragraph 3.

24. The *Valuation Manual* must specify all of the following:

a. Minimum valuation standards for and definitions of the policies or contracts subject to paragraph 3. Such minimum valuation standards shall be:

i. The commissioners reserve valuation method for life insurance contracts, or other than annuity contracts, subject to paragraph 3;

ii. The commissioners annuity reserve valuation method for annuity contracts subject to paragraph 3; and

iii. Minimum reserves for all other policies or contracts subject to paragraph 3.

b. Which policies or contracts or types of policies or contracts that are subject to the requirements of a principle-based valuation in paragraph 25 and the minimum valuation standards consistent with those requirements;

c. For policies and contracts subject to a principle-based valuation under paragraphs 25-27:

i. Requirements for the format of reports to the commissioner under paragraph 26.c. and which shall include information necessary to determine if the valuation is appropriate and in compliance with this Appendix;

ii. Assumptions shall be prescribed for risks over which the company does not have significant control or influence; and

iii. Procedures for corporate governance and oversight of the actuarial function, and a process for appropriate waiver or modification of such procedures.

d. For policies not subject to a principle-based valuation under paragraph 25-27, the minimum valuation standard shall either:

i. Be consistent with the minimum standard of valuation prior to the operative date of the *Valuation Manual*; or

ii. Develop reserves that quantify the benefits and guarantees, and the funding, associated with the contracts and their risks at a level of conservatism that reflects conditions that include unfavorable events that have a reasonable probability of occurring.

e. Other requirements, including, but not limited to, those relating to reserve methods, models for measuring risk, generation of economic scenarios, assumptions, margins, use of company experience, risk measurement, disclosure, certifications, reports, actuarial opinions and memorandums, transition rules and internal controls; and

f. The data and form of the data required under paragraph 28, with whom the data must be submitted, and may specify other requirements including data analyses and reporting of analyses.

Requirements of a Principle-Based Valuation

25. A company must establish reserves using a principle-based valuation that meets the following conditions for policies or contracts as specified in the *Valuation Manual*:

a. Quantify the benefits and guarantees, and the funding, associated with the contracts and their risks at a level of conservatism that reflects conditions that include unfavorable events that have a reasonable probability of occurring during the lifetime of the contracts. For polices or contracts with significant tail risk, reflects conditions appropriately adverse to quantify the tail risk.

b. Incorporate assumptions, risk analysis methods and financial models and management techniques that are consistent with, but not necessarily identical to, those utilized within the company's overall risk assessment process, while recognizing potential differences in financial reporting structures and any prescribed assumptions or methods.

c. Incorporate assumptions that are derived in one of the following manners:

i. The assumption is prescribed in the *Valuation Manual*.

ii. For assumptions that are not prescribed, the assumptions shall:

(a) Be established utilizing the company's available experience, to the extent it is relevant and statistically credible; or

(b) To the extent that company data is not available, relevant, or statistically credible, be established utilizing other relevant, statistically credible experience.

d. Provide margins for uncertainty including adverse deviation and estimation error, such that the greater the uncertainty, the larger the margin and resulting reserve.

26. A company using a principle-based valuation for one or more policies or contracts subject to paragraphs 25-27 as specified in the *Valuation Manual* shall:

a. Establish procedures for corporate governance and oversight of the actuarial valuation function consistent with those described in the *Valuation Manual*.

b. Provide to the commissioner and the board of directors an annual certification of the effectiveness of the internal controls with respect to the principle-based valuation. Such controls shall be designed to assure that all material risks inherent in the liabilities and associated assets subject to such valuation are included in the valuation, and that valuations are made in accordance with the *Valuation Manual*. The certification shall be based on the controls in place as of the end of the preceding calendar year.

c. Develop, and file with the commissioner upon request, a principle-based valuation report that complies with standards prescribed in the *Valuation Manual*.

27. A principle-based valuation may include a prescribed formulaic reserve component.

Experience Reporting for Policies In Force On or After the Operative Date of the Valuation Manual

28. A company shall submit mortality, morbidity, policyholder behavior, or expense experience and other data as prescribed in the *Valuation Manual*.

Appendix A-821

Annuity Mortality Table for Use in Determining Reserve Liabilities for Annuities

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 56—Separate Accounts

Purpose

1. The purpose of this Appendix is to recognize the following mortality tables for use in determining the minimum standard of valuation for annuity and pure endowment contracts: the 1983 Table "a," the Annuity 2000 Mortality Table, the 2012 Individual Annuity Reserving (2012 IAR) Table and the 1994 Group Annuity Reserving (1994 GAR) Table.

Definitions

2. As used in this Appendix "1983 Table 'a'" means that mortality table developed by the Society of Actuaries Committee to Recommend a New Mortality Basis for Individual Annuity Valuation and adopted as a recognized mortality table for annuities in June 1982 by the National Association of Insurance Commissioners.

3. As used in this Appendix "1994 GAR Table" means that mortality table developed by the Society of Actuaries Group Annuity Valuation Table Task Force and shown in the *Proceedings of the NAIC*.

4. As used in this Appendix "Annuity 2000 Mortality Table" means that mortality table developed by the Society of Actuaries Committee on Life Insurance Research and shown in the Proceedings of the NAIC.

5. As used in this Appendix, "Period table" means a table of mortality rates applicable to a given calendar year (the Period).

6. As used in this Appendix, "Generational mortality table" means a mortality table containing a set of mortality rates that decrease for a given age from one year to the next based on a combination of a Period table and a projection scale containing rates of mortality improvement.

7. As used in this Appendix, "2012 IAR Table" means that Generational mortality table developed by the Society of Actuaries Committee on Life Insurance Research and containing rates, qx2012+n, derived from a combination of the 2012 IAM Period Table and Projection Scale G2, using the methodology stated in paragraphs 13 and 14.

8. As used in this Appendix, "2012 Individual Annuity Mortality Period Life (2012 IAM Period) Table" means the Period table containing loaded mortality rates for calendar year 2012. This table contains rates, qx2012, developed by the Society of Actuaries Committee on Life Insurance Research and is shown in Appendices I and II.

9. As used in this Appendix, "Projection Scale G2 (Scale G2)" is a table of annual rates, $G2_x$, of mortality improvement by age for projecting future mortality rates beyond calendar year 2012. This table was developed by the Society of Actuaries Committee on Life Insurance Research and is shown in Appendices III and IV.

Individual Annuity or Pure Endowment Contracts

10. Except as provided in paragraph 12 of this Appendix, the Annuity 2000 Mortality Table shall be used for determining the minimum standard of valuation for any individual annuity or pure endowment contract issued on or after January 1, 2001, through December 31, 2014.

11. Except as provided in paragraph 12, the 2012 IAR Mortality Table shall be used for determining the minimum standard of valuation for any individual annuity or pure endowment contract issued on or after January 1, 2015.

12. The 1983 Table "a" without projection is to be used for determining the minimum standards of valuation for an individual annuity or pure endowment contract solely when the contract is based on life contingencies and is issued to fund periodic benefits arising from:

a. Settlements of various forms of claims pertaining to court settlements or out of court settlements from tort actions;

b. Settlements involving similar actions such as workers' compensation claims; or

c. Settlements of long term disability claims where a temporary or life annuity has been used in lieu of continuing disability payments.

Application of the 2012 IAR Mortality Table

13. In using the 2012 IAR Mortality Table, the mortality rate for a person age x in year (2012 + n) is calculated as follows:

$$q_x^{2012+n} = q_x^{2012} (1 - G2_x)^n$$

14. The resulting q_x^{2012+n} shall be rounded to three decimal places per 1,000, e.g., 0.741 deaths per 1,000. Also, the rounding shall occur according to the formula above, starting at the 2012 period table rate. For example, for a male age 30, $q_x^{2012} = 0.741$.

$q_x^{2013} = 0.741 * (1 - 0.010) ^ 1 = 0.73359$, which is rounded to 0.734
$q_x^{2014} = 0.741 * (1 - 0.010) ^ 2 = 0.7262541$, which is rounded to 0.726

A method leading to incorrect rounding would be to calculate q_x^{2014} as $q_x^{2013} * (1 - 0.010)$, or 0.734 * 0.99 = 0.727. It is incorrect to use the already rounded q_x^{2013} to calculate q_x^{2014}.

Group Annuity or Pure Endowment Contracts

15. The 1994 GAR Table shall be used for determining the minimum standard of valuation for any annuity or pure endowment purchased under a group annuity or pure endowment contract.

Application of the 1994 GAR Table

16. In using the 1994 GAR Table, the mortality rate for a person age x in year (1994 + n) is calculated as follows:

$$q_x^{1994+n} = q_x^{1994} (1 - AA_x)^n$$

where the q_x^{1994} and AA_xs are as specified in the 1994 GAR Table.

APPENDIX I

2012 IAM Period Table
Female, Age Nearest Birthday

AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$
0	**1.621**	30	**0.300**	60	**3.460**	90	**88.377**
1	**0.405**	31	**0.321**	61	**3.916**	91	**97.491**
2	**0.259**	32	**0.338**	62	**4.409**	92	**107.269**
3	**0.179**	33	**0.351**	63	**4.933**	93	**118.201**
4	**0.137**	34	**0.365**	64	**5.507**	94	**130.969**
5	**0.125**	35	**0.381**	65	**6.146**	95	**146.449**
6	**0.117**	36	**0.402**	66	**6.551**	96	**163.908**
7	**0.110**	37	**0.429**	67	**7.039**	97	**179.695**
8	**0.095**	38	**0.463**	68	**7.628**	98	**196.151**
9	**0.088**	39	**0.504**	69	**8.311**	99	**213.150**
10	**0.085**	40	**0.552**	70	**9.074**	100	**230.722**
11	**0.086**	41	**0.600**	71	**9.910**	101	**251.505**
12	**0.094**	42	**0.650**	72	**10.827**	102	**273.007**
13	**0.108**	43	**0.697**	73	**11.839**	103	**295.086**
14	**0.131**	44	**0.740**	74	**12.974**	104	**317.591**
15	**0.156**	45	**0.780**	75	**14.282**	105	**340.362**
16	**0.179**	46	**0.825**	76	**15.799**	106	**362.371**
17	**0.198**	47	**0.885**	77	**17.550**	107	**384.113**
18	**0.211**	48	**0.964**	78	**19.582**	108	**400.000**
19	**0.221**	49	**1.051**	79	**21.970**	109	**400.000**
20	**0.228**	50	**1.161**	80	**24.821**	110	**400.000**
21	**0.234**	51	**1.308**	81	**28.351**	111	**400.000**
22	**0.240**	52	**1.460**	82	**32.509**	112	**400.000**
23	**0.245**	53	**1.613**	83	**37.329**	113	**400.000**
24	**0.247**	54	**1.774**	84	**42.830**	114	**400.000**
25	**0.250**	55	**1.950**	85	**48.997**	115	**400.000**
26	**0.256**	56	**2.154**	86	**55.774**	116	**400.000**
27	**0.261**	57	**2.399**	87	**63.140**	117	**400.000**
28	**0.270**	58	**2.700**	88	**71.066**	118	**400.000**
29	**0.281**	59	**3.054**	89	**79.502**	119	**400.000**
						120	**1000.000**

APPENDIX II

2012 IAM Period Table
Male, Age Nearest Birthday

AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$	AGE	$1000 \cdot q_x^{2012}$
0	**1.605**	30	**0.741**	60	**5.096**	90	**109.993**
1	**0.401**	31	**0.751**	61	**5.614**	91	**123.119**
2	**0.275**	32	**0.754**	62	**6.169**	92	**137.168**
3	**0.229**	33	**0.756**	63	**6.759**	93	**152.171**
4	**0.174**	34	**0.756**	64	**7.398**	94	**168.194**
5	**0.168**	35	**0.756**	65	**8.106**	95	**185.260**
6	**0.165**	36	**0.756**	66	**8.548**	96	**197.322**
7	**0.159**	37	**0.756**	67	**9.076**	97	**214.751**
8	**0.143**	38	**0.756**	68	**9.708**	98	**232.507**
9	**0.129**	39	**0.800**	69	**10.463**	99	**250.397**
10	**0.113**	40	**0.859**	70	**11.357**	100	**268.607**
11	**0.111**	41	**0.926**	71	**12.418**	101	**290.016**
12	**0.132**	42	**0.999**	72	**13.675**	102	**311.849**
13	**0.169**	43	**1.069**	73	**15.150**	103	**333.962**
14	**0.213**	44	**1.142**	74	**16.860**	104	**356.207**
15	**0.254**	45	**1.219**	75	**18.815**	105	**380.000**
16	**0.293**	46	**1.318**	76	**21.031**	106	**400.000**
17	**0.328**	47	**1.454**	77	**23.540**	107	**400.000**
18	**0.359**	48	**1.627**	78	**26.375**	108	**400.000**
19	**0.387**	49	**1.829**	79	**29.572**	109	**400.000**
20	**0.414**	50	**2.057**	80	**33.234**	110	**400.000**
21	**0.443**	51	**2.302**	81	**37.533**	111	**400.000**
22	**0.473**	52	**2.545**	82	**42.261**	112	**400.000**
23	**0.513**	53	**2.779**	83	**47.441**	113	**400.000**
24	**0.554**	54	**3.011**	84	**53.233**	114	**400.000**
25	**0.602**	55	**3.254**	85	**59.855**	115	**400.000**
26	**0.655**	56	**3.529**	86	**67.514**	116	**400.000**
27	**0.688**	57	**3.845**	87	**76.340**	117	**400.000**
28	**0.710**	58	**4.213**	88	**86.388**	118	**400.000**
29	**0.727**	59	**4.631**	89	**97.634**	119	**400.000**
						120	**1000.000**

APPENDIX III

Projection Scale G2
Female, Age Nearest Birthday

AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$
0	**0.010**	30	**0.010**	60	**0.013**	90	**0.006**
1	**0.010**	31	**0.010**	61	**0.013**	91	**0.006**
2	**0.010**	32	**0.010**	62	**0.013**	92	**0.005**
3	**0.010**	33	**0.010**	63	**0.013**	93	**0.005**
4	**0.010**	34	**0.010**	64	**0.013**	94	**0.004**
5	**0.010**	35	**0.010**	65	**0.013**	95	**0.004**
6	**0.010**	36	**0.010**	66	**0.013**	96	**0.004**
7	**0.010**	37	**0.010**	67	**0.013**	97	**0.003**
8	**0.010**	38	**0.010**	68	**0.013**	98	**0.003**
9	**0.010**	39	**0.010**	69	**0.013**	99	**0.002**
10	**0.010**	40	**0.010**	70	**0.013**	100	**0.002**
11	**0.010**	41	**0.010**	71	**0.013**	101	**0.002**
12	**0.010**	42	**0.010**	72	**0.013**	102	**0.001**
13	**0.010**	43	**0.010**	73	**0.013**	103	**0.001**
14	**0.010**	44	**0.010**	74	**0.013**	104	**0.000**
15	**0.010**	45	**0.010**	75	**0.013**	105	**0.000**
16	**0.010**	46	**0.010**	76	**0.013**	106	**0.000**
17	**0.010**	47	**0.010**	77	**0.013**	107	**0.000**
18	**0.010**	48	**0.010**	78	**0.013**	108	**0.000**
19	**0.010**	49	**0.010**	79	**0.013**	109	**0.000**
20	**0.010**	50	**0.010**	80	**0.013**	110	**0.000**
21	**0.010**	51	**0.010**	81	**0.012**	111	**0.000**
22	**0.010**	52	**0.011**	82	**0.012**	112	**0.000**
23	**0.010**	53	**0.011**	83	**0.011**	113	**0.000**
24	**0.010**	54	**0.011**	84	**0.010**	114	**0.000**
25	**0.010**	55	**0.012**	85	**0.010**	115	**0.000**
26	**0.010**	56	**0.012**	86	**0.009**	116	**0.000**
27	**0.010**	57	**0.012**	87	**0.008**	117	**0.000**
28	**0.010**	58	**0.012**	88	**0.007**	118	**0.000**
29	**0.010**	59	**0.013**	89	**0.007**	119	**0.000**
						120	**0.000**

APPENDIX IV

Projection Scale G2
Male, Age Nearest Birthday

AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$	AGE	$G2_x$
0	**0.010**	30	**0.010**	60	**0.015**	90	**0.007**
1	**0.010**	31	**0.010**	61	**0.015**	91	**0.007**
2	**0.010**	32	**0.010**	62	**0.015**	92	**0.006**
3	**0.010**	33	**0.010**	63	**0.015**	93	**0.005**
4	**0.010**	34	**0.010**	64	**0.015**	94	**0.005**
5	**0.010**	35	**0.010**	65	**0.015**	95	**0.004**
6	**0.010**	36	**0.010**	66	**0.015**	96	**0.004**
7	**0.010**	37	**0.010**	67	**0.015**	97	**0.003**
8	**0.010**	38	**0.010**	68	**0.015**	98	**0.003**
9	**0.010**	39	**0.010**	69	**0.015**	99	**0.002**
10	**0.010**	40	**0.010**	70	**0.015**	100	**0.002**
11	**0.010**	41	**0.010**	71	**0.015**	101	**0.002**
12	**0.010**	42	**0.010**	72	**0.015**	102	**0.001**
13	**0.010**	43	**0.010**	73	**0.015**	103	**0.001**
14	**0.010**	44	**0.010**	74	**0.015**	104	**0.000**
15	**0.010**	45	**0.010**	75	**0.015**	105	**0.000**
16	**0.010**	46	**0.010**	76	**0.015**	106	**0.000**
17	**0.010**	47	**0.010**	77	**0.015**	107	**0.000**
18	**0.010**	48	**0.010**	78	**0.015**	108	**0.000**
19	**0.010**	49	**0.010**	79	**0.015**	109	**0.000**
20	**0.010**	50	**0.010**	80	**0.015**	110	**0.000**
21	**0.010**	51	**0.011**	81	**0.014**	111	**0.000**
22	**0.010**	52	**0.011**	82	**0.013**	112	**0.000**
23	**0.010**	53	**0.012**	83	**0.013**	113	**0.000**
24	**0.010**	54	**0.012**	84	**0.012**	114	**0.000**
25	**0.010**	55	**0.013**	85	**0.011**	115	**0.000**
26	**0.010**	56	**0.013**	86	**0.010**	116	**0.000**
27	**0.010**	57	**0.014**	87	**0.009**	117	**0.000**
28	**0.010**	58	**0.014**	88	**0.009**	118	**0.000**
29	**0.010**	59	**0.015**	89	**0.008**	119	**0.000**
						120	**0.000**

Appendix A-822

Asset Adequacy Analysis Requirements

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 54—Individual and Group Accident and Health Contracts
SSAP No. 56—Separate Accounts
SSAP No. 59—Credit Life and Accident and Health Insurance Contracts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)

Definitions

1. "Asset adequacy analysis" means an analysis of the adequacy of reserves and related actuarial items, in light of the assets supporting such reserves and related items, to meet the obligations of an insurer.

Asset Adequacy Analysis

2. The reserves and related items, when considered in light of the assets held by the company with respect to such reserves and related actuarial items including, but not limited to, the investment earnings on the assets, and the considerations anticipated to be received and retained under the policies and contracts, shall make adequate provision, according to presently accepted actuarial standards of practice, for the anticipated cash flows required by the contractual obligations and related expenses of the company.

3. If the company determines as the result of asset adequacy analysis that a reserve should be held in addition to the aggregate reserve held and calculated in accordance with methods set forth in Appendix A-820, the company shall establish the additional reserve.

4. Additional reserves established above and deemed not necessary in subsequent years may be released. The release of such reserves would not be deemed an adoption of a lower standard of valuation.

Appendix A-830

Valuation of Life Insurance Policies
(Including the Introduction and Use of New Select Mortality Factors)

Relevant SSAPs:
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

Relevant NAIC Model Laws/Regulations:
Standard Valuation Law (#820)
Actuarial Opinion and Memorandum Regulation (#822)

Purpose

1. The purpose of this appendix is to provide:

   a. Tables of select mortality factors and rules for their use;

   b. Rules concerning a minimum standard for the valuation of plans with nonlevel premiums or benefits; and

   c. Rules concerning a minimum standard for the valuation of plans with secondary guarantees.

2. The method for calculating basic reserves defined in this appendix will constitute the Commissioners' Reserve Valuation Method for policies to which this appendix is applicable.

Applicability

3. This appendix shall apply to all life insurance policies, with or without nonforfeiture values, issued on or after the effective date of this appendix, subject to the following exceptions and conditions. Nothing in this section shall be construed to expand the applicability of the Valuation of Life Insurance Policies Model Regulation to include life insurance policies exempted under this section.

   a. Exceptions

      i. This appendix shall not apply to any individual life insurance policy issued on or after the effective date of this appendix if the policy is issued in accordance with and as a result of the exercise of a reentry provision contained in the original life insurance policy of the same or greater face amount, issued before the effective date of this appendix, that guarantees the premium rates of the new policy. This appendix also shall not apply to subsequent policies issued as a result of the exercise of such a provision, or a derivation of the provision, in the new policy.

      ii. This appendix shall not apply to any universal life policy that meets all the following requirements:

         (a) Secondary guarantee period, if any, is five (5) years or less;

         (b) Specified premium for the secondary guarantee period is not less than the net level reserve premium for the secondary guarantee period based on the CSO valuation tables as defined in paragraph 9 and the applicable valuation interest rate. For contracts issued beginning January 1, 2004, the net level reserve premium is based on the ultimate mortality rates in the 2001 CSO Mortality Table; and

(c) The initial surrender charge is not less than 100 percent of the first year annualized specified premium for the secondary guarantee period.

Drafting Note: Policies with a secondary guarantee are described in paragraph 29.

iii. This appendix shall not apply to any variable life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts.

iv. This appendix shall not apply to any variable universal life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts.

v. This appendix shall not apply to a group life insurance certificate unless the certificate provides for a stated or implied schedule of maximum gross premiums required in order to continue coverage in force for a period in excess of one year.

vi. This appendix shall not apply to preneed policies, which follow the requirements of A-817.

b. Conditions

i. Calculation of the minimum valuation standard for policies with guaranteed nonlevel gross premiums or guaranteed nonlevel benefits (other than universal life policies), or both, shall be in accordance with the provisions of paragraphs 21-28.

ii. Calculation of the minimum valuation standard for flexible premium and fixed premium universal life insurance policies, that contain provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period shall be in accordance with the provisions of paragraphs 29-32.

Definitions

4. “Basic reserves” means reserves calculated in accordance with Appendix A-820, paragraphs 11-13.

5. “Contract segmentation method” means the method of dividing the period from issue to mandatory expiration of a policy into successive segments, with the length of each segment being defined as the period from the end of the prior segment (from policy inception, for the first segment) to the end of the latest policy year as determined below. For contracts beginning January 1, 2004, all calculations are made using the 2001 CSO Mortality Rate, and, if elected, the optional minimum mortality standard for deficiency reserves stipulated in paragraph 17. (or any other valuation mortality table adopted by the National Association of Insurance Commissioners (NAIC) after the effective date of this appendix for this purpose), and, if elected, the optional minimum mortality standard for deficiency reserves stipulated in paragraph 17 of this appendix. The length of a particular contract segment shall be set equal to the minimum of the value *t* for which G_t is greater than R_t (if G_t never exceeds R_t the segment length is deemed to be the number of years from the beginning of the segment to the mandatory expiration date of the policy), where G_t and R_t are defined as follows:

Attachment 1

$$G_t = \frac{GPx+k+t}{GP_{x+k+t-1}}$$

where: x = original issue age;

k = the number of years from the date of issue to the beginning of the segment;

t = 1, 2, ...; *t* is reset to 1 at the beginning of each segment;

$GP_{x+k+t-1}$ = Guaranteed gross premium per thousand of face amount for year *t* of the segment, ignoring policy fees only if level for the premium paying period of the policy.

$$R_t = \frac{q_{x+k+t}}{q_{x+k+t-1}}$$

However, R_t may be increased or decreased by one percent in any policy year, at the company's option, but R_t shall not be less than one;

where: x, k and t are as defined above, and

The value of "$q_{x+k+t-1}$" is the valuation mortality rate for deficiency reserves in policy year k+t, but using the unmodified select mortality rates if modified select mortality rates are used in the computation of deficiency reserves.

However, if GP_{x+k+t} is greater than 0 and $GP_{x+k+t-1}$ is equal to 0, G_t shall be deemed to be 1000. If GP_{x+k+t} and $GP_{x+k+t-1}$ are both equal to 0, G_t shall be deemed to be 0.

Drafting Note: The purpose of the one percent tolerance in the R factor is to prevent irrational segment lengths due to such things as premium rounding. For example, consider a plan in which gross premiums are designed at some point to be a ratio times the underlying ultimate mortality rates, where the ratio varies by issue age. The resulting segments may be greater than one year, because the guaranteed gross premiums are not expressed in fractional cents. The tolerance factor allows the creation of one year segments for a plan in which premiums parallel the underlying valuation mortality table.

6. "Deficiency reserves" means the excess, if greater than zero, of

   a. Minimum reserves calculated in accordance with Appendix A-820, paragraphs 19 and 20, over

   b. Basic reserves.

7. "Guaranteed gross premiums" means the premiums under a policy of life insurance that are guaranteed and determined at issue.

8. "Maximum valuation interest rates" means the interest rates defined in Appendix A-820, paragraphs 7-10 (Computation of Minimum Standard by Calendar Year of Issue – All Business) that are to be used in determining the minimum standard for the valuation of life insurance policies.

9. "1980 CSO valuation tables" means the Commissioners' 1980 Standard Ordinary Mortality Table (1980 CSO Table) without ten-year selection factors, referenced in Appendix A-820, and variations of the 1980 CSO Table approved by the NAIC, such as the smoker and nonsmoker versions approved in

December 1983.

Drafting Note: This appendix defines the 1980 CSO Tables without the existing ten -year select mortality factors to assure that, if select mortality factors are elected, only one set of factors may be applied to the base valuation mortality table.

10. "Scheduled gross premium" means the smallest illustrated gross premium at issue for other than universal life insurance policies. For universal life insurance policies, scheduled gross premium means the smallest specified premium described in paragraph 29.c., if any, or else the minimum premium described in paragraph 29.d.

11. a. "Segmented reserves" means reserves, calculated using segments produced by the contract segmentation method, equal to the present value of all future guaranteed benefits less the present value of all future net premiums to the mandatory expiration of a policy, where the net premiums within each segment are a uniform percentage of the respective guaranteed gross premiums within the segment. The uniform percentage for each segment is such that, at the beginning of the segment, the present value of the net premiums within the segment equals:

i. The present value of the death benefits within the segment, plus

ii. The present value of any unusual guaranteed cash value (see paragraph 24) occurring at the end of the segment, less

iii. Any unusual guaranteed cash value occurring at the start of the segment, plus

iv. For the first segment only, the excess of the Item (a) over Item (b), as follows:

(a) A net level annual premium equal to the present value, at the date of issue, of the benefits provided for in the first segment after the first policy year, divided by the present value, at the date of issue, of an annuity of one per year payable on the first and each subsequent anniversary within the first segment on which a premium falls due. However, the net level annual premium shall not exceed the net level annual premium on the nineteen-year premium whole life plan of insurance of the same renewal year equivalent level amount at an age one year higher than the age at issue of the policy.

(b) A net one-year term premium for the benefits provided for in the first policy year.

b. The length of each segment is determined by the "contract segmentation method," as defined in paragraph 5.

c. The interest rates used in the present value calculations for any policy may not exceed the maximum valuation interest rate, determined with a guarantee duration equal to the sum of the lengths of all segments of the policy.

d. For both basic reserves and deficiency reserves computed by the segmented method, present values shall include future benefits and net premiums in the current segment and in all subsequent segments.

Drafting Note: The segmentation requirement should not be limited to plans with no cash surrender values; otherwise companies could avoid segmentation entirely by designing policies with minimal (positive) cash values. Segmentation for plans with cash surrender values should be based solely upon gross premium levels. Basing segmentation upon the level of cash surrender values introduces complications because of the inter-relationship between minimum cash surrender values and gross premium patterns. The requirements of this appendix relating to reserves for plans with unusual cash values and to reserves if cash values exceed calculated reserves serve to link required reserves and cash surrender values. The calculation of segmented reserves shall not be linked to the occurrence of a positive unitary terminal reserve at the end of a segment. The requirement of this appendix to hold the greater of the segmented reserve or the unitary reserve eliminates the need for any linkage.

12. "Tabular cost of insurance" means the net single premium at the beginning of a policy year for one-year term insurance in the amount of the guaranteed death benefit in that policy year.

13. "Ten-year select factors" means the select factors referenced in Appendix A-820.

14. a. "Unitary reserves" means the present value of all future guaranteed benefits less the present value of all future modified net premiums, where:

i. Guaranteed benefits and modified net premiums are considered to the mandatory expiration of the policy; and

ii. Modified net premiums are a uniform percentage of the respective guaranteed gross premiums, where the uniform percentage is such that, at issue, the present value of the net premiums equals the present value of all death benefits and pure endowments, plus the excess of Item (a) over Item (b), as follows:

(a) A net level annual premium equal to the present value, at the date of issue, of the benefits provided for after the first policy year, divided by the present value, at the date of issue, of an annuity of one per year payable on the first and each subsequent anniversary of the policy on which a premium falls due. However, the net level annual premium shall not exceed the net level annual premium on the nineteen-year premium whole life plan of insurance of the same renewal year equivalent level amount at an age one year higher than the age at issue of the policy.

(b) A net one year term premium for the benefits provided for in the first policy year.

b. The interest rates used in the present value calculations for any policy may not exceed the maximum valuation interest rate, determined with a guarantee duration equal to the length from issue to the mandatory expiration of the policy.

Drafting Note: The purpose of this paragraph is to define as specifically as possible what has become commonly called the unitary method. Appendix A-820 does not define the term "unitary" for policies with nonlevel premiums or benefits; its requirement for reserves "computed by a method that is consistent with the principles of Appendix A-820" has not been uniformly interpreted.

15. "Universal life insurance policy" means any individual life insurance policy under the provisions of which separately identified interest credits (other than in connection with dividend accumulations, premium deposit funds, or other supplementary accounts) and mortality or expense charges are made to the policy.

General Calculation Requirements for Basic Reserves and Premium Deficiency Reserves

16. Prior to January 1, 2004, at the election of the company for any one or more specified plans of life insurance, the minimum mortality standard for basic reserves may be calculated using the 1980 CSO valuation tables with select mortality factors. Effective January 1, 2004, the 2001 CSO Mortality Table is the minimum standard for basic reserves (or any other valuation mortality table adopted by the NAIC after the effective date of the 2001 CSO table for this purpose). Prior to January 1, 2004 if select mortality factors are elected, they may be:

a. The ten-year select mortality factors referenced in Appendix A-820;

b. The select mortality factors in Attachment 1 of this appendix; or

Drafting Note: The select mortality factors for duration 1 through 15 in Attachment 1 of this appendix reflect the Society of Actuaries' data for the years 1983 through 1986, split by sex and smoking status, with fifteen years of mortality improvement, based on Society of Actuaries' Projection Scale A applied. A 50% margin was added. The factors were then graded to the 1980 CSO Tables over the next five durations. A 50% margin was deemed appropriate to provide a reasonable margin, with little likelihood that actual experience for significant blocks of business would exceed it.

c. Any other table of select mortality factors adopted by the NAIC after the effective date of this appendix for the purpose of calculating basic reserves.

17. Deficiency reserves, if any, are calculated for each policy as the excess, if greater than zero, of the quantity A over the basic reserve. The quantity A is obtained by recalculating the basic reserve for the policy using guaranteed gross premiums instead of net premiums when the guaranteed gross premiums are less than the corresponding net premiums. At the election of the company for any one or more specified plans of insurance, the quantity A and prior to January 1, 2004 the corresponding net premiums used in the determination of quantity A may be based upon the 1980 CSO valuation tables with select mortality factors (or any other valuation mortality table adopted by the NAIC after the effective date of this appendix). If select mortality factors are elected, they may be:

a. The ten-year select mortality factors referenced in Appendix A-820;

b. The select mortality factors in Attachment 1 of this appendix;

Effective January 1, 2004, the 2001 CSO Mortality Table is the minimum standard for deficiency reserves. If select mortality rates are used, they may be multiplied by X percent for durations in the first segment, subject to the conditions specified in Sections 17c. to iv. (a). In demonstrating compliance with those conditions, the demonstrations may not combine the results of tests that utilize the 1980 CSO Mortality Table with those tests that utilize the 2001 CSO Mortality Table, unless the combination is explicitly required by regulation or necessary to be in compliance with relevant Actuarial Standards of Practice.

Drafting Note: The select mortality factors in Attachment 1 of this appendix do not reflect the underwriting risk classes that have evolved since the period of the underlying experience. In light of this consideration and the recent recognition of the regulatory value of actuarial opinions, this appendix allows actuarial judgment to be used for deficiency reserves.

c. For durations in the first segment, X percent of the select mortality factors in Attachment 1 of this appendix, subject to the following:

i. X may vary by policy year, policy form, underwriting classification, issue age, or any other policy factor expected to affect mortality experience;

Attachment 1

ii. X is such that, when using the valuation interest rate used for basic reserves, Item (a) is greater than or equal to Item (b);

(a) The actuarial present value of future death benefits, calculated using the mortality rates resulting from the application of X;

(b) The actuarial present value of future death benefits calculated using anticipated mortality experience without recognition of mortality improvement beyond the valuation date;

iii. X is such that the mortality rates resulting from the application of X are at least as great as the anticipated mortality experience, without recognition of mortality improvement beyond the valuation date, in each of the first five (5) years after the valuation date;

iv. The appointed actuary shall increase X at any valuation date where it is necessary to continue to meet all the requirements of paragraph 17.c.;

v. The appointed actuary may decrease X at any valuation date as long as X continues to meet all the requirements of paragraph 17.c.; and

vi. The appointed actuary shall specifically take into account the adverse effect on expected mortality and lapsation of any anticipated or actual increase in gross premiums.

(a) If X is less than 100 percent at any duration for any policy, the following requirements shall be met:

(i) The appointed actuary shall annually prepare an actuarial opinion and memorandum for the company in conformance with the asset adequacy analysis requirements as outlined in Appendix A-822;

(ii) The appointed actuary shall disclose, in the Regulatory Asset Adequacy Issues Summary, the impact of the insufficiency of assets to support the payment of benefits and expenses and the establishment of statutory reserves during one or more interim periods; and

(iii) The appointed actuary shall annually opine for all policies subject to this appendix as to whether the mortality rates resulting from the application of X meet the requirements of paragraph 17.c. This opinion shall be supported by an actuarial report, subject to appropriate Actuarial Standards of Practice promulgated by the Actuarial Standards Board of the American Academy of Actuaries. The X factors shall reflect anticipated future mortality, without recognition of mortality improvement beyond the valuation date, taking into account relevant emerging experience.

d. Any other table of select mortality factors adopted by the NAIC after the effective date of this appendix for the purpose of calculating deficiency reserves.

18. This paragraph applies to both basic reserves and deficiency reserves. Any set of select mortality factors may be used only for the first segment. However, if the first segment is less than ten (10) years, the appropriate ten-year select mortality factors referenced in Appendix A-820 may be used thereafter through the tenth policy year from the date of issue.

Drafting Note: This appendix does not allow the use of select mortality factors beyond the first segment. The rationale is that the result of a premium increase that is sufficient to require a new segment will be increased lapsation, leading to mortality deterioration after the increase. Also, for policies that have reentry provisions, select mortality factors shall not be used in segments beginning after reentry unless a new policy is actually issued. However, this appendix allows the use of the ten-year select mortality factors referenced in Appendix A-820 beyond the first segment (but in no case beyond the tenth policy year) in recognition that the mortality deterioration is unlikely to occur to a significant degree within the first ten (10) years.

19. In determining basic reserves or deficiency reserves, guaranteed gross premiums without policy fees may be used where the calculation involves the guaranteed gross premium but only if the policy fee is a level dollar amount after the first policy year. In determining deficiency reserves, policy fees may be included in guaranteed gross premiums, even if not included in the actual calculation of basic reserves.

20. Reserves for policies that have changes to guaranteed gross premiums, guaranteed benefits, guaranteed charges, or guaranteed credits that are unilaterally made by the insurer after issue and that are effective for more than one year after the date of the change shall be the greatest of the following: (1) reserves calculated ignoring the guarantee, (2) reserves assuming the guarantee was made at issue, and (3) reserves assuming that the policy was issued on the date of the guarantee.

Calculation of Minimum Valuation Standard for Policies with Guaranteed Nonlevel Gross Premiums or Guaranteed Nonlevel Benefits (Other than Universal Life Policies)

21. Basic Reserves

a. Basic reserves shall be calculated as the greater of the segmented reserves and the unitary reserves. Both the segmented reserves and the unitary reserves for any policy shall use the same valuation mortality table and selection factors. At the option of the insurer, in calculating segmented reserves and net premiums, either of the adjustments described in subparagraph i. or ii. below may be made:

i. Treat the unitary reserve, if greater than zero, applicable at the end of each segment as a pure endowment and subtract the unitary reserve, if greater than zero, applicable at the beginning of each segment from the present value of guaranteed life insurance and endowment benefits for each segment.

ii. Treat the guaranteed cash surrender value, if greater than zero, applicable at the end of each segment as a pure endowment; and subtract the guaranteed cash surrender value, if greater than zero, applicable at the beginning of each segment from the present value of guaranteed life insurance and endowment benefits for each segment.

22. Deficiency Reserves

a. The deficiency reserve at any duration shall be calculated:

i. On a unitary basis if the corresponding basic reserve determined by paragraph 21 is unitary;

ii. On a segmented basis if the corresponding basic reserve determined by paragraph 21 is segmented; or

iii. On the segmented basis if the corresponding basic reserve determined by paragraph 21 is equal to both the segmented reserve and the unitary reserve.

b. Paragraph 22 shall apply to any policy for which the guaranteed gross premium at any duration is less than the corresponding modified net premium calculated by the method used in determining the basic reserves, but using the minimum valuation standards of mortality (specified in paragraph 17) and rate of interest.

c. Deficiency reserves, if any, shall be calculated for each policy as the excess if greater than zero, for the current and all remaining periods, of the quantity A over the basic reserve, where A is obtained as indicated in paragraph 17.

d. For deficiency reserves determined on a segmented basis, the quantity A is determined using segment lengths equal to those determined for segmented basic reserves.

23. Minimum Value

a. Basic reserves may not be less than the tabular cost of insurance for the balance of the policy year, if mean reserves are used. Basic reserves may not be less than the tabular cost of insurance for the balance of the current modal period or to the paid-to-date, if later, but not beyond the next policy anniversary, if mid-terminal reserves are used. The tabular cost of insurance shall use the same valuation mortality table and interest rates as that used for the calculation of the segmented reserves. However, if select mortality factors are used, they shall be the ten-year select factors referenced in Appendix A-820. In no case may total reserves (including basic reserves, deficiency reserves and any reserves held for supplemental benefits that would expire upon contract termination) be less than the amount that the policyowner would receive (including the cash surrender value of the supplemental benefits, if any, referred to above), exclusive of any deduction for policy loans, upon termination of the policy. Effective January 1, 2004, the valuation mortality table used in determining the tabular cost of insurance shall be the ultimate mortality rates in the 2001 CSO Mortality Table.

24. Unusual Pattern of Guaranteed Cash Surrender Values

Drafting Note: This requirement is independent of both the segmentation process and the unitary process. After the greater of the segmented or the unitary reserve has been determined, then this paragraph imposes an additional floor on the ultimate reserve. The purpose of this paragraph is to assure adequate funding of significant increases in guaranteed cash surrender values.

a. For any policy with an unusual pattern of guaranteed cash surrender values, the reserves actually held prior to the first unusual guaranteed cash surrender value shall not be less than the reserves calculated by treating the first unusual guaranteed cash surrender value as a pure endowment and treating the policy as an *n* year policy providing term insurance plus a pure endowment equal to the unusual cash surrender value, where *n* is the number of years from the date of issue to the date the unusual cash surrender value is scheduled.

b. The reserves actually held subsequent to any unusual guaranteed cash surrender value shall not be less than the reserves calculated by treating the policy as an *n* year policy providing term insurance plus a pure endowment equal to the next unusual guaranteed cash surrender value, and treating any unusual guaranteed cash surrender value at the end of the prior segment as a net single premium, where

i. *n* is the number of years from the date of the last unusual guaranteed cash surrender value prior to the valuation date to the earlier of:

(a) The date of the next unusual guaranteed cash surrender value, if any, that is scheduled after the valuation date; or

(b) The mandatory expiration date of the policy; and

ii. The net premium for a given year during the *n* year period is equal to the product of the net to gross ratio and the respective gross premium; and

iii. The net to gross ratio is equal to Item (a) divided by Item (b) as follows:

(a) The present value, at the beginning of the *n* year period, of death benefits payable during the *n* year period plus the present value, at the beginning of the n year period, of the next unusual guaranteed cash surrender value, if any, minus the amount of the last unusual guaranteed cash surrender value, if any, scheduled at the beginning of the *n* year period.

(b) The present value, at the beginning of the *n* year period, of the scheduled gross premiums payable during the *n* year period.

c. For purposes of this paragraph, a policy is considered to have an unusual pattern of guaranteed cash surrender values if any future guaranteed cash surrender value exceeds the prior year's guaranteed cash surrender value by more than the sum of:

i. One hundred ten percent (110%) of the scheduled gross premium for that year;

ii. One hundred ten percent (110%) of one year's accrued interest on the sum of the prior year's guaranteed cash surrender value and the scheduled gross premium using the nonforfeiture interest rate used for calculating policy guaranteed cash surrender values; and

iii. Five percent (5%) of the first policy year surrender charge, if any.

25. Optional Exemption for Yearly Renewable Term Reinsurance. At the option of the company, the following approach for reserves on YRT reinsurance may be used:

Drafting Note: Traditional reserves for yearly renewable term (YRT) reinsurance, the calculations of which this section describes, are already adequate and sufficient. However, without this option in the appendix, YRT reinsurance would be subject to the more complex segmentation calculations.

a. Calculate the valuation net premium for each future policy year as the tabular cost of insurance for that future year.

b. Basic reserves shall never be less than the tabular cost of insurance for the appropriate period, as defined in paragraph 23.

c. Deficiency reserves.

i. For each policy year, calculate the excess, if greater than zero, of the valuation net premium over the respective maximum guaranteed gross premium.

ii. Deficiency reserves shall never be less than the sum of the present values, at the date of valuation, of the excesses determined in accordance with subparagraph i. above.

d. Prior to January 1, 2004, for purposes of this paragraph, the calculations use the maximum valuation interest rate and the 1980 CSO mortality tables with or without ten-year select mortality factors, or any other table adopted after the effective date of this appendix by the NAIC for this purpose. Effective January 1, 2004, the calculations specified in this paragraph (25) shall use the ultimate mortality rates in the 2001 CSO Mortality Table.

e. A reinsurance agreement shall be considered YRT reinsurance for purposes of this paragraph if only the mortality risk is reinsured.

f. If the assuming company chooses this optional exemption, the ceding company's reinsurance reserve credit shall be limited to the amount of reserve held by the assuming company for the affected policies.

26. Optional Exemption for Attained-Age-Based Yearly Renewable Term Life Insurance Policies. At the option of the company, the following approach for reserves for attained-age-based YRT life insurance policies may be used:

Drafting Note: Traditional reserves for attained-age-based YRT policies, the calculations of which this subsection describes, are already adequate and sufficient. However, without this option in the appendix, these policies would be subject to the more complex segmentation calculations.

a. Calculate the valuation net premium for each future policy year as the tabular cost of insurance for that future year.

b. Basic reserves shall never be less than the tabular cost of insurance for the appropriate period, as defined in paragraph 23.

c. Deficiency reserves.

i. For each policy year, calculate the excess, if greater than zero, of the valuation net premium over the respective maximum guaranteed gross premium.

ii. Deficiency reserves shall never be less than the sum of the present values, at the date of valuation, of the excesses determined in accordance with subparagraph i. above.

d. Prior to January 1, 2004, for purposes of this paragraph, the calculations use the maximum valuation interest rate and the 1980 CSO valuation tables with or without ten-year select mortality factors, or any other table adopted after the effective date of this appendix by the NAIC for this purpose. Effective January 1, 2004, the calculations specified in this paragraph shall use the ultimate mortality rates in the 2001 CSO Mortality Table.

e. A policy shall be considered an attained-age-based YRT life insurance policy for purposes of this subsection if:

i. The premium rates (on both the initial current premium scale and the guaranteed maximum premium scale) are based upon the attained age of the insured such that the rate for any given policy at a given attained age of the insured is independent of the year the policy was issued; and

ii. The premium rates (on both the initial current premium scale and the guaranteed maximum premium scale) are the same as the premium rates for policies covering all insureds of the same sex, risk class, plan of insurance and attained age.

f. For policies that become attained-age-based YRT policies after an initial period of coverage, the approach of this subsection may be used after the initial period if:

i. The initial period is constant for all insureds of the same sex, risk class and plan of insurance; or

ii. The initial period runs to a common attained age for all insureds of the same sex, risk class and plan of insurance; and

iii. After the initial period of coverage, the policy meets the conditions of paragraph 26.e. above.

g. If this election is made, this approach shall be applied in determining reserves for all attained-age-based YRT life insurance policies issued on or after the effective date of this appendix.

27. Exemption from Unitary Reserves for Certain *n*-Year Renewable Term Life Insurance Polices. Unitary basic reserves and unitary deficiency reserves need not be calculated for a policy if the following conditions are met:

Drafting Note: Without this exemption, companies issuing certain *n*-year renewable term policies could be forced to hold reserves higher than *n*-year term reserves, even though in many cases gross premiums are well above valuation mortality rates.

a. The policy consists of a series of *n*-year periods, including the first period and all renewal periods, where *n* is the same for each period, except that for the final renewal period, n may be truncated or extended to reach the expiry age, provided that this final renewal period is less than 10 years and less than twice the size of the earlier n-year periods, and for each period, the premium rates on both the initial current premium scale and the guaranteed maximum premium scale are level;

b. Prior to January 1, 2004, the guaranteed gross premiums in all *n*-year periods are not less than the corresponding net premiums based upon the 1980 CSO Table with or without the ten-year select mortality factors. Effective January 1, 2004, the calculations specified in this paragraph shall use the ultimate mortality rates in the 2001 CSO Mortality Table; and

c. There are no cash surrender values in any policy year.

28. Exemption from Unitary Reserves for Certain Juvenile Policies. Unitary basic reserves and unitary deficiency reserves need not be calculated for a policy if the following conditions are met, based upon the initial current premium scale at issue:

a. At issue, the insured is age twenty-four (24) or younger;

b. Until the insured reaches the end of the juvenile period, which shall occur at or before age twenty-five (25), the gross premiums and death benefits are level, and there are no cash surrender values; and

c. After the end of the juvenile period, gross premiums are level for the remainder of the premium paying period, and death benefits are level for the remainder of the life of the policy.

Drafting Note: The jumping juvenile policy described has traditionally been valued in two segments. This exemption will allow that practice to continue without requiring the calculation of reserves on a unitary basis. However, within each segment, both basic and deficiency reserves shall comply with the segmented reserve requirements.

Calculation of Minimum Valuation Standard for Flexible Premium and Fixed Premium Universal Life Insurance Policies That Contain Provisions Resulting in the Ability of a Policyowner to Keep a Policy in Force Over a Secondary Guarantee Period

29. General

a. Policies with a secondary guarantee include:

i. A policy with a guarantee that the policy will remain in force at the original schedule of benefits, subject only to the payment of specified premiums;

ii. Prior to January 1, 2004 a policy in which the minimum premium at any duration is less than the corresponding one year valuation premium, calculated using the maximum valuation interest rate and the 1980 CSO valuation tables with or without ten-year select mortality factors, or any other table adopted after the effective date of this appendix by the NAIC for this purpose. Effective January 1, 2004, the one-year valuation premium shall be calculated using the ultimate mortality rates in the 2001 CSO Mortality Table; or

iii. A policy with any combination of subparagraph i. and ii.

Drafting Note: Universal life and variable universal life policies with secondary guarantees that meet the requirements of paragraph 3.a.ii. are not subject to this appendix.

b. A secondary guarantee period is the period for which the policy is guaranteed to remain in force subject only to a secondary guarantee. When a policy contains more than one secondary guarantee, the minimum reserve shall be the greatest of the respective minimum reserves at that valuation date of each unexpired secondary guarantee, ignoring all other secondary guarantees. Secondary guarantees that are unilaterally changed by the insurer after issue shall be considered to have been made at issue. Reserves described in paragraphs 30 and 31 below shall be recalculated from issue to reflect these changes.

c. Specified premiums mean the premiums specified in the policy, the payment of which guarantees that the policy will remain in force at the original schedule of benefits, but which otherwise would be insufficient to keep the policy in force in the absence of the guarantee if maximum mortality and expense charges and minimum interest credits were made and any applicable surrender charges were assessed.

d. For purposes of this paragraph, the minimum premium for any policy year is the premium that, when paid into a policy with a zero account value at the beginning of the policy year, produces a zero account value at the end of the policy year. The minimum premium calculation shall use the policy cost factors (including mortality charges, loads and expense charges) and the interest crediting rate, which are all guaranteed at issue.

e. The one-year valuation premium means the net one-year premium based upon the original schedule of benefits for a given policy year. The one-year valuation premiums for all policy years are calculated at issue. The select mortality factors defined in paragraphs 17.b., 17.c. and 17.d. may not be used to calculate the one-year valuation premiums.

f. The one-year valuation premium should reflect the frequency of fund processing, as well as the distribution of deaths assumption employed in the calculation of the monthly mortality charges to the fund.

30. Basic Reserves for the Secondary Guarantees. Basic reserves for the secondary guarantees shall be the segmented reserves for the secondary guarantee period. In calculating the segments and the segmented reserves, the gross premiums shall be set equal to the specified premiums, if any, or otherwise to the minimum premiums, that keep the policy in force and the segments will be determined according to the contract segmentation method as defined in paragraph 5.

31. Deficiency Reserves for the Secondary Guarantees. Deficiency reserves, if any, for the secondary guarantees shall be calculated for the secondary guarantee period in the same manner as described in paragraph 22 with gross premiums set equal to the specified premiums, if any, or otherwise to the minimum premiums that keep the policy in force.

32. Minimum Reserves. The minimum reserves during the secondary guarantee period are the greater of:

a. The basic reserves for the secondary guarantee plus the deficiency reserve, if any, for the secondary guarantees; or

b. The minimum reserves required by other appendices governing universal life plans.

Attachment 1

SELECT MORTALITY FACTORS

This Attachment contains tables of select mortality factors that are the bases to which the respective percentage of paragraphs 16.b., 17.b. and 17.c. are applied.

The six tables of select mortality factors contained herein include: (1) male aggregate, (2) male nonsmoker, (3) male smoker, (4) female aggregate, (5) female nonsmoker, and (6) female smoker.

These tables apply to both age last birthday and age nearest birthday mortality tables.

For sex-blended mortality tables, compute select mortality factors in the same proportion as the underlying mortality. For example, for the 1980 CSO-B Table, the calculated select mortality factors are eighty percent (80%) of the appropriate male table in this Attachment, plus twenty percent (20%) of the appropriate female table in this Attachment.

Attachment 1

SELECT MORTALITY FACTORS

Male, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	96	98	98	99	99	100	100	90	92	92	92	92	93	93	96	97	98	98	99	100
19	83	84	84	87	87	87	79	79	79	81	81	82	82	82	85	88	91	94	97	100
20	69	71	71	74	74	69	69	67	69	70	71	71	71	71	74	79	84	90	95	100
21	66	68	69	71	66	66	67	66	67	70	70	70	70	71	71	77	83	88	94	100
22	65	66	66	63	63	64	64	64	65	68	68	68	68	69	71	77	83	88	94	100
23	62	63	59	60	62	62	63	63	64	65	65	67	67	69	70	76	82	88	94	100
24	60	56	56	59	59	60	61	61	61	64	64	64	66	67	70	76	82	88	94	100
25	52	53	55	56	58	58	60	60	60	63	62	63	64	67	69	75	81	88	94	100
26	51	52	55	56	58	58	57	61	61	62	63	64	66	69	66	73	80	86	93	100
27	51	52	55	57	58	60	61	61	60	63	63	64	67	66	67	74	80	87	93	100
28	49	51	56	58	60	60	61	62	62	63	64	66	65	66	68	74	81	87	94	100
29	49	51	56	58	60	61	62	62	62	64	64	62	66	67	70	76	82	88	94	100
30	49	50	56	58	60	60	62	63	63	64	62	63	67	68	71	77	83	88	94	100
31	47	50	56	58	60	62	63	64	64	62	63	66	68	70	72	78	83	89	94	100
32	46	49	56	59	60	62	63	66	62	63	66	67	70	72	73	78	84	89	95	100
33	43	49	56	59	62	63	64	62	65	66	67	70	72	73	75	80	85	90	95	100
34	42	47	56	60	62	63	61	63	66	67	70	71	73	75	76	81	86	90	95	100
35	40	47	56	60	63	61	62	65	67	68	71	73	74	76	76	81	86	90	95	100
36	38	42	56	60	59	61	63	65	67	68	70	72	74	76	77	82	86	91	95	100
37	38	45	56	57	61	62	63	65	67	68	70	72	74	76	76	81	86	90	95	100
38	37	44	53	58	61	62	65	66	67	69	69	73	75	76	77	82	86	91	95	100
39	37	41	53	58	62	63	65	65	66	68	69	72	74	76	76	81	86	90	95	100
40	34	40	53	58	62	63	65	65	66	68	68	71	75	76	77	82	86	91	95	100
41	34	41	53	58	62	63	65	64	64	66	68	70	74	76	77	82	86	91	95	100
42	34	43	53	58	61	62	63	63	63	64	66	69	72	75	77	82	86	91	95	100
43	34	43	54	59	60	61	63	62	62	64	66	67	72	74	77	82	86	91	95	100
44	34	44	54	58	59	60	61	60	61	62	64	67	71	74	77	82	86	91	95	100
45	34	45	53	58	59	60	60	60	59	60	63	66	71	74	77	82	86	91	95	100
46	31	43	52	56	57	58	59	59	59	60	63	67	71	74	75	80	85	90	95	100
47	32	42	50	53	55	56	57	58	59	60	65	68	71	74	75	80	85	90	95	100
48	32	41	47	52	54	56	57	57	57	61	65	68	72	73	74	79	84	90	95	100
49	30	40	46	49	52	54	55	56	57	61	66	69	72	73	74	79	84	90	95	100
50	30	38	44	47	51	53	54	56	57	61	66	71	72	73	75	80	85	90	95	100
51	28	37	42	46	49	53	54	56	57	61	66	71	72	73	75	80	85	90	95	100
52	28	35	41	45	49	51	54	56	57	61	66	71	72	74	75	80	85	90	100	100
53	27	35	39	44	48	51	53	55	57	61	67	71	74	75	76	81	86	100	100	100
54	27	33	38	44	48	50	53	55	57	61	67	72	74	75	76	81	100	100	100	100
55	25	32	37	43	47	50	53	55	57	61	68	72	74	75	78	100	100	100	100	100

Attachment 1

Male, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	25	32	37	43	47	49	51	54	56	61	67	70	73	74	100	100	100	100	100	100
57	24	31	38	43	47	49	51	54	56	59	66	69	72	100	100	100	100	100	100	100
58	24	31	38	43	48	48	50	53	56	59	64	67	100	100	100	100	100	100	100	100
59	23	30	39	43	48	48	51	53	55	58	63	100	100	100	100	100	100	100	100	100
60	23	30	39	43	48	47	50	52	53	57	100	100	100	100	100	100	100	100	100	100
61	23	30	39	43	49	49	50	52	53	75	100	100	100	100	100	100	100	100	100	100
62	23	30	39	44	49	49	51	52	75	75	100	100	100	100	100	100	100	100	100	100
63	22	30	39	45	50	50	52	75	75	75	100	100	100	100	100	100	100	100	100	100
64	22	30	39	45	50	51	75	75	75	75	100	100	100	100	100	100	100	100	100	100
65	22	30	39	45	50	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
66	22	30	39	45	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
67	22	30	39	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
68	23	32	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
69	23	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
70	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
71	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
72	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
73	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
74	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
75	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
76	48	52	55	60	60	65	70	70	70	100	100	100	100	100	100	100	100	100	100	100
77	48	52	55	60	60	65	70	70	100	100	100	100	100	100	100	100	100	100	100	100
78	48	52	55	60	60	65	70	100	100	100	100	100	100	100	100	100	100	100	100	100
79	48	52	55	60	60	65	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	48	52	55	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	48	52	55	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	48	52	55	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	48	52	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	48	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Attachment 1

Male, Non-Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	93	95	96	98	99	100	100	90	92	92	92	92	95	95	96	97	98	98	99	100
19	80	81	83	86	87	87	79	79	79	81	81	82	83	83	86	89	92	94	97	100
20	65	68	69	72	74	69	69	67	69	70	71	71	72	72	75	80	85	90	95	100
21	63	66	68	71	66	66	67	66	67	70	70	70	71	71	73	78	84	89	95	100
22	62	65	66	62	63	64	64	64	67	68	68	68	70	70	73	78	84	89	95	100
23	60	62	58	60	62	62	63	63	64	67	68	68	67	69	71	77	83	88	94	100
24	59	55	56	58	59	60	61	61	63	65	67	66	66	69	71	77	83	88	94	100
25	52	53	55	56	58	58	60	60	61	64	64	64	64	67	70	76	82	88	94	100
26	51	53	55	56	58	60	61	61	61	63	64	64	66	69	67	74	80	87	93	100
27	51	52	55	58	60	60	61	61	62	63	64	66	67	66	67	74	80	87	93	100
28	49	52	57	58	60	61	63	62	62	64	66	66	63	66	68	74	81	87	94	100
29	49	51	57	60	61	61	62	62	63	64	66	63	65	67	68	74	81	87	94	100
30	49	51	57	60	61	62	63	63	63	64	62	63	66	68	70	76	82	88	94	100
31	47	50	57	60	60	62	63	64	64	62	63	65	67	70	71	77	83	88	94	100
32	46	50	57	60	62	63	64	64	62	63	65	66	68	71	72	78	83	89	94	100
33	45	49	56	60	62	63	64	62	63	65	66	68	71	73	74	79	84	90	95	100
34	43	48	56	62	63	64	62	62	65	66	67	70	72	74	74	79	84	90	95	100
35	41	47	56	62	63	61	62	63	66	67	68	70	72	74	75	80	85	90	95	100
36	40	47	56	62	59	61	62	63	66	67	68	70	72	74	75	80	85	90	95	100
37	38	45	56	58	59	61	62	63	66	67	67	69	71	73	74	79	84	90	95	100
38	38	45	53	58	61	62	63	65	65	67	68	70	72	74	73	78	84	89	95	100
39	37	41	53	58	61	62	63	64	65	67	68	70	71	73	73	78	84	89	95	100
40	34	41	53	58	61	62	63	64	64	66	67	69	71	73	72	78	83	89	94	100
41	34	41	53	58	61	61	62	62	63	65	65	67	69	71	71	77	83	88	94	100
42	34	43	53	58	60	61	62	61	61	63	64	66	67	69	71	77	83	88	94	100
43	32	43	53	58	60	61	60	60	60	60	62	64	66	68	69	75	81	88	94	100
44	32	44	52	57	59	60	60	59	59	58	60	62	65	67	69	75	81	88	94	100
45	32	44	52	57	59	60	59	57	57	57	59	61	63	66	68	74	81	87	94	100
46	32	42	50	54	56	57	57	56	55	56	59	61	63	65	67	74	80	87	93	100
47	30	40	48	52	54	55	55	54	54	55	59	61	62	63	66	73	80	86	93	100
48	30	40	46	49	51	52	53	53	54	55	57	61	62	63	63	70	78	85	93	100
49	29	39	43	48	50	51	50	51	53	54	57	61	61	62	62	70	77	85	92	100
50	29	37	42	45	47	48	49	50	51	54	57	61	61	61	61	69	77	84	92	100
51	27	35	40	43	45	47	48	50	51	53	57	60	61	61	62	70	77	85	92	100
52	27	34	39	42	44	45	48	49	50	53	56	60	60	62	62	70	77	85	100	100
53	25	31	37	41	44	45	47	49	50	51	56	59	61	61	62	70	77	100	100	100
54	25	30	36	39	43	44	47	48	49	51	55	59	59	61	62	70	100	100	100	100
55	24	29	35	38	42	43	45	48	49	50	56	58	59	61	62	100	100	100	100	100

Attachment 1

Male, Non-Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	23	29	35	38	42	42	44	47	48	50	55	57	58	59	100	100	100	100	100	100
57	23	28	35	38	42	42	43	45	47	49	53	55	56	100	100	100	100	100	100	100
58	22	28	33	37	41	41	43	45	45	47	51	53	100	100	100	100	100	100	100	100
59	22	26	33	37	41	41	42	44	44	46	50	100	100	100	100	100	100	100	100	100
60	20	26	33	37	41	40	41	42	42	45	100	100	100	100	100	100	100	100	100	100
61	20	26	33	37	41	40	41	42	42	75	100	100	100	100	100	100	100	100	100	100
62	19	25	32	38	40	40	41	42	75	75	100	100	100	100	100	100	100	100	100	100
63	19	25	33	36	40	40	41	75	75	75	100	100	100	100	100	100	100	100	100	100
64	18	24	32	36	39	40	75	75	75	75	100	100	100	100	100	100	100	100	100	100
65	18	24	32	36	39	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
66	18	24	32	36	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
67	18	24	32	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
68	18	24	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
69	18	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
70	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
71	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
72	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
73	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
74	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
75	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
76	48	52	55	60	60	65	70	70	70	100	100	100	100	100	100	100	100	100	100	100
77	48	52	55	60	60	65	70	70	100	100	100	100	100	100	100	100	100	100	100	100
78	48	52	55	60	60	65	70	100	100	100	100	100	100	100	100	100	100	100	100	100
79	48	52	55	60	60	65	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	48	52	55	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	48	52	55	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	48	52	55	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	48	52	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	48	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Attachment 1

Male, Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
19	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
20	98	100	100	100	100	100	100	99	99	99	100	99	99	99	100	100	100	100	100	100
21	95	98	99	100	95	96	96	95	96	97	97	96	96	96	96	97	98	98	99	100
22	92	95	96	90	90	93	93	92	93	95	95	93	93	92	93	94	96	97	99	100
23	90	92	85	88	88	89	89	89	90	90	90	90	89	90	92	94	95	97	98	100
24	87	81	82	85	84	86	88	86	86	88	88	86	86	88	89	91	93	96	98	100
25	77	78	79	82	81	83	83	82	83	85	84	84	84	85	86	89	92	94	97	100
26	75	77	79	82	82	83	83	82	83	84	84	84	84	85	81	85	89	92	96	100
27	73	75	78	82	82	83	83	82	82	82	82	84	84	80	81	85	89	92	96	100
28	71	73	79	82	81	82	83	81	81	82	82	82	80	80	81	85	89	92	96	100
29	69	72	78	81	81	82	82	81	81	81	81	77	80	80	81	85	89	92	96	100
30	68	71	78	81	81	81	82	81	81	81	76	77	80	80	81	85	89	92	96	100
31	65	70	77	81	79	81	82	81	81	76	77	79	81	81	83	86	90	93	97	100
32	63	67	77	78	79	81	81	81	76	77	77	80	83	83	85	88	91	94	97	100
33	60	65	74	78	79	79	81	76	77	77	79	80	83	85	85	88	91	94	97	100
34	57	62	74	77	79	79	75	76	77	79	79	81	83	85	87	90	92	95	97	100
35	53	60	73	77	79	75	75	76	77	79	80	82	84	86	88	90	93	95	98	100
36	52	59	71	75	74	75	75	76	77	79	79	81	83	85	87	90	92	95	97	100
37	49	58	70	71	74	74	75	76	77	78	79	81	84	86	86	89	92	94	97	100
38	48	55	66	70	72	74	74	75	76	78	79	81	83	85	87	90	92	95	97	100
39	45	50	65	70	72	72	74	74	75	77	79	81	84	86	86	89	92	94	97	100
40	41	49	63	68	71	72	73	74	74	76	78	80	83	85	86	89	92	94	97	100
41	40	49	63	68	71	72	72	72	73	75	76	78	81	84	85	88	91	94	97	100
42	40	49	62	68	70	71	71	71	71	73	75	76	81	83	85	88	91	94	97	100
43	39	50	62	67	69	69	70	70	70	71	73	76	79	83	85	88	91	94	97	100
44	39	50	60	66	68	69	68	69	69	69	71	74	79	81	85	88	91	94	97	100
45	37	50	60	66	68	68	68	67	67	67	69	73	78	81	85	88	91	94	97	100
46	37	48	58	63	65	67	66	66	66	67	71	74	78	81	84	87	90	94	97	100
47	36	47	55	61	63	64	64	64	65	67	71	75	79	81	84	87	90	94	97	100
48	35	46	53	58	60	62	63	63	65	67	72	75	79	81	83	86	90	93	97	100
49	34	45	51	56	58	59	61	62	63	67	72	77	80	81	83	86	90	93	97	100
50	34	43	49	53	55	57	60	61	63	67	73	78	80	81	81	85	89	92	96	100
51	32	42	47	52	55	57	60	61	63	67	73	78	80	83	84	87	90	94	97	100
52	32	40	46	50	54	56	60	61	63	67	73	78	81	84	85	88	91	94	100	100
53	30	37	44	49	54	56	59	61	65	67	74	79	83	85	87	90	92	100	100	100
54	30	36	43	48	53	55	59	61	65	67	74	80	84	85	89	91	100	100	100	100
55	29	35	42	47	53	55	59	61	65	67	75	80	84	86	90	100	100	100	100	100

Attachment 1

Male, Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	28	35	42	47	53	55	57	60	63	68	74	79	83	85	100	100	100	100	100	100
57	28	35	42	47	53	54	57	60	64	67	74	78	81	100	100	100	100	100	100	100
58	26	33	43	48	54	54	56	59	63	67	73	78	100	100	100	100	100	100	100	100
59	26	33	43	48	54	53	57	59	63	66	73	100	100	100	100	100	100	100	100	100
60	25	33	43	48	54	53	56	58	62	66	100	100	100	100	100	100	100	100	100	100
61	25	33	43	49	55	55	57	59	63	75	100	100	100	100	100	100	100	100	100	100
62	25	33	43	50	56	56	58	61	75	75	100	100	100	100	100	100	100	100	100	100
63	24	33	45	51	56	56	59	75	75	75	100	100	100	100	100	100	100	100	100	100
64	24	34	45	51	57	57	75	75	75	75	100	100	100	100	100	100	100	100	100	100
65	24	34	45	52	57	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
66	24	35	45	53	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
67	25	35	45	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
68	25	36	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
69	27	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
70	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
71	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
72	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
73	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
74	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
75	48	52	55	60	60	65	70	70	70	70	100	100	100	100	100	100	100	100	100	100
76	48	52	55	60	60	65	70	70	70	100	100	100	100	100	100	100	100	100	100	100
77	48	52	55	60	60	65	70	70	100	100	100	100	100	100	100	100	100	100	100	100
78	48	52	55	60	60	65	70	100	100	100	100	100	100	100	100	100	100	100	100	100
79	48	52	55	60	60	65	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	48	52	55	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	48	52	55	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	48	52	55	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	48	52	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	48	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Attachment 1

Female, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	99	100	100	100	100	100	100	100	93	95	96	97	97	100	100	100	100	100	100	100
18	83	83	84	84	84	84	86	78	78	79	82	84	85	88	88	90	93	95	98	100
19	65	66	68	68	68	68	63	63	64	66	69	71	72	74	75	80	85	90	95	100
20	48	50	51	51	51	47	48	48	49	51	56	57	58	61	63	70	78	85	93	100
21	47	48	50	51	47	47	48	49	51	53	57	60	61	64	64	71	78	86	93	100
22	44	47	48	45	47	47	48	49	53	54	60	61	63	64	66	73	80	86	93	100
23	42	45	44	45	47	47	49	51	53	54	61	64	64	67	69	75	81	88	94	100
24	39	40	42	44	47	47	50	51	54	56	64	64	66	69	70	76	82	88	94	100
25	34	38	41	44	47	47	50	53	56	57	64	67	69	71	73	78	84	89	95	100
26	34	38	41	45	49	49	51	56	58	59	66	69	70	73	70	76	82	88	94	100
27	34	38	41	47	50	51	54	57	59	60	69	70	73	70	71	77	83	88	94	100
28	34	37	43	47	53	53	56	59	62	63	70	73	70	72	74	79	84	90	95	100
29	34	38	43	49	54	56	58	60	63	64	73	70	72	74	75	80	85	90	95	100
30	35	38	43	50	56	56	59	63	66	67	70	71	74	75	76	81	86	90	95	100
31	35	38	43	51	56	58	60	64	67	65	71	72	74	75	76	81	86	90	95	100
32	35	39	45	51	56	59	63	66	65	66	72	72	75	76	76	81	86	90	95	100
33	36	39	44	52	58	62	64	65	66	67	72	74	75	76	76	81	86	90	95	100
34	36	40	45	52	58	63	63	66	67	68	74	74	76	76	76	81	86	90	95	100
35	36	40	45	53	59	61	65	67	68	70	75	74	75	76	75	80	85	90	95	100
36	36	40	45	53	55	62	65	67	68	70	74	74	74	75	75	80	85	90	95	100
37	36	41	47	52	57	62	65	67	68	69	72	72	73	75	74	79	84	90	95	100
38	34	41	44	52	57	63	66	68	69	70	72	71	72	74	75	80	85	90	95	100
39	34	40	45	53	58	63	66	68	69	69	70	70	70	73	74	79	84	90	95	100
40	32	40	45	53	58	65	65	67	68	69	70	69	70	73	73	78	84	89	95	100
41	32	40	45	53	57	63	64	67	68	68	69	69	69	73	74	79	84	90	95	100
42	32	40	45	52	56	61	63	65	66	68	69	68	70	74	75	80	85	90	95	100
43	31	39	45	51	55	59	61	65	65	66	68	69	69	74	77	82	86	91	95	100
44	31	39	45	50	54	58	61	63	64	66	67	68	71	75	78	82	87	91	96	100
45	31	38	44	49	53	56	59	62	63	65	67	68	71	77	79	83	87	92	96	100
46	29	37	43	48	51	54	59	62	63	65	67	69	71	77	78	82	87	91	96	100
47	28	35	41	46	49	54	57	61	62	66	68	69	71	77	77	82	86	91	95	100
48	28	35	41	44	49	52	57	61	63	66	68	71	72	75	77	82	86	91	95	100
49	26	34	39	43	47	52	55	61	63	67	69	71	72	75	75	80	85	90	95	100
50	25	32	38	41	46	50	55	61	63	67	69	72	72	75	74	79	84	90	95	100
51	25	32	38	41	45	50	55	61	63	66	68	69	71	74	74	79	84	90	95	100
52	23	30	36	41	45	51	56	61	62	65	66	68	68	73	73	78	84	89	100	100
53	23	30	36	41	47	51	56	61	62	63	65	66	68	72	72	78	83	100	100	100
54	22	29	35	41	47	53	57	61	61	62	62	66	66	69	70	76	100	100	100	100
55	22	29	35	41	47	53	57	61	61	61	62	63	64	68	69	100	100	100	100	100

Attachment 1

Female, Aggregate

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	22	29	35	41	45	51	56	59	60	61	62	63	64	67	100	100	100	100	100	100
57	22	29	35	41	45	50	54	56	58	59	61	62	63	100	100	100	100	100	100	100
58	22	30	36	41	44	49	53	56	57	57	61	62	100	100	100	100	100	100	100	100
59	22	30	36	41	44	48	51	53	55	56	59	100	100	100	100	100	100	100	100	100
60	22	30	36	41	43	47	50	51	53	55	100	100	100	100	100	100	100	100	100	100
61	22	29	35	39	42	46	49	50	52	80	100	100	100	100	100	100	100	100	100	100
62	20	28	33	39	41	45	47	49	80	80	100	100	100	100	100	100	100	100	100	100
63	20	28	33	38	41	44	46	80	80	80	100	100	100	100	100	100	100	100	100	100
64	19	27	32	36	40	42	80	80	80	80	100	100	100	100	100	100	100	100	100	100
65	19	25	30	35	39	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
66	19	25	30	35	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
67	19	25	30	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
68	19	25	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
69	19	64	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
70	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
71	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
72	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
73	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
74	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
75	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
76	60	60	64	68	68	72	75	75	80	100	100	100	100	100	100	100	100	100	100	100
77	60	60	64	68	68	72	75	75	100	100	100	100	100	100	100	100	100	100	100	100
78	60	60	64	68	68	72	75	100	100	100	100	100	100	100	100	100	100	100	100	100
79	60	60	64	68	68	72	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	60	60	64	68	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	60	60	64	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	60	60	64	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Attachment 1

Female, Non-Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	96	98	98	98	98	99	99	99	92	92	93	95	95	97	99	99	99	100	100	100
18	78	80	80	80	80	81	81	74	75	75	78	79	82	83	85	88	91	94	97	100
19	60	62	63	63	63	65	59	59	60	60	64	67	67	70	72	78	83	89	94	100
20	42	44	45	45	45	42	42	42	45	45	50	51	53	56	58	66	75	83	92	100
21	41	42	44	45	41	42	42	44	47	47	51	53	54	57	59	67	75	84	92	100
22	39	41	44	41	41	42	44	45	49	49	54	56	57	58	60	68	76	84	92	100
23	38	41	38	40	41	42	44	46	49	50	56	57	58	60	62	70	77	85	92	100
24	36	36	38	40	41	42	46	47	50	51	58	59	60	62	63	70	78	85	93	100
25	32	34	37	40	41	43	46	49	51	53	59	60	62	63	64	71	78	86	93	100
26	32	34	37	41	43	45	47	50	53	53	60	62	63	64	62	70	77	85	92	100
27	32	34	38	43	46	47	49	51	53	55	62	63	64	62	62	70	77	85	92	100
28	30	34	39	43	47	49	51	53	56	58	63	63	61	62	63	70	78	85	93	100
29	30	35	40	45	50	51	52	55	58	59	64	61	62	63	63	70	78	85	93	100
30	31	35	40	46	51	52	53	56	59	60	62	62	63	65	65	72	79	86	93	100
31	31	35	40	46	51	53	55	58	60	58	62	62	63	65	65	72	79	86	93	100
32	32	35	40	45	51	53	56	59	57	58	62	63	63	65	64	71	78	86	93	100
33	32	36	41	47	52	55	58	55	58	59	63	63	65	65	65	72	79	86	93	100
34	33	36	41	47	52	55	55	57	58	59	63	65	64	65	64	71	78	86	93	100
35	33	36	41	47	52	53	57	58	59	61	63	64	64	64	64	71	78	86	93	100
36	33	36	41	47	49	53	57	58	59	61	63	64	63	64	63	70	78	85	93	100
37	32	36	41	44	49	53	57	58	59	60	62	62	61	62	63	70	78	85	93	100
38	32	37	39	45	50	54	57	58	60	60	61	61	61	62	61	69	77	84	92	100
39	30	35	39	45	50	54	57	58	60	59	60	60	59	60	61	69	77	84	92	100
40	28	35	39	45	50	54	56	57	59	59	60	59	59	59	60	68	76	84	92	100
41	28	35	39	45	49	52	55	55	58	57	58	59	58	59	60	68	76	84	92	100
42	27	35	39	44	49	52	54	55	56	57	57	57	58	60	61	69	77	84	92	100
43	27	34	39	44	47	50	53	53	55	55	56	57	56	60	61	69	77	84	92	100
44	26	34	38	42	47	50	52	53	54	55	55	55	56	61	62	70	77	85	92	100
45	26	33	38	42	45	48	51	51	52	53	54	55	56	61	62	70	77	85	92	100
46	24	32	37	40	43	47	49	51	52	53	54	55	56	60	61	69	77	84	92	100
47	24	30	35	39	42	45	47	49	51	53	54	55	56	59	60	68	76	84	92	100
48	23	30	35	37	40	44	47	49	50	53	54	55	55	59	57	66	74	83	91	100
49	23	29	33	35	39	42	45	48	50	53	54	55	55	57	56	65	74	82	91	100
50	21	27	32	34	37	41	44	48	50	53	54	55	55	56	55	64	73	82	91	100
51	21	26	30	34	37	41	44	48	49	51	53	53	54	55	55	64	73	82	91	100
52	20	25	30	33	37	41	44	47	48	50	50	51	51	55	53	62	72	81	100	100
53	19	24	29	32	37	41	43	47	48	48	49	49	51	52	52	62	71	100	100	100
54	18	24	29	32	37	41	43	45	47	47	47	49	49	51	51	61	100	100	100	100
55	18	23	28	32	37	41	43	45	45	45	46	46	47	50	50	100	100	100	100	100

Attachment 1

Female, Non-Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	18	23	28	32	36	39	42	44	44	45	46	46	46	49	100	100	100	100	100	100
57	18	23	28	31	35	38	41	42	44	44	45	45	46	100	100	100	100	100	100	100
58	17	23	26	31	35	36	38	41	41	42	45	45	100	100	100	100	100	100	100	100
59	17	23	26	30	33	35	38	39	40	41	44	100	100	100	100	100	100	100	100	100
60	17	23	26	30	32	34	36	38	39	40	100	100	100	100	100	100	100	100	100	100
61	17	22	25	29	32	33	35	36	38	80	100	100	100	100	100	100	100	100	100	100
62	16	22	25	28	30	32	34	35	80	80	100	100	100	100	100	100	100	100	100	100
63	16	20	24	28	30	32	34	80	80	80	100	100	100	100	100	100	100	100	100	100
64	14	21	24	27	29	30	80	80	80	80	100	100	100	100	100	100	100	100	100	100
65	15	19	23	25	28	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
66	15	19	23	25	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
67	15	19	22	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
68	13	18	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
69	13	64	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
70	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
71	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
72	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
73	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
74	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
75	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
76	60	60	64	68	68	72	75	75	80	100	100	100	100	100	100	100	100	100	100	100
77	60	60	64	68	68	72	75	75	100	100	100	100	100	100	100	100	100	100	100	100
78	60	60	64	68	68	72	75	100	100	100	100	100	100	100	100	100	100	100	100	100
79	60	60	64	68	68	72	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	60	60	64	68	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	60	60	64	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	60	60	64	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Attachment 1

Female, Smoker

Issue Age	Duration 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
0-15	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
16	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
17	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
18	99	100	100	100	100	100	100	95	96	97	100	100	100	100	100	100	100	100	100	100
19	87	89	92	92	92	92	84	84	86	86	92	93	95	96	99	99	99	100	100	100
20	74	77	80	80	80	73	73	73	75	77	83	83	86	88	90	92	94	96	98	100
21	71	74	78	78	71	71	73	74	77	79	85	86	88	89	90	92	94	96	98	100
22	68	71	75	70	71	71	73	74	78	79	88	90	89	89	92	94	95	97	98	100
23	65	69	67	70	70	70	73	77	79	81	89	90	90	92	92	94	95	97	98	100
24	62	60	64	69	70	70	74	77	79	81	92	90	92	93	93	94	96	97	99	100
25	53	58	63	67	69	70	74	78	81	82	92	93	93	95	95	96	97	98	99	100
26	53	58	63	69	71	72	75	79	82	82	93	93	95	96	90	92	94	96	98	100
27	52	56	63	70	74	74	78	81	82	84	93	95	95	90	90	92	94	96	98	100
28	52	56	64	71	75	77	79	82	85	86	95	95	90	92	92	94	95	97	98	100
29	51	56	64	71	78	78	81	84	86	88	95	90	90	92	92	94	95	97	98	100
30	51	56	64	72	79	79	82	85	88	89	90	90	92	93	93	94	96	97	99	100
31	51	56	64	72	78	81	84	84	88	84	90	90	92	93	93	94	96	97	99	100
32	51	56	64	71	78	81	85	86	84	85	90	90	92	94	93	94	96	97	99	100
33	51	57	62	71	78	82	85	83	84	85	90	92	93	93	93	94	96	97	99	100
34	51	56	62	71	78	82	81	83	85	86	90	92	92	94	93	94	96	97	99	100
35	51	56	62	71	78	79	83	84	85	86	90	91	91	93	93	94	96	97	99	100
36	49	56	62	71	74	79	83	84	85	86	90	90	91	93	92	94	95	97	98	100
37	48	55	62	67	74	79	83	84	85	86	89	90	89	92	91	93	95	96	98	100
38	47	55	57	66	72	77	81	84	86	86	87	88	88	90	91	93	95	96	98	100
39	45	50	57	66	72	77	81	83	85	86	86	87	86	89	90	92	94	96	98	100
40	41	50	57	66	72	77	81	83	84	85	86	86	86	89	89	91	93	96	98	100
41	40	50	57	65	71	76	79	81	83	84	85	86	85	89	90	92	94	96	98	100
42	40	49	57	65	69	74	77	80	82	83	84	85	86	90	92	94	95	97	98	100
43	39	49	55	63	69	73	76	78	80	82	83	84	85	92	93	94	96	97	99	100
44	39	48	55	62	67	71	75	78	80	80	82	84	86	93	96	97	98	98	99	100
45	37	47	55	61	65	70	73	76	78	80	81	84	86	94	97	98	98	99	99	100
46	36	46	53	59	63	68	71	75	77	79	83	85	86	93	96	97	98	98	99	100
47	34	44	51	57	62	66	70	75	77	80	83	85	86	93	94	95	96	98	99	100
48	34	44	50	54	60	64	69	74	77	80	84	86	87	92	92	94	95	97	98	100
49	33	42	48	53	58	63	68	74	77	81	84	86	87	92	91	93	95	96	98	100
50	31	41	46	51	57	61	67	74	77	81	85	87	87	91	90	92	94	96	98	100
51	30	39	45	51	56	61	67	74	75	80	83	85	85	90	90	92	94	96	98	100
52	29	38	45	50	56	62	68	74	75	79	81	83	84	90	90	92	94	96	100	100
53	28	37	43	49	57	62	68	73	74	77	79	81	83	89	89	91	93	100	100	100
54	28	36	43	49	57	63	69	73	74	75	78	80	81	87	89	91	100	100	100	100
55	26	35	42	49	57	63	69	73	73	74	76	78	79	86	87	100	100	100	100	100

Attachment 1

Female, Smoker

Issue Age	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20+
56	26	35	42	49	56	62	67	71	72	74	76	78	79	85	100	100	100	100	100	100
57	26	35	42	49	55	61	66	69	72	73	76	78	79	100	100	100	100	100	100	100
58	28	36	43	49	55	59	63	68	69	72	76	78	100	100	100	100	100	100	100	100
59	28	36	43	49	54	57	63	67	68	70	76	100	100	100	100	100	100	100	100	100
60	28	36	43	49	53	57	61	64	67	69	100	100	100	100	100	100	100	100	100	100
61	26	35	42	48	52	56	59	63	66	80	100	100	100	100	100	100	100	100	100	100
62	26	33	41	47	51	55	58	62	80	80	100	100	100	100	100	100	100	100	100	100
63	25	33	41	46	51	55	57	80	80	80	100	100	100	100	100	100	100	100	100	100
64	25	33	40	45	50	53	80	80	80	80	100	100	100	100	100	100	100	100	100	100
65	24	32	39	44	49	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
66	24	32	39	44	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
67	24	32	39	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
68	24	32	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
69	24	64	68	72	72	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
70	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
71	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
72	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
73	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
74	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
75	60	60	64	68	68	72	75	75	80	80	100	100	100	100	100	100	100	100	100	100
76	60	60	64	68	68	72	75	75	80	100	100	100	100	100	100	100	100	100	100	100
77	60	60	64	68	68	72	75	75	100	100	100	100	100	100	100	100	100	100	100	100
78	60	60	64	68	68	72	75	100	100	100	100	100	100	100	100	100	100	100	100	100
79	60	60	64	68	68	72	100	100	100	100	100	100	100	100	100	100	100	100	100	100
80	60	60	64	68	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
81	60	60	64	68	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
82	60	60	64	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
83	60	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
84	60	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100
85+	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Appendix B
Interpretations of Statutory Accounting Principles

Introduction

Appendix B includes the final interpretations (INTs) of statutory accounting principles (SAPs) through December 2024. Reporting entities should note that interpretations are generally effective when finalized; therefore, the *Accounting Practices and Procedures Manual* (Manual) may not include every interpretation currently in effect due to the fact that it is published annually. As revisions are adopted, updates to the interpretations are tracked in the subsequent version of the Manual.

Historical

EITF Review/Rejected EITF Tracking

Beginning January 1, 1999, the Emerging Accounting Issues (E) Working Group (EAIWG) began addressing the Emerging Issues Task Force (EITF) opinions issued subsequent to 1996. In 2009, the EAIWG reached a consensus to incorporate rejected and non-applicable FASB EITFs that do not provide additional statutory accounting guidance in a listing within a designated interpretation. This interpretation (INT 99-00) included reference to all FASB EITFs, including those previously included in Appendix B as a statutory accounting interpretation, that were 1) rejected as not applicable to statutory accounting; 2) rejected without providing additional statutory guidance; or 3) rejected on the basis of issues rejected in a statement of statutory accounting principles (SSAP). In 2014, the Statutory Accounting Principles (E) Working Group (SAPWG) adopted a proposal to move all references to rejected GAAP material from INT 99-00 into *Issue Paper No. 99—Nonapplicable GAAP Pronouncements*. In 2015, Issue Paper No. 99 was moved to *Appendix D, Nonapplicable GAAP Pronouncements*.

Superseded SSAPs and Nullified INTs

In 2013, the SAPWG adopted a proposal to remove *Appendix H, Superseded SSAPs and Nullified Interpretations* from the Manual. Currently, these items are posted for public reference on the Statutory Accounting Principles (E) Working Group web page at *https://content.naic.org/cmte_e_app_sapwg.htm*.

Development Responsibilities

In 2015, the EAIWG was disbanded and its duties were absorbed by the SAPWG. The SAPWG is responsible for developing interpretations to address issues requiring interpretation, application or clarification of existing SAP.

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Interpretations of the Emerging Accounting Issues (E) Working Group and Statutory Accounting Principles (E) Working Group

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-03: Illustration of the Accounting/Reporting of Deposit-Type Contracts in Accordance with SSAP Nos. 51, 52 and 56

INT 00-03 Dates Discussed

December 6, 1999; March 13, 2000

INT 00-03 References

Current:
SSAP No. 51—Life Contracts
SSAP No. 52—Deposit-Type Contracts
SSAP No. 56—Separate Accounts

INT 00-03 Issue

1. Deposit-type contracts, as defined in SSAP No. 52 may be maintained in the general account or transferred to the separate account of an insurance company. During the process of preparing Blanks proposals to conform the reporting requirements to the SSAPs, the Impact of Codification on NAIC Publications Working Group noted an inconsistency in the reporting of deposit-type contracts between SSAP No. 52 and SSAP No. 56. At the 1999 NAIC Fall National Meeting, SSAP No. 56 was amended to clarify that the requirements of SSAP No. 52 are applicable to separate account deposit-type contracts.

2. Exhibit A is included as an illustration of accounting/reporting of separate account deposit-type contracts in accordance with SSAP Nos. 51, 52 and 56. Is this illustration consistent with the intent of the Codification of Statutory Accounting Principles (E) Working Group?

INT 00-03 Discussion

3. The Working Group reached a consensus that Exhibit A is consistent with the intent of the SSAPs.

INT 00-03 Status

4. No further discussion is planned.

Illustrative Example of the Accounting/Reporting of Deposit-Type Contracts in Accordance with SSAP No. 51 and SSAP No. 52

NOTE: Entries presented in this illustration may not reflect all accounting entries associated with the activity, e.g., some "due from" or "due to" entries are eliminated to simplify the example.

1. Contractholder surrendered an ordinary life insurance policy and elected to place the proceeds ($100,000) under a supplementary contract without life contingencies (SCWOLC).

General Account Statement

a.	Surrender Benefits & Withdrawals	$100,000	
	Liability for Deposit –Type Contracts		$100,000
b.	Aggregate Reserves for Life Policies	$100,000	
	Increase in Aggregate Reserves for Life Policies		$100,000

2. Insurer transfers, pursuant to contract provisions, $95,000 to separate account fund for SCWOLC contracts from general account fund for SCWOLC contracts; $5,000 is retained in the general account.

General Account Statement

a.	Liability for Deposit –Type Contracts	$95,000	
	Transfers to Separate Accounts		$95,000
b.	Transfers to Separate Account	$95,000	
	Cash		$95,000

Separate Accounts Statement

c.	Other transfers from General Account (net)	$95,000	
	Transfers on account of deposit-type contracts		$95,000
d.	Cash	$95,000	
	Other Transfers from General Account		$95,000
e.	Increase in liability for deposit-type contracts	$95,000	
	Liability for Deposit-Type Contracts		$95,000

3. Insurer establishes a $4,000 CARVM valuation allowance for this contract in the separate account fund.

Separate Accounts Statement

a.	Liability for Deposit-Type Contracts	$4,000	
	Increase in liability for deposit-type contracts		$4,000
b.	Change in expense allowances recognized in reserves	$4,000	
	Other transfers from General Account (net)		$4,000

General Account Statement

c.	Transfers to Separate Accounts (net)	$4,000	
	Transfer to/or (from) Separate Accounts		$4,000

4. Insurer's separate account fund for SCWOLC contracts assets earns $2,000 investment income that is immediately credited to the separate account fund for SCWOLC contracts.

Separate Accounts Statement

a.	Cash	$2,000	
	Net investment income		$2,000
b.	Increase in liability for deposit-type contracts	$2,000	
	Liability for Deposit-Type Contracts		$2,000

5. Contractholder is paid a $1,000 SCWOLC contract benefit from the separate account fund. The example has been simplified to show the cash flows from the Separate Account to the General Account and the payment to the contractholder from the General Account.

General Account Statement

a.	Cash	$1,000	
	Liability for Deposit-Type Contracts		$1,000
b.	Liability for Deposit-Type Contracts	$1,000	
	Cash		$1,000

Separate Accounts Statement

c.	Transfers on account of deposit-type contracts	$1,000	
	Cash		$1,000
d.	Liability for Deposit-type Contracts	$1,000	
	Increase in liability for deposit-type contracts		$1,000

6. Contractholder requests the insurer to purchase a variable annuity contract (insurance product) with $25,000 drawn from the separate account fund supporting the SCWOLC contract (deposit-type contract) and transfer it to a separate fund supporting variable annuities. This example has been simplified and ignores the internal cash exchange.

General Account Statement

a.	Transfers to Separate Accounts	$25,000	
	Premiums and Annuity Considerations		$25,000

Separate Accounts Statement

b.	Liability for Deposit-Type Contracts	$25,000	
	Increase in liability for deposit-type contracts		$25,000
c.	Transfers on account of deposit-type contracts	$25,000	
	Other transfers to general account (net)		$25,000
d.	Other transfers to general account (net)	$25,000	
	Net Premiums and Annuity Considerations		$25,000
e.	Increase in aggregate reserve for life, annuity	$25,000	
	Aggregate Reserve for life, annuity		$25,000

7. Contractholder in accordance with a Group GIC contract requests that $15,000 be withdrawn from the Group GIC Separate Account fund maintained by the insurer and transferred to the contractholder's Separate Account fund supporting the SCWOLC contract.

Separate Accounts Statement

a.	Liability for Deposit-Type Contracts (GIC)	$15,000	
	Increase in liability for deposit-type contracts		$15,000
b.	Transfers on account of deposit-type contracts	$15,000	
	Cash		$15,000
c.	Cash	$15,000	
	Transfers on account of deposit-type contracts		$15,000
d.	Increase in liability for deposit-type contracts	$15,000	
	Liability for Deposit-Type Contracts (SCWOLC)		$15,000

General Accounts Statement

e.	Other transfers to separate account (net)	$15,000	
	Liability for Deposit-Type Contracts (SCWOLC)		$15,000
f.	Liability for Deposit-Type Contracts (SCWOLC)	$15,000	
	Other transfers to separate account (net)		$15,000

8. Contractholder is assessed the annual administration fee of $100 for the SCWOLC contract.

Separate Accounts Statement

a.	Administration fees	$100	
	Cash		$100
b.	Liability for Deposit-type contracts	$100	
	Increase in liability for deposit-type contracts		$100

General Account Statement

c.	Cash	$100	
	Management fees		$100

"T" Accounts

General Account Statement

Balance Sheet

Cash

Xaction Ref.	Debit	Credit
Begin Bal.	100,000	
2b		95,000
5a	1,000	
5b		1,000
8c	100	
Total	101,100	96,000
Net	5,100	

Aggregate Reserves for Life Policies etc.

Xaction Ref.	Debit	Credit
Begin Bal.		100,000
1b	100,000	

Liab for Deposit-Type Contracts

Xaction Ref.	Debit	Credit
1a		100,000
2a	95,000	
5a		1,000
5b	1,000	
7e		15,000
7f	15,000	
Total	111,000	116,000
Net		5,000

Transfers to Sep Accts Pybl

Xaction Ref.	Debit	Credit
2a		95,000
2b	95,000	
3c	4,000	
7e	15,000	
7f		15,000
Total	114,000	110,000
Net	4,000	

Summary of Operations

Premiums & Considerations

Xaction Ref.	Debit	Credit
6a		25,000

Income from Fees . . From Sep Accts

Xaction Ref.	Debit	Credit
8c		100

Surrender Benefits

Xaction Ref.	Debit	Credit
1a	100,000	

Increase in Agg Res for Life Pol etc.

Xaction Ref.	Debit	Credit
1b		100,000

Transfers to Sep Accts

Xaction Ref.	Debit	Credit
3c		4,000
6a	25,000	
Total	25,000	4,000
Net	21,000	

Separate Accounts Statement

Balance Sheet

Cash

Xaction Ref.	Debit	Credit
Begin Bal.	15,000	
2d	95,000	
4a	2,000	
5c		1,000
7b		15,000
7c	15,000	
8a		100
Total	127,000	16,100
Net	110,900	

Aggregate Reserves for Life Policies etc.

Xaction Ref.	Debit	Credit
6e		25,000

Liab for Deposit-Type Contracts

Xaction Ref.	Debit	Credit
Begin Bal.		15,000
2e		95,000
3a	4,000	
4b		2,000
5d	1,000	
6b	25,000	
7a	15,000	
7d		15,000
8b	100	
Total	45,100	127,000
Net		81,900

Transfers to Gen Acct Pybl

Xaction Ref.	Debit	Credit
2c	95,000	
2d		95,000
3b		4,000
6c		25,000
6d	25,000	
Total	120,000	124,000
Net		4,000

Summary of Operations

Premiums & Considerations

Xaction Ref.	Debit	Credit
6d		25,000

Deposits Acct of Deposit-Type Contracts

Xaction Ref.	Debit	Credit
2c		95,000
5c	1,000	
6c	25,000	
7b	15,000	
7c		15,000
Total	41,000	110,000
Net		69,000

Net Invest Inc & Cap Gains

Xaction Ref.	Debit	Credit
4a		2,000

Change in Expense Allow

Xaction Ref.	Debit	Credit
3b	4,000	

Fees Assoc with Charges for Inv Mgmt etc.

Xaction Ref.	Debit	Credit
8a	100	

Increase in Agg Res for Life Cont etc.

Xaction Ref.	Debit	Credit
6e	25,000	

Increase in Liab for Deposit-Type Contracts

Xaction Ref.	Debit	Credit
2e	95,000	
3a		4,000
4b	2,000	
5d		1,000
6b		25,000
7a		15,000
7d	15,000	
8b		100
Total	112,000	45,100
Net	66,900	

General Account Instructions

NOTES TO FINANCIAL STATEMENTS

19. Separate Accounts

Illustration B:

Reconciliation of Net Transfers To or (From) Separate Accounts

1. Transfers as reported in the Summary of Operations of the Separate Accounts Statement:

a.	Transfers to Separate Accounts	$ 25,000
b.	Transfers from Separate Accounts	$ 4,000
c.	Net transfers to or (From) Separate Accounts (a) – (b)	$ 21,000

2. Reconciling Adjustments:

a.	____________________	$__________
b.	____________________	$__________
c.	____________________	$__________

3. Transfers as Reported in the Summary of Operations of the Life, Accident & Health Annual Statement

(1c) + (2) = $ 21,000

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

ASSETS	Current Year			Prior Year
	1 General Account Basis	2 Fair Value Basis	3 Total (Cols. 1 + 2)	4 Total
1. Bonds (Schedule D)				
2. Stocks (Schedule D):				
2.1 Preferred stocks				
2.2 Common stocks				
3. Mortgage loans on real estate (Schedule B)				
4. Real estate (Schedule A):				
4.1 Properties held for the production of income (less $…………encumbrances)				
4.2 Properties held for sale (less $………………………………encumbrances)				
5. Policy loans				
6. Cash (Schedule E, Part 1)		110,900	110,900	
7. Short-term investments (Schedule DA)				
8. Other invested assets (Schedule BA)				
9. Aggregate write-ins for invested assets				
10. Subtotals—Cash and invested assets (Lines 1 to 9)		110,900	110,900	
11. Investment income due and accrued				
12. Receivable for securities				
13. Net adjustment in assets and liabilities due to foreign exchange rates				
14. Aggregate write-ins for other-than-invested assets				
15. Lines 10 to 14		110,900	110,900	
DETAILS OF WRITE-INS				
0901.				
0902.				
0903.				
0998. Summary of remaining write-ins Line 9 from overflow page				
0999. Totals (Lines 0901 through 0903 + 0998) (Line 9 above)				
1401.				
1402.				
1403.				
1498. Summary of remaining write-ins for Line 14 from overflow page				
1499. Totals (Lines 1401 through 1403 plus 1498) (Line 14 above)				

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

LIABILITIES AND SURPLUS	Current Year 1 General Account Basis	2 Fair Value Basis	3 Total (Cols. 1 +2)	Prior Year 4 Total
1. Aggregate reserve for life, annuity and accident and health policies and contracts (Exhibit 6, Line 9999999, Col. 2)	....	25,000	25,000	....
2. Liability for deposit-type contracts (Exhibit 7, Line 9, Col. 1)	....	81,900	81,900	....
3. Interest Maintenance Reserve	....	....	....	....
4. Charges for investment management, administration and contract guarantees due or accrued	....	....	....	....
5. Investment expenses due or accrued (Exhibit 4, Line 24)	....	....	....	....
6. Investment taxes, licenses and fees due or accrued, excluding federal income taxes (Exhibit 5, Line 8)	....	....	....	....
7. Federal and foreign income taxes due or accrued (excluding deferred taxes)	....	....	....	....
8. Reserve for future federal income taxes	....	....	....	....
9. Unearned investment income (Exhibit 2, Line 14, Col. 2)	....	....	....	....
10. Other transfers to general account due or accrued (net) (including $....... accrued expense allowances recognized in reserves)	....	4,000	4,000	....
11. Remittances and items not allocated	....	....	....	....
12. Payable for securities	....	....	....	....
13. Net adjustment in assets and liabilities due to foreign exchange rates	....	....	....	....
14. Aggregate write-ins for liabilities				
15. Total Liabilities (including $...due or accrued net transfers to or (from) the general account)		110,900	110,900	
16. Contributed surplus	....	....	....	....
17. Aggregate write-ins for special surplus funds	....	....	....	....
18. Unassigned funds				
19. Surplus (Lines 16 through 18)				
20. Totals		110,900	110,900	
DETAILS OF WRITE-INS				
1401.	....	....	....	....
1402.	....	....	....	....
1403.	....	....	....	....
1498. Summary of remaining write-ins for Line 14 from overflow page	....	....	....	....
1499. Totals (Lines 1401 through 1403 plus 1498) (Line 14 above)				
1701.	....	....	....	....
1702.	....	....	....	....
1703.	....	....	....	....
1798. Summary of remaining write-ins for Line 17 from overflow page	....	....	....	....
1799. Totals (Lines 1701 through 1703 plus 1798) (Line 17 above)				

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

SUMMARY OF OPERATIONS	1 Current Year	2 Prior Year
1. Transfers to Separate Accounts:		
1.1 Net premiums and annuity considerations for life and accident and health policies and contracts	25,000	....
1.2 Considerations for supplementary contracts with life contingencies	....	....
1.3 Aggregate write-ins for other transfers to Separate Accounts		
1.4 Totals (Lines 1.1 to 1.3)	25,000	....
2. Transfers on account of deposit-type contracts (including $110,000 deposits less $41,000 withdrawals)	69,000	....
3. Net investment income and capital gains and losses (Exhibit 1, Line 9)	2,000	....
4. Aggregate write-ins for other income		
5. Totals (Lines 1.4 to 4)	96,000	
DEDUCT:		
6. Transfers from the Separate Account on account of contract benefits:		
6.1 Death benefits	....	....
6.2 Matured endowments	....	....
6.3 Annuity benefits	....	....
6.4 Payments on supplementary contracts with life contingencies	....	....
6.5 Accident and health benefits	....	....
6.6 Surrender benefits and withdrawals for life contracts	....	....
6.7 Aggregate write-ins for other transfers from Separate Accounts on account of contract benefits	....	....
7. Transfers on account of policy loans	....	....
8. Net transfer of reserves from or (to) Separate Accounts	....	....
9. Other transfers from the Separate Accounts:		
9.1 Federal and foreign income taxes incurred	....	....
9.2 Change in expense allowances recognized in reserves	4,000	....
9.3 Aggregate write-ins for other transfers from Separate Accounts		
10. Subtotals (Lines 6.1 to 9.3)	4,000	....
11. Fees associated with charges for investment management, administration and contract guarantees	100	....
12. Increase in aggregate reserve for life and accident and health policies and contracts	25,000	....
13. Increase in reserve for variable dividend accumulations	....	....
14. Increase in liability for deposit-type contracts	66,900	....
15. Increase in reserve for future federal income taxes	....	....
16. Aggregate write-ins for reserves and funds		
17. Totals (Lines 10 to 16)	96,000	
18. Net gain from operations (including $…………….unrealized capital gains) (Line 5 minus Line 17)	0	
SURPLUS ACCOUNT		
19. Surplus, December 31, prior year	....	....
20. Net gain from operations (Line 18)	....	....
21. Surplus contributed or (withdrawn) during year	....	....
22. Change in reserve on account of change in valuation basis, (increase) or decrease	....	....
23. Transfer from Separate Accounts of the change in expense allowances charged or credited to surplus	....	....
24. Aggregate write-ins for gains and losses in surplus	....	....
25. Surplus, December 31, current year (Page 3, Line 19)		
DETAILS OF WRITE-INS		
01.301.	....	....
01.302.	....	....
01.303.	....	....
01.398. Summary of remaining write-ins for Line 1.3 from overflow page	....	....
01.399. Totals (Lines 01.301 through 01.303 plus 01.398) (Line 1.3 above)		
0401.	....	....
0402.	....	....
0403.	....	....
0498. Summary of remaining write-ins for Line 4 from overflow page	....	....
0499. Totals (Lines 0401 through 0403 plus 0498) (Line 4 above)		
06.701.	....	....
06.702.	....	....
06.703.	....	....
06.798. Summary of remaining write-ins for Line 6.7 from overflow page	....	....
06.799. Totals (Lines 06.701 through 06.703 plus 06.798) (Line 6.7 above)		
09.301.	....	....
09.302.	....	....
09.303.	....	....
09.398. Summary of remaining write-ins for Line 9.3 from overflow page	....	....
09.399. Totals (Lines 09.301 through 09.303 plus 09.398) (Line 9.3 above)		
1601.	....	....
1602.	....	....
1603.	....	....
1698. Summary of remaining write-ins for Line 16 from overflow page	....	....
1699. Totals (Lines 1601 through 1603 plus 1698) (Line 16 above)		
2401.	....	....
2402.	....	....
2403.	....	....
2498. Summary of remaining write-ins for Line 24 from overflow page	....	....
2499. Totals (Lines 2401 through 2403 plus 2498) (Line 24 above)		

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

ASSETS	Current Year 1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	Prior Year 4 Net Admitted Assets
1. Bonds				
2. Stocks:				
2.1 Preferred stocks (Schedule D, Part 2, Section 1)				
2.2 Common stocks (Schedule D, Part 2, Section 2)				
3. Mortgage loans on real estate (Schedule B, Part 1):				
3.1 First liens				
3.2 Other than first liens				
4. Real estate (Schedule A):				
4.1 Properties occupied by the company (less $.......... encumbrances)				
4.2 Properties held for the production of income (less $.......... encumbrances)				
4.3 Properties held for sale (less $.......... encumbrances)				
5. Policy loans				
6. Premium notes, including $.......... for first year premiums				
7. Cash ($....…………………., Schedule E, Part 1) and short-term investments ($....………..….., Schedule DA, Part 2)	5,100		5,100	
8. Other invested assets (Schedule BA, Part 1)				
9. Receivable for securities				
10. Aggregate write-ins for invested assets				
11. Subtotals, cash and invested assets (Lines 1 to 10)	5,100		5,100	
12. Reinsurance ceded:				
12.1 Amounts recoverable from reinsurers (Schedule S, Part 2)				
12.2 Commissions and expense allowances due				
12.3 Experience rating and other refunds due				
12.4 Other amounts receivable under reinsurance contracts				
13. Electronic data processing equipment and software				
14. Federal and foreign income tax recoverable and interest thereon (including $………… net deferred tax asset)				
15. Guaranty funds receivable or on deposit				
16. Life insurance premiums and annuity considerations deferred and uncollected on in force business (less premiums on reinsurance ceded and less $........loading)				
17. Accident and health premiums due and unpaid				
18. Investment income due and accrued (Exhibit 2)				
19. Net adjustment in assets and liabilities due to foreign exchange rates				
20. Receivable from parent, subsidiaries and affiliates				
21. Amounts receivable relating to uninsured accident and health plans				
22. Amounts due from agents				
23. Other assets nonadmitted (Exhibit 12)				
24. Aggregate write-ins for other-than-invested assets				
25. Total assets excluding Separate Accounts business (Lines 11 to 24)	5,100		5,100	
26. From Separate Accounts Statement	110,900		110,900	
27. Total (Lines 25 and 26)	116,000		116,000	
DETAILS OF WRITE-INS				
1001.				
1002.				
1003.				
1098. Summary of remaining write-ins for Line 10 from overflow page				
1099. Totals (Lines 1001 through 1003 + 1098) (Line 10 above)				
2401.				
2402.				
2403.				
2498. Summary of remaining write-ins for Line 24 from overflow page				
2499. Totals (Lines 2401 through 2403 + 2498) (Line 24 above)				

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

LIABILITIES, SURPLUS AND OTHER FUNDS	1 Current Year	2 Prior Year
1. Aggregate reserve for life policies and contracts $................(Exhibit 8, Line 9999999) less $ .included in Line 6.3 (including $ Modco Reserve	....	....
2. Aggregate reserve for accident and health policies (Exhibit 9, Line 17, Col. 1) (including $.........Modco Reserve)	....	....
3. Liability for deposit-type contracts (Exhibit 10, Line 14, Col. 1) (including $........Modco Reserve)	5,000	....
4. Policy and contract claims:		
4.1 Life (Exhibit 11, Part 1, Line 4.4, Col. 1 less sum of Cols. 9, 10 and 11)	....	....
4.2 Accident and health (Exhibit 11, Part 1, Line 4.4, sum of Cols. 9, 10 and 11)	....	....
5. Policyholders' dividends $..and coupons $...due and unpaid (Exhibit 7, Line 10)	....	....
6. Provision for policyholders' dividends and coupons payable in following calendar year—estimated amounts:		
6.1 Dividends apportioned for payment to ...., 20 .... (including $ .... Modco Reserve)	....	....
. 6.2 Dividends not yet apportioned (including $ .... Modco Reserve)	....	....
6.3. Coupons and similar benefits (including $ .... Modco Reserve)	....	....
7. Amount provisionally held for deferred dividend policies not included in Line 6	....	....
8. Premiums and annuity considerations for life and accident and health policies and contracts received in advance less $...................discount; .... including $................accident and health premiums (Exhibit 1, Part 1, Col. 1, sum of Lines 4 and 14)	....	....
9. Policy and contract liabilities not included elsewhere:		
9.1 Surrender values on canceled policies	....	....
9.2 Provision for experience rating refunds, including $.. accident and health experience rating refunds	....	....
9.3 Other amounts payable on reinsurance, including $......................................assumed and $.........................ceded	....	....
9.4 Interest Maintenance Reserve (Page 33, Line 6)	....	....
10. Commissions to agents due or accrued-life and annuity contracts $........... accident and health $……. and deposit-type contract funds $	....	....
11. Commissions and expense allowances payable on reinsurance assumed	....	....
12. General expenses due or accrued (Exhibit 5, Line 12, Col. 5)	....	....
13. Transfers to Separate Accounts due or accrued (net) (including ($ 4,000) accrued for expense allowances recognized in reserves)	(4,000)	....
14. Taxes, licenses and fees due or accrued, excluding federal income taxes (Exhibit 6, Line 9, Col. 5)	....	....
15. Federal and foreign income taxes, including $.......................................on realized capital gains (losses) (including $.. net-deferred tax liability)	....	....
16. Unearned investment income (Exhibit 2, Line 9, Col. 2)	....	....
17. Amounts withheld or retained by company as agent or trustee	....	....
18. Amounts held for agents' account, including $.. agents' credit balances	....	....
19. Remittances and items not allocated	....	....
20. Net adjustment in assets and liabilities due to foreign exchange rates	....	....
21. Liability for benefits for employees and agents if not included above	....	....
22. Borrowed money $...and interest thereon $	....	....
23. Dividends to stockholders declared and unpaid	....	....
24. Miscellaneous liabilities:		
24.1 Asset valuation reserve (Page 34, Line 15, Col. 7)	....	....
24.2 Reinsurance in unauthorized companies	....	....
24.3 Funds held under reinsurance treaties with unauthorized reinsurers	....	....
24.4 Payable to parent, subsidiaries and affiliates	....	....
24.5 Drafts outstanding	....	....
24.6 Liability for amounts held under uninsured accident and health plans	....	....
24.7 Funds held under coinsurance	....	....
24.8 Payable for securities	....	....
24.9 Capital notes $……… and interest thereon $………	....	....
25. Aggregate write-ins for liabilities		
26. Total liabilities excluding Separate Accounts business (Lines 1 to 25)	1,000	
27. From Separate Accounts statement	110,900	....
28. Total liabilities (Lines 26 and 27)	111,900	
29. Common capital stock	....	....
30. Preferred capital stock	....	....
31. Aggregate write-ins for other than special surplus funds	....	....
32. Surplus notes	....	....
33. Gross paid in and contributed surplus (Page 3, Line 33, Col. 2 plus Page 4, Line 51.1, Col. 1)	....	....
34. Aggregate write-ins for special surplus funds	....	....
35. Unassigned funds (surplus)	....	
36. Less treasury stock, at cost:		....
36.1 .... shares common (value included in Line 29 $ ....)	....	....
36.2 .... shares preferred (value included in Line 30 $ ....)	....	....
37. Surplus (total Lines 31 + 32 + 33 + 34 + 35 - 36) (Including $.............in Separate Accounts Statement)		
38. Totals of Lines 29, 30 and 37 (Page 4, Line 55)		
39. Totals of Lines 28 and 38 (Page 2, Line 27, Col. 3)		
DETAILS OF WRITE-INS		
2501.	....	....
2502.	....	....
2503.	....	....
2598. Summary of remaining write-ins for Line 25 from overflow page	....	....
2599. Totals (Lines 2501 through 2503 plus 2598) (Line 25 above)		
3101.	....	....
3102.	....	....
3103.	....	....
3198. Summary of remaining write-ins for Line 31 from overflow page	....	....
3199. Totals (Lines 3101 through 3103 plus 3198) (Line 31 above)		
3401.	....	....
3402.	....	....
3403.	....	....
3498. Summary of remaining write-ins for Line 34 from overflow page	....	....
3499. Totals (Lines 3401 through 3403 plus 3498) (Line 34 above)		

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

	SUMMARY OF OPERATIONS (Excluding Unrealized Capital Gains and Losses)	1 Current Year	2 Prior Year
1.	Premiums and annuity considerations for life and accident and health policies and contracts (Exhibit 1, Part 1, Line 20.4, Col. 1, less Col. 11)	25,000	
2.	Considerations for supplementary contracts with life contingencies		
3.	Net investment income (Exhibit 2, Line 16)		
4.	Amortization of Interest Maintenance Reserve (IMR) (Page 33, Line 5)		
5.	Separate Accounts net gain from operations excluding unrealized gains or losses		
6.	Commissions and expense allowances on reinsurance ceded (Exhibit 1, Part 2, Line 26.1, Col. 1)		
7.	Reserve adjustments on reinsurance ceded		
8.	Miscellaneous Income:		
	8.1 Income from fees associated with investment management, administration and contract guarantees from Separate Accounts	100	
	8.2 Charges and fees for deposit-type contracts		
	8.3 Aggregate write-ins for miscellaneous income		
9.	Totals (Lines 1 to 8.3)	25,100	
10.	Death benefits		
11.	Matured endowments (excluding guaranteed annual pure endowments)		
12.	Annuity benefits (Exhibit 11, Part 2, Line 6.4, Cols. 4 + 8)		
13.	Disability benefits and benefits under accident and health policies		
14.	Coupons, guaranteed annual pure endowments and similar benefits		
15.	Surrender benefits and withdrawals for life contracts	100,000	
16.	Group conversions		
17.	Interest and adjustments on policy or deposit-type contract funds		
18.	Payments on supplementary contracts with life contingencies		
19.	Increase in aggregate reserves for life and accident and health policies and contracts	(100,000)	
20.	Totals (Lines 10 to 19)	0	
21.	Commissions on premiums, annuity considerations and deposit-type contract funds (direct business only) (Exhibit 1, Part 2, Line 31, Col. 1, less Col. 11)		
22.	Commissions and expense allowances on reinsurance assumed (Exhibit 1, Part 2, Line 26.2, Col. 1, less Col. 11)		
23.	General insurance expenses (Exhibit 5, Line 10, Cols. 1 + 2 + 3)		
24.	Insurance taxes, licenses and fees, excluding federal income taxes (Exhibit 6, Line 7, Cols. 1 + 2 + 3)		
25.	Increase in loading on deferred and uncollected premiums		
26.	Net transfers to or (from) Separate Accounts	21,000	
27.	Aggregate write-ins for deductions		
28.	Totals (Lines 20 to 27)	21,000	
29.	Net gain from operations before dividends to policyholders and federal income taxes (Line 9 minus Line 28)	4,100	
30.	Dividends to policyholders		
31.	Net gain from operations after dividends to policyholders and before federal income taxes (Line 29 minus Line 30)		
32.	Federal and foreign income taxes incurred (excluding tax on capital gains)		
33.	Net gain from operations after dividends to policyholders and federal income taxes and before realized capital gains or (losses) (Line 31 minus Line 32)		
34.	Net realized capital gains or (losses) less capital gains tax and transferred to the IMR (Exhibit 3, Footnote (a), Line 3C)		
35.	Net income (Line 33 plus Line 34)		
	CAPITAL AND SURPLUS ACCOUNT		
36.	Capital and surplus, December 31, prior year (Page 3, Line 38, Col. 2)		
37.	Net income (Line 35)		
38.	Change in net unrealized capital gains (losses)		
39.	Change in net unrealized foreign exchange capital gain (loss)		
40.	Change in net deferred income tax		
41.	Change in nonadmitted assets and related items (Exhibit 12, Line 6, Col. 3)		
42.	Change in liability for reinsurance in unauthorized companies		
43.	Change in reserve on account of change in valuation basis, (increase) or decrease (Exhibit 8A, Line 9999999, Col. 4)		
44.	Change in asset valuation reserve (Page 34, Lines 2 through 4 plus 8, 11 and 12, Col. 7)		
45.	Change in treasury stock (Page 3, Lines 36.1 and 36.2 Col. 2 minus Col. 1)		
46.	Surplus (contributed to) withdrawn from Separate Accounts during period		
47.	Other changes in surplus in Separate Accounts statement		
48.	Change in surplus notes		
49.	Cumulative effect of changes in accounting principles		
50.	Capital changes:		
	50.1 Paid in		
	50.2 Transferred from surplus (Stock Dividend)		
	50.3 Transferred to surplus		
51.	Surplus adjustment:		
	51.1 Paid in		
	51.2 Transferred to capital (Stock Dividend)		
	51.3 Transferred from capital		
	51.4 Change in surplus as a result of reinsurance		
52.	Dividends to stockholders		
53.	Aggregate write-ins for gains and losses in surplus		
54.	Net change in capital and surplus for the year (Lines 37 through 53)		
55.	Capital and surplus, December 31, current year (Lines 36 + 54) (Page 3, Line 38)		
	DETAILS OF WRITE-INS		
08.301.			
08.302.			
08.303.			
08.398.	Summary of remaining write-ins for Line 8.3 from overflow page		
08.399.	Totals (Lines 08.301 through 08.303 plus 08.398) (Line 8.3 above)		
2701.			
2702.			
2703.			
2798.	Summary of remaining write-ins for Line 27 from overflow page		
2799.	Totals (Lines 2701 through 2703 plus 2798) (Line 27 above)		
5301.			
5302.			
5303.			
5398.	Summary of remaining write-ins for Line 53 from overflow page		
5399.	Totals (Lines 5301 through 5303 plus 5398) (Line 53 above)		

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

CASH FLOW

		1 Current Year	2 Prior Year
	Cash from Operations		
1.	Premiums and annuity considerations for life and accident and health policies and contracts	25,000	
2.	Charges and fees for deposit-type contracts		
3.	Considerations for supplementary contracts with life contingencies		
4.	Net investment income		
5.	Commissions and expense allowances on reinsurance ceded		
6.	Fees associated with investment management, administration and contract guarantees from Separate Accounts	100	
7.	Aggregate write-ins for miscellaneous income		
8.	Total (Lines 1 to 7)	25,100	
9.	Death benefits		
10.	Matured endowments		
11.	Annuity benefits		
12.	Disability benefits and benefits under accident and health policies		
13.	Coupons, guaranteed annual pure endowments and similar benefits		
14.	Surrender benefits and withdrawals for life contracts	100,000	
15.	Group conversions		
16.	Interest and adjustments on policy or deposit-type contract funds		
17.	Payments on supplementary contracts with life contingencies		
18.	Total (Lines 9 to 17)	100,000	
19.	Commissions on premiums, annuity considerations and deposit-type contract funds		
20.	Commissions and expense allowances on reinsurance assumed		
21.	General insurance expenses		
22.	Insurance taxes, licenses and fees, excluding federal income taxes		
23.	Net transfers to or (from) Separate Accounts	25,000	
24.	Aggregate write-ins for deductions		
25.	Total (Lines 18 to 24)	125,000	
26.	Dividends paid to policyholders		
27.	Federal income taxes (excluding tax on capital gains)		
28.	Total (Lines 25 to 27)	125,000	
29.	Net cash from operations (Line 8 minus Line 28)	(99,900)	
	Cash from Investments		
30.	Proceeds from investments sold, matured or repaid:		
	30.1 Bonds		
	30.2 Stocks		
	30.3 Mortgage loans		
	30.4 Real estate		
	30.5 Other invested assets		
	30.6 Net gains (losses) on cash and short-term investments		
	30.7 Miscellaneous proceeds		
	30.8 Total investment proceeds (Lines 30.1 to 30.7)		
31.	Net tax on capital gains (losses)		
32.	Total (Line 30.8 minus Line 31)		
33.	Cost of investments acquired (long-term only):		
	33.1 Bonds		
	33.2 Stocks		
	33.3 Mortgage loans		
	33.4 Real estate		
	33.5 Other invested assets		
	33.6 Miscellaneous applications		
	33.7 Total investments acquired (Lines 33.1 to 33.6)		
34.	Net increase (or decrease) in policy loans and premium notes		
35.	Net cash from investments (Line 32 minus Line 33.7 minus Line 34)		
	Cash from Financing and Miscellaneous Sources		
36.	Cash provided:		
	36.1 Surplus notes, capital and surplus paid in		
	36.2 Borrowed money $.......................less amounts repaid $		
	36.3 Capital notes $.............. less amounts repaid $...........		
	36.4 Deposits on deposit-type contract funds and other liabilities without life or disability contingencies	115,000	
	36.5 Other cash provided		
	36.6 Total (Lines 36.1 to 36.5)	115,000	
37.	Cash applied:		
	37.1 Dividends to stockholders paid		
	37.2 Interest on indebtedness		
	37.3 Withdrawals on deposit-type contract funds and other liabilities without life or disability contingencies	110,000	
	37.4 Other applications (net)		
	37.5 Total (Lines 37.1 to 37.4)	110,000	
38.	Net cash from financing and miscellaneous sources (Line 36.6 minus Line 37.5)	5,000	
	RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS		
39.	Net change in cash and short-term investments (Line 29, plus Line 35, plus Line 38)	(94,900)	
40.	Cash and short-term investments:		
	40.1 Beginning of year	100,000	
	40.2 End of year (Line 39 plus Line 40.1)	5,100	
	DETAILS OF WRITE-INS		
0701.			
0702.			
0703.			
0798.	Summary of remaining write-ins for Line 7 from overflow page		
0799.	Totals (Lines 0701 through 0703 plus 0798) (Line 7 above)		
2401.			
2402.			
2403.			
2498.	Summary of remaining write-ins for Line 24 from overflow page		
2499.	Totals (Lines 2401 through 2403 plus 2498) (Line 24 above)		

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

EXHIBIT 7—DEPOSIT TYPE CONTRACTS

	1 Total	2 Guaranteed Interest Contracts	3 Supplemental Contracts and Annuities Certain	4 Dividend Accumulations or Refunds	5 Premium and Other Deposit Funds	6 Other
1. Balance at the beginning of the year	15,000	15,000	....	....	....	....
2. Deposits received during the year	110,000	....	110,000	....	....	....
3. Investment earnings credited to the account	2,000	....	2,000	....	....	....
4. Other net change in reserves	(4,000)	....	(4,000)	....	....	....
5. Fees and other charges assessed	100	....	100	....	....	....
6. Surrender charges	....	....	....	....	....	....
7. Net surrender or withdrawal payments	41,000	15,000	26,000	....	....	....
8. Other net transfers to or (from) General Accounts	....	....	....	....	....	....
9. Balance at the end of current year(Lines 1+2+3+4-5-6-7-8)	81,900	0	81,900			

Reconciliation of Exh. 7 to Summary of Operations:

Exh. 7, Column 1, Line 9	81,900
Exh. 7, Column 1, Line 1	15,000
Summary of Operations, Column 1, Line 14	66,900

Exh. 7, Column 1, Line 2	110,000
Exh. 7, Column 1, Line 7	41,000
Summary of Operations, Column 1, Line 2	69,000

Note: This illustration reflects 2001 financial statements and will not be subsequently updated.

EXHIBIT 10—DEPOSIT TYPE CONTRACTS

	1 Total	2 Guaranteed Interest Contracts	3 Supplemental Contracts and Annuities Certain	4 Dividend Accumulations or Refunds	5 Premium and Other Deposit Funds	6 Other
1. Balance at the beginning of the year before reinsurance	....	....	....	....	....	....
2. Deposits received during the year	115,000	....	115,000	....	....	....
3. Investment earnings credited to the account	....	....	....	....	....	....
4. Other net change in reserves	....	....	....	....	....	....
5. Fees and other charges assessed	....	....	....	....	....	....
6. Surrender charges	....	....	....	....	....	....
7. Net surrender or withdrawal payments	41,000	15,000	26,000	....	....	....
8. Other net transfers to or (from) Separate Accounts	69,000	(15,000)	84,000	....	....	....
9. Balance at the end of current year before reinsurance (Lines 1+2+3+4-5-6-7-8)	5,000	0	5,000	....	....	....
10. Reinsurance balance at the beginning of the year	....	....	....	....	....	....
11. Net change in reinsurance assumed	....	....	....	....	....	....
12. Net change in reinsurance ceded	....	....	....	....	....	....
13. Reinsurance balance at the end of the year (Lines 10+11-12)	....	....	....	....	....	....
14. Net balance at the end of current year after reinsurance (Lines 9-13)						

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-20: Application of SEC SAB No. 99, Materiality to the Preamble of the AP&P Manual

INT 00-20 Dates Discussed

June 12, 2000; September 20, 2000; June 11, 2001; October 16, 2001

INT 00-20 References

Current:
Preamble to the NAIC *Accounting Practices and Procedures Manual* (Preamble)

INT 00-20 Issue

1. In summary, SEC Staff Accounting Bulletin No. 99, *Materiality* (SAB No. 99) addresses two issues; 1) may a company or auditor assume the immateriality of items that fall below a percentage threshold set by management or its auditors to determine whether amounts and items are material to the financial statements? and 2) may a company make intentional immaterial misstatements in its financial statements? The SEC staff answers each question as NO and gives numerous references to FASB guidelines to support their opinion.

2. The issue is whether the responses outlined in SAB No. 99 can be applied to statutory accounting and the concept of materiality as defined in paragraphs 48-53 of the Preamble.

INT 00-20 Discussion

3. At the 2000 Spring National Meeting, the Statutory Accounting Principles (E) Working Group (SAPWG) reviewed SAB No. 99 for incorporation into the *Accounting Practices and Procedures Manual* (AP&P Manual or Manual). The SAPWG determined that no modifications to the Preamble were warranted and referred the issue to the NAIC/AICPA Working Group for their consideration. The SAPWG felt the SAB had applicability to management of reporting entities, independent auditors and State Examiners. The NAIC/AICPA WG reviewed the SAB and determined that an interpretation of the Preamble was a more effective way to adopt the SAB for statutory accounting. The NAIC/AICPA WG felt that the AP&P Manual reached a larger audience than the A/S Instructions or Examiner's Handbook.

4. The Working Group reached a consensus to adopt an interpretation of the concept of materiality based on certain matters outlined in SAB No. 99. The Working Group believes the responses below provide additional support for the concepts delineated in Section VII of the Preamble. The SAB contains numerous references to SEC guidelines and GAAP pronouncements that are not reflected in this interpretation as such matters are not necessarily applicable or appropriate for statutory financial reporting. The interpretative responses (as modified by this interpretation) are as follows:

> **QUESTION:** Paragraph 53 of the Preamble states "The provisions of this Manual need not be applied to immaterial items." May a reporting entity's management, state examiner or independent auditor of the entity's financial statements assume the immateriality of items that fall below a percentage threshold set by management, state examiner or independent auditor to determine whether amounts and items are material to the financial statements?
>
> **INTERPRETIVE RESPONSE** No. Over time, the NAIC is aware that reporting entities have developed quantitative thresholds as "rules of thumb" to assist in the preparation of their financial statements, and that state examiners and independent auditors also have used these thresholds in

their evaluation of whether items might be considered material to users of a reporting entity's financial statements. One rule of thumb in particular suggests that the misstatement or omission of an item that falls under a 5% of surplus threshold is not material in the absence of particularly egregious circumstances, such as self-dealing or misappropriation by senior management. Exclusive reliance on this or any percentage or numerical threshold has no basis in the accounting literature or the law.

The use of a percentage as a numerical threshold, such as 5% of surplus, may provide the basis for a preliminary assumption that - without considering all relevant circumstances - a deviation of less than the specified percentage with respect to a particular item on the reporting entity's financial statements is unlikely to be material. The NAIC has no objection to such a "rule of thumb" as an initial step in assessing materiality. But quantifying, in percentage terms, the magnitude of a misstatement is only the beginning of an analysis of materiality; it cannot appropriately be used as a substitute for a full analysis of all relevant considerations. Materiality concerns the significance of an item to users of the reporting entity's financial statements. A matter is "material" if there is a substantial likelihood that a reasonable person would consider it important.

QUESTION: May a reporting entity make intentional immaterial misstatements in its financial statements?

INTERPRETIVE RESPONSE No. In certain circumstances, intentional immaterial misstatements are unlawful.

Each reporting entity must make and keep books, records, and accounts, that, in reasonable detail, accurately and fairly reflect the acquisitions and dispositions of assets of the reporting entity and must maintain internal control that is sufficient to provide reasonable, but not absolute, assurances that, among other things, transactions are recorded as necessary to permit the preparation of financial statements in conformity with the revised *Accounting Practices and Procedures Manual*. In this context, determinations of what constitutes "reasonable assurance" and "reasonable detail" are based not on a "materiality" analysis but on the level of detail and degree of assurance that would satisfy prudent individuals in the conduct of their own affairs. It is unlikely that it is ever "reasonable" for a reporting entity to record misstatements or not to correct known misstatements as part of an ongoing effort directed by or known to senior management for the purpose of "managing" reported results or financial position.

The National Commission on Fraudulent Financial Reporting, also known as the Treadway Commission, in its 1987 report:

> The tone set by top management - the corporate environment or culture within which financial reporting occurs - is the most important factor contributing to the integrity of the financial reporting process. Notwithstanding an impressive set of written rules and procedures, if the tone set by management is lax, fraudulent financial reporting is more likely to occur.

Statement on Auditing Standards No. ("SAS") 54, "Illegal Acts by Clients," and SAS No. 82, "Consideration of Fraud in a Financial Statement Audit" provide guidance to the independent auditor. Pursuant to paragraph 38 of SAS 82, if the independent auditor determines there is evidence that fraud may exist, the independent auditor must discuss the matter with the appropriate level of management. The auditor must report directly to the audit committee fraud involving senior management and fraud that causes a material misstatement of the financial statements. Paragraph 4 of SAS No. 82 states that "misstatements arising from fraudulent financial reporting are intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users." SAS No. 82 further states that fraudulent financial reporting may involve falsification or alteration of accounting records; misrepresenting or omitting events, transactions or other information in the financial statements; and the intentional misapplication of accounting principles relating to amounts, classifications, the manner of presentation, or disclosures in the financial statements. The clear implication of SAS No. 82 is that immaterial misstatements may be fraudulent financial reporting.

Independent auditors that learn of intentional misstatements may also be required to (1) re-evaluate the degree of audit risk involved in the audit engagement, (2) determine whether to revise the nature, timing, and extent of audit procedures accordingly, and (3) consider whether to resign.

Intentional misstatements also may signal the existence of reportable conditions or material weaknesses in the reporting entity's system of internal accounting control designed to detect and deter improper accounting and financial reporting.

An auditor is required to report to the audit committee any reportable conditions or material weaknesses in a reporting entity's system of internal accounting control that the auditor discovers in the course of the examination of the registrant's financial statements.

INT 00-20 Status

5. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-24: EITF 98-13: Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of the Investee and EITF 99-10: Percentage Used to Determine the Amount of Equity Method Losses

INT 00-24 Dates Discussed

June 12, 2000; September 11, 2000

INT 00-24 References

Current:
SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities

Superseded:
SSAP No. 46—Investments in Subsidiary, Controlled, and Affiliated Entities
SSAP No. 88—Investments in Subsidiary, Controlled and Affiliated Entities, A Replacement of SSAP No. 46

INT 00-24 Issue

1. EITF 98-13 and Topic No. D-68, *Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of an Investee* (EITF 98-13 or Topic D-68) provides the FASB staff position that Accounting Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock* (APB No. 18) requires an investor that owns common (or other voting) stock and also (a) owns debt securities (including mandatorily redeemable preferred stock), (b) owns preferred stock, or (c) has extended loans to the investee to continue to report losses. Paragraph 13 of FASB Statement 114, *Accounting by Creditors for Impairment of a Loan* (FAS 114) as amended by FASB Statement 118, *Accounting by Creditors for Impairment of a Loan—Income Recognition and Disclosures* (FAS 118) provides that when a loan is impaired, a creditor shall measure impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate. Paragraph 12 of FASB Statement 115, *Accounting for Certain Investments in Debt and Equity Securities* (FAS 115) provides that investments in both debt securities not held to maturity and equity securities that have readily determinable fair values shall be carried at fair value.

2. EITF 99-10, *Accounting by an Equity Method Investor for Investee Losses When the Investor Has Loans to and Investments in Other Securities of an Investee* (EITF 99-10) and Topic No. D-68 provides the FASB staff position on an investor's accounting when more than one type of interest is held. Specifically, the FASB staff announced that APB No. 18 requires that when an investor owns common stock and also (a) owns debt securities (including mandatorily redeemable preferred stock), (b) owns preferred stock, or (c) has extended loans to the investee (collectively referred to as "other investments"), the equity method investor should continue to report losses up to the investor's investment carrying value, including any additional financial support made or committed to by the investor. EITF 98-13 provides guidance on the interaction between the applicable literature for those instruments and APB No. 18 for situations in which an investee is incurring losses and (a) an investor is not required to advance additional funds to the investee and (b) previous losses have reduced the common stock investment account to zero. However, neither Topic D-68 nor EITF 98-13 provides guidance on how an investor should calculate the amount of equity method losses or subsequent income in that circumstance.

3. The issue is, when an investor is required to account for a common stock investment using the equity method, how the equity method loss pickup from the application of APB No. 18 (when the

carrying amount of the common stock has been reduced to zero) interacts with the applicable literature relating to investments in the other securities of the investee (either FAS 114 or FAS 115), and if an investor owns common stock and "other investments" in an investee and is not required to advance additional funds to the investee and if previous losses have reduced the common stock investment account to zero, how additional equity method losses should be measured and recognized by the investor.

INT 00-24 Discussion

4. The Working Group reached a consensus to adopt the final conclusions reached in EITF 98-13 and 99-10 with modification as follows:

5. The EITF reached a consensus that in situations where (a) an investor is not required to advance additional funds to the investee and (b) previous losses have reduced the common stock investment account to zero, the investor should continue to report its share of equity method losses in its statement of operations to the extent of and as an adjustment to the adjusted basis of the other investments in the investee. The order in which those equity method losses should be applied to the other investments should follow the seniority of the other investments (that is, priority in liquidation). For each period, the adjusted basis of the other investments should be adjusted for the equity method losses, then the investor should apply SSAP No. 97 to the other investments, as applicable.

6. For purposes of this consensus, other investments in the investee include, but are not limited to, preferred stock, debt securities, and loans to the investee (collectively referred to as loans and securities). The cost basis of the other investments is the original cost of those investments adjusted for the effects of other-than-temporary write-downs, unrealized gains and losses, and amortization of any discount or premium on debt securities or loans. The adjusted basis is the cost basis adjusted for the valuation allowance account for an investee loan and the cumulative equity method losses applied to the other investments. Equity method income subsequently recorded should be applied to the adjusted basis of the other investments in reverse order of the application of the equity method losses (that is, equity method income is applied to the more senior securities first).

7. When the investor has loans and securities of the investee that are within the scopes of SSAP No. 97, the investor should perform the following in order to determine the amount of equity method loss to report at the end of a period:

a. Apply SSAP No. 97 to determine the maximum amount of equity method losses.

b. Determine whether the adjusted basis of the other investment(s) in the investee is positive.

i. When the adjusted basis is positive, the adjusted basis of the other investments should be adjusted for the amount of the equity method loss based on its seniority. For investments accounted for in accordance with *SSAP No. 30~~R~~—Unaffiliated Common Stock*, this adjusted basis becomes the security's basis from which subsequent changes in fair value are measured.

ii. When the adjusted basis reaches zero, equity method losses should cease being reported; however, the investor should continue to track the amount of unreported equity method losses for purposes of applying SSAP No. 97. (If one of the other investments is sold at a time when its carrying value exceeds its adjusted basis, the difference between the cost basis of that other investment and its adjusted basis at the time of sale represents equity method losses that were originally applied to that other investment but effectively reversed upon its sale. Accordingly, that excess represents unreported equity method losses that should continue to be tracked before future equity method income can be reported.

c. After applying SSAP No. 97, apply SSAP No. 30 to the adjusted basis of the other investments in the investee, as applicable. Apply appropriate statutory accounting principles to other investments that are not within the scope of SSAP No. 30.

8. The EITF reached a consensus that an investor should not recognize equity method losses based solely on the percentage of investee common stock held by the investor.

9. The EITF observed that an entity should utilize a single entity-wide approach to determine the amount of its equity method losses when previous losses have reduced the common stock investment account to zero and that the selected policy should be disclosed in the footnotes to the financial statements.

10. The provisions of these consensuses are effective for interim or annual periods beginning after January 1, 2001.

11. Refer to Exhibit 00-24A for an example that illustrates application of these consensuses.

INT 00-24 Status

12. No further discussion is planned.

Exhibit 00-24A
ILLUSTRATION OF THE APPLICATION OF THE INT 00-24 CONSENSUS'S

XYZ Investment in ABC Company

1. ABC Company is a life insurance company, formed January 2, 20X1 to sell health insurance in the state of New York. On January 2, 20X1, XYZ Insurance Company invested $500,000 in ABC, and purchased 100,000 shares of common stock at par, and 40,000 shares of preferred stock at par. ABC Preferred stock is non-voting, 5% cumulative.

2. XYZ determined it has obtained a controlling interest in ABC as XYZ owns 50% of the voting interests of ABC. XYZ accounted for its investment in ABC Insurance Company under the statutory equity method of accounting. The following table is selected information from the financial statements of ABC Insurance Company.

	1/2/20X1	12/31/20X1	12/31/20X2	12/31/20X3	12/31/20X4
Capital and Surplus:					
Common stock, $1 par, 200,000 shares issued and outstanding	$ 200,000	$ 200,000	$ 200,000	$ 200,000	$ 200,000
Preferred stock, $10 par, 100,000 shares issued and outstanding	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Surplus Notes			$ 500,000	$ 500,000	$ 500,000
Unassigned Funds (Surplus)		$ 130,000	($ 180,000)	($ 630,000)	($1,430,000)
Total Capital and Surplus	$1,200,000	$1,330,000	$1,520,000	$ 1,070,000	$ 270,000

	12/31/20X5	12/31/20X6	12/31/20X7	12/31/20X8	12/31/20X9
Capital and Surplus:					
Common stock, $1 par, 200,000 shares issued and outstanding	$ 200,000	$ 200,000	$ 200,000	$ 200,000	$ 200,000
Preferred stock, $10 par, 100,000 shares issued and outstanding	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Surplus Notes	$ 500,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Unassigned Funds (Surplus)	($1,980,000)	($1,830,000)	($1,280,000)	($ 430,000)	$ 820,000
Total Capital and Surplus	($280,000)	$ 370,000	$ 920,000	$1,770,000	$3,020,000

3. At 1/2/20X1, XYZ recorded the following entry to record its investment in ABC:

Investment in ABC Common stock	$ 100,000	
Investment in ABC Preferred stock	$ 400,000	
Cash		$ 500,000

To record initial investment in ABC Insurance Company.

4. During the year ended 12/31/20X1, ABC had statutory net income before dividends of $200,000. At 12/31/20X1, ABC declared and paid a 5% preferred dividend, and a common stock dividend of $.10 per share. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X1.

Investment in ABC Common stock	$ 75,000	
Unrealized Gain/Loss		$ 75,000

To record 20X1 unrealized gain on investment in ABC Common. (($200,000 - $50,000) * 50%)

Cash	$ 10,000	
Unrealized Gain/Loss	$ 10,000	
Dividend Income		$ 10,000
Investment in ABC Common stock		$ 10,000

To record 20X1 dividend on ABC Common. (100,000 shares * $.10)

5. During the year ended 12/31/20X2, ABC issued an 8% surplus note of $500,000. XYZ purchased 100% of the surplus note. During that same year, ABC incurred a statutory net loss before dividends of $250,000. At 12/31/20X2, ABC declared and paid a 5% preferred dividend, and a common stock dividend of $.05 per share. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Investment in ABC Surplus Notes	$ 500,000	
Cash		$ 500,000

To record investment in ABC Insurance Company surplus notes.

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X2.

Unrealized Gain/Loss	$ 150,000	
Investment in ABC Common stock		$ 150,000

To record 20X2 unrealized loss on investment in ABC Common. (($-250,000 - $50,000) * 50%)

Cash	$ 5,000	
Unrealized Gain/Loss	$ 5,000	
Dividend Income		$ 5,000
Investment in ABC Common stock		$ 5,000

To record 20X2 dividend on ABC Common. (100,000 shares * $.05)

6. During the year ended 12/31/20X3, ABC Insurance Company incurred a statutory net loss before dividends of $400,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X3.

Unrealized Gain/Loss	$ 182,000	
Investment in ABC Preferred stock		$ 172,000
Investment in ABC Common stock		$ 10,000

To record 20X3 unrealized loss on investment in ABC Common and Preferred.

Total net loss and preferred stock dividend ($450,000).
Common stock component reduces the Investment in ABC Common stock component to $0. (20,000 * 50%)

Total net loss and preferred dividend (-$400,000 - $50,000)	$450,000
Less amount used to reduce common stock investment to $0	20,000
Amount remaining to be allocated to investment in preferred	430,000
XYZ ownership % of preferred	40%
XYZ reduction in investment in preferred	$172,000

7. During the year ended 12/31/20X4, ABC Insurance Company incurred a statutory net loss before dividends of $750,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X4.

Unrealized Gain/Loss	$ 458,000	
Investment in ABC Preferred stock		$ 228,000
Investment in ABC Surplus note		$ 230,000

To record 20X4 unrealized loss on investment in ABC Preferred and Surplus Notes.

Total net loss and preferred stock dividend ($800,000).
Common stock component reduces the Investment in ABC Preferred stock component to $0. (570,000 * 40%)
Preferred stock component calculated as:

Total net loss and preferred dividend (-$750,000 - $50,000)	$800,000
Less amount used to reduce preferred stock investment to $0	570,000
Amount remaining to be allocated to investment in surplus note	230,000
XYZ ownership % of surplus note	100%
XYZ reduction in investment in ABC Surplus Notes	$230,000

8. During the year ended 12/31/20X5, ABC Insurance Company incurred a statutory net loss before dividends of $500,000. ABC Insurance Company did not declare any dividends, and no interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Dividends Receivable	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X5.

Unrealized Gain/Loss	$ 270,000	
Investment in ABC Surplus note		$ 270,000

To record 20X5 unrealized loss on investment in ABC Surplus Notes.

Total ABC net loss and preferred stock dividend (-$500,000 - $50,000).
Surplus Note component calculated as:

Total net loss and preferred dividend (-$500,000 - $50,000)	$550,000
XYZ ownership % of ABC Surplus Note	100%
	$550,000
Amount of unrealized loss recognized in 20X5	$270,000
Amount of unrealized loss suspended	$280,000

9. Since XYZ has not guaranteed any liabilities of ABC, the reduction they would recognize is limited to their remaining investment in ABC Surplus Notes. Therefore, they would only recognize a 20X5 unrealized loss on their investment in ABC of $270,000.

10. During the year ended 12/31/20X6, ABC Insurance Company realigned their marketing efforts and modified the products they were selling. ABC also issued an additional 8% surplus note of $500,000. This surplus note was purchased by an unaffiliated third party. During the year ended 12/31/X6, ABC Insurance Company had statutory net income before dividends of $200,000. ABC Insurance Company did not declare any dividends on common stock, but declared and paid current and dividends in arrears on preferred. XYZ recorded the following entries:

Cash	$ 80,000	
Dividends Receivable		$ 60,000
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X6, and receipt of preferred dividends receivable for 20X3, 20X4 and 20X5.

11. XYZ did not record any change in their investment in ABC Surplus Notes, ABC Preferred or ABC Common, since ABCs' net income after preferred dividends did not exceed the losses accumulated during the period that XYZ suspended recording unrealized losses.

12. The following amounts were tracked:

Total ABC net income and preferred stock dividend ($200,000 - $50,000).
Surplus Note component calculated as:

Total net income and preferred dividend ($200,000 - $50,000)	$150,000
XYZ ownership % of ABC Surplus Note	50%
Amount of unrealized loss suspended in 20X5	$ 75,000
Remaining amount of unrealized loss suspended	$280,000
	$205,000

13. During the year ended 12/31/20X7, ABC Insurance Company had statutory net income before dividends of $600,000. At 12/31/20X7, ABC declared and paid a 5% preferred dividend. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X7.

Investment in ABC Surplus Notes	$ 70,000	
Unrealized Gain/Loss		$ 70,000

To record 20X7 unrealized gain on investment in ABC Surplus Notes.

Total ABC net income and preferred stock dividend ($600,000 - $50,000).
Surplus Note component calculated as:

Total net income and preferred dividend ($600,000 - $50,000)	$550,000
XYZ ownership % of ABC Surplus Note	50%
	$275,000
Remaining amount of unrealized loss suspended in 20X5	$205,000
20X7 amount of unrealized gain on investment in ABC Surplus Note	$ 70,000

14. During the year ended 12/31/20X8, ABC Insurance Company had statutory net income before dividends of $900,000. At 12/31/20X8, ABC declared and paid a 5% preferred dividend. No interest or principal repayments of the surplus note were approved. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X8.

Total ABC net income and preferred stock dividend ($900,000 - $50,000).
Surplus Note component calculated as:

Total net income and preferred dividend ($900,000 - $50,000)	$850,000
XYZ ownership % of ABC Surplus Note	50%
20X8 amount of unrealized gain on investment in ABC Surplus Note	$425,000

Investment in ABC Surplus Notes	$ 425,000	
Unrealized Gain/Loss		$ 425,000

To record 20X8unrealized gain on investment in ABC Surplus Notes.

15. During the year ended 12/31/20X9, ABC Insurance Company had statutory net income, before interest on surplus notes and dividends, of $1,400,000. The Commissioner approved one year's interest payment on the surplus notes. At 12/31/20X9, ABC declared and paid a 5% preferred dividend, and a $.10 dividend per share on Common stock. XYZ recorded the following entries:

Cash	$ 20,000	
Dividend Income		$ 20,000

To record preferred dividend income from ABC Insurance Company for 20X9.

Cash	$ 40,000	
Interest Income		$ 40,000

To record surplus notes interest income from ABC Insurance Company for 20X9. ($500,000 * 8%)

Investment in ABC Surplus Notes	$ 5,000	
Investment in ABC Preferred Stock	$ 400,000	
Investment in ABC Common Stock	$ 130,000	
Unrealized Gain/Loss		$ 535,000

To record 20X9 unrealized gain on investment in ABC Common, Preferred and Surplus Notes.

Components computed as follows:

Total Net Income net of preferred stock dividend and interest on surplus notes ($1,400,000 - $50,000 - $80,000)	$ 1,270,000
Less amount needed to restore investment in surplus notes	($ 10,000)
Amount available for preferred stock and common stock investment restoration	$ 1,260,000
Amount needed to restore preferred stock component	($ 1,000,000)
Amount available to restore common stock component	$ 260,000

Surplus Notes component ($10,000 * 50%)	$ 5,000
Preferred Stock component ($1,000,000 * 40%)	$ 400,000
Common stock component ($260,000 * 50%)	$ 130,000

Cash	$ 10,000	
Unrealized Gain/Loss	$ 10,000	
Dividend Income		$ 10,000
Investment in ABC Common stock		$ 10,000

To record 20X9 dividend on ABC Common. (100,000 shares * $.10)

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-26: EITF 98-3: Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business

INT 00-26 Dates Discussed

June 12, 2000; September 11, 2000; March 5, 2006; June 11, 2006; December 10, 2006; March 10, 2007

INT 00-26 References

Current:
SSAP No. 95—Nonmonetary Transactions

Superseded:
SSAP No. 28—Nonmonetary Transactions

INT 00-26 Issue

1. The basic principle contained in APB Opinion No. 29, *Accounting for Nonmonetary Transactions* (APB No. 29) is that an exchange of nonmonetary assets should be recorded at fair value. Certain modifications to that basic principle are contained in paragraphs 20-23 of APB No. 29. Paragraph 21.b. provides that accounting for an exchange of productive assets for similar productive assets should be based on the recorded amount of the nonmonetary assets relinquished. Paragraph 4 of APB No. 29 states that Opinion is not applicable to business combinations.

2. APB Opinion No. 16, *Business Combinations* (APB No. 16) provides accounting guidance for business combinations. Paragraph 1 of APB No. 16 states that "a business combination occurs when a corporation and one or more incorporated or unincorporated businesses are brought together into one accounting entity. The single entity carries on the activities of the previously separate, independent enterprises."

3. It is not clear whether exchanges of certain types of assets, for example, radio stations, cable systems, and hotels, are considered exchanges of productive assets or business combinations.

4. The issues are whether the exchange of assets or groups of assets involving the receipt of a consolidated business can be considered an exchange of similar productive assets accounted for at historical cost pursuant to paragraph 21 of APB No. 29 and how a "business" should be defined.

5. In December of 2004, the Financial Accounting Standards Board (FASB) issued *FAS 153: Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29* (FAS 153), which addresses the measurement of exchanges of nonmonetary assets. It eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21.b. of APB No. 29, and replaces it with an exception for exchanges that do not have commercial substance. This statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. While the guidance referred to above has been amended, the statutory accounting guidance included in the following discussion is not impacted and remains in effect.

INT 00-26 Discussion

6. The Working Group reached a consensus to update the description of the issue by adding an explanatory paragraph 5, which discusses amendments to APB No. 29 resulting from FAS 153.

7. The Working Group reached a consensus to adopt the conclusions reached in EITF 98-3 with modification. APB No. 29 is adopted with SSAP No. 95. Although APB No. 16 is rejected in SSAP No. 68, the issues raised in EITF 98-3 are applicable to statutory accounting and SSAP No. 95. The modified conclusions of EITF 98-3 are outlined in paragraphs 8-15.

8. The EITF reached a consensus that the guidance below should be used to evaluate whether a business has been received in a nonmonetary exchange transaction.

9. A business is a self-sustaining integrated set of activities and assets conducted and managed for the purpose of providing a return to investors. A business consists of (a) inputs, (b) processes applied to those inputs, and (c) resulting outputs that are used to generate revenues. For a transferred set of activities and assets to be a business, it must contain all of the inputs and processes necessary for it to continue to conduct normal operations after the transferred set is separated from the transferor, which includes the ability to sustain a revenue stream by providing its outputs to customers.

10. The elements necessary for a transferred set to continue to conduct normal operations will vary by industry and by the operating strategies of the transferred set. An evaluation of the necessary elements should consider:

<u>Inputs</u>

a. Long-lived assets, including intangible assets, or rights to the use of long-lived assets.
b. Intellectual property.
c. The ability to obtain access to necessary materials or rights.
d. Employees.

<u>Processes</u>

e. The existence of systems, standards, protocols, conventions, and rules that act to define the processes necessary for normal, self-sustaining operations, such as (i) strategic management processes, (ii) operational processes, and (iii) resource management processes.

<u>Outputs</u>

f. The ability to obtain access to the customers that purchase the outputs of the transferred set.

11. A transferred set of activities and assets fails the definition of a business if it excludes one or more of the above items such that it is not possible for the set to continue normal operations and sustain a revenue stream by providing its products and/or services to customers. However, if the excluded item or items are only minor (based on the degree of difficulty and the level of investment necessary to obtain access to or to acquire the missing item(s)), then the transferred set is capable of continuing normal operations and is a business. The assessment of whether excluded items are only minor should be made without regard to the attributes of the transferee and should consider such factors as the uniqueness or scarcity of the missing element, the time frame, the level of effort, and the cost required to obtain the missing element. If goodwill is present in a transferred set of activities and assets, it should be presumed that the excluded items are minor and that the transferred set is a business.

12. The assessment of whether a transferred set is a business should be made without regard to how the transferee intends to use the transferred set. In other words, it is not relevant to the evaluation of whether the transferred set is a business whether the transferee will actually operate the set on a stand-alone basis or intends to continue using the transferred set in the same manner as the transferor.

13. If all but a de minimis amount of the fair value of the transferred set of activities and assets is represented by a single tangible or identifiable intangible asset, the concentration of value in the single asset is an indicator that an asset rather than a business is being received.

14. The level of working capital or the adequacy of financing necessary to conduct normal operations in the transferred set is not an indicator either way as to whether the set meets the definition of a business. Likewise, if the planned principal operations of the transferred set have commenced, the presence and/or expectation of continued operating losses while the set seeks to achieve the level of market share necessary to attain profitability is not an indicator of whether or not the set is a business. However, if the transferred set is in the development stage and has not commenced planned principal operations, the set is presumed not to be a business.

15. The determination of whether a transferred set of assets and activities is or is not a business is a three-step process. First, one must identify the elements included in the transferred set. Second, one must compare the identified elements in the transferred set to the complete set of elements necessary for the transferred set to conduct normal operations in order to identify any missing elements. Third, if there are missing elements, one must make an assessment as to whether the missing elements cause one to conclude that the transferred set is not a business. That assessment is based on the degree of difficulty or the level of investment (relative to the fair value of the transferred set) necessary to obtain access to or to acquire the missing elements. If the degree of difficulty and level of investment necessary to obtain access to or to acquire the missing elements are not significant, then the missing elements are considered minor and their absence would not cause one to conclude that the transferred set is not a business. The determination of the degree of difficulty or level of investment necessary to obtain access to or to acquire the missing elements requires significant judgment and is dependent on the particular facts and circumstances.

INT 00-26 Status

16. On March 10, 2007, the Working Group reached a consensus to remove SSAP No. 68 from the references section of this interpretation, as it should not be used to interpret SSAP No. 68. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 00-28: EITF 99-12: Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination

INT 00-28 Dates Discussed

June 12, 2000; September 11, 2000

INT 00-28 References

Current:
SSAP No. 68—Business Combinations and Goodwill

INT 00-28 Issue

1. APB No. 16, *Business Combinations* (APB No. 16) appears to include contradictory guidance about the date that should be used to value equity securities issued to effect a business combination accounted for using the purchase method. Paragraph 74 of APB No. 16 states that "the market price for a reasonable period before and after the date the terms of the acquisition are agreed to and announced should be considered in determining the fair value of securities issued." However, paragraph 94 of APB No. 16 refers to determining the cost of an acquired company as of the date of acquisition, which is defined in paragraph 93 as, "ordinarily . . . the date assets are received and other assets are given or securities are issued." This Issue addresses that apparent contradiction.

2. The interval between initiating and completing a business combination may involve an extended period of time. Although management of the companies involved may agree to and announce the terms of a business combination at the initiation date, internal or external contingencies, such as the need to obtain shareholder or regulatory approvals, may exist and prevent concurrent consummation of the combination. Because of the length of time that may be required to resolve those contingencies, the market price of the securities that are expected to be issued to effect a purchase business combination may fluctuate. As a result, the total cost of the acquired company assigned by the acquirer may vary significantly depending on the date that is used to value the securities that are issued.

3. The issues are:

   a. The date that should be used to value marketable equity securities of the acquirer issued to effect a business combination accounted for using the purchase method when the number of the acquirer's shares or amount of other consideration is not subject to change pursuant to the existing terms of the acquisition agreement

   b. The date that should be used as the measurement date to value equity securities of the acquirer issued in a purchase business combination if the number of the acquirer's shares or amount of other consideration to be issued could change pursuant to a formula in the initial acquisition agreement.

INT 00-28 Discussion

4. The Working Group reached a consensus to adopt the final conclusions reached in EITF 99-12, *Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination* (EITF 99-12) with modification. Although APB 16 is rejected in SSAP No. 68, the issues identified in EITF 99-12 are applicable to paragraph 3 of SSAP No. 68. The issue of cost is defined as:

> 3. The statutory purchase method of accounting is defined as accounting for a business combination as the acquisition of one entity by another. It shall be used for all purchases of SCA entities including partnerships, joint ventures, and limited liability companies. The acquiring reporting entity shall record its investment at cost. Cost is defined as the sum of: (a) any cash payment, (b) the fair value of other assets distributed, (c) the fair value of any liabilities assumed, and (d) any direct costs of the acquisition. Contingent consideration issued in a purchase business combination that is embedded in a security or that is in the form of a separate financial instrument shall be recorded by the issuer at fair value at the acquisition date.

5. As shown in subsection b of the excerpted paragraph above, SSAP No. 68 does not address the timing issues raised in EITF 99-12 of "other assets distributed".

6. The modifications to the conclusions reached in EITF 99-12 are as follows:

7. The EITF reached a consensus on Issue 1 that the value of the acquirer's marketable equity securities issued to effect a purchase business combination should be determined, pursuant to the guidance in paragraph 74 of APB No. 16, based on the market price of the securities over a reasonable period of time before and after the terms of the acquisition are agreed to and announced. In other words, the date of measurement of the value of the acquirer's marketable equity securities should not be influenced by the need to obtain shareholder or regulatory approvals. EITF members observed that the reasonable period of time referred to in paragraph 74 of APB No. 16 is intended to be very short, such as a few days before and after the acquisition is agreed to and announced. EITF members also observed that in transactions involving a hostile tender offer, the measurement date for the value of the acquirer's marketable equity securities occurs when the proposed transaction is announced and sufficient shares have been tendered to make the offer binding or when the proposed acquisition becomes nonhostile, as evidenced by the target company's agreement to the purchase price.

8. The EITF also reached a consensus that if the purchase price (the number of shares or the amount of other consideration) is subsequently changed as a result of further negotiations or a revised acquisition agreement, a new measurement date for valuing the acquirer's marketable equity securities that will be issued to effect the combination is established as of the date of the change. The Working Group clarified that if the change in the number of shares or other consideration is not substantive, a new measurement date does not result from the change.

9. The EITF addressed the accounting for contingent consideration issued to effect a purchase business combination in Issue No. 97-8, *Accounting for Contingent Consideration Issued in a Purchase Business Combination* (EITF 97-8). The measurement guidance in this Issue is to be applied to the acquirer's equity securities issued to effect a business combination accounted for using the purchase method, including those instruments that meet the criteria in EITF 97-8 for recording as part of the cost of the business acquired. (EITF 97-8 was adopted by the Working Group in SSAP No. 68.)

10. The EITF reached a consensus on Issue 2 that if the application of the formula results in a change to the number of shares or the amount of other consideration to be issued in the purchase business combination, then the first date on which the number of acquirer shares and the amount of other consideration become fixed without subsequent revision is the measurement date. That is, the measurement date is the earliest date, from the date the terms of the acquisition are agreed to and announced to the date of final application of the formula pursuant to the acquisition agreement, on which subsequent applications of the formula do not result in a change in the number of shares or the amount of other consideration. For example, assume the terms of a purchase business combination are agreed to and announced on March 1, 1999. Also assume that the purchase agreement includes a formula arrangement that specifies that an adjustment will be made to the number of shares issued in the business combination if the average closing security price for the 10 days ending June 30, 1999, is less than $16. If the 10-day average closing security price drops below $16 for the first time on June 1, 1999, and does not subsequently recover to an amount equal to or greater than $16 from June 1, 1999 through June 30, 1999, June 1, 1999 is the measurement date. However, if the originally announced number of shares or amount

of other consideration does not change as a result of final application of the formula, then the initial date that the terms were agreed to and announced is the measurement date. The EITF noted that a new measurement date does not occur as a result of the application of a nonsubstantive formula in the original agreement.

11. As another example, assume that the terms of the acquisition are agreed to and announced on March 31, 1999. The number of shares to be issued in the business combination is equal to $20 million divided by the June 30, 1999 closing market price of the acquirer's common stock; however, if the June 30, 1999 closing market price of the acquirer’s common stock is less than $16 or greater than $24, the exchange ratio is adjusted as follows: (a) if the closing market price is less than $16, the acquirer will issue 1,250,000 shares of its common stock for the outstanding common shares of the target company, and (b) if the closing market price is greater than $24, the acquirer will issue 833,000 shares of its common stock for the outstanding common shares of the target company. The variable exchange ratio represents a formula and, as a result, if the stock price changes during the period from March 31, 1999 through June 30, 1999, but remains within the $16-$24 range, the measurement date is June 30, 1999. However, if the acquirer’s closing common stock price exceeds $24 on June 1, 1999, and remains above $24 through June 30, 1999, the number of shares to be issued in the transaction becomes fixed on June 1, 1999, and that date is the measurement date.

12. The EITF also reached a consensus that the securities should be valued based on market prices a few days before and after the measurement date determined in Issue 2 but that the measurement period would not include any dates after the date the business combination is consummated.

13. The EITF reached a consensus that the consensus reached on Issue 1 should only be applied prospectively to purchase business combinations consummated on or after January 1, 2001. The EITF reached a consensus that the consensuses reached on Issue 2 should be applied prospectively to purchase business combinations initiated on or after January 1, 2001. An entity should apply its existing policy prior to the effective date of the consensus on Issue 2.

INT 00-28 Status

14. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 01-18: Consolidated or Legal Entity Level – Limitations on EDP Equipment, Goodwill and Deferred Tax Assets Admissibility

INT 01-18 Dates Discussed

March 26, 2001; June 11, 2001

INT 01-18 References

Current:
SSAP No. 16—Electronic Data Processing Equipment and Software
SSAP No. 19—Furniture, Fixtures, Equipment and Leasehold Improvements
SSAP No. 68—Business Combinations and Goodwill
SSAP No. 101—Income Taxes

Superseded:
SSAP No. 79—Depreciation of Nonoperating System Software – An Amendment to SSAP No. 16—Electronic Data Processing Equipment and Software
SSAP No. 10R—Income Taxes—A Temporary Replacement of SSAP No. 10

INT 01-18 Issue

1. Case Number 1: The reporting entity has several wholly-owned insurance company subsidiaries. The reporting entity will account for its investment in these subsidiaries at their underlying statutory equity in accordance with *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*.

2. Case Number 2: A reporting entity has deferred tax assets (DTAs) in excess of those that are allowed to be admitted in accordance with the guidance in SSAP No. 101 paragraph 11. The reporting entity files a consolidated tax return with one or more affiliates. Those affiliates have deferred tax liabilities (DTLs) that exceed the remaining DTAs available for admission after application of paragraphs 11.a. and 11.b. of SSAP No. 101 at the affiliates' legal entity level.

3. The accounting issues are:

Case Number 1:

When applying the limitations described in paragraph 11 of SSAP No. 101, paragraph 4 of SSAP No. 16, and paragraph 7 of SSAP No. 68 to the parent reporting entity's adjusted capital and surplus, is the reporting entity required to exclude any net deferred tax assets, EDP equipment and operating system software, and net positive goodwill included in its insurance subsidiaries' valuation? Or, is the limitation calculated solely based on the legal entity's adjusted capital and surplus?

The effect of looking solely at the legal entity is to allow for the "stacking" of intangibles, so that the parent reporting entity may effectively have more than the defined limitations "invested" in deferred tax assets, EDP equipment and operating system software and goodwill. These assets are limited at each subsidiary legal entity level.

Case Number 2:

Can the reporting entity offset its DTAs against existing gross DTLs of an affiliated entity? This offset would be pursuant to the allowance of an offset against existing DTLs under SSAP No. 101

paragraph 11.c. This offset would occur only after application of paragraphs 11.a. and 11.b. for both the reporting entity and the affiliate. The premise for the offset is that both entities file a consolidated federal income tax return and that future deductible items of the reporting entity are, by current tax law, able to offset future income items of the affiliate. The affiliates for this purpose would have to have a tax sharing agreement that required payment from one affiliate to another for loss usage.

INT 01-18 Discussion

4. The Working Group reached a consensus as follows:

Case Number 1:

The Working Group reached a consensus that in applying the limitations described in paragraph 11.b.ii. of SSAP No. 101, paragraph 4 of SSAP No. 16, and paragraph 7 of SSAP No. 68 to the parent reporting entity's adjusted capital and surplus, the reporting entity shall not exclude any net deferred tax assets, EDP equipment, operating system software, and net positive goodwill included in its insurance subsidiaries valuation.

Case Number 2:

The Working Group reached a consensus that the reporting entity shall not offset it's DTAs against existing gross DTLs of an affiliated entity.

INT 01-18 Status

5. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 01-25: Accounting for U.S. Treasury Inflation-Indexed Securities

INT 01-25 Dates Discussed

June 11, 2001; October 16, 2001; September 10, 2002; December 8, 2002; December 10, 2016; April 8, 2017

INT 01-25 References

Current:
SSAP No. 26—Bonds

INT 01-25 Issue

1. Treasury inflation-indexed securities are direct obligations of the United States government, and are backed by the full faith and credit of the government.[1] The principal is protected against inflation. Since the principal is indexed to the Consumer Price Index and grows with inflation, the investor is guaranteed that the real purchasing power of the principal will keep pace with the rate of inflation (Based on the Reference CPI-U, which has a three-month lag). Although deflation could cause the principal to decline, Treasury will pay at maturity an amount that is no less than the par amount as of the date the security was first issued.

2. Interest is also protected from inflation. The investor will receive semiannual interest payments, based on a fixed semiannual interest rate applied to the inflation-adjusted principal, so that the investor is guaranteed a real rate of return above inflation.

> Summary of the Structure and Index:
>
> Principal amount. The principal amount of Treasury inflation-indexed securities will be adjusted for changes in the level of inflation. The inflation-adjusted principal amount of the securities can be calculated daily. However, the inflation adjustment will not be payable by Treasury until maturity, when the securities will be redeemed at the greater of their inflation-adjusted principal amount or the principal amount of the securities on the date of original issuance (i.e., par).
>
> Index. The index for measuring the inflation rate will be the nonseasonally adjusted CPI-U (U.S. City Average All Items Consumer Price Index for All Urban Consumers). CPI-U was selected by Treasury because it is the best known and most widely accepted measure of inflation.
>
> Interest payments. Every six months Treasury will pay interest based on a fixed rate of interest determined at auction. Semiannual interest payments are determined by multiplying the inflation-adjusted principal amount by one-half the stated rate of interest on each interest payment date.
>
> Payment at maturity. If at maturity the inflation-adjusted principal is less than the par amount of the security (due to deflation), the final payment of principal of the security by Treasury will not be less than the par amount of the security at issuance. In such a circumstance, Treasury will pay an additional amount at maturity so that the additional amount plus the inflation-adjusted principal amount will equal the par amount of the securities on the date of original issuance. Initially, the securities will be issued with a 10-year maturity; however, Treasury expects to issue other maturities over time.

[1] The guidance prescribed within this interpretation is limited to treasury inflation-indexed securities backed by the full faith and credit of the United States Government. Inflation-indexed securities of foreign governments shall not follow the guidance within this interpretation and shall be accounted for and reported according to the applicable SSAP without adjustments for the inflation factor.

Stripping. The securities will be eligible for the STRIPS program (Separate Trading of Registered Interest and Principal of Securities) as of the first issue date. Unlike the conventional STRIPS program, however, interest components stripped from different inflation-indexed securities, at least initially, will not be interchangeable or fungible with interest components from other securities, even if they have the same payment or maturity date.

3. The accounting issue is how should changes to inflation-adjusted principal be recorded?

4. At the September 10, 2002 and December 8, 2002 the Working Group expanded this interpretation to address specific questions regarding U.S. Treasury Inflation-Indexed Securities purchased at either a premium or discount and how the inflation adjustment interacts with any such premium or discount, as well as the calculation of each of these amounts.

5. The following example will be used to highlight issues concerning the amortization of premium and inflation adjustment for a typical security:

Assume:	
Par value of TIP security	$500,000
Inflation factor at date of purchase	1.12075
Price at date of purchase	102.96875
Original issue date 6/30/X0	
Purchase date 06/30/X6	
Maturity date 06/30/X10	
Amount of inflation adjustment at date of purchase ($500,000 * .12075)	$60,375
Total purchase price ($500,000*1.12075*1.0296875)	$577,011
Premium at date of purchase ($577,011 - $500,000 - $60,375)	$16,636

6. The issues are:

Issue a. – If accretion or amortization should be recognized over the period of time the security is owned.

Issue b. – Assuming that at the end of the accounting period, 12/31/X6, the inflation factor is 1.13000, what the correct book value of the security would be.

Issue c. – Assuming that at the end of the accounting period, 12/31/X6, the inflation factor is 1.12000, what the correct value of the security would be.

Issue d. – How changes in accounting treatment would be handled.

INT 01-25 Discussion

7. At its October 16, 2001 meeting, the Working Group reached a consensus that the inflation adjustment be recognized as an unrealized gain until such time as it is paid, at which time it should be recognized as a realized gain. If there is a deflation adjustment, such amounts should only be recognized to the extent of any previously recognized inflation adjustment for that particular security, (reduce any unrealized gain on that security to zero) as the investor is guaranteed at maturity to receive at least the par amount of the security. (See paragraph 8.c. below for amendments to this paragraph adopted at the December 8, 2002 meeting.)

8. At its December 8, 2002 meeting, the Working Group reached a consensus on the following issues related to the purchase of a treasury inflation-indexed security at either a premium or a discount, how the inflation adjustment interacts with any such premium or discount, as well as the calculation of each of these amounts.

Issue a. – The $16,636 premium paid for the security should be amortized over the remaining life of the security. Therefore, if the inflation adjustment factor never changed from the 1.12075 at date of purchase, the security would have a book value at maturity of $560,375, the amount the reporting entity would receive at maturity date ($500,000*1.12075).

Issue b. – The reporting entity should record the unrealized gain/loss based on the difference in the inflation factor times the par amount, and amortize the premium over the remaining life of the security.

Issue c. – In the case where the inflation factor is reduced to a factor not less than 1.0000, the reporting entity should reflect the change in the inflation adjustment as well as amortization of premium. Paragraph 7 of this interpretation is amended as follows:

> 7. The Working Group reached a consensus that the inflation adjustment be recognized as an unrealized gain until such time as it is paid, at which time it should be recognized as a realized gain. If there is a deflation adjustment, such amounts should only be recognized to the extent the inflation factor is not reduced to an amount less than 1.0000 as the investor is guaranteed at maturity to receive at least the par amount of the security.

Issue d. - A change in accounting principle should be recorded per the requirements of *SSAP No. 3—Accounting Changes and Corrections of Errors*, paragraph 5:

> 5. The cumulative effect of changes in accounting principles shall be reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle. The cumulative effect is the difference between the amount of capital and surplus at the beginning of the year and the amount of capital and surplus that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods.

In the specific question noted, if the reporting entity is currently recognizing both amortization of premium as well as the change in the inflation adjustment factor as amortization of premium, there should not be a cumulative effect on surplus to record.

INT 01-25 Status

9. No further discussion is planned.

10. On April 8, 2017, the Statutory Accounting Principles (E) Working Group modified this interpretation, adding footnote 1 to clarify that the guidance within this interpretation is only applicable to Treasury inflation-indexed securities backed by the full faith and credit of the United States Government.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 01-31: Assets Pledged as Collateral

INT 01-31 Dates Discussed

October 16, 2001; December 10, 2001; March 18, 2002; September 12, 2004; December 5, 2004; March 3, 2012; August 31, 2012

INT 01-31 References

Current:
SSAP No. 4—Assets and Nonadmitted Assets
SSAP No. 103—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
INT 20-06: Participation in the 2020 TALF Program

Superseded/Nullified:
SSAP No. 18—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
SSAP No. 33—Securitization
SSAP No. 45—Repurchase Agreements, Reverse Repurchase Agreements and Dollar Repurchase Agreements
SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
INT 99-02: Accounting for Collateral in Excess of Debt Principal

INT 01-31 Issue

1. Insurers may enter into certain transactions that require the granting of a security interest in certain assets to another party to serve as collateral for their performance under a contract. The arrangement is commonly referred to as a pledge, typically accomplished by delivery of assets to the secured party or to an independent custodian. In these transactions, the pledging insurer typically (1) continues to receive the income on the pledged collateral and (2) can remove and substitute other securities with little or no advance notice to the secured party as long as they comply with related investment quality and market value agreement provisions. Examples include collateral pledged under investment, derivative, debt obligations and policyholder transactions.

2. Specific examples of collateral pledged for derivative and investment transactions include but are not limited to: (1) securities posted with a broker as margin for futures and options transactions, (2) securities pledged to secure credit exposure with swap counterparties, (3) securities pledged under reverse repurchase agreements or securitizations that are accounted for as secured borrowing transactions and (4) securities pledged under securities lending transactions.

3. Specific examples of collateral pledged for debt obligations and policyholder transactions include but are not limited to assets pledged to secure (1) debt borrowings from or insurance contracts issued to banking entities and (2) insurance contracts issued to governmental entities such as municipalities.

4. Under these transactions, the fair value of the securities pledged as collateral may exceed the contract balance (swap fair value, advance balance, policyholder account balance, etc). For this interpretation, this excess carrying value of securities pledged over the corresponding asset or contract balance is called the "overcollateralization" amount.

5. The accounting issue is whether the assets pledged as collateral under the various transactions mentioned above should be considered admitted assets.

INT 01-31 Discussion

6. The Working Group reached a consensus that if the collateral had not been pledged in the examples described above, it is assumed the underlying asset would be recorded as an admitted asset under SSAP No. 4 (e.g. they are readily marketable assets available to meet both current and future policyholder obligations). In addition, it is assumed that the asset would not be considered impaired under *SSAP No. 5—Liabilities, Contingencies and Impairments of Assets* due to a default, fair value decline, or other loss contingency.

7. Therefore, for the examples described above, the pledging insurer would record the collateral (including the overcollateralization amount) as an admitted asset until they have committed a contract default that has not been cured in accordance with the contract provisions. This accounting is in accordance with the provisions of SSAP No. 103. This consensus of reporting collateral as an admitted asset is further supported by SSAP Nos. 4 and 5 since generally, the insurer can readily substitute pledged assets. Additionally, an insurer may typically unwind the transaction allowing the assets to be available to the pledging insurer to meet policyholder obligations. Furthermore, no event has occurred to indicate an impairment or potential loss contingency with respect to such pledged assets. The fact that some pledged assets may constitute an overcollaterlization amount does not change this analysis. Accordingly, all assets pledged in support of these type transactions should also be admitted.

8. At the time of an uncured default, the provisions of paragraph 20 of SSAP No. 103~~R~~ shall be used to determine the appropriate accounting treatment for the collateral. If the secured party utilizes collateral to offset all or a portion of the liability owed by the pledging insurer as a result of the default, then the collateral amount utilized to offset the liability shall be removed from the balance sheet. At the same time, the amount of the liability that was offset should be removed from the balance sheet since that obligation has been satisfied through the secured party's utilization of that collateral. To the extent that an uncured default remains without the secured party utilizing the collateral to offset the obligation, the pledging insurer should only record an admitted asset for the amount of collateral that it can redeem.

INT 01-31 Status

9. As of March 18, 2002, the consensus position of this interpretation is consistent with the position of the NAIC Invested Asset (E) Working Group. This interpretation will be reviewed by the FAS 140 Subgroup of the NAIC Statutory Accounting Principles (E) Working Group in conjunction of its consideration of incorporating GAAP pronouncement *FAS 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, a replacement of FASB Statement 125* into the statutory accounting model. As such, this interpretation is subject to amendment pending disposition of the FAS 140 Subgroup's review of collateral and FAS 140 in its entirety.

10. On September 12, 2004, the Working Group noted that the review of FAS 140 was complete and INT 01-31 was listed as an interpretation of SSAP No. 91R. On March 3, 2012, the Working Group adopted with modification *FAS 166—Accounting for Transfers of Financial Assets, an Amendment of FAS 140* (FAS 166). With this adoption, there was no change to the consensus opinion within this interpretation, and this INT was listed as an interpretation of SSAP No. 103.

11. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 02-22: Accounting for the U.S. Terrorism Risk Insurance Program

INT 02-22 Dates Discussed

December 8, 2002; March 9, 2003; March 24, 2018

INT 02-22 References

Current:
SSAP No. 35—Guaranty Fund and Other Assessments
SSAP No. 62—Property and Casualty Reinsurance

INT 02-22 Issue

1. The Terrorism Risk Insurance Act of 2002 establishes a temporary Federal program in the Department of the Treasury that provides for a system of shared public and private compensation for insured losses resulting from acts of terrorism, i.e., subject losses. The Terrorism Insurance Program (or the "Program") requires that all entities that meet the definition of an insurer under the act (generally, commercial property/casualty insurers that are licensed in the U.S.) participate in the Program. The Program becomes effective upon enactment and runs through December 31, 2005. (For purposes of the act, there is a "Transition Period" that runs from enactment through December 31, 2002, and three "Program Years" that run from January 1st through December 31st of 2003, 2004, and 2005, respectively.) The amount of compensation paid to participating insurers under the Program is 90% of subject losses, after an insurer deductible, and subject to an annual cap. The deductible under the Program is 1% for the Transition Period, 7% for Program Year 1, 10% for Program Year 2, and 15% for Program Year 3. In each case, the deductible percentage is multiplied times the insurer's direct earned premiums from the calendar year immediately preceding the respective Transition or Program year. The annual cap limits the amount of terrorism losses paid by insurers and the amount of Federal reimbursement and is $100 billion for Program Year 1 (combined with the Transition Period), Program Year 2, and Program Year 3

2. The Program provides for the establishment of a mandatory surcharge on all covered policyholders to provide for recoupment of defined losses paid by the Department of Treasury. To the extent that the amount of Federal financial assistance exceeds the amount recovered through the mandatory surcharge, the Department of Treasury may impose a second surcharge. The two surcharges combined may not exceed 3% of the annual premium charged for the insured policy. The Program provides that the Department of the Treasury shall collect the surcharges and further provides that insurers shall collect the surcharges and remit such amounts collected to the Department of Treasury.

3. The issues are:

Issue 1: Does the Program result in a transfer of underwriting risk for terrorism losses to the Department of Treasury and, if so, how should the recovery from the Department of Treasury for terrorism losses be accounted for by insurers?

Issue 2: How should the imposition of the surcharges on policyholders by the Department of Treasury be accounted for by insurers?

INT 02-22 Discussion

4. The Working Group reached a consensus as follows:

> Issue 1: Because the Program results in losses from acts of terrorism (above the defined insurer deductibles) being paid by the Department of Treasury, there is a transfer of insurance risk and accordingly, the recovery of such losses should be reported as reinsured losses.
>
> Issue 2: Because the terrorism loss risk-spreading premium is imposed on policyholders as a surcharge and the Department of Treasury provides for insurers to collect the surcharge "and remit amounts collected to the Secretary," the surcharge generally meets the requirements of paragraph 16 of SSAP No. 35 and should be accounted for as such.

INT 02-22 Status

5. No further discussion is planned.

6. This interpretation will remain in effect as long as the Terrorism Risk Insurance Act is authorized by the U.S. Congress.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 04-17: Impact of Medicare Modernization Act on Postretirement Benefits

INT 04-17 Dates Discussed

September 14, 2004; December 5, 2004

INT 04-17 References

Current:
SSAP No. 92—Postretirement Benefits Other Than Pensions

Superseded:
SSAP No. 10R—Income Taxes
SSAP No. 14—Postretirement Benefits Other Than Pensions
SSAP No. 89—Accounting for Pensions, A Replacement of SSAP No. 8

INT 04-17 Issue

1. In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) became law. Under the Act, starting in 2006, retirees will have the ability to obtain prescription drug benefits through a new Medicare Part D program and companies that continue to provide postretirement prescription drug benefits to their retirees may be eligible to receive a new federal subsidy.

2. In May 2004, FASB adopted the Board directed FASB Staff Position (FSP) *FAS 106-2, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* (FSP FAS 106-2). The guidance found in FSP FAS 106-2 superseded the earlier guidance in *FSP FAS 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* and was intended as being the final guidance on this subject.

3. Questions have arisen regarding whether an employer that provides postretirement prescription drug coverage should recognize the effects of the Act on the plan's accumulated postretirement benefit obligation (APBO) and the employer's postretirement benefit costs and, if so, when and how to account for those effects.

INT 04-17 Discussion

4. The Working Group reached a consensus to adopt the final conclusions reached in FSP FAS 106-2 with the following modifications:

a. Postretirement benefits should be accounted for in accordance with SSAP No. 92.

b. Income Taxes should be accounted for in accordance with SSAP No. 101.

c. Calculations shall not exclude non-vested employees.

d. Any references to *FSP FAS 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* are removed as this guidance was superseded by FSP FAS 106-2.

e. The effective date is universal for both public and non-public entities.

5. Per FSP FAS 106-2:

> 3. The guidance in this FSP related to accounting for the subsidy applies only to the sponsor of a single-employer defined benefit postretirement health care plan for which (a) the employer has concluded that prescription drug benefits available under the plan to some or all participants for some or all future years are "actuarially equivalent" to Medicare Part D and thus qualify for the subsidy under the Act and (b) the expected subsidy will offset or reduce the employer's share of the cost of the underlying postretirement prescription drug coverage on which the subsidy is based. This interpretation also provides guidance for the disclosures about the effects of the subsidy for an employer that sponsors a postretirement health care benefit plan that provides prescription drug coverage but for which the employer has not yet been able to determine actuarial equivalency.
>
> 4. Although this FSP provides limited guidance on certain other related aspects of accounting and disclosure necessitated by the Act (for example, changes in assumed participation rates and health care cost trend rates, as well as income tax accounting) that guidance is not intended to supersede or in any way limit the application of other relevant authoritative literature. This FSP does not address the accounting for the subsidy in situations that may arise in which the expected subsidy exceeds the employer's share of the cost of the underlying postretirement prescription drug coverage on which the subsidy is based. It also does not address accounting for the subsidy by multiemployer health and welfare benefit plans or by the sponsors or participating employers of those plans.

6. The Act introduces two new features to Medicare that an employer needs to consider in determining those measurements: (a) a subsidy that is based on 28 percent of an individual beneficiary's annual prescription drug costs between $250 and $5,000 (subject to indexation and the provisions of the Act as to "allowable retiree costs") and (b) the opportunity for a retiree to obtain a prescription drug benefit under Medicare.

7. Per FSP FAS 106-2:

> 9. An employer's eligibility for the 28 percent subsidy depends on whether the prescription drug benefit available under its plan is at least "actuarially equivalent" to the Medicare Part D benefit. At present, detailed regulations necessary to implement the Act have not been issued, including those that would specify the manner in which actuarial equivalency must be determined, the evidence required to demonstrate actuarial equivalency, and the documentation requirements necessary to be entitled to the subsidy.[1] In addition, the magnitude of the subsidy for an employer depends on how many of the employer's Medicare-eligible retired Plan participants choose not to enroll in the *voluntary* Medicare Part D plan. Further, specific regulations regarding the payment/reimbursement mechanism for the subsidy are yet to be defined by the appropriate administrative agency. Accordingly, questions have been raised regarding whether the subsidy is substantively similar to other Medicare benefits that existed when Statement 106 was issued and therefore should be accounted for as a reduction of the APBO and net periodic postretirement benefit cost, or whether the subsidy represents a payment to the employer that is determined by reference to its plan's benefit payments but is not, in and of itself, a direct reduction of postretirement benefit costs. Under either view, there is also a question as to when the subsidy should be given accounting recognition.
>
> <u>Effect on Per Capita Claims Cost</u>
>
> 10. Regardless of the impact of the subsidy, the existence of prescription drug coverage under Medicare Part D may have an effect on an employer's per capita claims cost for a plan that currently provides a prescription drug benefit. That effect depends on (a) whether current and future retirees (or their beneficiaries under the employer-sponsored plan) enroll in the voluntary

[1] Section 1860D-11(c) of the Social Security Act, as amended by the Act, states that "the Secretary [of Health and Human Services] shall establish processes and methods for determining the actuarial valuation of prescription drug coverage."

Medicare Part D plan and (b) the Act's macro-socioeconomic effects on health care cost trends and consumers' behavior.

Plan Amendments

11. In response to the Act, or for other reasons, an employer may amend an existing plan (or establish a new one). To the extent that an employer amends a plan (positively or negatively), the APBO will be affected by the direct effects of the change in benefits attributed to employee services already rendered. If an amendment changes the determination as to the actuarial equivalency of benefits available under the plan, the expected subsidy to the employer also will change.

Income Tax Accounting

12. The Act excludes receipt of the subsidy from the taxable income of the employer for federal income tax purposes.[2] Accordingly, this interpretation addresses how that provision affects the accounting for the temporary difference related to the employer's accrued postretirement benefit cost under Statement 109, *Accounting for Income Taxes.*

FASB Staff Position

13. Paragraph 35 of Statement 106 specifies that health care coverage provided by Medicare shall be taken into account in measuring the employer's postretirement health care benefit obligation. Paragraph 40 of Statement 106 requires presently enacted changes in relevant laws to be considered in current period measurements of net periodic postretirement benefit cost and the APBO. Therefore, under that guidance, measures of the APBO and net periodic postretirement benefit cost on or after the date of enactment shall reflect the effects of the Act.

Effect of the Subsidy on Benefits Attributable to Past Service

14. When an employer initially accounts for the subsidy pursuant to the effective date and transition guidance in paragraphs 23–32, its effect on the APBO shall be accounted for as an actuarial experience gain pursuant to paragraphs 56 and 59 or 60 of Statement 106.

Effect of the Subsidy on Current Measures of Net Periodic Postretirement Benefit Cost

15. Because the subsidy affects the employer's share of its plan's costs, the subsidy is included in measuring the costs of benefits attributable to current service. Therefore, the subsidy reduces service cost (as defined in paragraph 47 of Statement 106) when it is recognized as a component of net periodic postretirement benefit cost.

Changes in Estimates

16. If an estimate of the expected subsidy subsequently changes—as a result of changes in regulations or legislation, changes in the underlying estimates of postretirement prescription drug costs, or for reasons other than a plan amendment—the effect of the change in estimate is an actuarial experience gain or loss pursuant to paragraph 56 of Statement 106.

Plan Amendments

17. If prescription drug benefits currently available under an existing plan are deemed not actuarially equivalent as of the date of enactment of the Act, but the plan is subsequently amended to provide actuarially equivalent benefits, the direct effect of the plan amendment on the APBO (that is, the effect of only the change in prescription drug coverage) and the effect on the APBO from any resulting subsidy to which the employer is expected to be entitled as a result of the amendment shall be combined. If that combined effect reduces the APBO, it is deemed to be an actuarial experience gain pursuant to paragraph 56 of Statement 106. If the combined effect

[2] New Section 139A of the Internal Revenue Code established by Section 1202 of the Act.

increases the APBO, it is deemed to be prior service cost that shall be accounted for pursuant to paragraphs 50-54 of Statement 106.

18. A plan that provides prescription drug benefits that previously were deemed actuarially equivalent under the Act may be subsequently amended to reduce its prescription drug coverage and that reduced coverage may not be considered actuarially equivalent. In that circumstance, any actuarial experience gain related to the subsidy previously recognized is unaffected. However, the combined net effect on the APBO of (a) the subsequent plan amendment that reduces benefits under the plan and thus disqualifies the benefits as actuarially equivalent and (b) the elimination of the subsidy shall be accounted for as prior service cost (credit) as of the date the amendment is adopted.

Income Tax Accounting

19. In the periods in which the subsidy affects the employer's accounting for the plan, it shall have no effect on any plan-related temporary difference accounted for under Statement 109 because the subsidy is exempt from federal taxation. That is, the measure of any temporary difference shall continue to be determined as if the subsidy did not exist. To illustrate, consider the following simple example.

> Prior to the adoption of this FSP, an employer's carrying amount of accrued postretirement benefit cost (the amount recognized in the statement of financial position) is $100 for a noncontributory, unfunded prescription drug benefit plan with only inactive participants who are not yet eligible to collect benefits. Assuming a tax rate of 35 percent and no corresponding tax basis for the accrued postretirement benefit cost, the employer would report a $35 deferred tax asset related to that $100 deductible temporary difference. Because the employer has a policy of amortizing gains and losses under paragraph 59 of Statement 106, upon adoption of the FSP and recognition of a $28 actuarial gain resulting from the subsidy, neither the carrying amount of accrued postretirement benefit cost nor the deferred tax asset would change. Subsequently, ignoring interest on the APBO (which includes interest on the subsidy), as the actuarial gain related to the subsidy is amortized as a component of net periodic postretirement benefit cost, the carrying amount of accrued postretirement cost would be reduced. However, the associated temporary difference and deferred tax asset would remain unchanged. That is, after the gain related to the subsidy is amortized in its entirety, the carrying amount of accrued postretirement benefit cost would be $72, and the deferred tax asset would remain at $35.

For purposes of simplicity, this example ignores complexities regarding the amount and timing of the subsidies reflected in the carrying amount of accrued postretirement benefit cost arising from any of the following: (a) netting gains and losses and application of the corridor amortization approach described in paragraph 59 of Statement 106, (b) recognition of additional subsidies through amortization of prior service costs that include effects of the subsidy, or (c) reduction in future service and interest costs. Those complexities must be considered in determining the temporary difference on which the deferred tax effects under Statement 109 will be based. However, providing detailed guidance on the application of Statement 109 to postretirement benefits other than pensions is beyond the scope of this FSP.

INT 04-17 Disclosures

8. Per FSP FAS 106-2:

20. Until an employer is able to determine whether benefits provided by its plan are actuarially equivalent, it shall disclose the following in financial statements for interim or annual periods:

a. The existence of the Act

b. The fact that measures of the APBO or net periodic postretirement benefit cost do not reflect any amount associated with the subsidy because the employer is unable to conclude whether the benefits provided by the plan are actuarially equivalent to Medicare Part D under the Act.

9. In interim and annual financial statements for the first period in which an employer includes the effects of the subsidy in measuring the net postretirement benefit cost and the first period in which an employer includes the effects of the subsidy in measuring net periodic postretirement benefit cost, it shall disclose the following:

a. The reduction in the net postretirement benefit cost for the subsidy related to benefits attributed to former employees.

b. The effect of the subsidy on the measurement of net periodic postretirement benefit cost for the current period. That effect includes (1) any amortization of the actuarial experience gain in (a) as a component of the net amortization called for by paragraph 49 of SSAP No. 92, (2) the reduction in current period service cost due to the subsidy, and (3) the resulting reduction in interest cost on the net postretirement benefit cost as a result of the subsidy.

c. Any other disclosures required by paragraph 66.p. of SSAP No. 92 which requires disclosure of "An explanation of any significant change in the benefit obligation or plan assets not otherwise apparent in the other disclosures required by this statement."

10. For purposes of the disclosures required by paragraph 66.a. of SSAP No. 92, an employer shall disclose gross benefit payments (paid and expected, respectively), including prescription drug benefits, and separately the gross amount of the subsidy receipts (received and expected, respectively).

INT 04-17 Effective Date and Transition

11. This interpretation is effective for reporting years beginning on or after January 1, 2005 with early adoption allowed. A change resulting from adoption of this interpretation should be accounted for as detailed in paragraphs 12 and 13. A change resulting from the adoption of this interpretation shall be accounted for as a change in accounting principle in accordance with SSAP No. 3.

12. Per FSP FAS 106-2:

> 24. … If the effects of the Act—including the subsidy, if any, changes in participation rates, and changes in estimated health care costs—cause the employer to conclude that enactment of the Act was not a "significant event" pursuant to paragraph 73 of Statement 106, the effects of the Act shall be incorporated in the next measurement of plan assets and obligations otherwise required by Statement 106 following the effective date of this FSP. If an employer concludes that enactment of the Act was a significant event, but either (a) benefits available under its plan are not actuarially equivalent to Medicare Part D or (b) the employer is unable to conclude (refer to paragraph 33) whether any benefits are actuarially equivalent, it shall measure any effects of the Act other than the subsidy (for example, changes in estimated participation rates or health care costs) at the next measurement date for plan assets and obligations required by paragraphs 28–32 of this FSP.

13. Per FSP FAS 106-2:

> 27. For a plan (a) that provides benefits that are considered actuarially equivalent as of the date of enactment, based on information that is available as of the date of adoption of this interpretation, and (b) for which enactment of the Act was a significant event, this interpretation provides two alternative methods of transition—retroactive application to the date of enactment (paragraphs 28–29) or prospective application from the date of adoption (paragraph 30).

Retroactive application to date of enactment

28. When this FSP is initially adopted, a remeasurement of the plan's assets and APBO, including the effects of the subsidy, if applicable, as well as the other effects of the Act, shall be made as of the earlier of (a) the plan's measurement date that normally would have followed enactment of the Act or (b) the end of the employer's interim or annual period that includes the date of the Act's enactment. As an alternative, employers are permitted, but not required, to perform that remeasurement as of the date of enactment. The measurement of the APBO shall be based on the plan provisions in place on the measurement date. Plan amendments occurring after the measurement date pursuant to (a) or (b) above shall not be anticipated in performing that measurement. However, if prior to the effective date of this FSP, a plan is amended so as to not be considered actuarially equivalent, the employer shall not reflect any effects of the subsidy in the transitional measurements required by this FSP. If the prescription drug coverage provided by a plan was amended after December 8, 2003, but before January 31, 2004 (the date before which plan amendments would not cause the deferral provided by FSP FAS 106-1 to expire), the effects of the prescription drug plan amendment and the consequential effects of the subsidy shall be accounted for pursuant to the applicable guidance in either paragraph 17 or 18 of this FSP.

29. The effects of measuring plan assets and obligations under paragraph 28 generally will not affect the accrued or prepaid postretirement benefit cost reported in the employer's statement of financial position as of the measurement date.[3] However, those measurements will affect net periodic postretirement benefit cost for periods subsequent to the date of the re-measurement.[4] To the extent that previously issued financial reports for periods prior to the effective date of this FSP would have been affected by the remeasurement of plan assets and obligations under paragraph 28, the requirements in paragraph 20 of APB Opinion No. 20, Accounting Changes, and paragraph 10 of FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, as applicable, shall be followed.[5] In calculating the effects on prior periods, the guidance in paragraphs 17 and 18 of this FSP applies to plan amendments adopted subsequent to the measurement date described in paragraph 28 but before the effective date of this FSP. The effects of any such amendment shall be determined as of the date the plan amendment is adopted. The following examples illustrate the application of the provisions in this paragraph.

Example A—Calendar Year-End, September 30 Measurement Date

Calendar Company, a public company, sponsors a postretirement health care benefit plan that provides prescription drug coverage. It has a December 31 year-end for financial reporting purposes and uses a September 30 measurement date pursuant to paragraph 72 of Statement 106. Calendar Company elected to defer any accounting for the effects of the Act pursuant to FSP FAS 106-1 and made that election in the quarter ending March 31, 2004, the first period in which the plan's accounting for the effects of the Act normally would have been reflected in Calendar Company's financial statements.

Calendar Company adopts the guidance in this FSP as of July 1, 2004, the beginning of its third quarter. Calendar Company and its actuarial advisors determine that benefits provided by the plan as of the date of enactment were at least actuarially equivalent to

[3] The paragraph 28 measurement would affect the statement of financial position if, pursuant to paragraph 60 of Statement 106, the employer has a policy of immediately recognizing gains and losses.

[4] Depending on the measurement date selected for the plan pursuant to paragraph 72 of Statement 106, the net periodic postretirement benefit cost may not be affected by the Act in the employer's reporting period immediately following the measurement required by paragraph 28. For example, for a public company with a December 31 fiscal year-end, the end of the employer's interim period that includes the date of enactment would be December 31, 2003. If that employer uses a September 30 measurement date pursuant to paragraph 72 of Statement 106, the effects of the Act on the plan would first affect net periodic postretirement benefit cost in the employer's interim period that begins April 1, 2004.

[5] Paragraph 10 of Statement 3 states that no cumulative effect of a change in accounting principle shall be included in net income of the interim period, other than the first interim period, in which the change is adopted. However, financial information for the pre-change interim periods of the fiscal year in which the change is made shall be restated on the basis of the new accounting principle whenever those pre-change interim periods are subsequently presented.

Medicare Part D, and, accordingly, Calendar Company will be entitled to the subsidy. Calendar Company performs an interim measurement of the effects of the Act on the APBO as of December 31, 2003, the end of its interim (and annual) period that includes the date of the Act's enactment and determines that the aggregate effect on service cost, interest cost, and amortization of gains and losses results in a reduction of $500 in annual net periodic postretirement benefit cost compared to that amount calculated without considering the effects of the Act.

The effect of applying this FSP has no cumulative effect on Calendar Company's retained earnings as of December 31, 2003. Because Calendar Company uses a September 30 measurement date, the accounting for the plan is reflected in Calendar Company's financial statements on a one-quarter lag. Therefore, the Act had no effect on net periodic postretirement benefit cost for the first quarter. Accordingly, in applying the guidance in Statement 3, Calendar Company reports net periodic postretirement benefit cost for the nine-month period ending September 30, 2004, reflecting $250 (the second and third quarter amounts) of the $500 annual reduction. Net periodic postretirement benefit cost included in third quarter results of operations reflects only that quarter's $125 reduction due to the Act. When presented for comparative purposes, for example in summary quarterly financial information in the annual report or for comparative purposes in the 2005 second quarter financial report, the results of operations for the second quarter of 2004 will be restated to reflect a $125 reduction in net periodic postretirement benefit cost due to the Act.

<u>Example B—April 30 Year-End, April 30 Measurement Date</u>

Spring Company, a public company, sponsors a postretirement health care benefit plan that provides prescription drug coverage. It has an April 30 year-end for financial reporting purposes and uses April 30 as the measurement date for plan assets and obligations under Statement 106. Spring Company elected to defer any accounting for the effects of the Act pursuant to FSP FAS 106-1 and made that election in the quarter ending January 31, 2004, the first period in which the plan's accounting for the effects of the Act normally would have been reflected in Spring Company's financial statements.

Spring Company adopts the guidance in this FSP as of August 1, 2004, the beginning of its second quarter. Spring Company and its actuarial advisors determine that benefits provided by the plan as of the date of enactment were at least actuarially equivalent to Medicare Part D, and, accordingly, Spring Company will be entitled to the subsidy. Spring Company measures the effects of the Act on the APBO as of January 31, 2004, the end of its interim period that includes the date of the Act's enactment and determines that the aggregate effect on service cost, interest cost, and amortization of gains and losses results in a reduction of $500 in annual net periodic postretirement benefit cost compared to that amount calculated without considering the effects of the Act.

Because the date for remeasuring the plan's assets and obligations required by this FSP—for an employer that elects retroactive application—occurs in Spring Company's prior fiscal year, the cumulative effect of applying the guidance in this FSP on Spring Company's retained earnings as of April 30, 2004, is $125 (the fourth quarter effect on net periodic postretirement cost, ignoring any deferred income tax effects, which may be none). That cumulative effect of a change in accounting principle is recognized in Spring Company's net income for the six months ending October 31, 2004. Assuming no other changes in assumptions or other gains and losses arise in the regularly scheduled April 30, 2004 measurement of the plan, pursuant to the guidance in Statement 3, Spring Company reports net periodic postretirement benefit cost for the six-month period ending October 31, 2004, reflecting $250 (the first and second quarter amounts) of the $500 annual reduction. Net periodic postretirement benefit cost included in second quarter results of operations reflects only that quarter's $125 reduction due to the Act. When presented for comparative purposes, for example in summary quarterly financial information in the annual report or for comparative purposes in the next fiscal year's first quarter financial report, the results of operations for the quarter ended July 31, 2004, will be restated to reflect the $125 reduction in net periodic postretirement benefit cost due to the Act and the $125 cumulative effect of the change in accounting principle.

Prospective application as of date of adoption

30. When this FSP is initially adopted, a remeasurement of the plan's assets and APBO, including the effects of the subsidy, if applicable, as well as the other effects of the Act, shall be made as of the beginning of the period of adoption pursuant to the guidance in paragraph 73 of Statement 106. The measurement of the APBO shall be based on the plan provisions in place on the measurement date and shall incorporate the best available current information regarding actuarial assumptions and discount rates. The results of that measurement shall be used to determine net periodic postretirement benefit cost in interim periods following the date of adoption until the next measurement date otherwise required by Statement 106. The following example illustrates the application of the provisions of this paragraph.

Example C—Calendar Year-End, September 30 Measurement Date

Calendar Company, a public company, sponsors a postretirement health care benefit plan that provides prescription drug coverage. It has a December 31 year-end for financial reporting purposes and uses a September 30 measurement date pursuant to paragraph 72 of Statement 106. Calendar Company elected to defer any accounting for the effects of the Act pursuant to FSP FAS 106-1 and made that election in the quarter ending March 31, 2004, the first period in which the plan's accounting for the effects of the Act normally would have been reflected in Calendar Company's financial statements.

Calendar Company adopts the guidance in this FSP as of July 1, 2004, the beginning of its third quarter. Calendar Company and its actuarial advisors determine that benefits provided by the plan as of the date of enactment were at least actuarially equivalent to Medicare Part D, and, accordingly, Calendar Company will be entitled to the subsidy. Calendar Company measures the effects of the Act on the APBO as of April 1, 2004, the beginning of the plan's interim period that corresponds to the plan sponsor's first reporting period beginning after June 15, 2004, and determines that the aggregate effect on service cost, interest cost, and amortization of gains and losses results in a reduction of $500 in annual net periodic postretirement benefit cost compared to that amount calculated without considering the effects of the Act.

Net periodic postretirement benefit cost for the quarters ending September 30 and December 31, 2004, reflecting the activity in the plan for the quarters ending June 30 and September 30, 2004, will include a $125 per quarter reduction in net periodic postretirement benefit cost due to the effects of the Act.

Nonpublic entity with only small plans

31. If enactment of the Act constitutes a significant event for a plan, a nonpublic entity that meets the criteria in paragraph 23 may follow the guidance in paragraph 28, including the related transition guidance described in paragraph 29, or may incorporate the effects of the Act prospectively in measures of net periodic postretirement benefit cost and plan assets and obligations for fiscal years beginning after December 15, 2004.

Employer That Did Not Elect Deferral

32. For an employer that did not elect the deferral option provided under FSP FAS 106-1 and whose previous accounting for the effects of the Act differs from the guidance in this FSP, the adoption of this FSP constitutes a change in accounting principle under Opinion 20. Accordingly, the cumulative effect of retroactive application of this FSP to the date of the Act's enactment shall be reflected in the financial statements following the provisions of paragraph 20 of Opinion 20 and paragraphs 9 and 10 of Statement 3, as applicable.

Subsequent Determination of Actuarial Equivalence Absent a Plan Amendment

33. When adopting this FSP, an employer and its actuarial consultants may be unable to determine the extent to which the benefits provided by a plan are actuarially equivalent as of the date of the initial measurement applying the guidance in this FSP. If clarifying regulations related to the Act or new information about the interpretation or determination of *actuarial equivalency* under the Act becomes available, the employer shall reconsider whether the benefits provided under its plan, as presently constructed, are actuarially equivalent.[6] If that reconsideration results in a conclusion that benefits provided by the plan are actuarially equivalent (or that additional benefits provided by the plan are actuarially equivalent in the case of a plan under which an employer previously had determined that some benefits were actuarially equivalent), that conclusion could be a significant event pursuant to paragraph 73 of Statement 106.[7] If the effects of the subsidy on the plan are significant, a measurement of plan assets and obligations shall be performed as of the date that actuarial equivalency is determined. Any effect on the APBO due to the subsidy shall be reflected as an actuarial gain consistent with the guidance in paragraph 14 of this FSP. Measures of net periodic postretirement benefit cost for subsequent periods would reflect the effects of those measurements (reported on a lag basis, if appropriate; refer to footnote 6). Prior financial statements shall not be retroactively adjusted nor shall a cumulative effect for prior periods be recognized in income.

INT 04-17 Status

14. No further discussion is planned.

[6] The guidance in this paragraph does not apply if a plan amendment is the event that gives rise to the employer's reconsideration of actuarial equivalency. The guidance in paragraphs 17 and 18 of this FSP apply to plan amendments.

[7] To the extent that some benefits under a plan are determined to be actuarially equivalent at the date of adoption of the FSP, the provisions of paragraphs 24–32 apply.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 04-21: EITF 02-9: Accounting for Changes That Result in a Transferor Regaining Control of Financial Assets Sold

INT 04-21 Dates Discussed

December 5, 2004; March 13, 2005; March 3, 2012; August 31, 2012

INT 04-21 References

Current:
SSAP No. 103—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities

Superseded:
SSAP No. 91R—Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities

INT 04-21 Issue

1. EITF No. 02-9, *Accounting for Changes That Result in a Transferor Regaining Control of Financial Assets Sold* (EITF 02-9) expands on a key concept presented in FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (FAS 140), paragraph 55. This key concept requires a transferred financial asset that has been accounted for as sold to be accounted for as "re-purchased" if the basis for that sale accounting subsequently becomes invalid.

2. The following is excerpted from EITF 02-9:

> 1. …One circumstance that has raised questions about the application of paragraph 55 occurs when the provisions of paragraph 55 are triggered because the transferor holds a contingent right such as a contingent call option on the transferred financial assets (for example, a removal of accounts provision or "ROAP") and the contingency has been met. This issue assumes that the transferee is not consolidated by the transferor.
>
> 2. Under Statement 140, rights held by the transferor (typically in the form of purchased options or forward purchase contracts) only preclude sale accounting under paragraph 9.c.(2) if they provide the transferor with (a) the unilateral right to cause the holder to return specific transferred financial assets, and (b) more than a trivial benefit. One class of contingent rights (including certain ROAPs 1) does not preclude sale accounting because it does not include unilateral rights. The most common type of ROAP is a default ROAP, which gives the holder the right but not the obligation to purchase (call) a loan that is in default (the meaning of default typically is specifically defined in each transaction). Such rights are common in credit card securitizations and in securitizations sponsored by the Government National Mortgage Association (GNMA) 2 and other governmental or quasi-governmental agencies. Once the contingency is met (in this case, when a given loan goes into default), the call option on that asset (loan) is no longer contingent. At that point, the transfer fails the criterion in paragraph 9.c.(2) of Statement 140 because the transferor has the unilateral right to purchase a specific transferred financial asset and obtains more than a trivial benefit. Under the requirements of paragraph 55, when a contingency related to a transferor's contingent right has been met, the transferor generally must account for the "re-purchase" of a specific subset of the financial assets transferred to and held by the qualifying entity. The transferor must do so regardless of whether it intends to exercise its call option.

3. Per EITF 02-9, the issues are:

Issue 1—How the transferor should account for the transferor's beneficial interests when the underlying assets are re-recognized under the provisions of paragraph 55 because the transferor's contingent right (for example, a ROAP or other contingent call option on the transferred financial assets) becomes exercisable, including whether any gain or loss should be recognized by the transferor when paragraph 55 is applied.

Issue 2—Whether under any circumstances a loan loss allowance should initially be recorded for loans that do not meet the definition of a security when they are re-recognized under the provisions of paragraph 55

Issue 3—How re-recognition under paragraph 55 of assets sold affects the accounting for the related servicing asset.

Issue 4—After a paragraph 55 event, how the transferor should account for the transferor's interests (other than the servicing asset).

INT 04-21 Discussion

4. EITF 02-9 consensus on each issue is as follows:

5. The Task Force reached a consensus on Issue 1 that upon application of paragraph 55, no gain or loss should be recognized in earnings with respect to any of the transferor's beneficial interests. Beneficial interests should be evaluated periodically for possible impairment, including at the time paragraph 55 is applied. A gain or loss may be recognized upon the exercise of a ROAP or similar contingent right with respect to the "re-purchased" transferred financial assets that were sold if the ROAP or similar contingent right held by the transferor is not accounted for as a derivative under Statement 133 and is not at-the-money, resulting in the fair value of those repurchased assets being greater or less than the related obligation to the transferee.

6. The Task Force reached a consensus on Issue 3 that under no circumstances should a loan loss allowance be initially recorded for loans that do not meet the definition of a security when they are re-recognized pursuant to paragraph 55.

7. The Task Force reached a consensus on Issue 4 that when a paragraph 55 event occurs, the accounting for the servicing asset related to the previously sold financial assets does not change as a result of the application of paragraph 55. That is, even though the transferor has regained control over the previously sold assets, the cash flows from those assets will contractually be paid to the SPE, which will then distribute the proceeds to satisfy its contractual obligations (including obligations to the beneficial interest holders). Because the transferor, as servicer, is still contractually required to collect the asset's cash flows for the benefit of the SPE and otherwise service the assets, it should continue to recognize the servicing asset and assess the asset for impairment as required by Statement 140.

8. The Task Force reached a consensus on Issue 5 that when a paragraph 55 event occurs, the transferor should continue to account for the transferor's interests in those underlying financial assets apart from any re-recognized financial assets. That is, the transferor's interests should not be combined with and accounted for with the re-recognized financial assets. However, a subsequent event that results in the transferor reclaiming those financial assets from the transferee—for example, the exercise of a ROAP or the consolidation by the transferor of the securitization entity in accordance with applicable generally accepted accounting principles, including Interpretation 46R—would result in a recombination of the transferor's interests with the underlying financial assets.

5. The Working Group reached a consensus to adopt EITF 02-9 as an interpretation of SSAP No. 103, with modification as follows:

a. Change references to FAS 140 to SSAP No. 103 including paragraph-specific references. Modify FAS 140, paragraph 55 references to refer to SSAP No. 103, paragraph 59.

b. Change references to FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* to SSAP No. 86 as an interpretation of SSAP No. 91R.

c. Remove reference to Interpretation 46R as FASB Interpretation No. 46, *Consolidation of Variable Interest Entities,* is pending review for statutory accounting. (The prior GAAP guidance in FASB Interpretation FIN 46 was rejected for statutory accounting in *SSAP No. 3—Accounting Changes and Corrections of Errors*.)

d. Limit the applicability of EITF 02-9, Issue 3 to only valuation allowances applicable to statutory accounting for mortgage loans and real estate under development as provided in *SSAP No. 37—Mortgage Loans* and real estate under development as discussed in *SSAP No. 38—Acquisition, Development and Construction Arrangements*.

6. This interpretation was originally effective for years beginning January 1, 2005, to be consistent with the original effective date of SSAP No. 91R. Revisions adopted to this interpretation on March 3, 2012, are in accordance with the adoption with modification of FAS 166 in a new SSAP to superseded SSAP No. 91R.

INT 04-21 Status

7. In 2009, *FAS 166, Accounting for Transfers of Financial Assets, an Amendment of FAS 140*, was issued. In addition to amending FAS 140, it also amended FASB EITF 02-9. FAS 166 was adopted for statutory accounting in SSAP No. 103 to supersede SSAP No. 91R. On March 3, 2012, corresponding revisions to INT 04-21 were also adopted to reflect the updated GAAP guidance adopted for statutory accounting interpreting SSAP No. 103. These changes will not be tracked in subsequent editions of the Manual.

8. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group and Statutory Accounting Principles (E) Working Group

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

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 05-05 Issue

1. The Medicare Modernization Act of 2003 (MMA) created a new program, commonly known as Medicare Part D, whereby Medicare recipients may obtain prescription coverage offered by insurers who have been approved by the Centers for Medicare and Medicaid Services (CMS). Insurers who offer Medicare Part D coverage will, starting in January 2006, receive several different types of funds relating to the program. Some of these funds relate to portions of the coverage that require an annual reconciliation, resulting in the return of any excess funds received. Other funds may be received (or may be required to be returned) to offset experience that is especially unfavorable (or, respectively, favorable).

2. How should the various components of the funds received or receivable by an insurer from Medicare Part D coverage be accounted for?

INT 05-05 Discussion

3. The attached appendix provides a listing of terms to which CMS ascribes a specific meaning. This list has been enhanced to include other terms in order to facilitate consistent application for accounting and the NAIC's risk-based capital (RBC) formula. It should be noted that the terms included in the attached appendix are, for the most part, defined by CMS. Consequently, the term "reinsurance payment" does not represent actual reinsurance as defined by *SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance*.

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. 54. 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.

5. The collectibility and any nonadmission of amounts receivable from the government insured or uninsured plans are addressed in SSAP No. 84, paragraph 22, and SSAP No. 47, paragraph 10 and paragraph 11, respectively.

INT 05-05 Status

6. On August 4, 2018, the Statutory Accounting Principles (E) Working Group updated this interpretation to add a description of the Coverage Gap Discount Program, amend existing guidance on program payments and update definitions. No further discussion is planned.

Appendix – Commonly Used Terms for Medicare Part D Coverage

The federal Centers for Medicare and Medicaid Services (CMS) oversees the Medicare Part D prescription drug coverage, including coverage provided through a stand-alone prescription drug plan (PDP) and coverage provided as part of a Medicare Advantage plan. CMS ascribed specific meaning to most of the following terms. Other terms have been defined below in order to facilitate consistent application.

Beneficiary Premium (Standard Coverage Portion) – The amount received from the Part D enrollee (directly, or from CMS after being withheld from Social Security benefits) as payment for the standard coverage. This includes any late enrollment penalties that the PDP sponsor receives for an enrollee. The beneficiary premium is accounted for as health premium.

Beneficiary Premium (Supplemental Benefit Portion) – The amount received from the Part D enrollee (directly, or from CMS after being withheld from Social Security benefits) as payment for supplemental benefits. The beneficiary premium is accounted for as health premium.

Coverage Gap Discount Program – The federal Affordable Care Act amended the Health Care and Education Act of 2010 (H. R. 4872) (HCERA) in 2011 to establish a discount program that would make manufacturer discounts available to applicable Medicare beneficiaries receiving applicable covered Part D drugs while in the coverage gap. Part D sponsors must provide the discounts for the applicable drugs in the coverage gap at point-of-sale. CMS coordinates the collection of discount payments from manufacturers and payment to Part D sponsors that provided the discount to applicable beneficiaries through a contractor. The coordination involves a standard process for paying Part D sponsors based on new information submitted to CMS on prescription drug event data. The Coverage GAP Discount Program is reconciled quarterly.

Coverage Year Reconciliation – A reconciliation made after the close of each calendar year to determine the amounts that a PDP sponsor is entitled to for the low-income subsidy (cost-sharing portion), the reinsurance payment, and the risk corridor payment adjustment. To the extent that interim payments (if any) from CMS exceeded the amounts determined by the reconciliation, the PDP sponsor must return the excess to the government; to the extent that interim payments (if any) from CMS fell short of the amounts determined by the reconciliation, the government will make an additional payment to the PDP sponsor. The coverage year reconciliation results in the low-income subsidy (cost-sharing portion) and the reinsurance payment being essentially a self-insured (by the government) component of the Part D coverage, subject to SSAP No. 47. The coverage year reconciliation also results in the treatment of the risk corridor payment adjustment as a retrospective premium adjustment, subject to SSAP No. 66.

Direct Subsidy – The amount the government pays to the PDP sponsor for the standard coverage. These payments are accounted for as health premium.

Low-Income Subsidy (Cost-Sharing Portion) – The amount the government pays to the PDP sponsor for additional benefits provided to low-income enrollees. The additional benefits may include payment for some or all of the deductible, the coinsurance, and the co-payment above the out-of-pocket threshold. These payments are accounted for as payments made under a self-insured plan.

Low-Income Subsidy (Premium Portion) – The amount the government pays to the PDP sponsor for low-income enrollees in lieu of part or all of the beneficiary premium (standard coverage portion). These payments are accounted for as health premium.

PDP Sponsor – The entity that provides stand-alone Part D coverage (as opposed to Part D coverage provided through a Medicare Advantage plan).

Reinsurance Payment – An amount paid by the government for benefit costs above the out-of-pocket threshold (see "Standard Coverage"). Generally, when costs exceed the out-of-pocket threshold, the government pays a specified percentage of the costs, the enrollee pays a percentage (or the specified co-payments which are updated based on cost trends for generic and for brand-name prescriptions), and the PDP sponsor pays the remainder. The amount paid by the government is treated as a claim payment made by a self-insured benefit plan rather than as revenue to the PDP sponsor, and the claims do not flow through the PDP sponsor's income statement. In cases where the government prepays the reinsurance payment on an estimated basis, the prepayment is treated as a deposit, which again does not pass through the PDP sponsor's income statement. The amount paid by the enrollee is paid directly to the pharmacy; therefore there is no required accounting for this amount by the PDP sponsor.

Part D Payment Demonstration – A payment from the government to a PDP sponsor participating in CMS's Part D Payment Demonstration. The payment demonstration is a special arrangement in which the PDP sponsor receives a predetermined per-enrollee capitation payment and the government no longer provides reinsurance for the specified percentage (example 80%) of costs in excess of the out-of-pocket threshold. Rather, the PDP sponsor assumes the risk for the specified percentage (example 80%) of costs, in addition to its normal percentage (example 15%) share of costs in excess of this threshold. However, risk corridor protection does still apply to this specified percentage (example 80%) share of costs. These payments are accounted for as health premium.

Reinsurance Coverage – The Medicare Part D provision under which the PDP sponsor may receive a reinsurance payment. This does not include payments under the Part D Payment Demonstration.

Risk Corridor Payment Adjustment – An amount by which the government adjusts its payments to the PDP sponsor, based on how actual benefit costs vary from the costs anticipated in the PDP sponsor's bid for the Part D contract (the "target amount" of costs). The government establishes thresholds for symmetric risk corridors around the target amount, using percentages of the target amount. If actual costs exceed the target amount but are less than the first threshold upper limit, then no adjustment is made. Risk corridor payment adjustments are accounted for as retrospective premium adjustments on retrospectively rated contracts.

Risk Corridor Protection – The Medicare Part D provision under which the PDP sponsor may receive (or pay) a Risk Corridor Payment Adjustment. Most employer plans providing Medicare Part D are not eligible for Risk Corridor Protection.

Standard Coverage – The Part D benefit design that conforms to certain standards prescribed by the government. The standard coverage comprises: no coverage for an annual initial deductible; coverage net of a coinsurance provision (the percentage of costs are payable by the insured) for costs up to an initial coverage limit; a range beyond the initial coverage limit (sometimes called the "coverage gap") in which the insured drug manufacturers and the PDP sponsor (for example, by 2020 insureds who are eligible for drug manufacturer discounts will pay 25% for qualifying brand and generic drugs, the PDP sponsor will be responsible for 25% of qualifying brand and 75% of generic drugs, and the drug manufacturer will be responsible for 50% of qualifying brand drugs); and an annual out-of-pocket threshold above which the insured pays the greater of a specified co-payment or a specified percentage of the drug cost. The various limits and thresholds are set at specified dollar amounts, which will be increased in later years based on the growth in drug expenditures. Wherever the term "standard coverage" is used as part of these instructions, the same treatment would be applied to coverage that has been approved as actuarially equivalent coverage. With respect to amounts above the out-of-pocket threshold, see the definitions of "Reinsurance Payment" and "Part D Payment Demonstration."

Supplemental Benefits – Benefits in excess of the standard coverage. These benefits typically will cover some portion of the deductible, the co-payments, or the coverage gap between the initial coverage limit and the out-of-pocket threshold. Supplemental benefits are part of an enrollee's Part D coverage, so they are not placed in the "Other" category in the RBC formula. However, they are not subject to either the reinsurance payment or the risk corridor payment adjustment, so they receive less favorable RBC treatment than the standard coverage.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO)

INT 06-02 Dates Discussed

March 5, 2006; June 11, 2006; September 10, 2006

INT 06-02 References

Current:
SSAP No. 26—Bonds
SSAP No. 30—Unaffiliated Common Stock
SSAP No. 32—Preferred Stock
SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies

INT 06-02 Issue

1. A certified capital company (CAPCO) is a state legislated venture capital firm that can be a partnership, corporation, trust or limited liability company, profit or not-for-profit, for which investors who invest cash to acquire an equity interest or qualified debt instrument receive state premium or income tax credit. Although these investments are sometimes termed by different acronyms, they will be referred to as a CAPCO for purposes of this issue.

2. A reporting entity that qualifies as a certified investor typically earns, in the year the investment is made, a vested credit against state premium or income taxes equal to greater than 100% of the investor's investment of certified capital, of which a certain percent (varies by state; example: 10%, 25%) may be taken in any taxable year. The credit to be applied in any one year may not exceed the entity's state premium or income tax liability for the taxable year. Any unused tax credit may be carried forward until the premium or income tax credit is used (varies by state; some indefinitely, in other instances there is a specified expiration date, such as 2010; 2020). In some cases, a certified investor may transfer or assign unused premium or income tax credits. In addition to tax credits, the CAPCO often pays a nominal amount of interest and has a specified principal repayment date. The CAPCO often provides for a mechanism that guarantees the principal repayment.

3. Depending on the terms of the agreement, a CAPCO may make prepayments of principal and interest on its indebtedness.

4. The accounting issues are:

Issue 1: How should investments in a CAPCO be accounted for?

Issue 2: If the CAPCO agreement provides for the majority of interest to be paid in advance, how should it be earned?

INT 06-02 Discussion

5. For Issue 1, the Working Group came to a consensus that reporting entities should account and report for investments in CAPCO's consistent with the agreement structure within the guidance provided below:

a. Investment in a debt instrument of a CAPCO shall be reported as a bond in accordance with the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and the designation assigned in the *NAIC Valuations of Securities* product prepared by the

NAIC Securities Valuation Office (Valuations of Securities manual) as stated in SSAP No. 26, paragraph ~~1120~~21.

b. Investment in an equity interest of a CAPCO shall be reported as common stock and reported at fair value as stated in SSAP No. 30, paragraph 9.

c. Investment in preferred stock interest of a CAPCO shall be reported as preferred stock in accordance with the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and the designation assigned in the *NAIC Valuations of Securities* product prepared by the NAIC Securities Valuation Office (Valuations of Securities manual) as stated in SSAP No. 32, paragraphs 20-23.

d. Investment in a Joint Venture, Partnership and Limited Liability Company (LLC) shall be reported in accordance with SSAP No. 48, paragraphs ~~5-6~~6-7. The reported value of the investment shall be decreased in proportion to the premium tax credits utilized.

e. The tax credits shall be recognized as a reduction of the tax liabilities as they are utilized. Tax credits received are not to be included in investment income.

6. For Issue 2, the Working Group came to a consensus that reporting entities should account for any prepaid interest received by the insurer to be recorded as an unearned interest liability and should be amortized over the life of the security. This is consistent with the treatment of prepaid interest in SSAP No. 37 and SSAP No. 49. This is also consistent with SSAP No. 34, which states that gross investment income should be reported as earned, and includes a change in unearned investment income.

INT 06-02 Status

7. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-07: Definition of Phrase "Other Than Temporary"

INT 06-07 Dates Discussed

September 10, 2006; December 10, 2006; December 11, 2023; January 10, 2024

INT 06-07 References

Current:
SSAP No. 26—Bonds
SSAP No. 30—Unaffiliated Common Stock
SSAP No. 32—Preferred Stock
SSAP No. 37—Mortgage Loans
SSAP No. 39—Reverse Mortgages
SSAP No. 41—Surplus Notes
SSAP No. 43—Asset-Backed Securities
SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies
SSAP No. 68—Business Combinations and Goodwill
SSAP No. 93—Investments in Tax Credit Structures
SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities
SSAP No. 105—Working Capital Finance Investments

Superseded:
SSAP No. 88—Investments in Subsidiary, Controlled, and Affiliated Entities, A Replacement of SSAP No. 46
SSAP No. 98—Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43—Loan-Backed and Structured Securities
SSAP No. 99—Accounting for Certain Securities Subsequent to an Other-Than-Temporary Impairment

Affects:
Nullifies the prior interpretation on this topic, *INT 02-07 Definition of Phrase "Other Than Temporary"*

INT 06-07 Issue

1. The *Accounting Practices and Procedures Manual* contains guidance for determining when an investment is considered impaired within each of the above identified statements. Those statements should also be used to determine the measurement of an impairment loss. Each of the above statements also makes reference to an "other than temporary" decline in fair value. This interpretation is designed to address questions related to that phrase, as well as summarize the statutory accounting process for determining when an investment is considered impaired.

Step 1: Determine Whether an Investment Is Impaired

2. The decision for determining when an investment is considered impaired is dictated by the applicable SSAP and the respective impairment indicators included in each of the SSAPs. If an impairment indicator is present, the determination of an impairment shall be assessed at the individual security or investment level as reported in the annual statement and supporting schedules. For those SSAPs that require the reporting entity to use the fair value to determine if an impairment has occurred, the determination of that value shall be consistent with how the term fair value is defined within *SSAP No. 100—Fair Value*. Once a reporting entity has determined that an impairment indicator is present, the reporting entity shall continue to evaluate whether the investment is impaired each subsequent reporting

period until either (a) the investment experiences a recovery of the fair value up to (or beyond) its carrying value or (b) the investor recognizes an other-than-temporary impairment loss.

Step 2: Evaluate Whether an Impairment Is Other Than Temporary

3. There are numerous factors to be considered when determining whether an impairment is other than temporary and their relative significance will vary from case to case. The Emerging Accounting Issues (E) Working Group (Working Group) has been asked if the phrase "other than temporary" should be interpreted to mean "permanent." The Working Group[1] believes the Statutory Accounting Principles (E) Working Group consciously chose the phrase "other than temporary" as the analysis was not intended to determine whether an individual security or investment was "permanently impaired." The fair value of assets may decline for various reasons. The market price may be affected by general market conditions, which reflect prospects for the economy as a whole, or by specific information pertaining to an industry or an individual company. Such declines require further investigation by management. Acting upon the premise that a write-down may be required, management should consider all available evidence to evaluate the fair value of its investment.

4. The Working Group believes that the following items are only a few examples of the factors, which, individually or in combination, indicate that a security's decline in value is specific to an issuer's fundamental credit difficulties, or that a non-interest related decline is other than temporary and that a write-down of the carrying value is required:

a. The length of time and the extent to which the fair value has been less than cost;

b. The financial condition and short-term prospects of the issuer, including any specific events that may influence the operations of the issuer, such as changes in technology, that may impair the earnings potential of the asset or the discontinuance of a segment of the business that may affect the future earnings potential; or

c. The intent and ability of the holder to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in value.

5. An interest related impairment should be deemed other-than-temporary when an investor has the intent to sell an investment, at the reporting date, before recovery of the cost of the investment. The investor should consider whether its cash or working capital requirements and contractual or regulatory obligations indicate that the investment may need to be sold before the forecasted recovery occurs. The term "interest related" includes a declining value due to both increases in the risk free interest rate and general credit spread widening. Credit spreads can widen or contract for a variety of reasons, including supply/demand imbalances in the marketplace or perceived higher/lower risk of an entire sector. If the declining value is caused, in whole or in part, due to credit spreads widening, but not due to fundamental credit problems of the issuer, the change in credit spreads is deemed to be interest related. Fundamental credit problems exist with the issuer when there is evidence of financial difficulty that may result in the issuer being unable to pay principal or interest when due.

6. Unless evidence exists to support the assertion that the decline in fair value below carrying value is temporary, a write-down, accounted for as a realized loss, should be recorded. In accordance with the guidance of the SSAPs, such loss should be recognized in income for the period in which other than temporary impairment is determined to have occurred. The adjusted carrying value reflecting the impairment loss of the individual security or investment shall be the new cost basis of the individual security or investment.

1 The recommendations provided by the Working Group were developed in part from SEC Staff Accounting Bulletin No. 59–*Noncurrent Marketable Equity Securities* (SAB 59). As such, readers of this interpretation should understand that SAB 59 has not been adopted as part of Statutory Accounting Principles as SAB's are not part of the Statutory Hierarchy (see Preamble).

7. The Working Group has also been asked if it is appropriate for reporting entities, independent auditors or state examiners to apply predefined thresholds to the phrase "other than temporary"? The Working Group is aware that certain insurers, independent auditors and state examiners, over time, have developed quantitative thresholds as "rules of thumb" to assist in the evaluation of asset impairment. One rule of thumb in particular suggests that if the fair value is less than its carrying value by 20 percent or more, then it is considered to be other than temporarily impaired. Another suggests that an asset is other than temporarily impaired if the fair value has been less than cost for more than 6 months. The use of a numerical threshold may provide the basis for a preliminary assumption that – without considering all relevant circumstances – an impairment may have occurred. Identifying the impairment is only the beginning of the analysis; it cannot appropriately be used as a substitute for a full analysis of all relevant qualitative considerations. Exclusive reliance on such thresholds removes the ability of management to apply its judgment, a concept inherent to the impairment model.

Step 3: If the Impairment is Other Than Temporary, the Cost Basis of the Individual Asset Shall Be Written Down to a New Cost Basis and the Amount of the Write-Down Is Accounted for as a Realized Loss

8. If an impairment is considered other than temporary, the cost or carrying value of the asset should be written down to reflect its value in accordance with the relevant SSAP. A company's management should follow the impairment guidance in the SSAP pertaining to that particular asset class while considering various factors on a case-by-case basis in determining the amount of the realized loss that should be recorded.

INT 06-07 Discussion

9. The Working Group reached a consensus to adopt with modification paragraph 6, 7 and 11 of *FSP FAS115-1/124-1: The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (FSP FAS 115-1/124-1). This INT rejects paragraphs 1-5, 8-10, 12-15, and 19 of FSP FAS 115-1/124-1. This INT does not address paragraphs 16-18 and footnote 1 to paragraph 7 of FSP FAS115-1/124-1.

10. Paragraphs 3-8 of this interpretation incorporate the guidance that was in *INT 02-07: Definition of Phrase "Other Than Temporary*," paragraphs 3-9, with an addition to clarify the general credit spread widening that was discussed in INT 02-07, paragraph 6. On final adoption of this interpretation, INT 02-07 is nullified.

11. FSP FAS 115-1/124-1 nullified the requirements of paragraphs 10-18 of EITF 03-01: *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (EITF 03-1) and carried forward the requirements of paragraphs 8, 9, 21 and 22 of the EITF to the FSP. The Working Group notes that the remaining paragraphs of EITF 03-01 either primarily related to the EITF process or are inconsistent with the current statutory model for impairment and are rejected. The Statutory Accounting Principles (E) Working Group is separately considering the disclosures related to the FSP.

12. FSP EITF 03-1-1: Effective Date of Paragraphs 10-20 of EITF Issue No. 03-1 (FSP EITF 03-1-1) was issued by the EITF on September 30, 2004, and delayed the effective date for the measurement and recognition guidance contained in paragraphs 10-20 of EITF 03-1. The delay of the effective date for paragraphs 10-20 of Issue 03-1 was superseded concurrent with the final issuance of FSP FAS 115-1/124-1 and as such, is rejected.

13. Effective December 31, 2023, the Working Group rejected *ASU 2016-13 Financial Instruments–Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, ASU 2018-19 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, ASU 2019-04 Codification Improvements to Topics 326, 815, 825, ASU 2019-10 Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases*

(Topic 842), ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments—Credit Losses, and *ASU 2020-03 Codification Improvements to Financial Instruments*. As a result, companies should continue to apply the relevant statutory accounting impairment guidance, which may reflect prior U.S. GAAP guidance.

INT 06-07 Status

14. INT 06-07 nullifies *INT 02-07: Definition of Phrase "Other Than Temporary."*

15. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-12: Tax Deposits Submitted in Accordance with Section 6603 of the Internal Revenue Service (IRS) Code

INT 06-12 Dates Discussed

September 10, 2006; December 10, 2006

INT 06-12 References

Current:
SSAP No. 101—Income Taxes

Superseded:
SSAP No. 10R—Income Taxes – A Temporary Replacement of SSAP No. 10

INT 06-12 Issue

1. The American Jobs Creation Act of 2004 enacted on October 22, 2004, added new section 6603 to the Internal Revenue Service Code (the Code) to permit a taxpayer to make a deposit with the Internal Revenue Service to suspend the running of interest under section 6601 on a potential underpayment of tax. A deposit may be made with respect to certain underpayments of tax that have not been assessed at the time of the deposit.

2. Section 6603(a) provides that a taxpayer may make a deposit with the Service that may be used by the Secretary to pay any income, gift, estate, or generation-skipping taxes imposed on the taxpayer under the Code, or certain excise taxes imposed on the taxpayer under the Code. Section 6603(b) provides that, to the extent that a deposit is used by the Service to pay tax, the tax shall be treated as paid on the date the deposit is made for purposes of computing interest on underpayments under section 6601.

3. Section 6603(c) provides that the Service will return to the taxpayer any amount of a deposit that the taxpayer requests in writing be returned unless the amount has previously been used to pay tax or the Service determines that collection of tax is in jeopardy.

4. The accounting issue is whether protective tax deposits meet the definition of current income tax recoverable as that term is used in SSAP No. 101, paragraph 9.

INT 06-12 Discussion

5. The Working Group reached a consensus that deposits made with the Internal Revenue Service, as described in paragraphs 1-3 of this interpretation, meet the definition of a current income tax recoverable as defined in SSAP No. 101, paragraph 9, as the reporting entity has made the deposit under its substantial authority and the deposit can be recovered upon written request.

6. Section 6603 tax deposits are admitted assets to the extent the section 6603 tax deposit complies with SSAP No. 101 and this guidance. The reporting entity shall report section 6603 tax deposits as assets within the caption "Current Federal and Foreign Income Tax Recoverable and Interest thereon." The section 6603 tax deposit asset and any related tax liability shall be presented on a gross basis for statutory reporting purposes.

Calculating Nonadmission

7. The reporting entity shall expense amounts previously used to pay tax.

8. The reporting entity shall nonadmit:

   a. amounts the Service has determined, or the reporting entity estimates it is probable the Service will determine, that collection of the tax from the reporting entity is in jeopardy for section 6603 tax deposit amounts in excess of the specifically established tax liability, or

   b. any portion of the deposit that the reporting entity does not reasonably expect to be recovered in a subsequent accounting period for section 6603 tax deposit amounts in excess of specifically established tax liability.

9. The term “specifically established tax liability” is a liability, that for financial reporting purposes, the reporting entity has recognized relating to the IRS Section 6603 tax deposit. The reporting entity intends this “specifically established tax liability” to be settled by applying the section 6603 tax deposit. In calculating nonadmission discussed in the paragraph 8, the reporting entity shall deduct the specifically accrued tax liability prior to the determination of whether the remaining amounts should be nonadmitted.

10. To illustrate the nonadmission criteria, consider the following two situations:

   a. IAOA insurer has a 6603 tax deposit of $100,000 and a federal income tax liability of $30,000 that IAOA intends to pay in the normal course of business. IAOA would not consider the tax liability when determining nonadmission of the section 6603 tax deposit. IAOA is not aware of any situations which would indicate that use of the deposit is in question and would admit the entire $100,000 tax deposit.

   b. TAI insurer has a $110,000 section 6603 tax deposit and has been notified by its tax department that an adverse tax finding of $45,000 was probable and may result in significant interest penalties. TAI recorded a “specifically established tax liability” of $45,000 and intends to use the section 6603 tax deposit to settle the $45,000 adverse tax finding. In determining the amount of the 6603 tax deposit to nonadmit, TAI would determine the amount in excess of the “specifically established tax liability, which is $65,000 ($110,000 – $45,000). This net amount of $65,000 is then evaluated for nonadmission, based on other relevant factors, if any. To continue the illustration, TAI became aware of an additional situation at the reporting date, which indicated that $10,000 of the section 6603 tax deposit is not reasonably expected to be recovered in a subsequent accounting period . As a result, TAI would nonadmit $10,000 of the tax deposit.

INT 06-12 Status

11. No further discussion is planned. The Working Group noted that *FIN 48: Accounting for Uncertainty in Income Tax, an interpretation of FASB Statement No. 109* (FIN 48) is pending review by the Statutory Accounting Principles (E) Working Group has the potential to impact the consensus in this interpretation. The Working Group will consider if the interpretation requires updating after the review of FIN 48 is complete.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 06-13: EITF 01-2: Interpretations of APB Opinion No. 29

INT 06-13 Dates Discussed

September 10, 2006; December 10, 2006

INT 06-13 References

Current:
SSAP No. 40—Real Estate Investments
SSAP No. 95—Nonmonetary Transactions

Superseded:
SSAP No. 77—Real Estate Sales – An Amendment to SSAP No. 40—Real Estate Investments

INT 06-13 Issue

1. The introduction to issues as described in *EITF 01-2: Interpretations of APB Opinion No. 29* is as follows:

> 1. The basic principle in Opinion 29 is that the accounting for nonmonetary transactions should be based on the fair values of the assets (or services) exchanged. The cost of a nonmonetary asset acquired in exchange for another nonmonetary asset is the fair value of the asset surrendered to obtain it, and a gain or loss for the difference between the carrying amount of the surrendered asset and its fair value should be recognized on the exchange. The fair value of the asset received should be used to measure the fair value of the asset surrendered (and the cost of the asset received) if it is more clearly evident than the fair value of the asset surrendered. Opinion 29 includes several modifications to that principle in circumstances in which (a) fair values of the assets exchanged are not readily determinable (paragraph 20.a. of Opinion 29), (b) the assets exchanged are products or properties held for sale in the same line of business to facilitate sales to customers other than the parties to the exchange (paragraph 20.b. of Opinion 29), (c) the assets exchanged are similar productive assets not held for sale in the ordinary course of business, [Note: See paragraph 44 of the STATUS section.] (d) the exchange involves an amount of monetary consideration (paragraph 22 of Opinion 29), and (e) the transaction represents a nonreciprocal transfer to owners (paragraph 23 of Opinion 29). Over the years, the Task Force has addressed several issues relating to the guidance in Opinion 29. The purpose of this Issue is to codify and reconcile the following Issues:
>
> *Issue No. 86-29, "Nonmonetary Transactions: Magnitude of Boot and the Exceptions to the Use of Fair Value"* (paragraphs 4-6, and 18-19)
>
> *Issue No. 87-17, "Spinoffs or Other Distributions of Loans Receivable to Shareholders"* (paragraphs 28-29)
>
> *Issue No. 87-29, "Exchange of Real Estate Involving Boot"* (paragraphs 25-27)
>
> *Issue No. 89-7, "Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity"* (paragraphs 21-24)
>
> *Issue No. 96-2, "Impairment Recognition When a Nonmonetary Asset Is Exchanged or Is Distributed to Owners and Is Accounted for at the Asset's Recorded Amount*" (paragraphs 33-39)
>
> *Issue No. 96-4, "Accounting for Reorganizations Involving a Non–Pro Rata Split-off of Certain Nonmonetary Assets to Owners"* (paragraphs 30-32)

Issue No. 98-7, "Accounting for Exchanges of Similar Equity Method Investments" (paragraph 11)

Issue No. 00-5, "Determining Whether a Nonmonetary Transaction Is an Exchange of Similar Productive Assets" (paragraphs 2-3, 9-10, and 12-17).

The Task Force observed that the transition guidance for the above Issues is governed by the original consensuses on those Issues.

2. As described in paragraph 44 in the STATUS section of *EITF 01-2, FAS 153: Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29* (FAS 153), was issued in December 2004 and eliminated the fair value measurement exception for nonmonetary exchanges of similar productive assets provided in APB 29 and replaces it with an exception from fair value measurement for nonmonetary exchanges that lack commercial substance. As a result, FAS 153 nullifies Issues 1(b), 1(c), 2-5, and 7 since those issues interpret the exception to fair value measurement for similar productive assets that was eliminated by FAS 153. FAS 153 was adopted with modification in *SSAP No. 95—Nonmonetary Transactions*. *FAS 144: Accounting for the Impairment or Disposal of Long-Lived Assets*, also amended APB 29 and resolved issues 13(a) and 13(b) of EITF 01-2. FAS 144 was adopted with modification in *SSAP No. 90—Impairment or Disposal of Real Estate Investments*. This interpretation addresses the remaining issues of EITF 01-2.

3. The following EITF issues listed above were adopted, rejected or determined to be not applicable to statutory accounting principles in their entirety, as follows:

- *EITF Issue No. 86-29, "Nonmonetary Transactions: Magnitude of Boot and the Exceptions to the Use of Fair Value*" – adopted in *SSAP No. 95—Nonmonetary Transactions*
- *EITF Issue No. 87-17, "Spinoffs or Other Distributions of Loans Receivable to Shareholders"* – determined to be not applicable to statutory accounting principles
- *EITF Issue No. 87-29, "Exchange of Real Estate Involving Boot*" – adopted in *SSAP No. 40—Real Estate Investments*
- *EITF Issue No. 89-7, "Exchange of Assets or Interest in a Subsidiary for a Noncontrolling Equity Interest in a New Entity"* – rejected in *SSAP No. 68—Business Combinations and Goodwill*
- *EITF Issue No. 96-4, "Accounting for Reorganizations Involving a Non-Pro Rata Split-off of Certain Nonmonetary Assets to Owners"* – rejected in *SSAP No. 95—Nonmonetary Transactions*

4. As EITF 01-2 was adopted to codify or reconcile the issues included in paragraph 1 of this interpretation, each issue will be described and discussed in paragraphs 5-18 of this interpretation.

INT 06-13 Discussion

5. Issue 6 and guidance per EITF 01-2:

Issue 6—If a nonmonetary exchange is required to be accounted for at fair value, whether full or partial gain recognition is appropriate in a circumstance in which one entity (Entity A) transfers its ownership of either a controlled productive asset or assets or a controlled business to another entity (Entity B) in exchange for a noncontrolling ownership interest in that entity (Entity B).

16. The Task Force reached a consensus on Issue 6 that if the fair value of the asset(s) given up (or of the ownership interest received if the fair value of that asset is more readily determinable) is less than its carrying value, that difference should be recognized as a loss.

[Note: See STATUS section.] If the fair value of the asset(s) given up (or of the ownership interest received if that asset's fair value is more readily determinable) is greater than its carrying value, then (a) a gain in the amount of that difference should be recognized if the entity accounts for the ownership interest received using the cost method, or (b) a partial gain should be recognized if the entity accounts for the ownership interest received using the equity method. The partial gain should be calculated as the amount described in (a), above, less the portion of that gain represented by the economic interest (which may be different from the voting interest) retained. For example, if Entity A exchanges an asset with a carrying value of $1,000 and a fair value of $2,000 for a 30 percent economic interest in Entity B, Entity A should recognize a gain of $700 [($2,000 - $1,000) × 70%]. Thus, the amount recorded for the ownership interest received is partially based on its fair value at the exchange date and partially based on the carryover amount of the asset(s) surrendered.

17. The Task Force observed that paragraph 20 of Opinion 29 requires that the accounting for a nonmonetary transaction subject to Opinion 29 should not be based on the fair values of the assets transferred unless those fair values are determinable within reasonable limits.

6. The STATUS section of EITF 01-2 states the following relative to Issue 6:

45. Issue 6 addresses whether full or partial gain recognition is appropriate in circumstances in which an entity transfers its ownership of either a controlled productive asset (or assets) or a controlled business to another entity in exchange for a noncontrolling ownership interest in that entity. Statement 153 amends the scope of Opinion 29 to exclude a transfer of assets to an entity in exchange for an equity interest in that entity. Statement 153 also amends Statement 140 to remove the scope exception in Statement 140 for exchanges of equity method investments for similar productive assets. Accordingly, transfers of equity method investments in exchange for other assets should be accounted for in accordance with Statement 140. However, Opinion 29 (as amended by Statement 153) and Statement 140 do not provide guidance on the accounting for transfers of nonfinancial assets in exchange for other assets. Therefore, the guidance in Issue 6 should continue to be applied in circumstances in which an entity transfers a nonfinancial asset (or assets) to another entity in exchange for a noncontrolling ownership interest in that entity and the exchange is required to be accounted for at fair value.

7. The Working Group reached a consensus to adopt the EITF 01-2 for Issue 6 guidance believing the economic interest relates to the ownership interest of Entity B in the above issue. This may or may not be different from the voting interest or controlling interest of Entity B. However, the GAAP guidance above for Issue 6 determines the proper accounting for the transactions between unrelated parties relative to the gain or loss on the nonmonetary transaction. This guidance establishes the cost basis for the ownership interest in Entity B to be recorded by Entity A. Subsequent to the transactions, existing guidance should apply for the ownership interest. For statutory purposes, the valuation of this ownership interest would then follow existing statutory guidance (e.g., *SSAP No. 30—Unaffiliated Common Stock* for Common Stock, *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* for Joint Ventures, *SSAP No. 97—Investments in Subsidiary, Controlled, and Affiliated Entities* for investments in SCA entities, etc.)

8. Issue 8 and guidance per EITF 01-2:

Exchanges Involving Monetary Consideration (Paragraph 22 of Opinion 29)

Issue 8(a)—What level of monetary consideration in a nonmonetary exchange causes the transaction to be considered monetary in its entirety and, therefore, outside the scope of Opinion 29.

19. The Task Force discussed an exchange of nonmonetary assets that would otherwise be based on recorded amounts but that also involves monetary consideration (boot). The Task Force reached a consensus that that transaction should be considered monetary (rather than nonmonetary) if the boot is significant, and agreed that "significant" should be defined as at least

25 percent of the fair value of the exchange. As a monetary transaction, both parties would record the exchange at fair value[1] (as discussed in Issue 8(b), below). If the boot in a transaction is less than 25 percent, the pro rata gain recognition guidance in paragraph 22 of Opinion 29 should be applied by the receiver of boot, and the payer of boot would not recognize a gain. The Task Force acknowledged that the ability to satisfactorily measure fair value is a prerequisite to the use of fair value.

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[1] For real estate transactions, see Issue 10.

Issue 8(b)—In a monetary exchange (required to be accounted for at fair value), whether "full or partial" gain recognition is appropriate if an entity transfers its ownership of a controlled asset, group of assets, or business to another entity in exchange for a noncontrolling ownership interest in the other entity.

20. The Task Force reached a consensus on Issue 8(b) that the gain should be computed in a manner consistent with the consensus reached in Issue 6. The Task Force reached a consensus that application of the consensus on Issue 8(b) is required for exchange transactions committed to after April 19, 2001. A transaction is committed to if the parties to the transaction have signed a binding, written agreement that specifically sets forth the principal provisions of the transaction. If any of the principal provisions are yet to be negotiated, or are subsequently changed, such a preliminary agreement does not qualify as a commitment for purposes of this consensus.

9. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issues 8(a) and 8(b) without modification.

10. Issue 9 and guidance per EITF 01-2:

Issue 9—In the monetary exchange described below, whether the amount of gain recognized should exceed the amount that would be computed pursuant to the guidance for Issue 8(b).

21. An enterprise transfers its ownership of an individual asset (or assets) or its ownership interest in a subsidiary to a newly created entity in exchange for an ownership interest in that entity that will be accounted for by the equity method and monetary consideration. The monetary consideration received exceeds the fair value of the portion of the surrendered asset that has been sold in the exchange. The excess monetary consideration is funded by proceeds from nonrecourse financing within the newly created entity. Subsequent to the transfer, the enterprise does not control the entity. The specifics of the transaction are as follows:

- Company A owns equipment with a book basis of $100 and an appraised value of $400.
- Company B, previously unrelated to Company A, creates a new subsidiary, Company X, and transfers cash of $60 to Company X.
- Company A transfers the equipment to Company X in exchange for shares of Company X stock that represent a 40 percent ownership interest in Company X. Simultaneously, Company X borrows $300 with recourse to only the equipment and pays Company A $360 cash.

22. The Task Force reached a consensus that if the enterprise has no actual or implied commitment, financial or otherwise, to support the operations of the new entity in any manner, a gain of $260 should be recognized. The investor's basis in the new entity should be no less than zero. The gain calculation is illustrated as follows:

Fair value of interest in equipment sold ($400 × 60%)	$ 240
Less: Cost of interest in equipment sold ($100 × 60%)	(60)
	$ 180
Plus: Additional gain to the extent of the negative investment	80*
Total gain recognized	$ 260

* The additional gain is calculated as follows:

Cost of equipment	$100
Less: Cost of interest in equipment sold	(60)
Remaining cost	40
Less: Cash received in excess of 60% of the equipment's fair value	(120)
Negative investment	$ (80)

23. Task Force members noted that specific facts and circumstances may affect gain recognition and that it would be impractical for the Task Force to consider all possible variations of the basic transaction described above.

24. The SEC Observer emphasized that any gain recognition is heavily dependent on a careful analysis of specific facts and circumstances. Gain recognition would not be appropriate if a significant uncertainty exists regarding realization or the enterprise has an actual or implied commitment to support the operations of the new entity in any manner (see, for example, SAB 81).

11. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issue 9 without modification. The Working Group also noted the following facts are important to this consensus:

- The monetary consideration in the example is considered significant under the consensus of Issue 8(b), and as such, Issue 9 is considered a **monetary exchange**.
- The monetary consideration received by Entity A in the transaction **exceeds the fair value of the portion of the surrendered asset**.
- The excess monetary consideration is funded by proceeds from nonrecourse financing within Company X. The $300 borrowing with recourse described in the example explicitly states **the recourse is only to the equipment and is not related to Entity A**.
- Prior to the transaction, Entity A and Entity B are unrelated parties. In exchange for the equipment, **Entity A receives shares of Company X stock representing a 40 percent ownership interest**.

In the example above, the monetary consideration received exceeds the fair value of the portion of the surrendered asset that has been sold in the exchange. When this occurs, additional gain should be recognized to ensure the basis in the ownership interest is not less than zero.

12. Issue 10 and guidance per EITF 01-2:

Exchanges of Real Estate Involving Monetary Consideration (Paragraph 22 of Opinion 29)

25. Statement 66 indicates that the accounting for exchanges of real estate is covered by Opinion 29 and not by Statement 66. However, as discussed above in Issue 8(a), the Task Force reached a consensus that an exchange of nonmonetary assets that would otherwise be based on recorded amounts under paragraph 21 of Opinion 29 but that involves boot should be considered a monetary (rather than nonmonetary) transaction if the boot is at least 25 percent of the fair value of the exchange. As a result, the Task Force reached a different consensus for exchanges

of either (a) real estate held for sale in the ordinary course of business for real estate to be sold in the same line of business or (b) real estate not held for sale in the ordinary course of business for similar real estate when the boot is at least 25 percent of the fair value of the exchange. (Those types of exchanges are referred to in Issues 10(a) and 10(b) as exchanges of similar real estate.)

Issue 10(a)—Whether Statement 66 applies to an exchange of similar real estate that is not subject to Opinion 29 because the transaction involves enough boot for the exchange to be considered monetary under the consensus for Issue 8(a).

26. The Task Force reached a consensus that a transaction involving an exchange of similar real estate that is considered a monetary transaction under Issue 8(a) because boot is at least 25 percent of the fair value of the exchange would be allocated between two components: a monetary portion and a nonmonetary portion. [Note: See STATUS section.] The allocation between the monetary and nonmonetary portions of the transaction should be based on their relative fair values at the time of the transaction. A Task Force member noted that Interpretation 43 provides guidance on when an asset is considered real estate.

Issue 10(b)—If applicable, how Statement 66 should be applied.

27. The Task Force reached a consensus that for the receiver of boot, the monetary portion would be accounted for under Statement 66 as the equivalent of a sale of an interest in the underlying real estate, and the nonmonetary portion would be accounted for based on the recorded amount (after reduction, if appropriate, for an indicated impairment in value) of the nonmonetary asset relinquished pursuant to paragraph 21 of Opinion 29. [Note: See STATUS section.] For the payer of boot, the monetary portion would be accounted for as an acquisition of real estate, and the nonmonetary portion would be accounted for pursuant to paragraph 21 of Opinion 29. Following is an example of the application of this consensus:

Assumptions

- Party A transfers real estate with a fair value of $2,000,000 (Party A's net book value of $1,500,000) to Party B and receives $400,000 cash, a $400,000 note from Party B payable to Party A, and real estate with a fair value of $1,200,000 (Party B's net book value of $800,000).
- The initial investment requirement for full accrual profit recognition under Statement 66 is 20 percent.
- The terms of the note from Party B to Party A would satisfy the continuing investment provisions necessary for application of the full accrual method. The interest rate on the note from Party B is a market rate, and the note is considered fully collectible.
- The values of the real estate transferred by both parties are readily determinable and clearly realizable at the exchange date.
- Neither party has any continuing involvement with the real estate transferred to the other.

Computation of Allocation by Both Party A and Party B

Monetary Portion of Transaction:

Total monetary consideration divided by total fair value of exchange	$800,000 ÷ $2,000,000 = 40%

For this example, the monetary portion of the transaction is the exchange of $400,000 cash and a $400,000 note for real estate with a fair value of $800,000 ($2,000,000 x 40%).

Nonmonetary Portion of Transaction:

Fair value of real estate exchanged divided by total fair value of exchange	$1,200,000 ÷ $2,000,000 = 60%

For this example, the nonmonetary portion of the transaction is the exchange of real estate with a fair value of $1,200,000 for similar real estate with a fair value of $1,200,000 ($2,000,000 x 60%).

Accounting by Party A (the Receiver of Monetary Consideration)

The monetary portion of the transaction qualifies for full accrual profit recognition because the cash down payment of $400,000 and the $400,000 note meet the criteria in paragraphs 9-12 of Statement 66 for a buyer's initial and continuing investment when applied to the monetary portion of the transaction. Accordingly, a gain of $200,000 ($800,000 total monetary consideration less $600,000 [$1,500,000 total net book value x 40%] pro rata portion of net book value) would be recorded at the date of sale.

The nonmonetary portion of the transaction does not qualify for gain recognition because the exchange involves similar real estate. The accounting basis of the new property equals $900,000 ($1,500,000 total net book value of the real estate exchanged less the $600,000 pro rata portion of net book value sold).

Accounting by Party B (the Payer of Monetary Consideration)

The monetary portion of the transaction represents an acquisition of real estate for the monetary consideration paid of $800,000.

The nonmonetary portion of the transaction does not qualify for gain recognition because the exchange involves similar real estate. The accounting basis of the new property equals $1,600,000 ($800,000 net book value of the real estate exchanged plus $800,000 total monetary consideration paid).

13. The STATUS section of EITF 01-2 states the following relative to Issues 10(a) and 10(b):

46. Issues 10(a) and 10(b) previously addressed circumstances in which an entity is involved in a real estate exchange that meet the following conditions: (1) the exchange includes boot that is at least 25 percent of the fair value of the exchange and (2) the exchange is either (a) real estate held for sale in the ordinary course of business for real estate to be sold in the same line of business or (b) real estate not held for sale in the ordinary course of business for similar real estate. Statement 153, however, eliminates the fair value measurement exception for nonmonetary exchanges of similar productive assets provided in Opinion 29 and replaces it with an exception from fair value measurement for nonmonetary exchanges that lack commercial substance. Therefore, Issues 10(a) and 10(b) address circumstances in which an entity is involved in a real estate exchange that meets the following conditions: (1) the exchange includes boot that is at least 25 percent of the fair value of the exchange and (2) the exchange meets one of the conditions set forth in paragraph 20 of Opinion 29.

14. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issues 10(a) and 10(b) with the modification to replace references to FAS 66: *Accounting for Sales of Real Estate* with references to *SSAP No. 40—Real Estate Investments*. In addition, reporting entities should note that as a result of the issuance of FAS 153, Issues 10(a) and 10(b) address circumstances in which an entity is involved in a real estate exchange that meets the following conditions: (1) the exchange includes boot that is at least 25 percent of the fair value of the exchange and (2) the exchange meets one of the conditions set forth in paragraph 20 of Opinion 29.

15. Issue 11 and guidance per EITF 01-2:

Nonreciprocal Transfers to Owners (Paragraph 23 of Opinion 29)

Spinoffs or Other Distributions of Loans Receivable to Shareholders

28. An enterprise distributes loans receivable to its owners by forming a subsidiary, transferring those loans receivable to the subsidiary, and then distributing the stock of that subsidiary to shareholders of the parent.

Issue 11—Whether the enterprise should report the distribution at book value as a spinoff or at fair value as a dividend-in-kind if the book value of the loans receivable, which may be either the "recorded investment in the receivable" or the "carrying amount of the receivable," is in excess of their fair value, and how the recipient should record the transaction.

29. The Task Force reached a consensus that the distribution should be reported at fair value by the enterprise and the recipient. Task Force members noted that the transaction is not a spinoff because the subsidiary does not constitute a business.[4] Rather, the transaction should be considered a dividend-in-kind. Under paragraph 23 of Opinion 29, dividends-in-kind are nonreciprocal transfers of nonmonetary assets to owners that should be accounted for at fair value if the fair value of the nonmonetary asset distributed is objectively measurable and would be clearly realizable to the distributing entity in an outright sale at or near the time of distribution. On July 5, 1989, subsequent to the date of the consensus, the SEC staff issued SAB 82, which discusses accounting for transfers of nonperforming assets by financial institutions and disclosure of the impact of financial assistance from regulators. In discussing the value at which a transfer of nonperforming assets should be recorded by the transferor financial institution, SAB 82 makes reference to the Task Force consensus on Issue 10, that an enterprise that distributes loans to its owners should report such distribution at fair value.

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[4] Issue 98-3 provides guidance on determining whether an asset group constitutes a business.

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16. The Working Group reached a consensus to adopt the EITF 01-2 guidance with the modification to replace the reference to paragraph 23 of APB Opinion 29 with paragraph 12 of SSAP No. 95, the reference in footnote 4 to EITF Issue 98-3 shall be replaced with INT 00-26: *EITF 98-3: Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business*.

17. Issue 12 and guidance per EITF 01-2:

Accounting for Reorganizations Involving a Non–Pro Rata Split-off of Certain Nonmonetary Assets to Owners

30. Some believe that paragraph 23 of Opinion 29 requires that nonreciprocal transfers of nonmonetary assets to owners on a non-pro rata basis be accounted for at fair value, without regard to the nature of the nonmonetary assets distributed. Others believe that Opinion 29 requires historical cost accounting for corporate liquidations or reorganizations involving the distribution to owners of all or a significant segment of the business, whether in a spinoff, split-off, or split-up and whether or not the distribution is on a pro rata basis.

31. Although Opinion 29 does not define the term split-off, federal income tax law states that a split-off is a transaction in which a parent company exchanges its stock in a subsidiary for parent company stock held by its shareholders. For federal income tax purposes, the exchange of shares need not be pro rata to all shareholders, or even include all shareholders, in order to be considered a tax-free split-off.

Issue 12—Whether a non-pro rata split-off of all or a significant segment of a business in a corporate plan of reorganization should be accounted for at historical cost or at fair value.

> 32. The Task Force reached a consensus that a non-pro rata split-off of a segment of a business in a corporate plan of reorganization should be accounted for at fair value. The Task Force also reached a consensus that a split-off of a targeted business, distributed on a pro rata basis to the holders of the related targeted stock, should be accounted for at historical cost. The Task Force observed that if the targeted stock was created in contemplation of the subsequent split-off, the two steps (creation of the targeted stock and the split-off) cannot be separated and should be viewed as one transaction with the split-off being accounted for at fair value.

18. The Working Group reached a consensus to adopt the EITF 01-2 guidance for Issue 12 with the modification to replace references to paragraph 23 of APB Opinion 29 with paragraph 12 of SSAP No. 95.

INT 06-13 Status

19. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 07-01: Application of the Scientific (Constant Yield) Method in Situations of Reverse Amortization

INT 07-01 Dates Discussed

March 10, 2007; June 2, 2007; August 13, 2023

INT 07-01 References

Current:
SSAP No. 26—Bonds
SSAP No. 43—Asset-Backed Securities

Superseded:
SSAP No. 98—Treatment of Cash Flows When Quantifying Changes in Valuation and Impairments, an Amendment of SSAP No. 43—Loan-Backed and Structured Securities

INT 07-01 Issue

1. SSAP No. 26 and SSAP No. 43 both reference the use of the scientific or constant yield method of amortization of a premium or a discount. ~~*SSAP No. 26R—Bonds* provides the following (bolding added for emphasis):~~

~~**Amortized Cost**~~

~~9. **Amortization of bond premium or discount shall be calculated using the scientific (constant yield) interest method taking into consideration specified interest and principal provisions over the life of the bond.** Bonds containing call provisions (where the issue can be called away from the reporting entity at the issuer's discretion) shall be amortized to the call or maturity value/date which produces the lowest asset value (yield to worst).~~

~~*SSAP No. 43R—Loan-Backed and Structured Securities* provides the following (bolding added for emphasis):~~

~~**Amortization**~~

~~8. **Amortization of premium or discount shall be calculated using the scientific (constant yield) interest method** and shall be recorded as an adjustment to investment income. The interest method results in a constant effective yield equal to the prevailing rate at the time of purchase or at the time of subsequent adjustments to book value. The amortization period shall reflect estimates of the period over which repayment of principal of the loan-backed securities is expected to occur, not the stated maturity period.~~

~~**Collection of All Contractual Cashflows is Probable**~~

~~12. The following guidance applies to loan-backed and structured securities for which it is probable that the investor will be able to collect all contractually required payments receivable. (Paragraphs 17-19 provide guidance for securities in which collection of all contractual cash flows is not probable and paragraphs 20-24 provide guidance for beneficial interests.) Prepayments are a significant variable element in the cash flow of loan-backed securities because they affect the yield and determine the expected maturity against which the yield is evaluated. Falling interest rates generate faster prepayment of the mortgages underlying the security, shortening its duration. This causes the reporting entity to reinvest assets sooner than expected at potentially less advantageous rates. This is called prepayment risk. Extension risk is created by rising interest rates which slow repayment and can significantly lengthen the duration of the security.~~

~~Differences in cash flows can also result from other changes in the cash flows from the underlying assets. If assets are delinquent or otherwise not generating cash flow, which should be reflected in the cash flow analysis through diminishing security cash flows, even if assets have not been liquidated and gain/losses have not been booked.~~

~~13. Changes in currently estimated cash flows, including the effect of prepayment assumptions, on loan-backed securities shall be reviewed periodically, at least quarterly. The prepayment rates of the underlying loans shall be used to determine prepayment assumptions. Prepayment assumptions shall be applied consistently across portfolios to all securities backed by similar collateral (similar with respect to coupon, issuer, and age of collateral). Reporting entities shall use consistent assumptions across portfolios for similar collateral within controlled affiliated groups. Since each reporting entity may have a unique method for determining the prepayment assumptions, it is impractical to set standard assumptions for the industry. Relevant sources and rationale used to determine each prepayment assumption shall be documented by the reporting entity.~~

~~14. Loan-backed securities shall be revalued using the currently estimated cash flows, including new prepayment assumptions, using either the prospective or retrospective adjustment methodologies, consistently applied by type of securities. However, if at any time during the holding period, the reporting entity determines it is no longer probable that they will collect all contractual cashflows, the reporting entity shall apply the accounting requirements in paragraphs 17-19.~~

~~15. The prospective approach recognizes, through the recalculation of the **effective yield** to be applied to future periods, the effects of all cash flows whose amounts differ from those estimated earlier and the effects and changes in projected cash flows. Under the prospective method, the recalculated effective yield will equate the carrying amount of the investment to the present value of the anticipated future cash flows. The recalculated yield is then used to accrue income on the investment balance for subsequent accounting periods. There are no accounting changes in the current period unless the security is determined to be other than temporarily impaired.~~

~~16. The retrospective methodology changes both the yield and the asset balance so that expected future cash flows produce a return on the investment equal to the return now expected over the life of the investment as measured from the date of acquisition. Under the retrospective method, the recalculated **effective yield** will equate the present value of the actual and anticipated cash flows with the original cost of the investment. The current balance is then increased or decreased to the amount that would have resulted had the revised yield been applied since inception, and investment income is correspondingly decreased or increased.~~

2. This interpretation~~The following~~ identifies three situations where, using a constant yield methodology for determining amortization or accretion, changes in amortized value move in the opposite direction of what is expected. That is, if a security is purchased at a premium, the constant yield methodology will, in certain cases, cause the amortized value to move to a discount during the life of the security. Conversely, if the security were purchased at a discount, the constant yield methodology will, in certain cases, cause the amortized value to move to a premium during the life of the security.

Accounting Issues:

3. The fundamental accounting questions are

Issue 1: When applying the constant yield method to loan-backed or structured securities, can amortized value be interpreted to represent the discounted cash flows?

Issue 2: Should a security purchased at a premium be allowed to move to a discount, or should a discount be allowed to move to a premium, if this occurs as a result of applying the scientific (constant yield) interest method."

Issue 3: On the subject of Parity (described in example 3), is it appropriate under statutory accounting guideline to "assume away" day delay and subsequently eliminate amortizing to a value less than par? If so, should a payment date assumption or a record date assumption be used?

4. Following are practical situations where a security purchased at a premium will have increases in amortized value, and where a security purchased at a discount will have decreases in amortized value. The question is should the scientific (constant yield) method be interpreted to allow these securities to be amortized as illustrated below.

Example 1

5. This first example examines a stepped coupon bond purchased at a discount. At time of acquisition the future interest rate adjustments are known, and so are taken into account in the yield calculation. This example illustrates how a (theoretical) stepped coupon bond, without a call schedule, could result in the amortized value changing from a discount to a premium.

Description: FEDERAL HOME LN MTG CORP MTN
Maturity: 03-18-2019
Int Type: Stepped Coupon not callable
03/18/2004 4.000%
03/18/2007 6.000%
03/18/2013 8.000%
Purchase Date: 3/18/2004
Purchase Price: 97.125
Based on this information, the effective annual yield at acquisition is: 6.3246%

6. The following illustrates the semiannual amortization schedule determined at time of acquisition. The amortized values represent the sum of the discounted future cash flows at each payment date. Based on the purchase price and cash flow assumptions, the semiannual yield is 3.1623%.

Pay Date	Par Value	Interest Rate Annual	Interest Payment	Total Payment	Income	Accr Disc	Amort Value
3/18/2004	1,000,000.00			(971,250.00)			971,250.00
9/18/2004	1,000,000.00	4.0000%	20,000.00	20,000.00	30,713.97	10,713.97	981,963.97
3/18/2005	**1,000,000.00**	**4.0000%**	**20,000.00**	**20,000.00**	**31,052.78**	**11,052.78**	**993,016.75**
9/18/2005	**1,000,000.00**	**4.0000%**	**20,000.00**	**20,000.00**	**31,402.30**	**11,402.30**	**1,004,419.05**
3/18/2006	1,000,000.00	4.0000%	20,000.00	20,000.00	31,762.88	11,762.88	1,016,181.92
9/18/2006	1,000,000.00	4.0000%	20,000.00	20,000.00	32,134.86	12,134.86	1,028,316.78
3/18/2007	1,000,000.00	4.0000%	20,000.00	20,000.00	32,518.60	12,518.60	1,040,835.38
9/18/2007	1,000,000.00	6.0000%	30,000.00	30,000.00	32,914.48	2,914.48	1,043,749.86
3/18/2008	1,000,000.00	6.0000%	30,000.00	30,000.00	33,006.64	3,006.64	1,046,756.50
9/18/2008	1,000,000.00	6.0000%	30,000.00	30,000.00	33,101.72	3,101.72	1,049,858.22
3/18/2009	1,000,000.00	6.0000%	30,000.00	30,000.00	33,199.81	3,199.81	1,053,058.02
9/18/2009	1,000,000.00	6.0000%	30,000.00	30,000.00	33,300.99	3,300.99	1,056,359.02
3/18/2010	1,000,000.00	6.0000%	30,000.00	30,000.00	33,405.38	3,405.38	1,059,764.40
9/18/2010	1,000,000.00	6.0000%	30,000.00	30,000.00	33,513.07	3,513.07	1,063,277.47
3/18/2011	1,000,000.00	6.0000%	30,000.00	30,000.00	33,624.17	3,624.17	1,066,901.64
9/18/2011	1,000,000.00	6.0000%	30,000.00	30,000.00	33,738.77	3,738.77	1,070,640.41
3/18/2012	1,000,000.00	6.0000%	30,000.00	30,000.00	33,857.00	3,857.00	1,074,497.41
9/18/2012	1,000,000.00	6.0000%	30,000.00	30,000.00	33,978.98	3,978.98	1,078,476.39
3/18/2013	1,000,000.00	6.0000%	30,000.00	30,000.00	34,104.80	4,104.80	1,082,581.19
9/18/2013	1,000,000.00	8.0000%	40,000.00	40,000.00	34,234.61	(5,765.39)	1,076,815.80
3/18/2014	1,000,000.00	8.0000%	40,000.00	40,000.00	34,052.29	(5,947.71)	1,070,868.09
9/18/2014	1,000,000.00	8.0000%	40,000.00	40,000.00	33,864.20	(6,135.80)	1,064,732.30
3/18/2015	1,000,000.00	8.0000%	40,000.00	40,000.00	33,670.17	(6,329.83)	1,058,402.47
9/18/2015	1,000,000.00	8.0000%	40,000.00	40,000.00	33,470.00	(6,530.00)	1,051,872.47
3/18/2016	1,000,000.00	8.0000%	40,000.00	40,000.00	33,263.50	(6,736.50)	1,045,135.97
9/18/2016	1,000,000.00	8.0000%	40,000.00	40,000.00	33,050.47	(6,949.53)	1,038,186.45
3/18/2017	1,000,000.00	8.0000%	40,000.00	40,000.00	32,830.71	(7,169.29)	1,031,017.16
9/18/2017	1,000,000.00	8.0000%	40,000.00	40,000.00	32,603.99	(7,396.01)	1,023,621.15
3/18/2018	1,000,000.00	8.0000%	40,000.00	40,000.00	32,370.11	(7,629.89)	1,015,991.26
9/18/2018	1,000,000.00	8.0000%	40,000.00	40,000.00	32,128.83	(7,871.17)	1,008,120.08
3/18/2019	1,000,000.00	8.0000%	40,000.00	1,040,000.00	31,879.92	(8,120.08)	1,000,000.00
Subtotal						28,750.00	

7. As can be seen from this schedule, the amortized value quickly changes from a discount situation to a premium situation. The question is should the accretion of the discount end when the discount is fully amortized, i.e. when Amortized Value = Par Value. In the above, this would occur somewhere between 3/18/05 and 9/18/05. Or, is it proper to report the amortized value as the sum of the discounted cash flows at a given point in time using the effective yield at acquisition? (Note: A prospective method is not applicable for this situation since the cash flows are known at time of acquisition, and those assumptions will not change over time.)

Example 2

8. The second situation explores a variable rate security using the Retrospective Method of Amortization. This example exemplifies the issue identified as "**Drift**." As variable interest rates are not known in advance, adjustments to yields must be made whenever a new interest rate becomes effective. Using the retrospective method, the effective yield is calculated based upon the purchase price, and the actual received and the projected future cash flows. For simplicity's sake, a bond with a single principal payment at maturity is used, but similar results would occur if the security were any type of variable rate instrument.

9. The situation presented below shows the cash flow assumptions at purchase when there is only one known interest rate. Immediately following, are the effects of using a retrospective adjustment, once the second interest rate is known and applied.

Original Purchase Assumptions:	
Par value:	1,000,000.00
Price:	98.000
Cost:	980,000.00
Acq Date:	01/022006
Maturity Date:	12/15/2009
Interest rate:	2.000%
Pays:	Quarterly
Effective Annual Yield:	2.53326%
Qrtrly Yield:	.63332%

Pay Date	Par Value	Int Rate	Int Recvd	Prin Recd	Total Cash	Income	Accretion Discount	Amortized Value
1/2/2006	1,000,000	2.00%	(944.44)		(980,944.44)			980,000.00
3/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	5,034.16	978.60	980,978.60
6/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,212.69	1,212.69	982,191.29
9/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,220.37	1,220.37	983,411.67
12/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,228.10	1,228.10	984,639.77
3/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,235.88	1,235.88	985,875.65
6/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,243.71	1,243.71	987,119.36
9/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,251.58	1,251.58	988,370.94
12/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,259.51	1,259.51	989,630.45
3/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,267.49	1,267.49	990,897.94
6/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,275.51	1,275.51	992,173.45
9/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,283.59	1,283.59	993,457.04
12/15/2008	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,291.72	1,291.72	994,748.76
3/15/2009	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,299.90	1,299.90	996,048.66
6/15/2009	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,308.13	1,308.13	997,356.80
9/15/2009	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,316.42	1,316.42	998,673.22
12/15/2009	1,000,000	2.00%	5,000.00	1,000,000.00	1,000,000.00	6,324.76	1,326.78	-

10. Based on the purchase assumptions, the amortization schedule for this security is normal. The accretion of discount is a smooth curve, and the amortized value approaches par value at maturity. As previously indicated, the following shows the interest rate adjusted for the accrual period ending 3/15/08. The original purchase assumptions are as stated above. The interest payments from 3/15/06 through 12/15/07 are paid based on the 2.000% annual interest rate effective from issue date (12/15/05) through 12/14/07. For accrual period beginning 12/15/07, however, the interest rate adjusts to 3.500%. Using a retrospective methodology, the following amortization schedule results:

Pay Date	Par Value	Int Rate	Int Recvd	Prin Recd	Total Cash	Income	Accretion Discount	Amortized Value
1/2/2006	1,000,000	2.00%	(944.44)		(980,944.44)			980,000.00
3/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	6,510.55	2,455.00	982,455.00
6/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,046.82	3,046.82	985,501.81
9/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,071.77	3,071.77	988,573.58
12/15/2006	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,096.93	3,096.93	991,670.51
3/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,122.30	3,122.30	994,792.81
6/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,147.87	3,147.87	997,940.67
9/15/2007	1,000,000	2.00%	5,000.00	0.00	5,000.00	8,173.65	3,173.65	1,001,114.33
12/15/2007	1,000,000	**2.00%**	**5,000.00**	**0.00**	**5,000.00**	**8,199.64**	**3,199.64**	**1,004,313.97**
3/15/2008	1,000,000	**3.50%**	**8,750.00**	**0.00**	**8,750.00**	**8,225.85**	**(524.15)**	**1,003,789.82**
6/15/2008	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,221.56	(528.44)	1,003,261.38
9/15/2008	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,217.23	(532.77)	1,002,728.61
12/15/2008	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,212.87	(537.13)	1,002,191.48
3/15/2009	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,208.47	(541.53)	1,001,649.94
6/15/2009	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,204.03	(545.97)	1,001,103.98
9/15/2009	1,000,000	3.50%	8,750.00	0.00	8,750.00	8,199.56	(550.44)	1,000,553.54
12/15/2009	1,000,000	3.50%	8,750.00	1,000,000.00	1,008,750.00	8,195.05	(553.54)	-

11. From this, it is apparent that the amortized value quickly breaks out of the cost / par range and becomes a premium situation. The book value for the periods prior to 12/15/07 would have been reported at the original amortized values as determined in the prior spreadsheet. On the 12/31/07 annual statement there would be a retrospective catch-up adjustment.

12. Because of the variability of cash flows, recalculating a yield based on the retrospective method and applying that yield to calculate an amortized value can cause a security to bust out of the cost / par range, and the amortization (accretion) to move in the "wrong direction." For variable rate, interest only, and principal only asset backed securities, the additional complication caused by day delay would also come into play.

Example 3

13. The third example represents a mortgage backed security purchased at a slight premium. This situation illustrates what is described as **"Parity."** American Banker Online describes parity as "The parity price at which the yield of a mortgage-backed bond equals its net coupon rate. Securities with parity amortize to a value less than 100.

14. Parity occurs because the accrual date, usually the last day of the month, is many days prior to the payment date, typically 15, or 25 days for a mortgage backed security, and up to 45, or 55 days (or longer) for a collateralized mortgage obligation. The following is a simplified example using a mortgage backed security. The assumption is that the security is purchased at a slight premium (price = 100.1000). Because of day delay, however, the parity price is not 100, but is approximately 99.90.

CUSIP: 123456-AB-1 (Made up)
Description: Sample Mortgage Backed Security
Final payment date: 01/15/2006
Int Rate: 5.50%
Day Delay: 44
CPR: 6%

Purchase Date:	2/15/2004
Purchase Price:	100.1000
Par Purchased:	1,000,000.00
Annual Yield (SIA)	5.16841%
Periodic (monthly) Yield	0.43070%
Interest Rate	5.500%

	Prin Red	Principal	Book	Total Incm	Int Incm	Amort	Amort Fctr
2/15/2004		1,000,000.00	1,001,000.00	-	(2,138.89)	-	1.00100
3/15/2004	46,066.11	953,933.89	954,767.44	4,311.32	4,477.77	(166.45)	1.00087
4/15/2004	45,822.29	908,111.60	908,790.15	4,112.19	4,267.19	(155.00)	1.00075
5/15/2004	45,579.72	862,531.88	863,066.88	3,914.17	4,057.72	(143.56)	1.00062
6/15/2004	45,338.40	817,193.48	817,596.34	3,717.24	3,849.37	(132.13)	1.00049
7/15/2004	45,098.32	772,095.16	772,377.29	3,521.39	3,642.12	(120.73)	1.00037
8/15/2004	44,859.48	727,235.68	727,408.48	3,326.64	3,435.97	(109.33)	1.00024
9/15/2004	44,621.87	682,613.81	682,688.66	3,132.95	3,230.91	(97.95)	1.00011
10/15/2004	44,385.48	638,228.33	638,216.60	2,940.35	3,026.93	(86.58)	0.99998
11/15/2004	44,150.31	594,078.02	593,991.06	2,748.80	2,824.04	(75.23)	0.99985
12/15/2004	43,916.35	550,161.67	550,010.81	2,558.32	2,622.22	(63.89)	0.99973
1/15/2005	43,683.59	506,478.08	506,274.66	2,368.90	2,421.47	(52.57)	0.99960
2/15/2005	43,452.03	463,026.05	462,781.38	2,180.53	2,221.78	(41.25)	0.99947
3/15/2005	43,221.66	419,804.39	419,529.77	1,993.20	2,023.15	(29.95)	0.99935
4/15/2005	42,992.48	376,811.91	376,518.63	1,806.92	1,825.58	(18.66)	0.99922
5/15/2005	**42,764.48**	**334,047.43**	**333,746.76**	**1,621.67**	**1,629.05**	**(7.38)**	**0.99910**
6/15/2005	**42,537.66**	**291,509.77**	**291,212.98**	**1,437.45**	**1,433.57**	**3.88**	**0.99898**
7/15/2005	42,312.00	249,197.77	248,916.12	1,254.26	1,239.12	15.14	0.99887
8/15/2005	42,087.50	207,110.27	206,855.00	1,072.08	1,045.71	26.38	0.99877
9/15/2005	41,864.16	165,246.11	165,028.45	890.93	853.32	37.61	0.99868
10/15/2005	41,641.97	123,604.14	123,435.31	710.78	661.95	48.83	0.99863
11/15/2005	41,420.92	82,183.22	82,074.43	531.64	471.60	60.04	0.99868
12/15/2005	41,201.01	40,982.21	40,944.66	353.50	282.25	71.24	0.99908
1/15/2006	40,982.21	-	-	176.35	93.92	37.55	*

* The last amortization calculation is an adjustment to bring book value to 0.

15. By looking at the amortization factors, which represent amortized value / remaining principal, it is evident that the security quickly goes from a premium situation to a discount situation between 5/15/2005 and 6/15/2005. Due to Parity, the security does not amortize to a value of 100, but to a slight discount.

16. In addressing the issue of parity for REMICs, the tax code allows for accruing interest and calculating Original Issue Discount (OID) on a payment date to payment date basis, thereby eliminating the discrepancy between the accrual periods and the payment dates. Another method of eliminating parity would be to use the accrual end date (record date) plus one as the assumed payment date. Both methods sync up the accrual period and the payment date, essentially eliminating day delay.

17. Is it appropriate under statutory accounting guideline to "assume away" day delay and subsequently eliminate amortizing to a value less than par? If so, should a payment date assumption or a record date assumption be used?

INT 07-01 Discussion

18. The Working Group came to the following consensuses:

Issue 1: When applying the constant yield method to loan-backed or structured securities, can amortized value be interpreted to represent the discounted cash flows?

19. The Working Group noted that in the case of loan-backed or asset-backed securities; the unamortized balance of an issue at any point in time will represent the present value of all future cash flows discounted to the present using the constant yield.

Issue 2: Should a security purchased at a premium be allowed to move to a discount, or should a discount be allowed to move to a premium, if this occurs as a result of applying the scientific (constant yield) interest method."

20. It has been noted that certain anomalies will exist with certain types of bonds, loan-backed and structured securities when applying the constant yield method. These anomalies can cause a premium to move to a discount, or a discount to move to a premium.

21. Some think that the value should be frozen once this occurs. However, both SSAP No. 26~~R~~ and SSAP No. 43~~R~~ are clear that the scientific (constant yield) interest method is required to be used when accreting/amortizing the discount/premium on a bond, loan-backed or structured security.

22. The Working Group noted that recording a discount or a premium and accreting/amortizing to par is consistent with a held to maturity approach that results in no gain or loss at maturity. Although it could be argued that freezing a discount or premium, or stopping at par at a particular point in time, would achieve the same result, this approach appears to ignore the fundamentals of the issue that have led to the anomalies. The Working Group noted that ignoring the facts of the issue in order to prevent the original premium or original discount from reversing is inappropriate, and that the above examples demonstrate that fact. Therefore, a security purchased at a premium is allowed to move to a discount, and that a discount is allowed to move to a premium, if this occurs as a result of applying a constant yield method.

Issue 3: On the subject of Parity (described in example 3), is it appropriate under statutory accounting guideline to "assume away" day delay and subsequently eliminate amortizing to a value less than par? If so, should a payment date assumption or a record date assumption be used?

23. It has been noted for mortgage backed securities; interest is often "earned" as of the end of the month but not paid until a later date. This delay known as the "day delay" is often 10-25 days depending on the contract. The yields as provided by "Bloomberg," are Security Industry Association (SIA)

compliant yields, which do not "assume away 'day delay'", but produce amortization to a value of less than 100, as seen in the example. After discussion, the Working Group determined that the difference between amortizing to the earned record date or to the payment date for the securities described in issue 3 is typically immaterial. Therefore, the Working Group determined to continue to allow flexibility in amortization for the day delay.

24. The user of this interpretation should also note that amortization continues to apply the effective yield method in the above situations provided that doing so does not conflict with other statutory requirements in the SSAPs. For example, yield to worst is still a continuing requirement and other SVO requirements are still in effect, etc.

INT 07-01 Status

25. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 08-05: EITF 02-11: Accounting for Reverse Spinoffs

INT 08-05 Dates Discussed

March 29, 2008; May 31, 2008

INT 08-05 References

Current:
SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items
SSAP No. 95—Nonmonetary Transactions

INT 08-05 Issue

1. *EITF 02-11: Accounting for Reverse Spinoffs* (EITF 02-11) was issued in September 2002 to address whether to account for spinoffs as reverse spinoffs based on the substance, instead of the legal form, of such transactions. In a reverse spinoff, the legal spinnee should be treated as though it were the spinnor for accounting purposes. *(In spinoff transactions, the 'spinnor' is the entity transferring assets, whereas the term 'spinnee' refers to the new entity.)*

2. As noted within EITF 02-11:

> 1. An entity may desire to reorganize its operations in response to its business needs. For example, an entity (the "spinnor") may transfer assets into a new legal spun-off entity (the "spinnee") and distribute the shares of the spinnee to its shareholders, without the surrender by the shareholders of any stock of the spinnor. Such a transaction is commonly referred to as a "spinoff." Consider the following example:
>
> > Big Company owns and operates a mall and a retail store that occupies the anchor store position in that mall. The mall and the store are managed by two separate divisions. The shareholders of Big Company would like to split Big Company into two companies so that each can focus on its own operations. To achieve this, Big Company transfers the mall's assets and operations into a newly created subsidiary, Mall Company, and distributes the shares of Mall Company to its shareholders on a pro rata basis in a spinoff.
>
> 2. A spinoff allows an entity to be reorganized in a manner that allows it to meet the needs of its owners. However, there may be other benefits as well. If the spinoff qualifies as a nontaxable reorganization, the distribution results in no taxable gain being recognized by either the spinnor or its shareholders. Additionally, if the spinnee is subsequently sold by the shareholders, the double taxation that would have occurred if a company sold its subsidiary directly and distributed the proceeds to its shareholders is avoided.
>
> 3. The accounting guidance for spinoffs is provided in Opinion 29. Although the basic principle underlying Opinion 29 is that the accounting for nonmonetary transactions should be based on the fair values of the assets (or services) involved, it provides a modification to that basic principle for nonreciprocal transfers to owners (such as spinoffs). Opinion 29, paragraph 23 (as amended by Statement 144), states:
>
> > Accounting for the distribution of nonmonetary assets to owners of an enterprise in a spin-off or other form of reorganization or liquidation or in a plan that is in substance the rescission of a prior business combination should be based on the recorded amount (after reduction, if appropriate, for an indicated impairment of value) of the nonmonetary assets distributed. A prorata distribution to owners of an enterprise of shares of a subsidiary or other investee company that has been or is being consolidated or that has been or is being accounted for under the equity method is to be considered to be

equivalent to a spin-off. Other nonreciprocal transfers of nonmonetary assets to owners should be accounted for at fair value if the fair value of the nonmonetary asset distributed is objectively measurable and would be clearly realizable to the distributing entity in an outright sale at or near the time of the distribution.

4. Accordingly, under Opinion 29, an entity's distribution of the shares of a wholly owned or consolidated subsidiary to its shareholders should be recorded based on the carrying value of the subsidiary. Regardless of whether the spun-off operations will be sold immediately after the spinoff, the transaction should not be accounted for as a sale of the accounting spinnee followed by a distribution of the proceeds.

5. In certain cases, the spinoff of a subsidiary to its shareholders is such that the legal form of the transaction does not match its substance. That is, in certain circumstances, the spinnee will be the continuing entity. The issue is whether to account for a spinoff as a reverse spinoff based on the substance instead of the legal form of the transaction. In a reverse spinoff, the legal spinnee should be treated as though it were the spinnor for accounting purposes (accounting spinnor).

6. Consider the following example:

Snack Food Company owns two subsidiaries—Ice Cream Subsidiary and Snack Subsidiary. Ice Cream Subsidiary is significantly larger and more profitable than Snack Subsidiary. The shareholders of Snack Food Company would like to continue the ice cream operations and dispose of the snack food operations. To facilitate this, Snack Food Company distributes the shares of Ice Cream Subsidiary to the shareholders thereby creating Ice Cream Company. The shareholders are then able to dispose of the operations of Snack Food Company (now solely comprising Snack Subsidiary operations) by selling the shares directly to a third party and, at the same time, retain ownership of the Ice Cream Company.

Accounting for the above transaction based upon its legal form would present Snack Food Company as the spinnor with Ice Cream Company as the spinnee. However, in substance, Snack Food Company has disposed of Snack Subsidiary and continued its ice cream operations. The legal form of the spinoff may have been driven primarily by tax planning strategies. Accounting for the transaction based on its substance depicts Ice Cream Company as the accounting spinnor and Snack Food Company as the accounting spinnee.

3. Per EITF 02-11, paragraph 5, the issue is whether to account for a spinoff as a reverse spinoff based on the substance instead of the legal form of the transaction. In a reverse spinoff, the legal spinnee should be treated as though it were the spinnor for accounting purposes (accounting spinnor).

4. The FASB Emerging Issues Task Force reached the following consensus in paragraphs 7-8 of EITF 02-11:

7. The Task Force reached a consensus that reverse spinoff accounting is appropriate when treatment of the legal spinnee as the accounting spinnor results in the most accurate depiction of the substance of the transaction for shareholders and other users of the financial statements. The Task Force observed that the determination of whether reverse spinoff accounting is appropriate is a matter of judgment that depends on an evaluation of all relevant facts and circumstances.

8. The Task Force reached a consensus that in determining whether reverse spinoff accounting is appropriate, a presumption should exist that a spinoff should be accounted for based on its legal form, in other words, that the legal spinnor is also the accounting spinnor. However, that presumption may be overcome. An evaluation of the following indicators should be considered in that regard. Nevertheless, no one indicator should be considered presumptive or determinative.

5. The FASB Emerging Issues Task Force identified the following indicators that a spinoff should be accounted for as a reverse spinoff in paragraph 8 of EITF 02-11:

- **The size of the legal spinnor and the legal spinnee**—All else being equal, in a reverse spinoff, the accounting spinnor (legal spinnee) is larger than the accounting spinnee (legal spinnor). The determination of which entity is larger is based on a comparison of the assets, revenues, and earnings of the two entities. There are no established "bright lines" that should be used to determine which entity is the larger of the two.

- **The fair value of the legal spinnor and the legal spinnee**—All else being equal, in a reverse spinoff, the fair value of the accounting spinnor (legal spinnee) is greater than that of the accounting spinnee (legal spinnor).

- **Senior management**—All else being equal, in a reverse spinoff, the accounting spinnor (legal spinnee) retains the senior management of the formerly combined entity. Senior management generally consists of the chairman of the board, chief executive officer, chief operating officer, chief financial officer, and those divisional heads reporting directly to them, or the executive committee if one exists.

- **Length of time to be held**—All else being equal, in a reverse spinoff, the accounting spinnor (legal spinnee) is held for a longer period than the accounting spinnee (legal spinnor). A proposed or approved plan of sale for one of the separate entities concurrent with the spinoff may identify that entity as the accounting spinnee.

INT 08-05 Discussion

6. The EITF consensus is that reverse spinoff accounting is appropriate when treatment of a legal spinnee as the accounting spinnor results in the most accurate depiction of the substance of the transaction for shareholders and other users of the financial statements. The Task Force observed that the determination of whether reverse spinoff accounting is appropriate is a matter of judgment that depends on an evaluation of all relevant facts and circumstances.

7. The Task Force consensus indicated that a presumption should exist that a spinoff should be accounted for based on its legal form (legal spinnor is the accounting spinnor); however that presumption can be overcome based on an evaluation of indicators that may suggest when a reverse spinoff exists (legal spinnee would be accounting spinnor).

8. In various instances within the statutory accounting guidelines, guidance is incorporated to promote accounting in accordance with the substance of transactions instead of their legal form. The Working Group reached a consensus to adopt EITF 02-11, indicating that reverse spinoff accounting is appropriate when treatment of a legal spinnee as the accounting spinnor results in the most accurate depiction of the substance of the transaction. In situations in which reverse spinoff accounting is judged to be most appropriate, this will result with the carrying value of the spinnee, instead of the spinnor, being utilized in determining the spinoff distribution to shareholders.

9. The following examples have been incorporated from EITF 02-11 to illustrate situations in which a spinoff should be accounted for in accordance with the legal form or as a reverse spinoff:

<u>Example 1</u> - Retail Company, a retail store chain, has a wholly owned restaurant subsidiary. The retail and restaurant operations are operated independently with a small executive management team overseeing both. Since the two have unrelated operations, the shareholders believe that the two operations should be separated by way of a spinoff. They believe that this will allow those separate companies to pursue opportunities in their respective industries and maximize their individual value. In order to accomplish the spinoff, Retail Company creates a new legal entity, Restaurant Company, into which the assets and operations of the restaurant subsidiary are

transferred. The shares of Restaurant Company are then distributed to the shareholders of Retail Company on a pro rata basis.

The executive management team of Retail Company will be divided between the two entities. A comparison of the two companies is presented below:

(In 000s)	Assets	Revenues	Net Income	Fair Value
Retail	$500	$410	$150	$675
Restaurant	$100	$ 75	$21	$170

Evaluation: Based on an analysis of the indicators in this example, the spinoff should be accounted for in accordance with its legal form. That is, the transaction should not be accounted for as a reverse spinoff. Retail Company should be designated as the accounting spinnor based on the first two indicators listed below.

- Retail Company has substantially larger operations than Restaurant Company.
- The fair value of Retail Company is greater than Restaurant Company.
- The management team is allocated between the two operations.
- There are no planned or likely disposals of either Retail Company or Restaurant Company.

The designation of Retail Company as the accounting spinnor will provide the most accurate depiction of the transaction to shareholders and other users of the financial statements because, in substance, Retail Company has spun off its Restaurant Company into a separate company.

Example 2 - Retail Company, a retail store chain, has a wholly owned restaurant subsidiary. The retail and restaurant operations are operated independently, with a small executive management team overseeing both. While the restaurant subsidiary has grown rapidly, the retail operations have deteriorated steadily due to increased competition. The shareholders believe that the two operations should be separated by way of a spinoff. Management intends to dispose of the retail operations. In order to accomplish the spinoff, Retail Company creates a new legal entity, Restaurant Company, into which the assets and operations of the restaurant subsidiary are transferred. The shares of Restaurant Company are then distributed to the shareholders of Retail Company on a pro rata basis.

The executive management team of the combined entity will be assigned primarily to Restaurant Company, as the intent is to dispose of Retail Company (now solely comprising the retail operations). A comparison of certain statistics of the two companies is presented below:

(In 000s)	Assets	Revenues	Net Income	Fair Value
Retail	$300	$210	$ 35	$375
Restaurant	$600	$450	$150	$700

Evaluation: Based on an analysis of the indicators in this example, the spinoff should be accounted for as a reverse spinoff. Restaurant Company, although the legal spinnee, should be designated as the accounting spinnor based on the following:

- Restaurant Company has substantially larger operations than Retail Company.
- The fair value of Restaurant Company is greater than that of Retail Company.
- The management team is primarily assigned to Restaurant Company.
- Management intends to dispose of Retail Company upon finalizing the spinoff.

The designation of Restaurant Company as the accounting spinnor will provide the most accurate depiction of the transaction to shareholders and other users of the financial statements, as, in substance, Retail Company has disposed of its retail operations and continued its restaurant operations.

INT 08-05 Status

10. No further discussion is planned.

Interpretation of the Emerging Accounting Issues (E) Working Group

INT 15-01: ACA Risk Corridors Collectibility

INT 15-01 Dates Discussed

October 19, 2015; November 5, 2015

INT 15-01 References

Current:
SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act

INT 15-01 Issue

1. The federal Affordable Care Act (ACA) includes three types of risk sharing programs known as risk adjustment, reinsurance and risk corridors. The risk corridors program is a temporary program that is effective for benefit years beginning in 2014 through 2016 and applies to Qualified Health Plans (QHPs) in the individual and small group markets whether sold on or outside of an exchange.

2. The risk corridors program creates a mechanism for sharing risk for allowable costs between the federal government and QHP issuers – collecting charges from the issuer if the issuer's QHP premiums exceed claims costs of QHP enrollees by a certain amount, and making payments to the issuer if the issuer's premiums fall short by a certain amount, subject to certain adjustments for taxes, administrative expenses, and other costs and payments. The risk corridors program is intended to protect against inaccurate rate setting by limiting the extent of QHP issuer losses and gains. In the event that risk corridors program collections are not sufficient to cover all the required distributions, the ACA allows the use of other sources of federal funding for the required distributions, subject to the availability of appropriations.

3. On April 11, 2014, the U.S. Department of Health and Human Services (HHS) issued a bulletin titled ''Risk Corridors and Budget Neutrality," which described how it intended to administer risk corridors over the three-year life of the program. HHS stated that if risk corridors collections for a particular year are insufficient to make full risk corridors payments for that year, risk corridors payments for the year will be reduced pro rata to the extent of any shortfall. The HHS noted that lacking other appropriations or sources of funding, subsequent year program collections would first be applied to the unpaid program balances of preceding years. In December 2014, federal funds were not appropriated for the federal costs of the risk-sharing program.

4. On October 1, 2015, HHS announced proration results for 2014 risk corridors payments. Based on current data from QHP issuers' risk corridors submissions, issuers will pay $362 million in risk corridors charges, and have submitted for $2.87 billion in risk corridors payments for 2014. As of October 1, 2015, assuming full collections of risk corridors charges, this will result in a proration rate of 12.6 percent. HHS will begin collection of risk corridors charges in November 2015, and will begin remitting risk corridors payments to issuers starting December 2015. The announcement noted that the risk corridor payment and charge amounts reflected in the October 1, 2015, bulletin do not reflect any payment or charge adjustments due to resubmissions after September 15, 2015, or the effect of subsequent appeals.

5. There was diversity in practice regarding the accrual of 2014 risk corridors receivables for the first two quarters of 2015. Some entities did not accrue material amounts for the risk corridors receivables or did not accrue any amount due to the lack of federal government appropriations, and pursuant to the requirement in *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*, which requires that preparers be conservative and diligent in developing their estimates. Other entities appear to have accrued the full amount of funds estimated to be received under the risk corridors program. For some entities the

accrued receivables represent a material amount of surplus and uncollectibility or delayed collectibility represents a solvency concern.

6. At a minimum, impairment analysis and/or updated estimates are required under SSAP No. 107 for the 2014 risk corridors receivables. In determining the amount to be impaired, one issue identified is that 2015 and 2016 collections may not be sufficient to cover the full 2014 program requests.

7. The accounting issues are:

Issue 1: **Determining the Amount of Impairment –** The 2015 and 2016 program collections may not be sufficient to fund the shortfall of 2014 program requests. Therefore, the accounting issue identified is how to determine the required impairment amount.

Issue 2: **Nonadmittance** – The accounting questions regarding nonadmission have been focused on the amounts in excess of the confirmed proration payment of 12.6%, of which there is a reasonable and probable expectation that the 2015 and 2016 program collections will cover some portion of the 2014 benefit year shortfall.

An accounting issue identified is whether nonadmittance is required or permitted to be applied to the 2014 program benefits in excess of the 12.6% prorated amount for which reporting entities have a reasonable and probable expectation of future collection. Even if an entity has a reasonable and probable expectation of payment of the amount in excess of the confirmed proration of 12.6%, extended delays in payment are expected.

Issue 3: **Timing of Impairment or Nonadmittance Recognition** – The HHS notice of the 12.6% proration amount was provided on October 1, 2015; however, prior to October 1, there were other indicators that the risk corridors program would have 2014 benefit shortfalls (in April and December of 2014 as detailed above and other public reports). Doubts about program collectibility of receivables and problems with estimations are among the reasons many entities did not accrue risk corridors receivables or only accrued immaterial amounts. The accounting issue identified is whether impairment recognition is required to be reflected in the September 30, 2015, financial statements.

Issue 4: **Accrual of 2015 and 2016 Receivables** – Shall the accrual of receivables for the benefit years 2015 and 2016 continue to be estimated?

INT 15-01 Discussion

8. For Issue 1, impairment analysis and/or updated estimates for the 2014 risk corridors receivables are required under SSAP No. 107.

9. The Working Group determined that impairment is indicated if an entity accrued as of the reporting date under the 2014 Risk Corridors program more than they have a reasonable expectation of receiving. SSAP No. 107, paragraph 59.e. (quoted below), requires evaluation of the collectibility of all amounts receivable from the risk corridors program for each reporting period, and if in accordance with *SSAP No. 5—Liabilities, Contingencies and Impairments of Assets* it is probable that risk corridors receivables are uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made.

> 59. Risk corridors assessments meet the definition of liabilities as set forth in SSAP No. 5. Risk corridors receivables due to the reporting entity meet the definition of an asset and are admissible to the extent that they meet all of the criteria in this statement.
>
> a. Assumptions used in estimating retrospective premium adjustments shall be consistent with the assumptions made in recording other assets and liabilities necessary to reflect the underwriting results of the reporting entity such as claim and loss reserves (including IBNR) and contingent commissions. Contingent

commissions and other related expenses shall be adjusted in the same period the additional or return retrospective premiums are recorded.

b. The additions or reductions to premium revenue resulting from the risk corridors program are recognized over the contractual period of coverage, to the extent that such additions or reductions are reasonably estimable. Reporting entities shall be aware of the significant uncertainties involved in preparing estimates and be both diligent and conservative in their estimations. Risk corridors payables and receivables shall be estimated based on experience to date. The method used to estimate the payables and receivables shall be reasonable and consistent between reporting periods. In exercising the judgment required to prepare reasonable estimates for the financial reporting of risk corridors program payables and receivables, the statutory accounting concept of conservatism shall be followed. In addition, reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity's estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. In addition, the estimates shall be consistent with other financial statement assertions and the pricing scenarios used by the reporting entity.

c. The risk corridors receivables are from a federal governmental program. Amounts over 90 days due shall not cause the receivable to be treated as a nonadmitted asset based solely on aging.

d. Provided that the risk corridors receivables due the reporting entity are determined in a manner that is consistent with the requirements of this statement, the receivables are admitted assets until determination of impairment or payment denial is received from the governmental entity or government-sponsored entity administering the program. Upon notification that payments to be paid to the reporting entity will be less than the recorded receivables, any amount in excess of the confirmed amount shall be written off and charged to income, except for amounts that are under appeal. Any receivable for risk adjustment amounts under appeal shall be reflected as a nonadmitted asset.

e. Evaluation of the collectibility of all amounts receivable from the risk corridors program shall be made for each reporting period. If, in accordance with SSAP No. 5~~R~~, it is probable that the risk corridors receivables are uncollectible, any uncollectible receivable shall be written off and charged to income in the period the determination is made. If it is reasonably possible, that a portion of the balance determined in accordance with this paragraph is not anticipated to be collected and is therefore not written off, the disclosure requirements outlined in SSAP No. 5~~R~~ shall be followed.

f. Reporting shall be consistent with SSAP No. 66—Retrospectively Rated Contracts, paragraph 9 guidance on reporting for retrospective premium.

10. Current facts and circumstances must be taken into account when determining impairment. In accordance with SSAP No. 107, paragraph 59.e., any uncollectible receivable shall be written off and charged to income in the period the determination is made. The Working Group noted that the following are some, but not an all-inclusive list of the relevant factors to consider in determining the amount of impairment to include:

a. Amounts in excess of the proration amount of 12.6% must be evaluated for impairment.

b. Judgment is involved in the determination of the impairment amount.

c. Information used in determination of impairment shall be based on the most current and reliable information available.

d. Other known or probable changes in program collections or funding must also be evaluated, including the possibility of fewer contributors or lesser collections due to insolvencies.

e. The intent and ability of the reporting entity to remain in business for a period of time sufficient to allow for recovery of risk corridors receivables.

11. The Working Group noted that the impaired amount would be based on the facts and circumstances and is required to be evaluated at each reporting period by management.

12. For Issue 2, SSAP No. 107 addresses nonadmittance in paragraph 59.c., noting that, "Amounts over 90 days due shall not cause the receivable to be treated as a nonadmitted asset based solely on aging." However, SSAP No. 107 does not preclude nonadmittance for other reasons. In addition, SSAP No. 4 provides that:

> "The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third party interests should not be recognized on the balance sheet, and are, therefore, considered nonadmitted."

13. The lack of appropriations, documented program shortfalls and known extended payment delays are indicative that some of the program receivables are not available to meet policyholder obligations when due, and therefore, evaluation for possible nonadmittance under SSAP No. 4 in addition to impairment evaluation is appropriate.

14. The Working Group discussed that nonadmission was appropriate for amounts that have a reasonable and probable expectation of recovery which are not currently available to pay claims. In this case, 2014 amounts in excess of the 12.6% proration amount which have not been written off for impairment, and have a reasonable expectation of delayed recovery shall be nonadmitted. The Working Group discussed that amounts in excess of the proration amount which are nonadmitted, shall remain nonadmitted until additional proration amounts are confirmed by HHS or other information of a sufficient nature supports that collectibility is probable and reasonable. Consistent with SSAP No. 107, paragraph 59, the statutory accounting concept of conservatism shall be followed when estimating amounts; reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity's estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. Consistent with Issue 4, below, estimates shall not assume the availability of federal funds unless such federal funds are appropriated by Congress for the federal costs of the risk sharing program.

15. Such admitted amounts should also have a reasonably short time horizon to ensure that amounts will be available to pay policyholder claims. Some regulators and reporting entities may also take the position that it is probable that risk corridors receivables accrued during the 2014 plan year are uncollectible in excess of 12.6% proration, and therefore, any amounts in excess of proration would be fully written off. If this were the case, the 12.6% prorated balance would be admitted unless extended payment delays or other information cause a reevaluation of admissibility.

16. For Issue 3, the October 1 notification from HHS provided evidence of the estimated amount of proration for the underfunded program. The underfunded program was a condition that existed at the date of the September 30, 2015, balance sheet. Therefore, in accordance with *SSAP No. 9—Subsequent Events*, paragraph 11 (quoted below) this would be a Type I subsequent event that would be reflected in the financial statements for the third quarter. Type I events include estimates inherent in the process of preparing financial statements.

11. The following are examples of Type I recognized subsequent events:

a. If the events that gave rise to litigation had taken place before the balance sheet date and that litigation is settled, after the balance sheet date but before the financial statements are issued or are available to be issued, for an amount different from the liability recorded in the accounts, then the settlement amount should be considered in estimating the amount of liability recognized in the financial statements at the balance sheet date.

b. Subsequent events affecting the realization of assets, such as receivables and inventories or the settlement of estimated liabilities, should be recognized in the financial statements when those events represent the culmination of conditions that existed over a relatively long period of time. For example, a loss on an uncollectible trade account receivable as a result of a customer's deteriorating financial condition leading to bankruptcy after the balance sheet date but before the financial statements are issued or are available to be issued ordinarily will be indicative of conditions existing at the balance sheet date. Thus, the effects of the customer's bankruptcy filing shall be considered in determining the amount of uncollectible trade accounts receivable recognized in the financial statements at the balance sheet date.

17. For Issue 4, the Working Group determined that risk corridors receivables for the 2015 and 2016 benefit years estimated in accordance with SSAP No. 107, paragraphs 59.b. and 59.e. are nonadmitted 1) until such time that the prior benefit year is paid in full and 2) until additional proration amounts are confirmed by HHS or other information of a sufficient nature supports that collectibility is probable and reasonable. Consistent with SSAP No. 107, paragraph 59, the statutory accounting concept of conservatism shall be followed when estimating amounts; reporting entities are required to have sufficient information to determine a reasonable estimate. Part of ensuring sufficient information requires that the reporting entity's estimate is based on demonstrated knowledge of the impacts of the other risk-sharing programs on the risk corridors program and the terms of the risk corridors program. Estimates shall not assume the availability of federal funds unless such federal funds are appropriated by Congress for the federal costs of the risk corridors program.

INT 15-01 Status

18. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 18-03: Additional Elements Under the Tax Cuts and Jobs Act

INT 18-03 Dates Discussed

May 14, 2018; August 4, 2018

INT 18-03 References

Current:
SSAP No. 101—Income Taxes

INT 18-03 Issue

1. This interpretation has been issued to provide statutory accounting and reporting guidance for the following items under the federal Tax Cuts and Jobs Act (TCJA) as additional guidance to *SSAP No. 101—Income Taxes*:

a. Repatriation Transition Tax (RTT)

b. Alternative Minimum Tax (AMT) Credit

c. Global Intangible Low-Taxed Income (GILTI)

Issue 1 – Repatriation Transition Tax

2. The Repatriation Transition Tax (RTT) is a one-time transition tax on untaxed foreign earnings of foreign subsidiaries of U.S. companies. Under section 965 of the Internal Revenue Code (IRC), these earnings are deemed to be repatriated. Under the IRC guidance, foreign earnings held in the form of cash and cash equivalents are taxed at a 15.5% rate, and the remaining earnings are taxed at an 8% rate.

a. The RTT is calculated in the 2017 and, in some cases, the 2018 tax return. It is not a temporary tax item and does not reverse in subsequent years.

b. The RTT is an amount owed under the revised tax law, and is not impacted by future taxable income.

c. Although the full amount of the calculated RTT is owed, companies can elect to pay the liability over eight years under a set IRC schedule. If electing to make installment payments, the future RTT payments are due regardless whether a company has future taxable income or losses.

Issue 2 – Alternative Minimum Tax Credit

3. The Alternative Minimum Tax (AMT) credit is, pursuant to the provisions of the TCJA, a tax refund of AMT amounts paid in prior periods. The AMT credit can be recovered through an offset to regular taxes or received as a refund.

a. A reporting entity could realize all of its AMT receivable in the 2018 tax year if it is used to reduce its regular tax obligation. (It could also be used fully in 2019-2021 in this manner.)

b. If the AMT credit carryforward is not used to reduce regular taxes, it can be recovered as a refund (50%) to the extent not so used in tax years 2018 through 2020, with a 100% refund in 2021 to the extent not used to reduce 2021 regular tax liability.

c. If the AMT credit will be received as a refund (and not as an offset to tax liability), it may be subject to U.S. federal administrative sequestration requirements, which could reduce the amount paid by the federal government. (In 2017, the sequestration percentage was 6.6%, but this percentage varies yearly.)

d. U.S. GAAP guidance permits reporting the AMT credit as a current-year recoverable or as a deferred tax asset (DTA).

Issue 3 - Global Intangible Low-Taxed Income Tax - Description

4. The Global Intangible Low-Taxed Income (GILTI) tax is a new tax under the TCJA and is calculated each year on a portion of a controlled foreign corporation's active income.

a. GILTI is included in 2018 and subsequent year tax returns. An amount owed for GILTI in any tax year is not a temporary tax item and does not reverse in subsequent years. GILTI is a current income tax.

b. Assessments of changes in the basis differences in foreign entities could result in calculations of deferred tax items related to GILTI. The issue is whether existing basis differences will result in GILTI when they reverse. Although these deferred items may be theoretically correct, such calculations are expected to be very complex and require aggregate assessments that consider all companies within a consolidated tax group.

c. In January 2018, the *Financial Accounting Standards Board* (FASB) *Staff Q&A Topic 740, No. 5 Accounting for Global Intangible Low Taxed Income* identified that reporting entities may make an election to recognize deferred items under GILTI. (The recognition of the deferred items does not impact current tax recognition for GILTI, but whether basis differences for foreign controlled entities shall result in deferred tax assets or deferred tax liabilities.) The FASB Staff Q&A Topic 740, No. 5 also identified that FASB staff will be monitoring how entities that pay tax on GILTI are accounting for and disclosing these deferred effects over the next few quarters. The FASB staff will provide a subsequent update so the FASB can consider whether accounting and disclosure improvements are needed for U.S. GAAP.

INT 18-03 Discussion

5. The Statutory Accounting Principles (E) Working Group consensuses for accounting and reporting for the noted items are included below.

Issue 1 – Repatriation Transition Tax:

6. The Repatriation Transition Tax (RTT) is a current-year tax item captured in SSAP No. 101, paragraph 3. The amount payable shall be recognized as a current-year expense with a liability recognized as "current federal and foreign income taxes" and not as a deferred tax liability (DTL), regardless if an entity elects to make installment payments of the amount owed or pays the amount in full.

Disclosure

7. Reporting entities that are subject to the RTT shall include the following in a narrative disclosure as part of the income tax disclosures in Note 9:

a. RTT owed under the TCJA.

b. Schedule of payments made and expected future payments to satisfy the RTT liability. This disclosure shall explicitly identify whether the insurance entity has remitted full payment of the RTT, or whether the reporting entity is electing to pay the liability under the permitted installments. If the reporting entity fully remitted the RTT, disclosure of the RTT and the remitted payment is only required in the year-end 2018 financial statements. Reporting entities electing to make installment payments shall include the disclosure beginning in the year-end 2018 financial statements and continuing through the year-end statutory financial statements for the year in which the last installment payment was remitted.

Issue 2 – Alternative Minimum Tax Credit:

8. The Alternative Minimum Tax (AMT) credit qualifies as a current income tax recoverable pursuant to paragraph 9 of SSAP No. 101. Although qualifying as a current-year recoverable, some companies may elect to report the AMT credit as a DTA. Although the AMT refund qualifies as a current income tax recoverable, in order to mirror provisions permitted under U.S. GAAP, reporting entities may elect to report the AMT credit as either a current-year recoverable or as a DTA. If reported as a DTA, it would be subject to the statutory accounting admittance limitations for DTAs. If the AMT credit accounted for as a DTA exceeds statutory admittance provisions, it would be nonadmitted under SSAP No. 101.

Disclosure

9. Reporting entities with an AMT credit shall include the following narrative disclosure as part of the income tax disclosures in Note 9:

a. Identification of whether the AMT credit was recognized as a current-year recoverable or DTA.

b. The balance of the AMT credit carryforward as of the beginning of the year; the amount of the AMT credit recovered during the year; other current-year adjustments to the AMT credit carryforward; the balance of the AMT credit carryforward at the end of the year; the amount, if any, by which the ending balance has been reduced for sequestration; and the amount, if any, by which the reporting entity has elected to nonadmit. (This disclosure intends to capture any nonadmittance of the AMT credit by the reporting entity prior to application of the DTA admittance limitations reflected in SSAP No. 101.)

(These disclosures shall be made on an accrual basis beginning in the 2018 year-end statutory financial statements and continuing through the year-end statutory reporting period in which the AMT credit is fully utilized/received.)

Issue 3 – Global Intangible Low-Taxed Income Tax:

10. Under statutory accounting, reporting entities shall not recognize deferred GILTI tax for basis differences in foreign entities. GILTI tax from the current-year tax return is treated as a current-year tax item captured in SSAP No. 101, paragraph 3. The amount payable shall be recognized as a current-year expense with a liability recognized as a current federal and foreign income tax.

11. As an exception to this general rule, reporting entities are permitted to recognize deferred tax items for basis differences expected to reverse as GILTI in future years if they have recognized deferred tax items for basis differences expected to reverse as GILTI under U.S. GAAP. However, a reporting entity that has recognized deferred tax items for GILTI under U.S. GAAP may follow the statutory accounting general rule (no recognition of deferred tax items). Reporting entities that recognize deferred tax items for GILTI shall explicitly disclose this item in Note 9, beginning with the 2018 year-end statutory financial statements.

INT 18-03 Status

12. Any accounting change required by INT 18-03 shall, if not otherwise covered by *INT 18-01: Updated Tax Estimates Under the Tax Cuts and Jobs Act*, be recognized as a change in accounting estimate, pursuant to *SSAP No. 3—Accounting Changes and Corrections of Errors.*

13. The consensuses adopted in this interpretation provide information regarding the RTT, AMT credit and GILTI under the federal Tax Cuts and Jobs Act, and the statutory accounting assessment for reporting and disclosure for each of these items.

14. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 19-02: Freddie Mac Single Security Initiative

INT 19-02 Dates Discussed

February 6, 2019; April 6, 2019

INT 19-02 References

Current:
SSAP No. 26—Bonds
SSAP No. 43—Asset-Backed Securities

INT 19-02 Issue

1. This interpretation has been issued to provide a limited-scope exception to the exchange and conversion guidance in *SSAP No. 26—Bonds* as well as prescribe guidance in *SSAP No. 43~~R—Loan-Backed and Structured~~Asset-Backed Securities* for instruments converted in accordance with the Freddie Mac Single Security Initiative. Under this initiative, reporting entities will be permitted to exchange "45-day securities" for "55-day securities" without any material change to the securities, or to the loans that back the securities. (With the exchange, there would be a 10-day delay in payment cycle.)

2. Information on the Freddie Mac Single Security Initiative (Freddie Mac Gold PC Exchange). Information is also available via the noted link: *http://www.freddiemac.com/mbs/exchange/faqs.html*.

a. Freddie Mac will offer holders of 45-day, TBA-eligible and non-TBA-eligible Gold PCs and Giants the option to exchange their eligible 45-day securities for 55-day Freddie Mac securities and float compensation. For the TBA-eligible security exchanges, the 55-day corresponding security will be a Uniform Mortgage-Backed Security (UMBS™) or Supers, while for non-TBA eligible exchanges, the corresponding security will be a 55-day Freddie Mac MBS or Giant MBS.

b. Most elements of the new 55-day security received upon exchange will exactly match those of the PC or Giant being exchanged – most fundamentally, the cash flows of the 55-day security will ultimately be backed by the same loans as the original PC or Giant. Each new 55-day security will mostly have the same characteristics as the corresponding PC such as unpaid principal balance, pool factor, and weighted average coupon. The 55-day security will have a new CUSIP, prefix, pool number, and issuance date.

c. Freddie Mac is offering the exchange to promote liquidity in the 55-day TBA-eligible market. The exchange of non-TBA eligible securities for 55-day Freddie Mac MBS will help provide greater consistency across Freddie Mac's fixed-rate securities population. After the Single Security Initiative's implementation, all new issue Freddie Mac Single Family fixed-rate securities will have a 55-day payment delay.

d. Exchanges will be initiated at the option of the investor and will not be mandatory. The exchange offer is expected to open in May 2019, the month prior to the Single Security Initiative go-live. The Dealer-facilitated path will stay open for the foreseeable future, while the Direct-to-Freddie Mac exchange path is expected to stay open for 3-5 years.

e. Investors will receive a one-time payment that will be the approximate fair value compensation for the 10 days' delay of the bond's payment, or float compensation. For the Direct-to-Freddie Mac exchange path, this compensation will be paid through a one-time cash payment. For the Dealer-facilitated path, it is anticipated that the dealer will likely net the float compensation payment from the buy-back price of the 55-day security. Freddie Mac will treat the float compensation payment as a tax-free adjustment to the security basis. As such, for those investors that execute their exchange through the Direct-to-Freddie Mac path, Freddie Mac does not intend to report the payment as taxable income to the investor or to the IRS. However, Freddie Mac is not dictating to investors how they must treat the payment. Some investors may conclude, after consulting with their tax advisors, that the float compensation is taxable income when received**.**

INT 19-02 Discussion

3. The Working Group reached a consensus to incorporate a limited-scope exception to *SSAP No. 26—Bonds* and prescribe guidance for SSAP No. 43 specific to securities exchanged as part of the Freddie Mac Single Security Initiative. This limited-scope exception requires continuation of the amortized cost basis of the security surrendered to the new security received in the exchange. This is an exception to the guidance in SSAP No. 26 that requires fair value of the surrendered security to become the cost basis for the received security, unless the fair value of the security received is more clearly evident. Although there is not explicit guidance for exchanges in SSAP No. 43, an entity referring to other statutory accounting standards for application, (such as *SSAP No. 95—Nonmonetary Transactions)* would infer a fair value measurement, rather than a continuation of the amortized cost basis.

4. By continuing the amortized cost basis, the reporting entity shall not recognize any gains or losses (from comparison of fair value to the amortized cost basis) as a result of the exchange. This is considered appropriate as most of the elements of the security held after the exchange will exactly match the security surrendered, including unpaid principal balance, pool factors and weighted average coupon. Furthermore, the cash flows of the new securities will be ultimately backed by the same loans as the original security.

5. This interpretation also permits reporting entities to adjust the security's basis (decrease) for the float compensation received. This treatment agrees to how Freddie Mac will treat the compensation payment. This treatment was determined by Freddie Mac after receiving confirmation from the Securities Exchange Commission (SEC) that the SEC does not object to the treatment of the exchange as a minor modification of an existing security. Freddie Mac has also identified that it does not intend to report the float compensation as taxable income to the investor or the IRS, but has identified that the holders of the securities must rely on their own tax and accounting advisors in determining the best course of action.

INT 18-03 Status

6. The consensus adopted in this interpretation shall remain applicable as long as securities are exchanged under the Freddie Mac Single Security Initiative. This interpretation is only applicable for the specific exchange program reviewed and shall not be inferred to other security exchanges.

7. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 20-01: ASUs 2020-04, 2021-01 & 2022-06 – Reference Rate Reform

INT 20-01 Dates Discussed

March 26, 2020; April 15, 2020; May 20, 2021, March 22, 2023, August 13, 2023

INT 20-01 References

Current:
SSAP No. 15—Debt and Holding Company Obligations
SSAP No. 22—Leases
SSAP No. 86—Derivatives

This INT applies to all SSAPs with contracts within scope of ASU 2020-04, which allows for modifications due to reference rate reform and provides for the optional expedient to be accounted for as a continuation of the existing contract.

INT 20-01 Issue

1. This interpretation has been issued to provide statutory accounting and reporting guidance for the adoption with modification of *ASU 2020-04 – Reference Rate Reform (Topic 848), Facilitation of the Effects of Reference Rate Reform on Financial Reporting*, *ASU 2021-01, Reference Rate Reform (Topic 848), Scope*, and *ASU 2022-06, Reference Rate Reform (Topic 848), Deferral of the Sunset Date of Topic 848* for applicable statutory accounting principles. The Financial Accounting Standards Board (FASB) issued ASU 2020-04, ASU 2021-01, and ASU 2022-06 to provide optional, transitional and expedient guidance as a result of reference rate reform.

2. Reference rate reform typically refers to the transition away from referencing the London Interbank Offered Rate (LIBOR), and other interbank offered rates (IBORs), and moving toward alternative reference rates that are more *observable* or transaction based. In July 2017, the governing body responsible for regulating LIBOR announced it will no longer require banks to continue LIBOR submissions after 2021 – likely sunsetting both the use and publication of LIBOR. An important note is that while LIBOR is the primary interbank offering rate, other similar rates are potentially affected by reference rate reform.

3. With a significant number of financial contracts solely referencing IBORs, their discontinuance will require organizations to reevaluate and modify any contract that does not contain a substitute reference rate. A large *volume* of contracts and other arrangements, such as debt agreements, lease agreements, and derivative instruments, will likely need to be modified to replace all references of interbank offering rates that are expected to be discontinued. While operational, logistical, and legal challenges exist due to the sheer volume of contracts that will require modification, accounting challenges were presented as contract modifications typically require an evaluation to determine whether the modifications result in the establishment of a new contract or the continuation of an existing contract. As is often the case, a change to the critical terms (including reference rate modifications) typically requires remeasurement of the contract, or in the case of a hedging relationship, a dedesignation of the transaction.

4. The overall guidance in ASU 2020-04 is that a qualifying modification (as a result of reference rate reform) should not be considered an event that requires contract remeasurement at the modification date or reassessment of a previous accounting determination. FASB concluded that as reference rate changes are a market-*wide* initiative, one that is required primarily due to the discontinuance of LIBOR, it is outside the control of an entity and is the sole reason compelling an entity to make modifications to contracts or hedging strategies. As such, FASB determined that the traditional financial reporting requirements of discontinuing

such contracts and treating the modified contract as an entirely new contract or hedging relationship would, 1) not provide decision-useful information to financial statement users, and 2) require a reporting entity to incur significant costs in the financial statement preparation and potentially reflect an adverse financial statement impact, one of which may not accurately reflect the intent or economics of a modification to a contract or hedging transaction.

5. Guidance in ASU 2020-04 allows a method to ensure that the financial reporting results would continue to reflect the intended continuation of contracts and hedging relationships during the period of the market-wide transition to alternative reference rates – thus, generally not requiring remeasurement or dedesignation if certain criteria are met.

6. Guidance in ASU 2021-01 expanded the scope of ASU 2020-04 by permitting the optional, transitional, expedient guidance to also include derivative contracts that undergo a similar transition but do not specifically reference a rate that is expected to be discontinued. While these contract modifications do not reference LIBOR (or another reference rate expected to be discontinued), the changes are the direct result of reference rate reform and were deemed to be eligible for similar exception treatment. ASU 2021-01 allows for modifications in interest rates indexes used for margining, discounting or contract price alignment, as a result of reference rate reform initiatives (commonly referred to as a "discounting transition") to be accounted for as a continuation of the existing contract and hedge accounting. On August 13, 2023, the Working Group added the guidance in ASU 2022-06 which only acts to defer the sunset date of Topic 848 from December 31, 2022, to December 31, 2024, after which entities will no longer be permitted to apply the relief from the prior ASUs.

7. The optional, expedient and exceptions guidance provided by the amendments in ASU 2020-04, ASU 2010-01, and ASU 2022-04 are applicable for all entities. However, they are only effective as of March 12, 2020, through December 31, 2024. This is because the amendments are intended to provide relief related to the accounting requirements in U.S. generally accepted accounting principles (U.S. GAAP) due to the effects of the market-wide transition away from IBORs. The relief provided by the amendments is temporary in its application in alignment with the expected market transition period. However, the FASB will monitor the market-wide IBOR transition to determine whether future developments warrant any changes, including changes to the end date of the application of the amendments in this ASU. If such an update occurs, the Working Group may also consider similar action. It is not expected that the Working Group will take action prior to or in the absence of a FASB amendment.

8. The accounting issues are:

a. Issue 1: Should a reporting entity interpret the guidance in ASU 2020-04 as broadly accepted for statutory accounting?

b. Issue 2: Should the optional, expedient and exception guidance in ASU 2020-04 apply to debt and other service agreements addressed in SSAP No. 15?

c. Issue 3: Should the optional, expedient and exception guidance in ASU 2020-04 apply to lease transactions addressed in SSAP No. 22?

d. Issue 4: Should the optional, expedient and exception guidance in ASU 2020-04 apply to derivative transactions addressed in SSAP No. 86?

e. Issue 5: Should the optional, expedient and exception guidance in ASU 2021-01 apply to derivative transactions addressed in SSAP No. 86?

INT 20-01 Discussion

9. For Issue 1, the Working Group came to the consensus that ASU 2020-04 shall be adopted, to include the same scope of applicable contracts or transactions for statutory accounting with the only modification related to a concept not utilized by statutory accounting, as noted below. The Working Group

agreed the amendments provide appropriate temporary guidance that alleviate the following concerns due to reference rate reform:

a. Simplifies accounting analyses under current U.S. GAAP and statutory accounting principles (SAP) for contract modifications.

   i. All contracts within scope of ASU 2020-04, which allows for modifications due to reference rate reform and provides for the optional expedient to be accounted for as a continuation of the existing contract.

b. Allows hedging relationships to continue without dedesignation upon a change in certain critical terms.

c. Allows a change in the designated benchmark interest rate to a different eligible benchmark interest rate in a fair value hedging relationship.

d. Suspends the assessment of certain qualifying conditions for fair value hedging relationships for which the shortcut method for assuming perfect hedge effectiveness is applied.

e. Simplifies or temporarily suspends the assessment of hedge effectiveness for cash flow hedging relationships.

f. The only SAP modification to this ASU is related to the option to sell debt currently classified held-to-maturity. This concept is not employed by statutory accounting and thus is not applicable.

10. For Issue 2, the Working Group came to the consensus that debt and service agreement modifications, as a result of reference rate reform, should not typically rise to the level of requiring a reversal and rebooking of the liability, as SSAP No. 15 states such liabilities should only be derecognized if extinguished. A reference rate modification should not generally require de-recognition and re-recognition under statutory accounting. Nonetheless, for clarity and consistency with ASU 2020-04, the Working Group came to the consensus that should an eligible contract be affected by reference rate reform, then the temporary guidance in ASU 2020-04 shall apply.

11. For Issue 3, the Working Group came to the consensus that lease modifications, solely caused by reference rate reform and ones eligible for optional expedience, likely do not rise to the level of a modification requiring re-recognition as a new lease under statutory accounting. SSAP No. 22~~R~~, paragraph 17 states only modifications in which grant the lessee additional rights shall be accounted for as a new lease. These *changes* are outside the scope allowed for optional expedience in ASU 2020-04. Nonetheless, for clarity and consistency with ASU 2020-04, the Working Group came to a consensus that if an eligible lease affected by reference rate reform, then the temporary guidance in ASU 2020-04 shall apply.

12. For Issue 4, the Working Group came to the consensus that ASU 2020-04 shall be applied to derivative transactions as the following considerations provided in the ASU are appropriate for statutory accounting:

a. For any hedging relationship, upon a change to the critical terms of the hedging relationship, allow a reporting entity to continue hedge accounting rather than dedesignate the hedging relationship.

b. For any hedging relationship, upon a change to the terms of the designated hedging instrument, allow an entity to change its systematic and rational method used to recognize the excluded component into earnings and adjust the fair value of the excluded component through earnings.

c. For fair value hedges, allow a reporting entity to change the designated hedged benchmark interest rate and continue fair value hedge accounting.

d. For cash flow hedges, adjust the guidance for assessment of hedge effectiveness to allow an entity to continue to apply cash flow hedge accounting.

13. For Issue 5, the Working Group came to a consensus on May 20, 2021, that ASU 2021-01 shall be applied to derivative transactions for statutory accounting. Accordingly, derivative instruments that are modified to change the reference rate used for margining, discounting, or contract price alignment that is a result of reference rate reform (regardless of whether the reference rate that is expected to be discontinued) are eligible for the exception guidance afforded in ASU 2020-04 in that such a modification is not considered a change in the critical terms that would require dedesignation of the hedging relationship. In addition, for all derivatives (those qualifying for hedge accounting, those that do not qualify for hedge accounting and replication (synthetic asset) transactions (RSAT)), a reporting entity may account for and report modifications (that are within the scope of INT 20-01) as a continuation of the existing contract even when the legal form of the modification is a termination of the original contract and its replacement with a new reference rate reform contract. This includes in-scope modifications of centrally cleared swap contracts whether they are automatically transitioned at a cessation date or voluntarily executed prior to cessation.

14. Additionally, for U.S. GAAP purposes, if an entity has not adopted the amendments in *ASU 2017-12, Derivatives and Hedging*, it is precluded from being able to utilize certain expedients for hedge accounting. For statutory accounting purposes, only the hedge documentation requirements were adopted from ASU 2017-12, while the remainder of the items are pending statutory accounting review. The Working Group concluded that all allowed expedient methods are permitted as elections for all reporting entities under statutory *accounting*. However, if a reporting entity is a U.S. GAAP filer, the reporting entity may only make elections under ASU 2017-12 if such elections were also made for their U.S. GAAP financials.

INT 20-01 Status

15. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 20-06: Participation in the 2020 TALF Program

INT 20-06 Dates Discussed

May 5, 2020; May 20, 2020

INT 20-06 References

SSAP No. 64—Offsetting and Netting of Liabilities
SSAP No. 103—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities
INT 01-31: Assets Pledged as Collateral

INT 20-06 Issue

1. The Federal Reserve reestablished the Term Asset-Backed Securities Loan Facility (TALF) on March 23, 2020, to support the flow of credit to consumers and businesses. The TALF program will enable the issuance of asset-backed securities (ABS) backed by student loans, auto loans, credit card loans, loans guaranteed by the Small Business Administration (SBA), and certain other assets.

2. Under the TALF program, the Federal Reserve will lend on a non-recourse basis to holders of certain AAA-rated ABS backed by newly and recently originated consumer and small business loans. The Federal Reserve will lend an amount equal to the market value of the ABS less a haircut and will be secured at all times by the ABS. Treasury, using the Exchange Stabilization Fund (ESF), will also make an equity investment in the special purpose vehicle (SPV) established by the Federal Reserve for this facility.

3. The TALF is established by the Federal Reserve under the authority of Section 13(3) of the Federal Reserve Act, with approval of the Treasury Secretary.

4. Per review of public data available from the prior 2009 TALF program, there were a limited number of insurance reporting entities that were the actual borrower (entity that directly received the loan) under the TALF program. Rather, in most instances, insurance reporting entities were a material investor to the actual borrower. Per the TALF data, a material investor reflects the entity or individual with 10 percent or greater beneficial ownership interest in any class of securities of a borrower. Such ownership interest may be a direct, intermediate or ultimate interest. Due to the different methods of participating in the TALF program, this interpretation focuses on both reporting entity borrowers and reporting entity investors.

5. For reporting entity borrowers (entity that directly received the loan), the accounting issues addressed in this interpretation include:

   a. How the loan received, and collateral provided shall be reported within the statutory financial statements.

   b. Whether the pledged assets shall be reported as admitted assets as the collateral pledged to the TALF program is not permitted to be substituted.

6. For reporting entities that are not the direct borrowers, but represent investors to the direct borrower, the accounting issues addressed in this interpretation include:

a. How the reporting entity shall report their investment to a TALF borrower.

b. Whether the reporting entity investor is permitted to pledge assets under the TALF program, and retain admittance, when the reporting entity is not the direct borrower under the TALF program.

7. The April 9, 2020, term sheet for the 2020 TALF program:

https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200409a1.pdf

Term Asset-Backed Securities Loan Facility

Effective April 9, 2020
(The Board of Governors of the Federal Reserve System ("Board") and Secretary of the Treasury may make adjustments to the terms and conditions described in this term sheet. Any changes will be announced on the Board's website.)

Facility:
The TALF is a credit facility authorized under section 13(3) of the Federal Reserve Act intended to help meet the credit needs of consumers and businesses by facilitating the issuance of asset-backed securities ("ABS") and improving the market conditions for ABS more generally.

The TALF will serve as a funding backstop to facilitate the issuance of eligible ABS on or after March 23, 2020. Under the TALF, the Federal Reserve Bank of New York ("Reserve Bank") will commit to lend to a special purpose vehicle ("SPV") on a recourse basis. The Department of the Treasury will make an equity investment of $10 billion in the SPV, as described below.

The TALF SPV initially will make up to $100 billion of loans available. The loans will have a term of three years; will be nonrecourse to the borrower; and will be fully secured by eligible ABS.

Eligible Borrowers:
All U.S. companies that own eligible collateral and maintain an account relationship with a primary dealer are eligible to borrow under the TALF. For the purpose of this document, a U.S. company is defined as a business that is created or organized in the United States or under the laws of the United States and that has significant operations in and a majority of its employees based in the United States.

Eligible Collateral:
Eligible collateral includes U.S. dollar denominated cash (that is, not synthetic) ABS that have a credit rating in the highest long-term or, in the case of non-mortgage backed ABS, the highest short-term investment-grade rating category from at least two eligible nationally recognized statistical rating organizations ("NRSROs") and do not have a credit rating below the highest investment-grade rating category from an eligible NRSRO. All or substantially all of the credit exposures underlying eligible ABS must have been originated by a U.S. company, and the issuer of eligible collateral must be a U.S. company. With the exception of commercial mortgage-backed securities ("CMBS"), eligible ABS must be issued on or after March 23, 2020. CMBS issued on or after March 23, 2020, will not be eligible. For CMBS, the underlying credit exposures must be to real property located in the United States or one of its territories. Eligible collateral must be ABS where the underlying credit exposures are one of the following:

1) Auto loans and leases;
2) Student loans;
3) Credit card receivables (both consumer and corporate);
4) Equipment loans and leases;
5) Floorplan loans;

6) Insurance premium finance loans;
7) Certain small business loans that are guaranteed by the Small Business Administration;
8) Leveraged loans; or
9) Commercial mortgages.

Eligible collateral will not include ABS that bear interest payments that step up or step down to predetermined levels on specific dates. In addition, the underlying credit exposures of eligible collateral must not include exposures that are themselves cash ABS or synthetic ABS.

To be eligible collateral, all or substantially all of the underlying credit exposures must be newly issued, except for legacy CMBS.

The feasibility of adding other asset classes to the facility or expanding the scope of existing asset classes will be considered in the future.

Conflicts of interest: Eligible borrowers and issuers of eligible collateral will be subject to the conflicts of interest requirements of section 4019 of the CARES Act.

Restriction on single-asset single-borrower ("SASB") CMBS and commercial real estate collateralized loan obligations ("CRE CLOs"): SASB CMBS and CRE CLOs will not be eligible collateral.

Restrictions on CLO loan substitution: Only static CLOs will be eligible collateral.

Collateral Valuation: Haircut schedule is below. The haircut schedule is consistent with the haircut scheduled used for the TALF established in 2008.

Pricing: For CLOs, the interest rate will be 150 basis points over the 30-day average secured overnight financing rate ("SOFR"). For SBA Pool Certificates (7(a) loans), the interest rate will be the top of the federal funds target range plus 75 basis points. For SBA Development Company Participation Certificates (504 loans), the interest rate will be 75 basis points over the 3-year fed funds overnight index swap ("OIS") rate. For all other eligible ABS with underlying credit exposures that do not have a government guarantee, the interest rate will be 125 basis points over the 2-year OIS rate for securities with a weighted average life less than two years, or 125 basis points over the 3-year OIS rate for securities with a weighted average life of two years or greater. The pricing for other eligible ABS will be set forth in the detailed terms and conditions.
Fees: The SPV will assess an administrative fee equal to 10 basis points of the loan amount on the settlement date for collateral.

Maturity: Each loan provided under this facility will have a maturity of three years.

Investment by the Department of the Treasury: The Department of the Treasury, using the Exchange Stabilization Fund, will make an equity investment of $10 billion in the SPV.

Non-Recourse: Loans made under the TALF are made without recourse to the borrower, provided the requirements of the TALF are met.

Prepayment: Loans made under the TALF will be pre-payable in whole or in part at the option of the borrower, **but substitution of collateral during the term of the loan generally will not be allowed.**

Program Termination: No new credit extensions will be made after September 30, 2020, unless the TALF is extended by the Board of Governors of the Federal Reserve System and the Department of the Treasury.

Other Terms and Conditions: More detailed terms and conditions will be provided at a later date, primarily based off of the terms and conditions used for the 2008 TALF. In addition, the Federal Reserve reserves the right to review and make adjustments to these terms and conditions –

including size of program, pricing, loan maturity, collateral haircuts, and asset and borrower eligibility requirements – consistent with the policy objectives of the TALF.

INT 20-06 Discussion

For Reporting Entity Borrowers - Insurance Reporting Entity Received the Loan

8. Reporting entity borrowers shall report the cash received under the TALF program with a corresponding liability. The liability shall be captured in scope of *SSAP No. 15—Debt and Holding Company Obligations* and reported as "borrowed money." The disclosures in SSAP No. 15 shall be completed. Once the cash received has been reinvested, the reporting entity shall report the acquired asset in accordance with the applicable statement of statutory accounting principle.

9. Reporting entity borrowers shall report asset-backed securities pledged to the TALF program as restricted assets with the appropriate code in the investment schedules and disclosed in accordance with *SSAP No. 1—Accounting Policies, Risks & Uncertainties and Other Disclosures*, and in General Interrogatory, Part 1: 25.30 – Pledged as Collateral. Assets pledged to the TALF program are subject to the underlying asset risk-based capital charge but are excluded from an additional "restricted asset" risk-based capital charge. (As a carryover from the 2009 TALF Program, existing provisions in the risk-based capital instructions instruct the removal of assets pledged to the TALF program reported as restricted assets in the General Interrogatories.)

10. Reporting entity borrowers are permitted to continue reporting pledged asset-backed securities as admitted assets in the statutory financial statements if the following two conditions are met:

a. Asset qualified as an admitted asset before it was pledged to the TALF program.

b. The reporting entity has not committed an uncured contract default.

11. As the TALF program specifically identifies that substitution of pledged collateral during the term of the loan will generally not be allowed, this interpretation provides an exception to existing statutory accounting requirements. Pursuant to *INT 01-31: Assets Pledged as Collateral*, a pledged asset shall be readily substitutable in order to be admitted in the statutory financial statements. With the exception in this interpretation, assets held by the insurance reporting entity (borrower) that are pledged to the TALF program can be admitted even though they are not generally substitutable.

12. Reporting entity borrowers shall not net the obligation to return the liability and the pledged collateral in the statutory financial statements. The criteria for a valid right of offset in *SSAP No. 64—Offsetting and Netting of Assets and Liabilities* has not been met for these transactions. Specifically, the reporting entity does not have the right to offset the amount owed under the TALF program and the reporting entity does not intend to setoff the amount owed. Although the collateral pledged could be claimed under the TALF program in the event that the insurer reporting entity commits a loan repayment default, the ability to claim pledged collateral does not represent a "right of setoff" with the counterparty.

13. Although the transaction is similar to a repurchase agreement accounted for as a secured borrowing, the TALF transaction is not a repurchase transaction. As such, the provisions and disclosures for repurchase agreements are not applicable.

14. In the event that a reporting entity commits a contract default, and the pledged collateral is retained under the TALF program, the reporting entity shall follow the guidance in SSAP No. 103~~R~~, paragraph 20, in removing the pledged assets and liability from the statutory financial statements.

For Reporting Entity Investors - Insurance Reporting Entity Does Not Receive the Loan but is an "Investor" to an Entity that was the Direct TALF Borrower

15. Reporting entity investors shall report the investment in the borrower in accordance with the underlying nature of the investment and the relationship with the borrower. The underlying investments will be subject to the reporting and RBC requirements for the applicable SSAP and reporting schedule:

a. If the borrower is a limited liability company (LLC), the investment shall be reported in accordance with *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies.*

b. If the borrower is a private equity fund (e.g., joint venture), the investment shall be reported in accordance with *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies.*

c. If the borrower is an affiliate, the investment shall be reported in accordance with *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities.*

16. Reporting entity investors are not permitted to admit assets pledged to the TALF program if they are not the direct borrower. This is because the return of the assets would be contingent on the action of the actual borrower to the TALF program and not the reporting entity. This provision is consistent with *SSAP No. 4—Assets and Nonadmitted Assets*, footnote 2:

> If assets of an insurance entity are pledged or otherwise restricted by the action of a related party, the assets are not under the exclusive control of the insurance entity and are not available to satisfy policyholder obligations due to these encumbrances or other third-party interests. Thus, pursuant to SSAP No. 4, paragraph 2(c), such assets shall not be recognized as an admitted asset on the balance sheet. Additional guidance for assets pledged as collateral is included in INT 01-31.

INT 20-06 Consensus

17. The Working Group reached a consensus to prescribe statutory accounting guidance for insurance reporting entity involvement in the 2020 TALF Program. Pursuant to this consensus:

a. Reporting entities borrowers who directly receive the TALF loan shall follow guidance in paragraphs 8-14 of this interpretation for the statutory accounting and reporting. As detailed in paragraph 11, this interpretation provides an exception to allow admitted asset reporting for the pledged securities although the TALF program does not permit the pledged assets to be generally substitutable.

b. Reporting entities that do not directly receive the TALF loan, but are investors to borrowers that receive the TALF loan, shall follow the provisions in paragraphs 15-16 for the statutory accounting and reporting.

18. The provisions detailed in this interpretation are applicable for the duration of the 2020 TALF loan program.

INT 20-06 Status

19. No further discussion planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 20-09: Basis Swaps as a Result of the LIBOR Transition

INT 20-09 Dates Discussed

July 15, 2020; July 30, 2020

INT 20-09 References

Current:
SSAP No. 86—Derivatives

INT 20-09 Issue

1. This interpretation is to provide statutory accounting and reporting guidance for "basis swaps." Basis swaps within the scope of this interpretation are defined as compulsory derivatives issued by Central Clearing Parties (CCP), for certain cleared derivatives, issued solely in response to the market-wide transition away from the London Interbank Offered Rate (LIBOR) and toward the Secured Overnight Financing Rate (SOFR).

2. SOFR is a broad measure of the cost of borrowing cash overnight, generally collateralized by Treasury Securities. It represents nearly a risk-free rate that is correlated with other money market rates and is fully transaction based (thus ensuring full transparency), by reflecting a broad measure of overnight U.S. Treasury repurchase transactions. In conjunction with the transition from LIBOR, many alternative reference rates, such as the Effective Federal Funds Rate (EFFR), an interest rate typically utilized by banks representing a charge for overnight loans, used to meet regulatory reserve requirements, are also being transitioned to SOFR. Accordingly, under the general topic referred to as "Reference Rate Reform," contracts which reference or utilize LIBOR or EFFR, are anticipated to be modified to reference SOFR.

3. The Statutory Accounting Principles (E) Working Group previously adopted *INT 20-01: Reference Rate Reform*, which substantially adopted *ASU 2020-04 – Reference Rate Reform* and applies to all SSAPs with contracts within scope of ASU 2020-04. INT 20-01 allows for contract modifications, due to reference rate reform, to be accounted for as a continuation of the existing contract and thus not requiring remeasurement. Among other things, INT 20-01 allows for 1) certain hedging relationships to continue without requiring dedesignation upon a change in certain critical terms (i.e., changing reference rates), and 2) changes in the designated benchmark interest rate to a different eligible benchmark interest rate in a fair value hedging relationship. INT 20-01 recognized that many of these contracts, as part of the discontinuance of LIBOR, will transition to SOFR, an industry recognized preferred benchmark rate.

4. CCPs will make a similar transition, converting open derivative end-of-day valuation calculations from EFFR to SOFR. This transition will occur in two steps, both of which are anticipated to occur on October 16. First, the CCPs will conduct a *standard end-of day valuation* cycle based on EFFR. Then, the CCP will conduct a *special valuation cycle* on those same positions, however utilizing SOFR as the new, ongoing discounting rate. Based on the differences between EFFR and SOFR, the CCP will issue cash adjustments to each account to offset the value adjustments arising from the change in discount rates and additionally will issue mandatory EFFR/SOFR basis swaps, thus restoring the account holder's original risk profile.

5. *SSAP No. 86—Derivatives* addresses the recognition and measurement of derivatives used for hedging, income generation, and replication transactions. Additionally, guidance is provided for derivatives not utilized for one of these broad categories (known as "other derivatives"). Derivatives that are classified

as “other derivatives” are nonadmitted under SSAP No. 86, whereas derivatives in the other categories are admitted provided they conform to the requirements of the statement.

6. The accounting issues are:

   a. Issue 1: How should EFFR/SOFR basis swaps be classified and reported in the statutory financial statements?

   b. Issue 2: How should EFFR/SOFR basis swaps be valued in the statutory financial statements?

INT 20-09 Discussion

7. For Issue 1, the Working Group reached a consensus that mandatory basis swaps issued by CCPs, in response to reference rate reform, shall be classified as a derivative used for “hedging.” In collaboration with industry representatives, Working Group support staff has confirmed that a significant majority of the derivatives transacted through a CCP meet the definition of a hedging transaction. By using this “used for hedging” classification, instead of an “other derivative” classification, the basis swap derivative received will be admitted under SSAP No. 86.

8. For Issue 2, the Working Group reached a consensus that although the instrument shall be considered a hedging derivative, the instrument shall not be considered or reported as an “effective” hedging derivative (using the “hedge accounting” measurement approach permitted in SSAP No. 86), unless the instrument qualifies, with the required documentation, as a highly effective hedge under SSAP No. 86. Unless the effective hedge requirements are met, the instruments shall be reported on Schedule DB, utilizing the category of “Hedging Other.” Pursuant to the guidance in SSAP No. 86, if the basis swap derivative is not an effective hedge, the derivative shall be accounted for at fair value and the changes in fair value shall be recorded as unrealized gains or unrealized losses (referred to as fair value accounting.)

INT 20-09 Status

8. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 22-01: Freddie Mac When-Issued K-Deal (WI Trust) Certificates

INT 22-01 Dates Discussed

April 4, 2022; May 24, 2022

INT 22-01 References

Current:
SSAP No. 43—Asset-Backed Securities
SSAP No. 86—Derivatives

INT 22-01 Issue

1. This interpretation is to address questions on the accounting and reporting for Freddie Mac "When-Issued K-Deal (WI Trust) Certificates" (WI Program). Ultimately, the question is whether the structure should be initially captured in scope of *SSAP No. 43~~R—Loan-Backed and Structured~~Asset-Backed Securities* or as a forward contract in scope of *SSAP No. 86—Derivatives*.

2. The design of the WI Program is summarized as follows:

   a. Investor acquires WI Trust certificates, which are backed by cash held in the WI Trust and pay a fixed coupon amount funded from a Freddie Mac guarantee.

   b. Within 90 days, the trust uses the cash to acquire newly issued K-Deal structured pass-through certificates (SPCs) meeting certain pooling parameters laid out in the respective WI Offering Circular Supplement. K-Deal SPC (s) are Freddie Mac-issued structured pass-through certificates backed by the corresponding class of certificates issued by a separate REMIC trust that holds multifamily fixed-rate mortgage loans. The cash flows from the mortgage loans held by the REMIC trust provide pass-through payments to holders of the K-Deal SPCs.

   c. An investor can choose to continue to hold the WI Trust certificates or exchange dollar-for-dollar their WI securities into the underlying K-Deal SPCs. In either case, the investor receives a pass-through of cash flows generated by the mortgages held in the REMIC trust and the performance of the K-Deal SPCs is guaranteed by Freddie Mac. If continuing to hold the WI Trust certificates – rather than convert the certificates to K-deal SPCs – the K-Deal SPCs are held by the WI Trust, who in turn passes the cashflows to WI Trust investors. The WI Trust certificates benefit from Freddie Mac payment guarantee which guarantees that any cashflows collected from the K-Deal SPCs will be paid to the WI certificate holders.

3. Additional characteristics on this program include the following:

   a. The WI Trust certificates are public securities and tradeable shortly after pricing.

   b. The WI Trust certificates are backed by a Freddie Mac guarantee from acquisition.

   c. From acquisition of the WI Trust certificates, the investor receives fixed coupon amounts reflective of the investment terms of the K-Deal SPCs.

d. The WI Trust is obligated to acquire, and Freddie Mac is required to sell, the K-Deal SPCs at the amount stated at the time of initial investment. Meaning, the investor is not at a risk of loss, nor will experience any variation in outcome due to underlying variables that occur from the time of initial investment in the WI Trust until the K-Deal SPCs are acquired. If market forces change the purchase price of the K-Deal SPCs during the 90-days after initial acquisition of the WI Trust certificates, then Freddie Mac is still required to sell the K-Deal certificates at the terms agreed to at original investment. Ultimately, the investor is guaranteed an investment in K-Deal SPCs that reflects the notional value of the WI Trust-certificates and coupon terms at initial acquisition. (For example, if the investor acquired $100 million of WI Trust certificates at acquisition, when the K-Deals are subsequently acquired, the entity will receive $100 million of K-Deal SPCs with the same payment terms regardless of any market impacts.)

e. In the event that Freddie Mac is unable to acquire the K-Deal SPCs within the 90-day period, Freddie Mac is required to return the principal to the investor as well as provide a yield maintenance payment calculated using the full coupon payments that would have been received over the course of the investment.

f. In the event that the investor elects to exchange the WI Trust certificates to the K-Deal SPCs, the investor receives an equivalent principal amount of the K-Deal SPCs of the same class. Although the investment will have a change in CUSIP, any such exchange is not deemed to be a taxable event as described in the respective Offering Circular Supplements for the WI Certificates. As such investors will not recognize a gain or loss on the exchange and investors will be treated as continuing to own the interests that were owned immediately prior to the exchange. Stated differently, any gains or losses on the exchanged WI-Certificates are "rolled into" the investors' new K-Deal Certificate position.

4. The question of whether the structure is a loan-backed or structured security, or a derivative is primarily focused on the initial acquisition and the 90-day (or less) timeframe before the WI Trust acquires K-Deal certificates. The question is whether the initial 90-day acquisition of the WI Trust certificate, prior to the trust's acquisition of the K-Deal certificates, represents a forward contract required to be accounted for under SSAP No. 86. Key excerpts from SSAP No. 86 are as follows:

a. The definition of a derivative instrument from SSAP No. 86, paragraph 4:

> 4. "Derivative instrument" means an agreement, option, instrument or a series or combination thereof:
>
> a. 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
>
> b. 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.

b. The definition of a forward contract from SSAP No. 86, paragraph 5.d.:

> 5.d. "Forwards" are agreements (other than futures) between two parties that commit one party to purchase and the other to sell the instrument or commodity underlying the contract at a specified future date. Forward contracts fix the price, quantity, quality, and date of the purchase and sale. Some forward contracts involve the initial payment of cash and may be settled in cash instead of by physical delivery of the underlying instrument.

5. This interpretation intends to clarify whether investments in the Freddie Mac WI Program shall be initially captured in scope of SSAP No. 86 or captured in scope of SSAP No. 43.

INT 22-01 Discussion

6. This interpretation clarifies that investments in the Freddie Mac WI Program shall be captured in scope of SSAP No. 43 from initial acquisition, and not as a derivative forward contract, for the following reasons:

a. The WI Program is fully guaranteed by Freddie Mac and ensures that the investor will receive pass-through certificates, backed my mortgage loans held in trust, that reflect the terms of the investment set at original acquisition. In the event that the K-Deal certificates cannot be acquired, Freddie Mac is guaranteed to provide payment to the investor that reflects the full principal and interest per the original terms of the agreement, which reflects the payments that would have been received overtime if K-Deal certificates had been acquired.

b. The definition of a forward contract in SSAP No. 86 reflects an agreement between two parties that commit one party to purchase and another party to sell the instrument underlying the contract at a specified future date. With the WI Trust Program, the investor does not have a future commitment to acquire securities, as the investor acquires the WI Trust certificate on day one of the transaction, and the investor is not required to convert the WI Trust certificates at any time. This WI Trust certificate is not a derivative instrument, as at the time of acquisition, the certificate reflects a tradeable investment in a trust structure backed by cash and a Freddie Mac guarantee of cash flows in accordance with terms established at original acquisition. In addition to having no variation to the investor as a result of an underlying interest, there is no requirement on the investor to take delivery of a different investment. The ability to convert the WI Trust certificate to a K-Deal certificate is strictly an election to the investor and is not a requirement to receive the pass-through cash flows per the terms of the initial investment.

c. The WI Program, and resulting obligation of Freddie Mac, ultimately reflects an investment where the investor receives pass-through cash flows generated from mortgage loans acquired and held in trust. This investment dynamic is within the scope of SSAP No. 43, paragraphs 2-4[1]:

> 2. Loan-backed securities are defined as securitized assets not included in structured securities, as defined below, for which the payment of interest and/or principal is directly proportional to the payments received by the issuer from the underlying assets, including but not limited to pass-through securities, lease-backed securities, and equipment trust certificates.
>
> 3. Structured securities are defined as loan-backed securities which have been divided into two or more classes for which the payment of interest and/or principal of any class of securities has been allocated in a manner which is not proportional to payments received by the issuer from the underlying assets.
>
> 4. Loan-backed securities are issued by special-purpose corporations or trusts (issuer) established by a sponsoring organization. The assets securing the loan-backed obligation are acquired by the issuer and pledged to an independent trustee until the issuer's obligation has been fully satisfied. The investor only has direct recourse to the issuer's assets but may have secondary recourse to third parties through insurance or guarantee for repayment of the obligation. As a result,

[1] The guidance cited predates revisions to SSAP No. 43, which became effective January 1, 2025. Further review is planned in 2025.

the sponsor and its other affiliates may have no financial obligation under the instrument, although one of those entities may retain the responsibility for servicing the underlying assets. Some sponsors do guarantee the performance of the underlying assets.

d. The WI Program, and treatment as a SSAP No. 43 security, is consistent with the current guidance for TBA securities when an insurer intends to take possession of the resulting mortgage-backed security. A TBA security reflects the pre-purchase of mortgage-backed securities prior to the finalization of the security issuance. Pursuant to the annual statement instructions, TBA securities are to be reported on Schedule D-1, Long-Term Bonds, unless the structure more closely resembles a derivative. This determination depends on how a company uses the TBA. (For example, if a company intended to assume the mortgage-backed security once issued, the TBA would be captured on Schedule D-1 at initial acquisition. If a reporting entity was to continually trade/roll TBA exposures, this would be more characteristics of a derivative and would be captured on Schedule DB as a derivative.)

INT 22-01 Consensus

5. The Statutory Accounting Principles (E) Working Group reached a consensus that investments in the WI Trust Program shall be captured in scope of SSAP No. 43 from initial acquisition.

6. If a reporting entity elects to convert WI Trust SPC securities into K-Deal SPC securities, the guidance in the Annual Statement Instructions, Schedule D, Part 3 and Part 4, shall be followed. Per that guidance, the transition from a WI Trust to a K-Deal shall not be reported as a disposal or acquisition. As the terms and cost basis of the SPC certificates would be identical, and the change would only reflect a CUSIP number change, a disposal and reacquisition shall not be recorded.

7. Excerpt from Annual Statement Instructions, Schedule D, Part 3 and 4:

> This schedule should include a detailed listing of all securities that were purchased/acquired during the current reporting year that are still owned as of the end of the current reporting year (amounts purchased and sold during the current reporting year are reported in detail on Schedule D, Part 5, and only in subtotal in Schedule D, Part 3). This should include all transactions that adjust the cost basis of the securities. Thus, it should not be used for allocations of TBAs to specific pools subsequent to initial recording in Schedule D, Part 3, or other situations such as CUSIP number changes.

INT 22-01 Status

8. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 22-02: Third Quarter 2022 through Second Quarter 2023 Reporting of the Inflation Reduction Act - Corporate Alternative Minimum Tax

INT 22-02 Dates Discussed

October 6, 2022; October 24, 2022, November 16, 2022; December 13, 2022; April 12, 2023; May 16, 2023

INT 22-02 References

Current:
SSAP No. 9—Subsequent Events
SSAP No. 101—Income Taxes

INT 22-02 Issue

Key Provisions of the Inflation Reduction Act

1. The Inflation Reduction Act (Act) was enacted on August 16, 2022, and included a new corporate alternative minimum tax (CAMT). The Act and the CAMT go into effect for tax years beginning after 2022. Reporting entities shall refer to the Act and the resulting regulations and other tax guidance to determine application, but a non-authoritative high-level summary based on information at the time of initial INT discussion regarding the CAMT is as follows:

a. The CAMT is 15% of the corporation's "adjusted financial statement income" for the tax year, reduced by corporate alternative minimum foreign tax credit.

b. The CAMT will only apply to "applicable corporations" (determined on an affiliated group basis) with average adjusted financial statement income in excess of $1 billion for the three prior tax years. This threshold is reduced to $100 million in the case of certain foreign-parented corporations. When a corporation becomes subject to the CAMT, it remains an applicable corporation for purposes of the CAMT, even if its average adjusted financial statement income is less than $1 billion, unless an exception applies.

c. A corporation's adjusted financial statement income is the amount of net income or loss the corporation reports on its applicable financial statement. The income is adjusted for various purposes including certain adjustments in the case of consolidated returns or for foreign income.

d. The Act includes references to the tax codes which provides a hierarchy for determining the "applicable financial statement." At a high level, the first choice is U.S. generally accepted accounting principles (U.S. GAAP) financial statements; the second choice is international financial reporting standards (IFRS) financial statements. If U.S. GAAP and IFRS financial statements are not available, the financial statements filed by the taxpayer with any other regulatory or government body is acceptable. If the taxpayer is part of an affiliated group of corporations filing a consolidated return, the adjustable financial statement income for the group considers the group's applicable financial statement.

e. To determine its U.S. federal income tax liability, an applicable corporation will need to compute taxes under both systems—the regular tax system and the CAMT system. The CAMT is payable to the extent the tentative CAMT exceeds the regular corporate income tax. Any CAMT paid is available indefinitely as a credit carryover that could reduce future regular tax in future years if the regular tax liability is in excess of CAMT tax liability.

f. The Act directs the Treasury to issue regulations and other guidance relate to implementing the CAMT, so several issues are pending detailed clarifications including clarifying the definition of an applicable corporation, and providing guidance on the starting point for, and adjustments to, adjusted financial statement income, as well as the handling of separate company tax returns when required under current tax law that are unique to the insurance industry.

Interpretation Issues

2. This interpretation is focused on addressing third quarter 2022 transition accounting and reporting aspects of the new CAMT. While most insurers will not be subject to the CAMT, for those that know that they are subject, and those that could be subject to the CAMT, there are a variety of reporting uncertainties, particularly regarding reporting for third quarter 2022.

3. The CAMT is effective for the tax years on or after 2023.

4. Both statutory accounting principles and U.S. GAAP require the effects of tax changes on deferred taxes, including the valuation allowance (future realizability of existing DTAs) in the period in which the legislation is enacted (third quarter 2022). *SSAP No. 101—Income Taxes*, paragraph 7.e. requires the statutory valuation allowance adjustment as a direct reduction in the gross DTA if, based on the weight of available evidence, it is more likely than not that some or all of the gross DTAs will not be realized. Gross DTA less the statutory valuation allowance results in adjusted gross DTAs. The statutory valuation allowance adjustment is not reported as a separate line in the statutory financial statements (it is an off-balance sheet item that reduces the gross DTAs). The statutory valuation allowance is disclosed.

5. The statutory accounting calculation for admissible DTAs is determined using adjusted gross DTAs (gross DTAs reduced by the valuation allowance). For statutory accounting, admittance of adjusted gross DTAs in SSAP No. 101 depends on a three-component calculation, for which the second step limits admittance of adjusted gross DTAs to those that are expected to be realized in a timeframe that does not exceed three years. The actual number of years permitted depends on specifics for each reporting entity (type and other information about the reporting entity), but the maximum timeframe is three years. The last step admits DTAs which can be offset by DTLs.

6. Guidance in *SSAP No. 9—Subsequent Events* requires consideration of Type I and Type II[1] subsequent events through the date of the statutory financial statements and the date of issuance of the audited financial statements, or the date in which audited financial statements are available to be issued. For subsequent events identified after the statutory financial statements are filed (example, March 1), but before the audited financial statements are issued (example, June 1), reporting entities are generally required by their domestic state to amend their filed statutory financial statements to ensure that the statutory financial statements and the audited financial statements are consistent. Under this guidance, as additional information is made available on the impact of the Act, or information becomes available to update estimates and assessments, under existing statutory accounting guidance in SSAP No. 9, reporting entities would need to identify updated estimates as a Type I subsequent event in the audited financial statements.

[1] A Type I subsequent event relates to an event or transaction that provides additional evidence with respect to conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Under SSAP No. 9, entities shall recognize in the financial statements the effects of all material Type I subsequent events. A Type II subsequent event pertains to events or transactions that provide evidence to conditions that did not exist at the balance sheet date but arose after that date. Type II events are disclosed in the financial statements.

Issue 1 – Consideration of the Act for Third Quarter 2022 Financial Statements

7. During the period of enactment (third quarter 2022) reporting entities filing statutory financial statements would normally have to consider the applicability of the CAMT and if applicable, determine the impact on the statutory valuation allowance as well as assess DTAs for admissibility (e.g., realization timeframe). These elements will be collectively referred to as "calculations impacted by the Act" or "calculations impacted by the CAMT."

8. This interpretation will address the issue for what reporting entities are required to report or disclose regarding the calculations impacted by the CAMT for September 30, 2022, financial statements.

Issue 2 – Consideration of Subsequent Events for Third Quarter 2022 Financial Statements

9. SSAP No. 9 requires consideration of subsequent events through the date of the statutory financial statements and the date of issuance of the audited financial statements, or the date in which audited financial statements are available to be issued.

10. For reporting entities that materially revise or establish calculations impacted by the CAMT subsequent to September 30, 2022 (including the statutory valuation allowance, the timing of determination of net admitted DTAs, and the determination of the applicability of the CAMT), this interpretation will address the extent a Type I or Type II subsequent event assessment is required for third quarter 2022 financial reporting.

INT 22-02 Discussion

11. The Statutory Accounting Principles (E) Working Group consensuses to the noted issues are included below.

Response: Issue 1 – Consideration of the Act for Third Quarter 2022 Financial Statements

12. Reporting entities that are aware they will be subject to the CAMT would normally reflect the effects of the Act on the calculations impacted by the CAMT if reasonably estimable for third quarter 2022. Because of the timing of the adoption of the Act and the considerable number of unknown variables for September 30, 2022, reporting, the Working Group has determined that a reasonable estimate is not determinable for third quarter 2022 interim financial statements for the calculations impacted by the CAMT.

13. Because reasonable estimates of calculations impacted by the CAMT are not determinable, reporting entities shall not recognize impacts related to CAMT for third quarter 2022 financial statements, but shall make the following disclosures regarding the CAMT and the Act:

a. The Act was enacted during the reporting period on August 16, 2022.

b. A statement regarding whether the reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined if it expects to be liable for CAMT in 2023. For example:

i. The reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined that it does not expect to be liable for CAMT in 2023.

ii. The reporting entity (or the controlled group of corporations of which the reporting entity is a member) has not determined as of the reporting date if it will be liable for CAMT in 2023. The third quarter 2022 financial statements do not include an estimated impact of the CAMT because a reasonable estimate cannot be made.

iii. The reporting entity (or the controlled group of corporations of which the reporting entity is a member) has determined that it expects to be liable for CAMT in 2023. The third quarter 2022 financial statements do not include an estimated impact of the CAMT, because a reasonable estimate cannot be made.

Response: Issue 2 – Consideration of Subsequent Events for Third Quarter 2022 Financial Statements

14. For third quarter 2022 reporting, CAMT updated estimates or other calculations affected by the Act determined subsequent to third quarter statutory financial statement or filing date shall not be recognized as Type I subsequent events. Meaning, amended financial statements are not required to reflect updated estimates subsequent to the third quarter filing date and prior to the filing the third quarter financial statements. With the disclosure required under Issue 1, additional subsequent event disclosure (such as what would be required for Type II event) is not required.

15. Reporting entities shall be working in good faith to complete the accounting for the changes adopted under the Act.

INT 22-02 Status

16. The consensuses in this interpretation were adopted on October 24, 2022, to provide reporting guidance regarding the calculations impacted by the CAMT and provide limited-scope, limited-time exceptions to the valuation allowance and DTA calculations in response to legislation under SSAP No. 101 as well as Type I subsequent event requirements in SSAP No. 9 for September 30, 2022, statutory reporting. As detailed, the exceptions to SSAP No. 101 and SSAP No. 9 are effective for third quarter 2022.

17. On December 13, 2022, the Working Group adopted a consensus to extend this interpretation for December 31, 2022, and first quarter 2023 statutory financial statements. For application as of year-end 2022 and first quarter 2023:

a. Consistent with paragraphs 12 and 13, the Working Group has concluded that a reasonable estimate is not determinable for December 31, 2022, and March 31, 2023, therefore impacts related to the CAMT in the year-end 2022 and March 31, 2023, financial statements are not required.

b. Consistent with paragraph 14, CAMT updated estimates or other calculations affected by the Act determined subsequent to filing the December 31, 2022, and March 31, 2023, financial statements shall not be recognized as Type I subsequent events.

c. For year-end 2022 financial statements, the subsequent event exception is expanded to encompass events that occur prior to the issuance of statutory financial statements as well as events that occur before the date the audited financial statements are issued, or available to be issued. This provision intends to prevent reporting entities from having to amend statutory financial statements from material Type I subsequent events as a result of updated information / estimates received after the reporting date of year-end 2022 statutory financial statements pertaining to the accounting for the enactment of the Act.

18. On May 16, 2023, the Working Group adopted a consensus to extend this interpretation for the second quarter 2023 statutory financial statements. For application to the second quarter 2023 financial statements, reporting entities shall follow the guidance in this interpretation paragraphs 17.a. through 17.c.

19. With the extension, this interpretation will be automatically nullified on August 16, 2023.

20. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 23-01: Net Negative (Disallowed) Interest Maintenance Reserve

INT 23-01 Dates Discussed

April 10, 2023, June 28, 2023, August 13, 2023

INT 23-01 References

Current:
SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve
Annual Statement Instructions

INT 23-01 Issue

1. The statutory accounting guidance for interest maintenance reserve (IMR) and the asset valuation reserve (AVR) is within *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*, but the guidance within SSAP No. 7 is very limited. It provides a general description, identifies that IMR/AVR shall be calculated and reported per the guidance in the applicable SSAP, and if not explicit in the SSAP, in accordance with the annual statement instructions. The SSAPs most often simply direct allocation to (or between) IMR and AVR, with the bulk of the guidance residing within the annual statement instructions.

2. As detailed in SSAP No. 7, paragraph 2, the guidance for IMR and AVR applies to life and accident and health insurance companies and focuses on IMR and AVR liability recognition and distinguishing between IMR and AVR:

> 2. Life and accident and health insurance companies shall recognize liabilities for an AVR and an IMR. The AVR is intended to establish a reserve to offset potential credit-related investment losses on all invested asset categories excluding cash, policy loans, premium notes, collateral notes and income receivable. The IMR defers recognition of the realized capital gains and losses resulting from changes in the general level of interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the investments sold. The IMR also applies to certain liability gains/losses related to changes in interest rates. These gains and losses shall be amortized into investment income over the expected remaining life of the liability released.

3. The IMR guidance in the annual statement instructions provides information on the net balance. A positive IMR represents net interest rate realized gains and is reported as a liability on a dedicated reporting line. A negative disallowed IMR represents net interest rate realized losses and is reported as a miscellaneous other-than-invested write-in asset in the general account and nonadmitted.

4. IMR balances between the general account and separate accounts are separate and distinct. Meaning, a net negative IMR in the general account only represents activity that occurred in the general account that was allocated to IMR. However, the net positive or negative balance of the general account influences how the net positive or negative balances are reported in separate account statements (and vice versa). (A net negative IMR balance in the general account may not be disallowed if there is a covering net positive IMR in the separate account. Negative IMR that is not disallowed is reported as a contra-liability.) The instructions for reporting the net negative and positive balances are detailed in the annual statement instructions:

Line 6 – Reserve as of December 31, Current Year

Record any positive or allowable negative balance in the liability line captioned "Interest Maintenance Reserve" on Page 3, Line 9.4 of the General Account Statement and Line 3 of the Separate Accounts Statement. A negative IMR balance may be recorded as a negative liability in either the General Account or the Separate Accounts Statement of a company only to the extent that it is covered or offset by a positive IMR liability in the other statement.

If there is any disallowed negative IMR balance in the General Account Statement, include the change in the disallowed portion in Page 4, Line 41 so that the change will be appropriately charged or credited to the Capital and Surplus Account on Page 4. If there is any disallowed negative IMR balance in the Separate Accounts Statement, determine the change in the disallowed portion (prior year less current year disallowed portions), and make a direct charge or credit to the surplus account for the "Change in Disallowed Interest Maintenance Reserve" in the write-in line, in the Surplus Account on Page 4 of the Separate Accounts Statement. The following information is presented to assist in determining the proper accounting:

General Account IMR Balance	Separate Account IMR Balance	Net IMR Balance
Positive	Positive	Positive (See rule a)
Negative	Negative	Negative (See rule b)
Positive	Negative	Positive (See rule c)
Positive	Negative	Negative (See rule d)
Negative	Positive	Positive (See rule e)
Negative	Positive	Negative (See rule f)

Rules:

a. If both balances are positive, then report each as a liability in its respective statement.

b. If both balances are negative, then no portion of the negative balances is allowable as a negative liability in either statement. Report a zero for the IMR liability in each statement and follow the above instructions for handling disallowed negative IMR balances in each statement.

c. If the general account balance is positive, the separate accounts balance is negative and the combined net balance is positive, then all of the negative IMR balance is allowable as a negative liability in the Separate Accounts Statement.

d. If the general account balance is positive, the separate account balance is negative, and the combined net balance is negative, then the negative amount not covered by the positive amount is not allowable. Report only the allowable portion as a negative liability in the Separate Accounts Statement and follow the above instructions for handling the disallowed portion of negative IMR balances in the Separate Accounts Statement.

e. If the general account balance is negative, the separate account balance is positive, and the combined net balance is positive, then all of the negative IMR balance is allowable as a negative liability in the General Account Statement.

f. If the general account balance is negative, the separate account balance is positive, and the combined net balance is negative, then the negative amount not covered by the positive amount is not allowable. Report only the allowable portion as a negative liability in the General Account Statement and follow the above instructions for handling the disallowed portion of negative IMR balances in the General Account Statement.

5. In October 2022, the ACLI requested the Statutory Accounting Principles (E) Working Group to reassess the guidance for net negative (disallowed) IMR, with a request to consider admittance of those

amounts. The ACLI noted that the nonadmittance of disallowed negative IMR can have adverse negative ramifications for insurers with two key themes:

a. In general, rising interest rates are favorable to the financial health of the insurance industry and policyholders. However, with negative IMR, there is an inappropriate perception of decreased financial strength through lower surplus and risk-based capital.

b. Negative IMR could impact the rating agency view of the industry or incentivize companies to avoid prudent investment transactions that are necessary to avoid mismatches between assets and liabilities. In either scenario, negative IMR encourages short-term non-economic activity that is not in the best long-term interest of a reporting entity's financial health or its policyholders.

6. In considering the request, the Working Group concluded that, for year-end 2022, there would be no change to statutory accounting guidance and deviations from statutory accounting principles would need to be approved via a permitted or prescribed practice. The Working Group then held company-specific educational sessions in January 2023 to receive detailed information regarding negative IMR and received a subsequent comment letter from the ACLI.

7. During the 2023 Spring National Meeting, the Working Group further discussed the topic of negative IMR and directed NAIC staff to proceed with drafting guidance for a 2023 solution and to begin work towards a long-term solution.

INT 23-01 Discussion

8. This interpretation prescribes limited-time, optional, statutory accounting guidance, as an exception to the existing guidance detailed in SSAP No. 7 and the annual statement instructions that requires nonadmittance of net negative (disallowed) IMR as a short-term solution. Specifically, this interpretation impacts the annual statement instruction rules regarding disallowed negative IMR detailed in rules 'b,' 'd' and 'f' shown in paragraph 4.

9. Reporting entities are permitted to admit net negative (disallowed) IMR with the following restrictions:

a. Reporting entities that qualify pursuant to paragraph 9.b., are permitted to admit net negative (disallowed) IMR up to 10% of the reporting entity's adjusted general account[1] capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for its most recently filed statement with the domiciliary state commissioner. The capital and surplus shall be adjusted to exclude any net positive goodwill, EDP equipment and operating system software, net deferred tax assets and admitted[2] net negative (disallowed) IMR.

b. Reporting entities applying this interpretation are required to have a risk-based capital (RBC) greater than 300% authorized control level (ACL) after an adjustment to total adjusted capital (TAC) that reflects a reduction to remove any net positive goodwill, EDP equipment and operating system software, net deferred tax assets and admitted net negative (disallowed) IMR. Compliance with this adjusted RBC calculation shall be affirmed for all

[1] The general account capital and surplus includes surplus reflected in the separate account; therefore, an aggregation of general account and separate account surplus is not necessary.

[2] As the separate account does not have "admitted" assets, broad reference to "admitted net negative (disallowed) IMR" throughout this interpretation includes what is admitted in the general account and what is recognized as an asset in the separate accounts.

quarterly and annual financial statements for which net negative (disallowed) IMR is reported as an admitted asset in the general account or recognized as an asset in the separate accounts. Reporting entities shall provide documentation to illustrate compliance with this requirement upon state regulator request. Reporting entities with an adjusted RBC calculation of 300% ACL or lower are not permitted to admit net negative (disallowed) IMR in the general account or recognize IMR assets in the separate accounts.

c. The net negative (disallowed) IMR permitted for admittance shall not include losses from derivatives that were reported at fair value prior to derivative termination[3] unless the reporting entity has historically followed the same process for interest-rate hedging derivatives that were terminated in a gain position. In other words, there is a requirement for documented, historical evidence illustrating that unrealized gains from derivatives reported at fair value were reversed to IMR (as a liability) and amortized as part of IMR. Reporting entities that do not have evidence of this past application are required to remove realized losses from derivatives held at fair value from the net negative (disallowed) IMR balance to determine the amount permitted to be admitted. Reporting entities that begin a new process for the use of hedging derivatives, perhaps with a theoretical process to treat derivative losses and derivative gains similarly, but do not have evidence illustrating the historical treatment of derivative gains through IMR are not permitted to include derivative losses in the net negative (disallowed) IMR permitted to be admitted. This evidence is required separately for the general account, insulated separate account and non-insulated separate account if losses from derivatives previously reported at fair value are currently being allocated to IMR in those accounts.

10. Reporting entities that admit net negative (disallowed) IMR shall follow the following process:

a. All net negative (disallowed) IMR in the general account shall first be admitted until the capital and surplus percentage limit, as detailed in paragraph 9.a., is reached.

b. If all general account net negative (disallowed) IMR has been fully admitted, and the reporting entity is still below the paragraph 9.a. capital and surplus limit, then the reporting entity can report net negative (disallowed) IMR as an asset in the separate accounts. Reporting entities that have both insulated and non-insulated separate accounts shall recognize IMR assets proportionately between the insulated and non-insulated statements until the aggregated amount recognized as an admitted asset in the general account and as an asset in the insulated and non-insulated statements reaches the percentage limit of capital and surplus detailed in paragraph 9.a.

11. Reporting entities that admit net negative (disallowed) IMR in the general account shall report the admittance in the balance sheet as follows:

a. Reporting entities shall report the net negative (disallowed) IMR as an aggregate write-in to miscellaneous other-than-invested assets (line 25) (named as “Admitted Disallowed IMR”) on the asset page. The net negative (disallowed) IMR shall be admitted to the extent permitted per paragraph 9.a., with the remaining net negative (disallowed) IMR balance nonadmitted.

b. Reporting entities shall allocate an amount equal to the general account admitted net negative (disallowed) IMR from unassigned funds to an aggregate write-in for special surplus funds (line 34) (named as “Admitted Disallowed IMR”). Although dividends are

[3] Reference to derivative termination throughout this interpretation includes all actions that close out a derivative, including, but not limited to, termination, expiration, settlement, or sale.

contingent on state specific statutes and laws, the intent of this reporting is to provide transparency and preclude the ability for admitted negative IMR to be reported as funds available to dividend.

12. Reporting entities that record net negative (disallowed) IMR as an asset in the separate account shall report the recognition in the balance sheet as follows:

a. Reporting entities shall report the permitted net negative (disallowed) IMR as an aggregate write-in to miscellaneous other-than-invested assets (line 15) (named as "Recognized Disallowed IMR") on the asset page.

b. Reporting entities shall allocate an amount from surplus equal to the asset recognized as disallowed IMR as an aggregate write-in for special surplus funds (line 19) (named as "Recognized Disallowed IMR) on the liabilities and surplus page.

13. Reporting entities admitting net negative (disallowed) IMR are required to complete the following disclosures in the annual and quarterly financial statements for IMR:

a. Reporting entities that have allocated gains/losses to IMR from derivatives that were reported at fair value prior to the termination of the derivative shall disclose the unamortized balances in IMR from these allocations separately between gains and losses.

b. Reporting entities shall complete a note disclosure that details the following:

i. Net negative (disallowed) IMR in aggregate and allocated between the general account, insulated separate account and non-insulated account,

ii. Amounts of negative IMR admitted in the general account and reported as an asset in the separate account insulated and non-insulated blank,

iii. The calculated adjusted capital and surplus per paragraph 9.a., and

iv. Percentage of adjusted capital and surplus for which the admitted net negative (disallowed) IMR represents (including what is admitted in the general account and what is recognized as an asset in the separate account).

c. Reporting entities shall include a note disclosure that attests to the following statements:

i. Fixed income investments generating IMR losses comply with the reporting entity's documented investment or liability management policies,

ii. IMR losses for fixed income related derivatives are all in accordance with prudent and documented risk management procedures, in accordance with a reporting entity's derivative use plans and reflect symmetry with historical treatment in which unrealized derivative gains were reversed to IMR and amortized in lieu of being recognized as realized gains upon derivative termination.

iii. Any deviation to 13.c.i was either because of a temporary and transitory timing issue or related to a specific event, such as a reinsurance transaction, that mechanically made the cause of IMR losses not reflective of reinvestment activities.

iv. Asset sales that were generating admitted negative IMR were not compelled by liquidity pressures (e.g., to fund significant cash outflows including, but not limited to excess withdrawals and collateral calls).

INT 23-01 Status

14. The consensuses in this interpretation were adopted on August 13, 2023, to provide limited-time exception guidance to SSAP No. 7 and the annual statement instruction for the reporting of net negative (disallowed) IMR. The provisions within this interpretation are permitted as a short-term solution until December 31, 2025, and will be automatically nullified on January 1, 2026.

15. The effective date of this interpretation may be adjusted (nullified earlier or with an extended effective date timeframe) in response to Statutory Accounting Principles (E) Working Group actions to establish statutory accounting guidance specific to net negative (disallowed) IMR.

16. No further discussion is planned.

Application Guidance for Admitting / Recognizing Net Negative (Disallowed) IMR

General Account:

1. Net negative IMR in the general account that exceeds net positive IMR in the separate accounts is considered “disallowed” general account IMR. (Determination of the disallowed IMR in the general account shall be compared against the aggregate IMR balance in all separate accounts.)

2. Net negative disallowed IMR in the general account shall be reported as an aggregate write-in for other-than-invested assets as “Admitted Disallowed IMR” on line 25 of the asset page and nonadmitted. The change in nonadmittance shall be reported on line 41 in the summary of operations.

3. To the extent the reporting entity is permitted to admit net negative disallowed IMR pursuant to the provisions in this interpretation, the reporting entity shall admit the disallowed IMR reported on line 25 of the asset page to the extent permitted, with the change in nonadmittance reflected on line 41 in the summary of operations.

4. Reporting entities shall report an amount equal to the general account admitted net negative (disallowed) IMR as an aggregate write-in for special surplus funds (line 34 of the Liabilities, Surplus an Other Funds page) named as “Admitted Disallowed IMR.”

5. Reporting entities shall include note disclosures in the quarterly and annual financial statements as required in paragraph 13 of the interpretation.

Separate Account:

6. Net negative IMR in the separate account (aggregated IMR in both insulated and non-insulated separate accounts) that exceeds net positive IMR in the general account is considered “disallowed” separate account IMR. If the aggregate separate account IMR is positive, with a negative IMR in the insulated separate account and positive IMR in non-insulated separate account (or vice versa), then the negative IMR in the insulated separate account is not permitted to be reported as an asset. In those situations, the separate account has an aggregate positive IMR balance.

7. Net negative (disallowed) IMR in the separate account permitted to be recognized as an asset, as the admittance in the general account did not utilize the full percentage of adjusted capital and surplus permitted within this interpretation, shall be proportionately divided between insulated and non-insulated separate accounts if both separate accounts are in a negative position. If the separate account IMR is an aggregate net negative, but only one separate account blank is in a negative position, then only the separate account blank with a net negative position can recognize disallowed IMR as an asset.

8. If negative IMR in the separate account has previously been recognized as a direct charge to surplus, the reporting entity shall recognize an asset as an aggregate write-in for other-than-invested assets as “Recognized Disallowed IMR” on line 15 of the separate account asset page, with an offsetting credit to surplus. This credit to surplus shall reverse the charge previously recognized. This process shall continue in subsequent quarters if additional separate account IMR is permitted as an asset to the extent IMR was previously taken as a direct charge to surplus. Once prior surplus impacts have been fully eliminated, then the entity shall follow the guidance for new net negative (disallowed) IMR as detailed in the following paragraph. If subsequent quarters result with a decline in the permitted IMR asset in the separate account, then the asset shall be credited with an offsetting charge to surplus.

9. If the reporting entity enters a net negative (disallowed) IMR position (meaning, there has not been a prior charge to surplus for net negative (disallowed) IMR), then the entity shall recognize the asset as an aggregate write-in for other-than-invested assets as "Disallowed IMR" on line 15 of the separate account balance sheet, with an offsetting credit to IMR (line 3 of the liability page) until the IMR liability equals zero. This process shall continue in subsequent quarters if additional net negative IMR is generated from operations and is permitted as an asset under the provisions of this interpretation. If subsequent quarters result with a decline in the permitted IMR asset in the separate account, then the asset shall be credited with an offsetting charge to surplus.

10. Reporting entities shall report an amount equal to the asset recognized reflecting net negative (disallowed) IMR as an aggregate write-in for special surplus funds (line 19) (named as "Recognized Disallowed IMR." This shall be included in each separate account statement (insulated and non-insulated) if net negative disallowed IMR is recognized as an asset in that statement.

11. Reporting entities shall include note disclosures in the quarterly and annual financial statements as required in paragraph 13 of the interpretation.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax

INT 23-03 Dates Discussed

August 13, 2023; September 21, 2023

INT 23-03 References

Current:
SSAP No. 4—Assets and Nonadmitted Assets
SSAP No. 9—Subsequent Events
SSAP No. 101—Income Taxes

INT 23-03 Issue

Key Provisions of the Inflation Reduction Act

1. The Inflation Reduction Act (Act) was enacted on August 16, 2022, and included a new corporate alternative minimum tax (CAMT). The CAMT is effective for tax years beginning after 2022. Reporting entities shall refer to the Act and the resulting regulations and other tax guidance to determine application, but a high-level summary of the CAMT is below.

   a. The tentative CAMT is 15% of the corporation's "adjusted financial statement income" for the tax year, reduced by corporate alternative minimum foreign tax credit.

   b. The CAMT differs from the previous traditional alternative minimum tax that applied under pre-2018 tax law in that it starts at a financial statement measure (book income) – not an Internal Revenue Code taxable income calculation. Adjusted financial statement income does not include other comprehensive income including unrealized gains and losses on available for sale securities. The determination of whether the CAMT applies is made on a tax-controlled group basis (scope determination), the tentative CAMT is based on the group's adjusted financial statement income (not adjusted regular taxable income), and any tax due (liability determination) is based on a comparison of consolidated tentative CAMT to consolidated regular tax (non-CAMT).

   c. The CAMT applies only to corporations (determined on a tax-controlled group basis as defined for federal income tax purposes, this could include standalone unaffiliated entities which meet the specified income thresholds – see paragraph 3) with average annual adjusted financial statement income in excess of $1 billion for three prior taxable years. The threshold is reduced to $100 million in the case of certain foreign-owned corporations. A corporation that meets the applicable threshold is an "applicable corporation." Applicable corporations generally remain applicable corporations for subsequent taxable years unless certain limited exceptions apply. Applicable corporation status means that CAMT must be tentatively determined and compared to regular (non-CAMT) tax liability.

   d. A corporation's adjusted financial statement income is the amount of net income or loss the corporation reports on its applicable financial statement. The income is adjusted for various purposes including certain adjustments in the case of consolidated returns or for foreign income.

e. The Act includes references to the tax code which provides a hierarchy for determining the applicable financial statement. At a high level, the first choice is U.S. generally accepted accounting principles (GAAP) financial statements; the second choice is international financial reporting standards (IFRS) financial statements. If GAAP and IFRS financial statements are not available, the financial statements filed by the taxpayer with any other regulatory or government body are acceptable. If the taxpayer is part of a tax-controlled group of corporations, the group's applicable financial statement is the applicable financial statement for each member of the group.

f. To determine its U.S. federal income tax liability, an applicable corporation will need to compute taxes under both systems – the regular tax system and the CAMT system. The CAMT is payable to the extent the tentative CAMT exceeds the sum of the regular corporate income tax plus base erosion and anti-abuse tax (BEAT) liability.

g. Any CAMT paid is available indefinitely as a credit carryover that would reduce future regular tax in future years when the regular tax liability is in excess of the tentative CAMT liability. That is, the CAMT credit can be used to reduce the regular tax but not below tentative CAMT liability.

h. A foreign tax credit (FTC) may reduce the tentative minimum CAMT. Note that unused FTCs may be carried forward for 5 years. General business credits can generally offset up to 75% of the sum of regular and minimum tax.

2. This interpretation is focused on addressing accounting and reporting aspects of the CAMT. As most reporting entities will not be above the applicable corporation threshold and will not be subject to the CAMT calculation, this guidance has been developed as an interpretation. While most insurers will not be applicable corporations, this interpretation provides comprehensive statutory accounting guidance for all reporting entities with respect to the CAMT. This interpretation incorporates a principles-based approach for purposes of statutory accounting for the CAMT.

3. Although it is likely that most insurers that are applicable corporations will be members of a tax-controlled group of corporations and included in a consolidated federal income tax return with other members of the group, this interpretation applies to all reporting entities subject to the CAMT, whether an unaffiliated corporation[1] that files a separate tax return, a member of a tax-controlled group not included in the common parent company's consolidated tax return that files a separate company tax return or a separate consolidated tax return with other members of the group, or as a member of the common parent's consolidated return group.

4. For reporting entities that are included in a consolidated tax return, the fundamental statutory tax accounting issue for the CAMT is how to reflect in the reporting entity's separate company financial statements a portion of what is essentially an add-on tax for a consolidated tax return group that is based on the group's financial statement income and group tax rate. Even if a member of a tax-controlled group of corporations files its own separate federal income tax return, the tax law does not provide for a separate company scope determination, but rather looks to the tax-controlled group for applicable corporation status and determination of the applicable financial statement.

INT 23-03 Discussion

5. The discussion along with the Statutory Accounting Principles (E) Working Group tentative consensuses are included below.

[1] As used herein, an "unaffiliated" corporation is one that is not a member of a tax-controlled group.

Categories of Reporting Entities

6. In an annual determination of applicable corporation status, all reporting entities are separated into one of the following categories:

a. Nonapplicable reporting entities

b. Applicable reporting entities

c. Applicable reporting entities with tax allocation agreement (also called tax sharing agreements) exclusions

Nonapplicable Reporting Entities

7. Nonapplicable reporting entities are reporting entities that do not reasonably expect to be an applicable corporation either as a member of a tax-controlled group of corporations[2] or individually as an unaffiliated corporation, for the taxable year that includes the current reporting period. Nonapplicable reporting entities are not required to calculate or recognize a payable for CAMT. If a reporting entity is not subject to pay CAMT, then they will have no CAMT credit carryforward. For nonapplicable reporting entities, further assessment of the CAMT is not required for current or deferred tax computations, and the remaining accounting components of the interpretation do not apply. Applicable disclosures are required.

8. A reporting entity that was an applicable corporation for the preceding taxable year shall reasonably expect to be an applicable corporation for the current taxable year, unless one of the tax law exceptions to continued applicable corporation status applies.

Applicable Reporting Entities

9. Applicable reporting entities are reporting entities that reasonably expect to be applicable corporations for the taxable year that includes the current reporting period, either individually as an unaffiliated corporation or as a member of a tax-controlled group of corporations[3]. Applicable reporting entities are required to consider CAMT in current and deferred tax computations in the manner set forth in this interpretation.

10. Because CAMT is not payable by an applicable corporation unless it is in excess of regular tax liability, the CAMT calculations for applicable reporting entities within this interpretation may or may not result in different current and deferred income taxes than if the CAMT was not taken into account. (Applicable reporting entities with tax allocation agreement exclusions that meet the requirements of paragraph 11 of this interpretation shall follow the guidance in paragraph 12 of this interpretation.)

Applicable Reporting Entities with Tax Allocation Agreement Exclusions

11. Applicable reporting entities with tax allocation agreement exclusions are reporting entities that qualify as an applicable corporation as a member of a tax-controlled group of corporations pursuant to

[2] A reporting entity that is a member of a tax-controlled group that does not reasonably expect to be applicable corporation on a group basis is not required to make a separate company determination as the CAMT is determined on a group basis.

[3] Determination of applicable reporting entity within a tax-controlled group is subject to the tax law. A reporting entity within a tax-controlled group is captured with the group's applicable corporation status regardless of if they were excluded from the consolidated tax return and filed their own separate return. For example, if the reporting entity is a life insurance company and i) the group has not made a "life-nonlife" consolidated return election, or ii) the reporting entity has been recently acquired and is excluded from the life-nonlife consolidated return for a period of 5 years.

paragraphs 9 and 10 of this interpretation, and is a party to a tax allocation agreement that is in effect for the reporting period that has all of the following terms:

a. The reporting entity is excluded from charges for any portion of the group's CAMT, and

b. The reporting entity is not allocated any portion of the group's CAMT credit carryover.

12. Reporting entities with tax allocation agreement exclusions which qualify under paragraph 11 of this interpretation, are not required to calculate, or recognize CAMT in their current or deferred tax computations. Even with the tax allocation agreement exclusions, the general current tax liability guidance pursuant to *SSAP No. 101—Income Taxes*, paragraph 3 continues to apply. This guidance requires the reporting entity to recognize the amount the reporting entity has paid or is payable, which includes any additional amount the reporting entity expects to pay on behalf of its co-obligors.

Accounting for Applicable Reporting Entities

Impact of Tax Allocation Agreements

13. This interpretation is based on the principle that the statutory accounting for the CAMT for reporting entities included in a consolidated tax return should be matched to the CAMT charges reasonably estimated to be paid by the reporting entity and the corresponding CAMT credits reasonably estimated to be received by the reporting entity. For such reporting entities, this interpretation applies the provisions of the intercompany tax allocation agreement[4] (also referred to as a tax sharing agreement) that governs allocation of consolidated taxes to individual members of the group.

14. SSAP No. 101, paragraph 16 provides that in the case of a reporting entity that files a consolidated income tax return with one or more affiliates, income tax transactions between the affiliated parties shall be recognized if such transactions are economic transactions as defined in *SSAP No. 25—Affiliates and Other Related Parties*; are pursuant to a written tax allocation agreement; and income taxes incurred are accounted for in a manner consistent with the principles of FAS 109 the predecessor of what is now ASC 740, as modified by SSAP No. 101.

15. For a reporting entity that is included in a consolidated tax return and is subject to a qualifying tax allocation agreement which is consistent with paragraphs 16 and 17 of SSAP No. 101, the amount of CAMT payable (expense) or CAMT credit carryforward is recognized in accordance with the tax allocation agreement.

Recognition of CAMT Payable

16. Reporting entities that are applicable corporations, excluding those having qualifying tax allocation agreement exclusions per paragraph 11 of this interpretation, are required to take CAMT payable into account in the calculation of current income tax expense pursuant to SSAP No. 101. Reporting entities shall accrue the CAMT owed, reflecting the amount owed as a separate return filer or in accordance with the amount allocated through the consolidated tax return group's tax sharing agreement pursuant to paragraph 15 of this INT.

[4] SSAP No. 101, paragraphs 16 and 17 provide requirements for tax allocation agreement recognition. Tax allocation agreements are also subject to internal revenue service requirements and are subject to domiciliary regulator review under the Insurance Holding Company System Regulatory Act (Model #440), which also requires that the terms of intercompany agreements be fair and reasonable. In assessing fair and reasonable, state insurance regulators are encouraged to assess the terms of the TSA for allocations to the insurance reporting entity for both CAMT payables and CAMT credit carryforwards.

17. Consistent with SSAP No. 101, paragraph 8, changes in deferred tax assets (DTAs) and deferred tax liabilities (DTLs), including changes attributable to changes in tax rates and changes in tax status, if any, shall be recognized as a separate component of gains and losses in unassigned funds (surplus) as "change in net deferred income tax," excluding any change reflected in unrealized capital gains.

18. Paragraph 8.3 of SSAP No. 101 Exhibit A – Implementation Questions and Answers (Q&A) is not applicable to reporting entities subject to CAMT through a tax-controlled group structure. This exclusion is provided due to the consolidated nature of the CAMT calculation. Any theoretical separate entity calculation of the CAMT liability may be unrelated to the actual consolidated tax return computations and to the tax allocation agreement allocation of liability.

Recognition of CAMT Credit Deferred Tax Asset

19. Reporting entities shall recognize a corresponding DTA which represents the non-expiring tax credit carryforward equal and offsetting to the current CAMT accrued. The CAMT credit can be used to reduce regular tax in future years when the regular tax liability is in excess of the tentative CAMT liability as permitted under the tax law. The CAMT credit carryforward is a type of deferred tax asset.

Impact of CAMT to the Statutory Valuation Allowance

20. *SSAP No. 101—Income Taxes*, paragraph 7.e. requires the statutory valuation allowance adjustment as a direct reduction in the gross DTA if, based on the weight of available evidence, it is more likely than not that some or all of the gross DTAs will not be realized. Gross DTA less the statutory valuation allowance results in adjusted gross DTAs. The statutory valuation allowance adjustment is not reported as a separate line in the statutory financial statements (it is an off-balance sheet item that reduces the gross DTAs). The statutory valuation allowance is disclosed.

21. The determination of a statutory valuation allowance[5] for CAMT credit deferred tax assets depends on whether the reporting entity is part of a consolidated tax return group or a separate tax return filer:

a. Consolidated Tax Return Group: A reporting entity that is an applicable entity and a member of consolidated tax return group shall utilize the statutory valuation assessment for the CAMT credit deferred tax assets completed at the consolidated tax return group level. A reporting entity is not required to adjust the group statutory valuation allowance for CAMT credit deferred tax assets. Rather, the group determined statutory valuation allowance and the resulting credit deferred tax asset deemed to be more likely than not to be realized, is permitted to be allocated (consistent with tax allocation agreement) to the reporting entity and reflected as an CAMT credit adjusted gross DTA. The reporting entity shall continue to have a separate statutory valuation allowance calculation for non-CAMT deferred tax assets as required under SSAP No. 101. The combination of the CAMT credit adjusted gross deferred tax asset (as received from the group) and the adjusted gross deferred tax assets from non-CAMT deferred tax assets shall equal the total adjusted gross deferred tax assets reviewed for admittance within the scope of this interpretation.

b. Separate Tax Return Filer: A reporting entity that is an applicable entity and files a separate tax return, is required to complete a statutory valuation allowance for all deferred tax assets, including CAMT credit deferred tax assets, in determining their total adjusted gross DTAs. (The CAMT credit deferred tax assets can be assessed separately from non-

[5] Although reporting entities may conclude that the non-expiring CAMT DTA more likely than not will ultimately be realized, reporting entities will not be able to utilize the tax credit until the reporting entity if a separate tax return filer, or the tax consolidated group of corporations if the reporting entity is a member of such group , are no longer CAMT payors and have sufficient tax liability that permits the group the ability to use the CAMT credits.

CAMT deferred tax assets in determining whether the deferred tax asset is more likely than not to be realized.) The total adjusted gross deferred tax assets are then reviewed for admittance within the scope of this interpretation.

22. A reporting entity is allowed an accounting policy election to either consider or disregard CAMT when evaluating the need for a valuation allowance for its non CAMT deferred tax assets.[6] The accounting policy election applies for valuation allowance purposes only – that is, in the determination of adjusted gross deferred tax assets other than the CAMT credit deferred tax assets. This accounting policy election cannot be used to avoid a valuation allowance analysis for CAMT credit DTAs. The accounting policy election must be disclosed in the notes to the financial statements and applied consistently in subsequent reporting periods.

Admissibility

Admittance - Implications of Group Tax Assessment (Related Parties)

23. For reporting entities that are applicable corporations as they are a member of a tax-controlled group of corporations, the reporting entity may be subject to the CAMT, or be hindered from utilizing the CAMT credit, through the actions of their consolidated tax return group related parties. (As noted in footnote 5, although a reporting entity may have earned an non-expiring tax credit through payment of CAMT, the reporting entity is not eligible to utilize that tax credit until the consolidated tax return group has sufficient tax liability that allows the members of the group to utilize their tax credit. This means that on a group basis they are no longer CAMT payors.) *SSAP No. 4—Assets and Nonadmitted Assets* requires assets that are restricted by the action of a related party to be nonadmitted assets.

> SSAP No. 4, Footnote 2: If assets of an insurance entity are pledged **or otherwise restricted by the action of a related party, the assets are not under the exclusive control of the insurance entity and are not available to satisfy policyholder obligations due to these encumbrances or other third-party interests. Thus, pursuant to paragraph 2, such assets shall not be recognized as an admitted asset on the balance sheet.** Additional guidance for assets pledged as collateral is included in INT 01-31.

24. A key focus of this interpretation is the admittance of the CAMT deferred tax assets (credits). However, it is recognized that under the existing statutory accounting guidance in SSAP No. 4 a reporting entity recognizing CAMT credit deferred tax assets would not be permitted to admit those deferred tax assets if as part of a consolidated tax return group the ability to receive those CAMT credits is explicitly linked to the actions of other entities within the group. If the group on a collective basis does not incur enough tax to allow utilization of the tax credits, then the reporting entity cannot use the tax credits, regardless of the income or tax paid by the reporting entity. This aspect is not impacted by the tax sharing agreement. Although the tax sharing agreement may specify how the CAMT credits will be allocated among the group, such tax credits allocated to the reporting entity can only be realized when the group qualifies for the credit.

25. For the CAMT credit adjusted gross deferred tax assets allocated to the reporting entity to be eligible to be admitted, this interpretation provides an exception to the guidance in SSAP No. 4, footnote 2, recognizing that the impact to ultimately utilize the allocated tax credits is dependent on the actions of the other parties within the group.

[6] SSAP No. 101, FAS 109 and ASC 740 do not specifically address whether future years' CAMT should be anticipated in a valuation allowance assessment for non-CAMT DTAs. Accordingly, an accounting policy election is allowed for GAAP purposes as to whether to consider or disregard CAMT when evaluating the need for a valuation allowance for non-CAMT DTAs.

Admittance – Adjusted Gross DTAs

26. The guidance in SSAP No. 101 allows admittance of adjusted gross DTAs (gross DTAs reduced by the statutory valuation allowance) pursuant to a three-component calculation, for which the second step limits admittance of adjusted gross DTAs to those that are expected to be realized in a timeframe that does not exceed three years. The actual number of years to realization permitted depends on specifics for each reporting entity (type and other information about the reporting entity), but the maximum timeframe is three years. The last step (SSAP No. 101, paragraph 11.c.) admits DTAs which can be offset by DTLs.

27. Due to the following aspects regarding the CAMT credits, specific admittance guidance for the CAMT credit DTAs has been established:

a. The CAMT credit is a tax credit DTA that does not expire. As long as the reporting entity is a CAMT payor or is part of a tax-consolidated group that is a CAMT payor, the reporting entity cannot utilize the tax credit.

b. The ability to utilize the CAMT credit is contingent on the actions and tax paying behaviors of the consolidated tax return group. Although the reporting entity may be paying sufficient tax above the CAMT threshold, if other parties within the group do not act in a similar manner, putting the group below the CAMT threshold, then the CAMT credit cannot be utilized by the reporting entity.

28. With these noted limitations in utilization of the earned tax credits, reporting entities are only permitted to admit CAMT credits if the reporting entity tax projections (if a separate tax return filer) or projections of the tax-consolidated group (if a member of such group) indicate that the CAMT credit will be realizable within the stated timeframes using the applicable SSAP No. 101, paragraph 11 realization table thresholds[7]. This means that the tax projections will have sufficient tax liability that permits utilization of the CAMT credits. For example, a reporting entity with greater than 300% ExDTA ACL RBC can only admit CAMT credits that are expected to be realized (consistent with the tax allocation agreement) in three years. Reporting entities that have ExDTA ACL RBC between 200-300% can only admit CAMT credits that are expected to be realized in one year. If a reporting entity cannot project (either on its own if a separate return filer or at the group if a consolidated tax return group member) sufficient tax liability that allows them to utilize the CAMT credit within the applicable realizable timeframes for admittance, then the portion of CAMT credits that cannot be utilized are required to be nonadmitted under SSAP No. 101, paragraph 11.b.

29. CAMT credits included in the SSAP No. 101, paragraphs 11 and 11.b. calculation as they are expected to be realized within the applicable 1 or 3 year permitted timeframes shall then be combined with non-CAMT adjusted gross deferred tax assets and admitted to the extent that the total DTAs admitted under paragraph 11.b. do not exceed the capital and surplus percentage limit for the company type. All references to SSAP No. 101, paragraph 11.b. include the modifications in this Interpretation.

30. Reporting entities shall use the Realization Threshold Limitations Tables in SSAP No. 101, paragraph 11.b. as applicable to the entity for determination of the admissibility of the CAMT credits. The percentage limitations of capital and surplus of and the projected realization periods continue to apply to admitted adjusted gross DTAs, including the adjusted gross DTA for any CAMT credit DTA.

31. A reporting entity which meets or exceeds the top line of the applicable of the Realization Threshold Limitation Table (Ex. 3 years and 15%) is **not required** to take the CAMT into account in calculating the

[7] The examples in this paragraph reference Ex-DTA ACL RBC, however, SSAP No. 101, paragraph 11.b. also includes realization threshold tables which apply to non-RBC filers.

"with and without[8]" tax liability for purposes of determining the amount expected to be realized under SSAP No. 101, paragraph 11.b. for non-CAMT DTAs. Specifically, the reporting entity's "with and without" regular tax liability is not reduced by CAMT, if any, reasonably expected to be incurred during the SSAP No. 101, paragraph 11.b. applicable period. In the case of a reporting entity included in a consolidated federal income tax return, the amount expected to be incurred refers to the portion of the consolidated CAMT, if any, reasonably expected to be allocable to the reporting entity pursuant to the group's tax allocation agreement. However, any admitted CAMT credits in this step must be realizable within the applicable time period specified in the applicable Realization Threshold Limitation Table (Ex, top line - 3 years), determined consistent with the tax allocation agreement. The post-valuation allowance adjusted gross DTA for any CAMT credit DTA is admitted following the guidance in SSAP No. 101, paragraph 11.b.i. as modified by this Interpretation. The 15% limitation of capital and surplus which is provided in SSAP No. 101, paragraph 11.b.ii. continues to apply to admitted adjusted gross DTAs, including the adjusted gross DTA for any CAMT credit DTA.

32. A reporting entity which meets the second line of the applicable Realization Threshold Limitation Table (Ex. 1 year and 10%), the amount expected to be realized under SSAP No. 101, paragraph 11.b.i. within the applicable period determined under paragraph 11.b. is based on the reporting entity's "with and without" regular tax liability reduced by CAMT, if any, reasonably expected to be incurred during the paragraph 11.b. applicable period. In the case of a reporting entity included in a consolidated federal income tax return, the amount expected to be realized is reduced by the portion of the consolidated CAMT, if any, reasonably expected to be allocable to the reporting entity pursuant to the group's tax allocation agreement. CAMT credit utilization during the applicable period is recognized based on the same principles, – that is, as an admitted DTA. The purpose of these computations is to account for CAMT in deferred taxes in the same manner as CAMT would be reflected in current taxes.

33. A reporting entity which meets or is below the third line of the applicable Realization Threshold Limitation Table (Ex. 0 years and 0%), is not permitted to admit either CAMT credit DTAs or non-CAMT DTAs under SSAP No. 101, paragraph 11.b.

34. The adjusted gross DTA for any CAMT credit carryforward which does not qualify for admission under SSAP No. 101, paragraph 11.b. is permitted to be recognized as an offset against DTLs in accordance with SSAP No. 101, paragraph 11.c. The reporting entity shall admit the remaining amount of adjusted gross DTAs, after application of paragraphs 11.a. and 11.b. that can be offset against existing gross DTLs. The reporting entity shall consider the character (i.e., ordinary versus capital) of the DTAs and DTLs such that offsetting would be permitted in the tax return under existing enacted federal income tax laws and regulations.

Admittance - Projections

35. Projections of CAMT liability, if any, (and CAMT credit utilization) during the applicable period involve forward-looking data, groupings, of assets and liabilities, estimates and other adjustments for both the reporting entity and the group of which it is a member. The manner in which this is done shall be conducted in a reasonable and consistent manner. A reporting entity shall retain internal documentation to support these computations and the methodologies so employed. Modifications to the estimation methodology are permitted should events or circumstances change from a previous period – such as a change in materiality or administrative costs associated with the computations, or system changes that affect the level of detail available. Entities that make such modifications should be prepared to rationalize the

[8] "With and without" is further described in SSAP No. 101.

changes. Disclosure of material modifications, and the general reason for such, should be made in the notes to the financial statements.[9]

Admittance - Tax Planning Strategies

36. SSAP No. 101 provides that tax-planning strategies are required to be considered in the valuation allowance analysis and may be considered in determining the admission of DTAs under SSAP No. 101, paragraph 11. For reporting entities that are part of a consolidated tax return group, tax planning strategies impacting the CAMT are determined at a group level, as long as the tax planning strategies at the group level do not conflict with tax planning strategies at the reporting level and vice versa. For reporting entities that are separate tax return filers, a reporting entity must consider tax-planning strategies in making the valuation allowance analysis required under this interpretation.

Transition Guidance

37. Even though the CAMT was enacted in 2022 and generally became effective January 1, 2023, the requirements for statutory tax accounting for the CAMT have effectively been deferred by INT 22-02. This paragraph provides the applicable transition rules for year-end 2023 statutory accounting for requests for a timely-filed tax allocation agreement amendment or a new tax allocation agreement for the 2023 taxable year.

a. Because the CAMT was newly enacted effective for 2023, tax allocation agreements in effect for periods prior to the 2023 taxable year include no explicit provisions relating to the CAMT. Thus, applicable reporting entities (with and without tax allocation agreement exclusions) may need to amend tax allocation agreements to deal with the CAMT effective for the entire 2023 taxable year. A reporting entity would file a request for amendment to a tax allocation agreement or a new tax allocation agreement on Form D – Prior Notice of a Transaction as required under the *Insurance Holding Company System Regulatory Act* (Model #440) and the related regulation, (Model #450) with its applicable domiciliary regulator(s) and commercial domiciliary regulator(s).

b. Time is of the essence in both requesting and approving tax allocation agreement amendments or a new tax allocation agreement relating to the CAMT for the 2023 taxable year to be applicable to the 2023 reporting period. Accordingly, if, a reporting entity files the applicable Form D request(s) for tax allocation agreement amendment or a new tax allocation agreement prior to the end of 2023 to address the CAMT for 2023 and subsequent taxable years, and the domiciliary regulator has confirmed in writing that they have no objections to using the new tax allocation agreement amendment or new tax allocation agreement, while under review. The reporting entity shall be allowed to account for the tax allocation agreement as applicable for the entire 2023 reporting period.

c. If the final approved tax allocation agreement differs in its treatment of the CAMT allocation from the tax allocation agreement originally requested on the Form D, the difference shall be recorded as follows:

i. If Form D approval occurs subsequent to the balance sheet date, but before the issuance of the statutory financial statements and before the date the audited financial statements are issued, or available to be issued, such approval shall be considered a Type I subsequent event within the meaning of *SSAP No. 9—Subsequent Events.*

[9] See paragraph 2.9 of the *SSAP No. 101 Q&A* for similar requirements in the context of grouping of assets and liabilities for measurement.

ii. If the Form D approval occurs after the period which defines a subsequent event in SSAP No. 9, the difference created by such approval shall be recognized and disclosed in the period in which the approval is given.

d. The transition guidance in paragraph 37 does not apply to a reporting entity that does not file a Form D request for a CAMT-related tax allocation agreement amendment or a new tax allocation agreement prior to the end of 2023.

38. Consistent with *SSAP No. 3—Accounting Changes and Corrections of Errors,* paragraph 4, initial application of this interpretation shall not be considered a change in accounting principle, but instead application of a new principle for the first time.

Disclosures

39. The reporting entity shall disclose whether it is a nonapplicable reporting entity; an applicable reporting entity with tax allocation agreement exclusions or an applicable reporting entity.

40. Additionally, the following disclosures shall be made in the notes to the financial statements of applicable reporting entities (which do not have tax allocation agreement exclusions in accordance with paragraph 11 of this interpretation):

a. If the reporting entity has made an accounting policy election to either consider or disregard CAMT when evaluating the need for a valuation allowance for its non-CAMT DTAs described in paragraph 22 of this interpretation.

b. Any disclosure of material modifications to the methodology used to project CAMT as required by paragraph 35 of this interpretation.

41. Relevant disclosures required by SSAP No. 101 also apply to, including but not limited to, the following:

a. The disclosure of the statutory valuation allowance as required by SSAP No. 101, paragraph 21.

b. The disclosure of tax planning strategies is required by SSAP No. 101. In the disclosure required by SSAP No. 101, paragraph 28.b., a statement as to whether the reporting entity may be charged with a portion of CAMT incurred by the consolidated group (or credited with a portion of the consolidated group's CAMT credit utilization).

c. Inclusion of CAMT credit DTAs, if any, in the disclosure required by SSAP No. 101, paragraph 26.a. regarding the origination dates and expiration of tax credit carry forwards.

d. The impact of CAMT planning strategies, if any, in the disclosure required by SSAP No. 101, paragraph 22.f.

INT 23-03 Status

42. The consensuses in this interpretation are effective beginning with year-end 2023 financial statements and periods thereafter.

43. No further discussion is planned.

Examples

Basic Facts Used in All Examples

44. The reporting entity is a member of a tax-affiliated group of corporations that files consolidated federal income tax returns which reasonably expects to be an applicable corporation for 20X3.

a. Reporting entity also has $200x of non-CAMT adjusted gross DTAs (i.e., has already reduced by any required valuation allowance of $40x). Of this $200x of which $150x reverses over the 3-year applicable period 20X4-20X6 and is expected to be realized.

b. At the end of 20X3, reporting entity has a $50x CAMT credit DTA (pursuant to the consolidated group's tax allocation agreement, reporting entity was allocated a portion of the group's expected 20X3 current CAMT expense, which reporting entity included in its 20X3 current tax expense).

c. The consolidated group of which the reporting entity is a member establishes a $20x valuation allowance against its $50x CAMT credit DTA, resulting in a CAMT adjusted gross DTA of $30x that is more likely than not to be realized.

d. The reporting entity makes an accounting policy election to disregard CAMT when evaluating the need for a valuation allowance for its non-CAMT DTAs.

e. Reporting entity's capital and surplus for purposes of calculating the limitation under SSAP No. 101, paragraph 11.b. ii. is $2,000. Therefore, the 15% of surplus limitation is $300 (based on the top line of the applicable SSAP No. 101 paragraph 11.b. realization threshold limitation table), the 10% limitation is $200 (based on the second line of the applicable SSAP No. 101 paragraph 11.b. realization threshold limitation table).

f. For the purposes of these examples any DTA admittance under SSAP No. 101, paragraphs 11.a. and 11.c. is ignored.

Example 1 – Applicable reporting entity meets or exceeds the top line of the relevant SSAP No. 101, paragraph 11.b. Realization Threshold Limitation table (Ex. 3 years, 15%).

45. The basic facts above apply with the following additional information:

a. For 20x3, the reporting entity exceeds the first line of the applicable realization threshold limitation in SSAP No. 101, paragraph 11.b. for use of a 3-year applicable period and the limitation of capital and surplus is 15%. Pursuant to paragraph 31 of this interpretation, the reporting entity would not have to take the CAMT into account in calculating the “with and without” tax liability for purposes of determining the amount expected to be realized under SSAP No. 101, paragraph 11.b.i.

b. The consolidated tax return group has assessed and determined that the CAMT credit DTA amounts after the valuation allowance of $30x is expected to be utilized in 20x4and 20x5but $15x of CAMT would be incurred in 20x6.

46. The reporting entity admits the $30x adjusted gross DTA for its portion of the allocated CAMT credit DTA expected to be utilized within three years and admits the $150x non-CAMT adjusted gross DTA after valuation allowance than can be utilized within three years. Therefore, the admitted non-CAMT DTA and admitted CAMT credit DTA would total $180x ($150 +$30 =$180).

47. Although the consolidated group is expecting to incur CAMT during the 3-year period, the reporting entity does not reduce its non-CAMT admitted DTAs by the $15x the CAMT expected to be allocated under the tax allocation agreement to the reporting entity during the three years (pursuant to paragraph 31 of this Interpretation). Note that if the consolidated tax return group had assessed and determined that only a portion of the CAMT credit DTA after the valuation allowance was expected to be utilized in 20x4 20x5 and 20x6 then the reporting would only admit its allocation (per its tax allocation agreement) of the amount of CAMT credit DTA that will be utilized by the consolidated group during the 3 years.

48. The $180 is less than the $300 15% of surplus limitation in paragraph 11.b.ii., so it is not a limiting factor. (However, if reporting entity’s 15% of surplus limitation under paragraph 11.b.ii. was $175x, the reporting entity’s admitted adjusted gross DTA would be further reduced to $175).

	DTA	Valuation Allowance	Not Recoverable Within 3 Years	DTA Admitted Standalone	Impact of Consol. DTA	Admitted DTA under 11bi	15% surplus limitation under 11bii	Nonadmitted DTAs
DTAs	240	-40	-50	150		150		50
CAMT credit DTA	50	-20	0		30	30	-	-
totals	**290**	**-60**	**-50**	**150**	**30**	**180**	**300**	**50**

Example 2 – Applicable entity, that meets level 2 on the relevant SSAP No. 101, paragraph 11.b. Realization Threshold Limitation table (Ex.-1 year 10%).

49. The basic facts above apply with the following additional information:

a. For 20x3, the reporting entity meets the second line of the applicable realization threshold limitation in SSAP No. 101, paragraph 11.b. for use of a 1-year applicable period and the limitation of capital and surplus is 10%. Pursuant to paragraph 32 of this interpretation, the reporting entity would have to also apply the with and without calculation of the determination of the impact of the CAMT on the realization of DTAs.

b. The consolidated group of which the reporting entity is a member expects to incur CAMT in 20x4, of which $10 is expected to be allocated under the tax allocation agreement to reporting entity. The reporting entity reduces its $150x of non-CAMT admitted adjusted gross DTAs by its $10x share of the consolidated CAMT expected to be incurred in 20x4.

50. The reporting entities admitted DTA would be $140x. The result is an adjusted gross non-CAMT DTA of $150x, minus the $10 impact of the consolidated CAMT (with and without) equals 140 admitted DTA.

51. The resulting $140x of DTA admitted under paragraph 11.b.i., which is less than the $200x paragraph is less than the $200 10% of surplus limitation in paragraph 11.b.ii., so it is not a limiting factor.

	DTA	Valuation Allowance	Not Recoverable Within 1 Year	DTA Admitted Standalone	Impact of Consol. DTA and VA	Admitted DTA under 11bi	10% surplus limitation under 11bii	Nonadmitted DTAs
DTAs	240	-40	-50	150	-10	140		60
CAMT credit DTA	50	-20	-30				-	30
totals	**290**	**-60**	**-80**	**150**	**-10**	**140**	**200**	**90**

Example 3 – Applicable entity with qualifying tax allocation agreement exclusions.

52. The basic facts situation applies.

a. Similar to Example 1, the reporting entity meets the exceeds the first line of the applicable realization threshold limitation in SSAP No. 101, paragraph 11.b. for use of a 3-year applicable period and the limitation of capital and surplus is 15%.

b. The reporting entity is excluded pursuant to the tax allocation agreement from any allocation of CAMT or CAMT credit utilization in a qualifying tax allocation agreement as described in paragraph 11 of this interpretation.

53. Accordingly, the reporting entity for 20x3, would be excluded from the CAMT calculations, and the reporting entity's admitted adjusted gross DTA would be $150x. which is the amount after the valuation allowance of $40 and the $50 reduction for the amount not recoverable within 3 years.

54. The $150 is less than the $300 15% of surplus limitation in paragraph 11.b.ii., so it is not a limiting factor.

	DTA	Valuation Allowance	Not Recoverable Within 3 Years	DTA Admitted Standalone	Impact of Consol. DTA and VA	Admitted DTA under 11bi	15% surplus limitation under 11bii	Nonadmitted DTAs
DTAs	240	-40	-50	150		150		50
CAMT credit DTA	0						-	-
totals	**240**	**-40**	**-50**	**150**		**150**	**300**	**50**

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 23-04: Scottish Re Life Reinsurance Liquidation Questions

INT 23-04 Dates Discussed

October 23, 2023; October 24, 2023; December 1, 2023; January 10, 2024

INT 23-04 References

Current:
SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance

INT 23-04 Issue

Background

1. Liquidations of U.S. licensed reinsurers are uncommon. Due to a 2023 liquidation order of a U.S.-based life reinsurer, life industry cedents have requested an interpretation to address the accounting and reporting for reinsurance receivables from the reinsurer's estate. This interpretation is intended to be applied generically; however, the following circumstances are relevant to the accounting issues identified.

a. The recent liquidation order was for Scottish Re, a U.S. life reinsurance entity, which was in regulatory supervision for several years.

b. The life reinsurer was not assuming new business but was receiving ongoing premium on yearly renewable contracts.

c. The 2023 liquidation order cancelled reinsurance contracts on a cut-off basis, effective September 30, 2023.

d. Settlement from the reinsurer's estate is expected to exceed one year.

e. Settlement from the reinsurer's estate to the ceding entities is expected to be less than 100%. That is, cedents are expected to receive a portion of what they are owed.

f. Some ceding insurers established trusts to hold assets backing the reserves under the reinsurance agreements.

Interpretation Discussion

2. This interpretation is applicable only to the accounting and reporting of reinsurance recoverables from Scottish Re, a U.S.-based life reinsurer in liquidation. The Statutory Accounting Principles (E) Working Group consensuses to the noted issues are included below.

Issue 1 – Commutation or Recapture of a Life Reinsurance Contract

3. If a liquidation order cancels a life reinsurance contract on a cut-off basis, should the life reinsurance commutation guidance in S*tatement of Statutory Accounting Principle*s (*SSAP) No. 61—Life, Deposit-Type and Accident and Health Reinsurance* be used as the primary accounting guidance for the commutation?

4. Yes. SSAP No. 61, paragraph 58, provides the primary guidance for a life reinsurance commutation. The guidance provides that:

> **Recaptures and Commutations**
>
> 58. A recapture or a commutation of a reinsurance agreement is a transaction which results in the complete and final settlement and discharge of all present and future obligations between the parties arising out of the agreement or a portion of the agreement. Commuted and recaptured balances shall be accounted for by writing them off through the accounts, exhibits and schedules in which they were originally recorded. The assumed reserves and reserve credits taken are eliminated by the reinsurer and ceding entity, respectively. The reinsurer and ceding entity must also make any required IMR liability adjustment changes. Any net gain or loss is reported in the summary of operations.

Issue 2 – Impairment of Reinsurance Recoverables

5. The reinsurer that was previously in regulatory supervision and is now in liquidation was known to have financial difficulties and many ceding entities have either established valuation allowances and/or written off reinsurance recoverables as impairment losses. Questions have been received in response to the diversity in practice on whether the ceding entities were reporting impairment losses or were reporting a valuation allowance on all categories of their expected reinsurance recoverables from the reinsurer which is now in liquidation.

6. Do reporting entities have the choice of setting up a valuation allowance or applying the impairment guidance in SSAP No. 61 to the reinsurance recoverables from the life reinsurer in liquidation?

7. No. Reporting entities do not have a choice of a valuation allowance or applying impairment analysis. SSAP No. 61, paragraph 42, requires impairment analysis of uncollectible reinsurance amounts in accordance with *SSAP No. 5—Liabilities, Contingencies and Impairments of Asset.* The guidance requires that impaired amounts shall be written off through a charge to the Statement of Operations utilizing the same accounts which established the reinsurance recoverables. SSAP No. 5 and SSAP No. 61 do not permit a valuation allowance.

8. The liquidation order of a reinsurer should prompt an impairment analysis of all amounts recoverable from the reinsurer with a write-off of amounts not expected to be recovered.

9. The impairment analysis shall be updated at every reporting date.

Issue 3 – Reporting of Reinsurance Recoverables

10. The liquidation order results in a commutation and recapture of business for the ceding entity. A liquidation will determine the reinsurer's estate assets, then determine payments based on liquidation priority. This will result in a delay in settlement from the estate of the reinsurer. As previously detailed, the amounts paid by the estate shall be impaired to the amount expected to be received by the ceding entities.

11. Where shall the ceding entity report the remaining receivables for the reinsurer's estate?

12. In accordance with the recapture and commutation guidance in SSAP No. 61, paragraph 58 (quoted above), the ceding entity shall remove balances through the schedules and exhibits originally reported. No reserve credit or contra-liabilities shall be reported. The reinsurance reserve credits shall be removed. Gains or losses are reported in the summary of operations.

13. Based on preliminary information received, it is expected that there will be an amount receivable for paid claims incurred before the reinsurance contract cancellation. This amount shall be reported on the asset page line 16.1 - Amounts Recoverable from Reinsurers.

14. Amounts recoverable from the reinsurer's estate for claims incurred before the reinsurance contract cancellation and unpaid as of the reporting date shall be reported on the asset page line 16.3 - Other Amounts Receivable Under Reinsurance Contracts.

15. If the ceding entity owes amounts to the reinsurer's estate, the amounts shall be reported as a liability on line 9.3 - Other Amounts Payable on Reinsurance.

16. After impairing the recoverables, any other amount expected to be recovered from the reinsurer's estate shall be reported on line 25 Aggregate Write-ins for Other Than Invested Assets.

Issue 4 – Admissibility of Reinsurance Recoverables

17. As noted above, quarterly impairment analysis of collectability is required. After evaluating for impairment, if there are remaining receivables from the reinsurer's estate, do those assets qualify as admitted reinsurance recoverable assets?

18. Reinsurance recoverables from Scottish Re in liquidation are admitted as follows:

a. The reinsurance recoverable amount from Scottish Re from paid claims incurred prior to the reinsurance contract cancellation which are reported on the asset page line 16.1 - Amounts Recoverable from Reinsurers which are not in dispute are admitted after impairment review.

b. To the extent reinsurance amounts recoverable are secured by assets in an Appendix A-785 - Credit for Reinsurance compliant trust, such recoverable amounts may be admitted to the extent the that the amounts are not in dispute and that the collateral in an Appendix A-785 compliant trust is sufficient.

19. Other reinsurance recoverables, which are not identified as admitted assets in paragraph 18 are nonadmitted until received. This includes amounts either in dispute or not secured by collateral in a trust that is compliant with Appendix A-785.

Issue 5 – Disclosures

20. Do the relevant disclosures in SSAP No. 61 and other relevant SSAPs apply to a commuted life reinsurance contract which has not been fully settled due to a liquidation?

21. Yes. The relevant disclosures in SSAP No. 61 and other relevant SSAPs continue to apply to a life reinsurance contract which is commuted and recaptured due to a liquidation. These disclosures include but are not limited to the disclosures regarding commutation, uncollectible reinsurance and anything else that is required.

22. Disclosure in the reinsurance notes to the financial statements shall include additional information necessary to obtain an understanding of the impact of Scottish Re reinsurance counterparties in liquidation, including but not limited to, reinsurance payable liabilities, reinsurance recoverables by paid claims and other amounts, information regarding the status of any collateral and its fair value. Where applicable, reporting entities should disclose any individual components (e.g., unreimbursed claims or provisions for future losses) of recoverable amounts that are presented in the aggregate on the financial statements. The

disclosure shall include measurement, impairment and collectability of any reinsurance recoverables including timing of expected payments and nonadmitted amounts.

INT 23-04 Summary

23. Although readers should refer to the detailed guidance above, a summary of the key provisions is as follows:

a. Issue 1 – Commutation or Recapture of a Life Reinsurance Contract: Follow SSAP No. 61, paragraph 58, as it provides primary recapture and commutation guidance.

b. Issue 2 – Impairment of Reinsurance Recoverables: SSAP No. 61 paragraph 42, requires impairment of uncollectible reinsurance in accordance with SSAP No. 5.

c. Issue 3 – Reporting of Reinsurance Recoverables: Follow the recapture and commutation guidance in SSAP No. 61, then analyze for impairment. Report reinsurance payables separate from reinsurance recoverables. Amounts related to paid and unpaid claims incurred prior to reinsurance contract cancellation are reported on asset page line 16.1 - Amounts Recoverable from Reinsurers and asset page line 16.3 - Other Amounts Receivable Under Reinsurance Contracts, respectively. Any remaining reinsurance recoverables from the reinsurance counterparty after impairment assessment shall be reported on the asset page line 25 Aggregate Write-ins for Other than Invested Assets.

d. Issue 4 – Admissibility of Reinsurance Recoverables: Admit amounts related to claims incurred prior to contract cancellation which have been paid by the reporting entity as of the reporting date (reported on asset page line 16.1 - Amounts Recoverable from Reinsurers) which are not in dispute after impairment review. Admit reinsurance recoverables which are not in dispute, and which are secured by collateral in an A-785 compliant trust. Nonadmit all amounts recoverable from a life reinsurer in liquidation which are either in dispute or which are not secured by collateral in a trust compliant with Appendix A-785.

e. Issue 5 – Disclosures: Follow existing applicable disclosures and provide additional information sufficient to understand the nature and impact of a reinsurance counterparty in liquidation as described in paragraph 22.

INT 23-04 Status

24. The consensuses in this interpretation were adopted on January 10, 2024, with an effective date of reporting periods on or after December 31, 2023.

25. No further discussion is planned.

Interpretation of the Statutory Accounting Principles (E) Working Group

INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers

INT 24-01 Dates Discussed

August 13, 2024, October 4, 2024, November 17, 2024

INT 24-01 References

Current:
SSAP No. 21—Other Admitted Assets
SSAP No. 26—Bonds

INT 24-01 Issue

1. The principles-based bond definition was adopted in August 2023 with an effective date of January 1, 2025. In response to questions presented, question-and-answer implementation guidance was developed to assist with consistent assessment and application under the principles-based bond definition.

INT 24-01 Discussion

2. The Working Group reached consensus that Exhibit A provides question-and-answer guidance consistent with the intent of the principles-based bond definition, including application of debt securities that qualify for bonds under SSAP No. 26 and guidance for debt securities that do not qualify as bonds under SSAP No. 21.

INT 24-01 Status

3. This interpretation, and the question-and-answer guidance in Exhibit A is effective January 1, 2025. Consideration of further components may occur if future questions are received on the application of the principles-based bond guidance.

4. No further discussion is planned.

Exhibit A – Principles-Based Bond Definition Implementation Questions and Answers

Index to Questions:

1. Q – When assessing whether a security has substantive credit enhancement, how should future cash flows be considered? Should future expected cash flows be incorporated into the overcollateralization disclosure? [SSAP No. 26, paragraph 6.a. and 10.a.]

1.1 A – There are two components to this question: 1) how to consider future cash flows in assessing substantive credit enhancement; and 2) how to disclose the overcollateralization percentage. For the first component, the purpose of the substantive credit enhancement concept is to determine whether the creditor is in a different economic position than owning the underlying collateral directly. This includes evaluating all forms of economic value that the creditor has recourse to, including "hard," saleable assets, contractual or expected future cash flows, operating entity guarantees or other sources, and determining whether there is another party that absorbs substantive losses in economic value before the creditor experiences any losses.

Note however, **if** a reporting entity performs a quantitative assessment to support its conclusion, it should not double-count economic value. For example, in a lease-backed ABS, if the reporting entity incorporates future lease payments into its analysis, it should also consider the future, depreciated value of the "hard assets" rather than the current saleable value.

1.2 The second component of the question is how to complete the overcollateralization percentage disclosure on Schedule D, which is required for Non-Financial ABS that do not meet the practical expedient criteria and Financial ABS that are not self-liquidating. It was noted that including a quantification of all forms of economic value discussed in 1.1, which may include not only "hard," saleable assets but also future cash flows or operating entity guarantees, would be cumbersome to complete for each applicable investment, both at origination and an ongoing basis. It would also make the disclosure difficult to interpret, as it would not be apparent whether the overcollateralization is in the form of assets that could be liquidated upon default, or future cash flows which may be less readily able to be liquidated. Based on the discussion, it was determined that it would be most expedient, as well as most useful to annual statement users, for the overcollateralization percentage to only include "hard," saleable assets. For example, if a structure involved the leasing of railcars, and the structure had railcars and the associated lease cashflows pledged to the ABS Issuer as collateral, only the value of those railcars to the outstanding debt would be included in the disclosure. (This calculation is based on the value of the railcars, and not their future leasing potential.) Overcollateralization determined by the discounting of future cash flows is not permitted to be included in the disclosure.

1.3 Reporting entities shall report 'zero' when there is no "hard asset" overcollateralization in a structure on Schedule D. The column should not be left blank. A zero response is not standalone evidence that a structure does not qualify for bond reporting. A debt security can qualify for bond reporting without "hard asset" overcollateralization.

2. Q – Are securities issued by foreign governments or foreign government agencies considered Issuer Credit Obligations? [SSAP No. 26, paragraph 7.a.]

2.1 A – The examples of issuer credit obligations (ICO) in paragraph 7 are not all inclusive. Governmental entities are operating entities based on their substance, which does not change based on country. Securities issued as obligations of foreign governments or foreign government agencies are expected to be considered ICOs, unless the substance is more aligned with ABS. Schedule D-1-1 includes a reporting line for "Non-U.S. Sovereign Jurisdiction Securities." Foreign securities that reflect ABS, similar to US agency backed RMBS for example, are also expected to be considered ABS. Such ABS are anticipated to be reported on D-1-2 on the most appropriate reporting line that does not reflect a guarantee by the U.S. government.

3. Q – Are "Municipals" always Issuer Credit Obligations? [SSAP No. 26, paragraph 7.c. and 11]

3.1 A – The question received inquired on the classification of "municipals" noting the various structures and designs, and the explicit reporting lines on Schedule D-1-1 for general obligation and special revenue municipal structures. The answer to this question is that the naming convention of investment structures does not determine whether the investment qualifies for reporting as a bond or whether the investment is an issuer credit obligation (ICO) or asset-backed security (ABS). The first step in determining if an investment qualifies as a bond is whether it reflects a creditor-relationship in substance. The second step is determining whether the structure is an ICO or ABS, and that determination focuses on the primary source of cash flows that provides payment of interest and principal to the debtholder. Municipal securities are subject to the same assessment as other structures as to whether the cash flows are generated by the operations of an operating entity (the municipality) or whether the cash flows are generated from collateral outside of the operations of the municipality in determining whether the security shall be classified as ICO or ABS. However, this distinction is not always clear for several types of common municipal securities which warrants some additional interpretive guidance to promote consistency and streamline implementation efforts. The following summarizes preliminary assessments based on common designs of these structures. These assessments are contingent on the actual substance of the investment and shall not be inferred based on naming convention if the investment being reviewed does not conform to the traditional design.

a. General Obligation Municipal Bonds – These bonds are backed by the full faith and credit of the government issuer (municipality), which is an operating entity with the power to tax residents to pay bondholders. These securities, as general obligations of an operating entity (the municipality), would qualify as ICOs as explicitly stated in paragraph 7.c. of SSAP No. 26, and shall be reported in the "Municipal Bonds – General Obligation" reporting line.

b. Special Revenue Municipal Bonds – These bonds are not backed by the government's general taxing power but by revenues from a specific municipality-owned project or source, such as highway tolls, water and sewer, electric utility, lease fees or usage charges. Payment of interest and principal depends on the adequacy of the revenues derived from the project. Although the operating asset and/or its associated cash flows are often walled off in a bankruptcy remote SPV in order to facilitate more efficient financing of such projects, the primary purpose is still to raise debt capital to fund a component of a municipality's operations. Both paragraph 7.c. and 11 of SSAP No. 26 explicitly contemplate securities of this type qualifying as ICO, and shall be reported in the "Municipal Bonds – Special Revenue" reporting line.

c. Tax Revenue Bonds – These bonds are backed from certain dedicated tax revenues overseen by the municipality, such as sales taxes, gasoline or tobacco taxes, hotel or tourist taxes, special tax assessments or incremental property taxes. Payment of interest and principal depends on the adequacy of tax revenue. Although the obligation is secured only by a single revenue source, rather than the full faith and credit of the municipality, it is still backed by the municipality's taxing authority and is ultimately used to facilitate the raising of financing to be used in funding the needs and responsibilities of the municipality. Tax revenue bonds are determined to have the substance of an ICO and should be reported in the "Municipal Bonds – Special Revenue" reporting line.

d. Housing Bonds – These securities may be issued by a state or local government housing authority to facilitate construction or rehabilitation of multi-family apartments for low to moderate income residents. The bonds are secured by a pledge of rental or lease revenues and/or mortgage payments. These bonds generally only have recourse to the assets or mortgages pledged. These securities are not backed by the operations of the municipality, the financing is not being used to fund any operations of the municipality and the primary source of repayment are non-municipal collateral assets. Based on these observations, their substance appears to more closely reflect that of an ABS and shall be assessed for bond qualification under the ABS requirements. If qualifying as ABS, these structures shall be reported on Schedule D-1-2, likely as a non-guaranteed, non-agency, mortgage-backed security.

e. Conduit Bonds – These debt securities are issued by a government entity as a conduit for the benefit of a business or non-governmental enterprise, such as a manufacturing company, developer, college, hospital or non-profit organization. Revenues pledged by the business or enterprise are used to pay interest and principal on the investments. The government issuer is not responsible for making payments on the bonds if the business or enterprise defaults. These debt securities will need to be assessed to determine whether the structure qualifies as an ICO or ABS. If the structure is backed by the creditworthiness of a single operating entity (such as a college), then the structure is expected to be an ICO. If qualifying as an ICO, the specific reporting line used should be the one that most closely reflects the nature of the investment. If historical reporting and/or market conventions would consider the ICO investment to be a municipal security, then it would be reasonable for the investment to be reported as a special-revenue municipal bond. However, this reporting is contingent on the ICO classification. If the structure represents an ABS (such as a conduit bond secured by housing assets or mortgages pledged), it should not be reported as a municipal on Schedule D-1-1 simply due to historical reporting or market convention as a municipal bond.

4. Q – Should common types of "Sports Deals" be classified as ICO or ABS? [SSAP No. 26, paragraphs 7-8]

4.1 A – There are two main types of leaguewide sports financing vehicles, with the key difference being whether or not noteholders have recourse to the individual sports teams.

4.2 Leaguewide Deals **with** Recourse to Teams – The League sets up an SPV or Trust that serves to aggregate debt issued by multiple teams within the League. The SPV (Trust) issues a Note, representing the aggregation of each underlying team's debt obligation. Through the SPV, Noteholders have recourse back to each individual team for its respective debt on a several (but not joint) basis. The Notes are also secured by Franchise rights for each team that participates in the financing and all revenues from current and future League media contracts and typically other ancillary revenue streams (e.g. online/streaming revenues, royalty fees from sports gear sold to fans, etc.). No cross-collateralization among teams or their respective revenue streams, but Noteholders have some protection from the League (which exercises considerable control over individual teams) and a pledge of team ownership rights as collateral. Should any individual team default, the League could (and in all practicality, would) step in to orchestrate a sale of the team, otherwise Noteholders could take ownership of the team.

4.3 The question raised was whether this type of deal would fall under the ICO or ABS criteria. Each team represents an operating entity, and each are individual obligors for their pro rata portion of the financing. Though the direct issuer is an SPV, it is being used to facilitate the efficient raising of debt capital by the individual teams/operating entities, as opposed to redistributing or transforming the underlying risk. In addition, the league itself is an operating entity, and though it is not a direct obligor on the financing, it has a significant role in the facilitation of the financing, its actions can significantly impact the paying ability of the individual teams and it has levers it can and would pull to ensure debtholders receive payment. Through discussion of this example, it was determined that the substance was more aligned with that of an ICO than an ABS. Under one perspective, the league could be viewed as a single-operating entity with all of its affiliated teams being part of that operating entity. This would allow the debt to be considered a "single operating entity backed obligation" under paragraph 7.g. of SSAP No. 26. Under another perspective, debtholders effectively hold debt obligations of each of the individual teams. If each team were to individually issue their debt to the noteholders, rather than through a coordinated offering, the noteholders would be in no different economic situation and each individual security would qualify as an ICO. As a result, this investment is effectively a series of "single operating entity backed obligations" under paragraph 7.g. Based on these observations, it was determined that this type of deal is an ICO in substance.

4.4 Leaguewide Deals **without** Recourse to Teams – Each participating team sells its share of all current and future contracted media revenues (and other ancillary revenues) to a newly created, bankruptcy remote subsidiary of the team in a true sale. The subsidiary then pledges the purchased assets to an SPV/Trust set up by the League. The SPV/Trust then issues Notes to investors. The structure has many features associated with ABS securities, including a bankruptcy-remote legal opinion, a true sale legal opinion, debt service reserves, and a payment waterfall (with Noteholders receiving priority of payment). The Notes are secured by revenues generated from the media contracts and other ancillary revenues (e.g. online/streaming revenues, royalty fees from sports gear sold to fans, etc.).

4.5 Unlike the previous example, these securities do not have recourse to an operating entity. They have all of the characteristics of a securitization of a revenue stream. Therefore, they must be evaluated under the ABS criteria. Also, there is a performance obligation for the cash flows to become collectible, as the product must be provided in order for the revenue to be generated (i.e. games must be played). As a result, the collateral are deemed to be non-financial assets, requiring the security to be assessed under the non-financial ABS criteria.

5. Q – Do cashflows produced by non-financial assets backing an ABS have to actually be used to make interest and principal payments throughout the life of the debt security for an investment to qualify as a non-financial backed ABS under the meaningful cash flow test? [SSAP No. 26, paragraph 8]

5.1 A – The principles-based bond definition is clear that the collateral supporting non-financial ABS must have a means of producing meaningful cash flows through other than sale or refinancing. However, it does not specify whether those cash flows must actually be used to pay the principal and interest in all scenarios. For example, it is not uncommon for an ABS to allow cash flows to be paid to equity holders prior to the debt tranches being repaid, so long as no covenants or triggering events have been breached. The example given was a continuation of the leaguewide sports deal **without** recourse to the individual teams as discussed in Question #4 in which the ABS was backed by current and future contracted media revenues (non-financial assets). The notes were issued as non-amortizing bullet maturities (e.g., 100% balloon payments). Therefore, the base case expectation is that the bonds will be refinanced at maturity. However, after full analysis, it was identified that the non-financial assets backing the structure generated substantially more cash flows over the life of the debt security than what would be needed to provide all interest and principal payments and would produce enough cash flows to "turbo" amortize and pay 100% of principal and interest in a short time frame if refinancing were not to occur. Additionally, there exist covenants (e.g. upon a significant decrease in media revenue) which, if triggered, would cause all cash flows to be diverted away from the equity holders and used to "turbo" amortize the debt. The question is, does the fact that the base case expectation is that the cash flows will not be used to pay down the debt result in the ABS lacking meaningful cash flows? Based on these discussions, it was determined that this situation would not preclude a conclusion that meaningful cash flows exist. Despite the meaningful cash flows not being used to pay the debt in the base case, the creditor still has rights to them and would collect them prior to experiencing any loss upon default. Therefore, all such cash flows available to creditors may be included in the assessment of meaningful cash flows.

6. Q – How should CMBS Interest Only (IO) strips be assessed under the PBBD? [SSAP No. 26, paragraphs 8-10]

6.1 A – The question pertains to the classification of CMBS IO strips that are paid from the excess spread of a CMBS structure. Excess spread is the excess of the interest collected on the underlying commercial mortgages over the contractual interest to be paid on the issued securitized tranches. In these instances, the IO strip is "linked" to either a specific tranche (such as a specific B-rated or AAA-rated tranche), or the IO strip could be linked to a combination of the issued tranches (from the residual tranche through the top AAA tranche). The tranche or tranches to which an IO is linked refers to the notional amount of principal from which the IO interest is calculated. Regardless of which tranche an IO is linked to, it is paid pari-passu with AAA rated tranche. The calculation of the IO strip interest to be paid is the product of the remaining principal of the linked debt tranche and the contractual rate of the IO strip and the contractual rate is equal to the difference between the weighted average coupon of the underlying loans, and the weighted average coupon of the issued securitization tranches. The contractual rate of the IO strip is recalculated each period based on the loan and debt tranche balances that remain outstanding. For example, if weighted average coupon on the underlying loans is 9.2% and the weighted average coupon on the securitization tranches is 8%, the contractual rate on the CMBS IO is 1.2%. If the IO strip is linked to the BBB tranche and the BBB tranche has a principal value of $1,000, there would be a monthly coupon payment of $1.00 [(1.2% / 12 months) * 1,000]. The CMBS IO holder would receive their contractual interest pari-passu with the AAA tranche, meaning they would receive all contractual interest prior to any of the subordinated securitization tranches being entitled to receive interest. When losses or principal payments are applied to the linked securitization tranche, the notional amount on which the CMBS IO interest is calculated is reduced until fully paid or written off.

6.2 In assessing these structures under the bond definition, IO strips should be considered in the same manner as a debt security that reflect both principal and interest components. That is, for a CMBS security (a financial asset-backed security), the structure would be required to have substantive credit enhancement to qualify for bond classification. For these CMBS structures, even if the IO tranches may always be paid pari-passu with the AAA tranche, an assessment must still occur on whether there is substantive credit enhancement. If the IO tranche is linked to a debt tranche, or a combination of debt tranches, that have substantive credit enhancement, then the IO is also considered to have substantive credit enhancement resulting in an ABS bond classification. If the IO tranche is linked to a tranche that does not have substantive credit enhancement, or a combination of debt tranches that includes a tranche that does not have substantive credit enhancement (such as the residual tranche), the IO strip would also not be considered to have substantive credit enhancement and shall be classified as a non-bond debt security. This is because it would lack substantive credit enhancement to absorb losses before the notional balance from which the IO interest is calculated is reduced. As a result, principal losses on the underlying loans would result in an economic loss to the IO if there is no credit enhancement to absorb them.

7. Q – How should debt securities that reflect Single Asset Single Borrower (SASB) Commercial Mortgage Loan (CML) securitizations be assessed under the PBBD? [SSAP No. 26, paragraphs 8-10]

7.1 A – The question pertains to SASB commercial mortgage-backed security (CMBS) structures which involve securitizing a single mortgage loan collateralized by one property owned by a single borrower. Although structures can vary, SASBs are usually associated with high-value properties with many long-term tenants where the mortgage loan is too large for a single lender to hold. By securitizing the loan into rated, tradeable securities, it facilitates access to a broader lender base than would exist for commercial mortgage loans. SASB CMBS structures can issue multiple tranches with different priorities of payment, or they can issue one single tranche (i.e., uni-tranche) that simply passes through the cash flows of the underlying mortgage. In either scenario, the principal and interest payments on the underlying loan provide the cash flows to service the principal and interest on the issued debt securities. Usually, the principal and interest on the commercial mortgage loan and the issued securities are equal except for fees and expenses for servicing and structuring paid by the ABS Issuer.

7.2 Under the PBBD concepts, SASBs should be assessed as asset-backed securities (ABS), as the repayment of principal and interest is derived from the cash flows of the underlying collateral and not the general creditworthiness of an operating entity. SASB CMBS structures are not expected to qualify for reporting as issuer credit obligations reflecting a debt security fully supported by an underlying contractual obligation of a single operating entity pursuant to SSAP No. 26, paragraph 7.g. Although the ultimate cash flows for repayment are expected to be derived from the leasing of the property, the lease cash flows are typically not pledged and there are typically multiple lessees, thus not qualifying under paragraph 7.g. Under the ABS criteria, a SASB CMBS reflects a financial asset-backed structure (as a mortgage loan is a financial asset), therefore the debt security must qualify under the substantive credit enhancement concept to qualify for bond reporting. Determination of whether the debt issuance has substantive credit enhancement is contingent on the actual structure (multi-tranche or uni-tranche) and position of the security within the structure.

7.3. The senior tranches (those above the most junior tranche) in a multi-tranche SASB are expected to qualify under the substantive credit enhancement criteria, as the subordinated tranches will absorb losses first. Assuming the subordination is significant enough to be considered substantive, the subordination of the lowest tranche puts the reporting entity that holds a more senior tranche in a different economic position than if the mortgage loan was held directly.

7.4 The lowest tranche of a multi-tranche SASB, any tranche in which the subordinated tranches below it do not provide substantive credit enhancement, and uni-tranche SASBs are not expected to qualify for reporting as a bond as they do not meet the requirement for substantive credit enhancement. For these situations, the reporting entity is not in a different economic position than if they held the underlying mortgage loan directly. This is true regardless of the LTV or overcollateralization of the property compared to the underlying mortgage loan as the bond definition does not contemplate a broad look-through of the underlying collateral to indirect subordination. This is most clearly illustrated in Example 1 of Exhibit A of SSAP No. 26 which does not contemplate looking through the mortgage loan collateral to overcollateralization of the mortgage loans themselves through recourse to the underlying properties. While this is a legitimate source of overcollateralization, it represents overcollateralization of the mortgage loans in relation to the underlying properties, not overcollateralization of the debt securities in relation to the mortgage loans. The investor is in the same economic position as holding the mortgage loans directly. Therefore, these structures fail the substantive credit enhancement requirement and do not qualify for reporting as a bond.

7.5 SASB structures that do not qualify for reporting as a bond shall be captured as non-bond debt securities on Schedule BA within the reporting line specific for "Debt Securities That Lack Substantive Credit Enhancement." Life reporting entities can file these debt securities within the NAIC SVO to obtain an NAIC designation that can be used for RBC.

8. Q – Do synthetic or referenced pool structures within an ABS disqualify the ABS for reporting on Schedule D-1-2? [SSAP No. 26, paragraph 9]

8.1 A – The principles-based bond definition refers to ABS as being repaid with cash flows produced by collateral "owned" by the issuer. The term "owned" as used for this purpose is not necessarily intended to align with a legal view of ownership, but rather, all economic value to which the creditor has recourse. This may include rights to assets or payments derived through assignment, or other provisions. An example that has become common due to evolving banking regulations was discussed whereby a bank has a portfolio of auto loans but wants to transfer their credit risk without transferring or selling their loans. The bank creates a special purpose trust (or vehicle) to which the bank issues a "credit linked note" (effectively equivalent to a "credit risk transfer") which references the performance of the bank's portfolio of auto loans. The securities issued by the special purpose trust (e.g., debt tranche(s) and an equity tranche) are exposed to the reference pool of collateral and the payments received are linked to the credit and principal payment risk of the underlying borrowers captured in the reference pool. The specific underlying collateral, and whether it resides within the ABS, or if the ABS references a collateral item/pool that generates cash flows is not a determining factor as long as the ABS Issuer has contractual rights to the cash flows produced to repay the debt. An ABS Issuer that owns derivatives in the structures (such as a credit default swap or total return swap) that solely transfers the performance of the referenced pool into the ABS structure does not automatically disqualify ABS classification, but the assessment of derivatives within a structure must be closely considered. Structures with derivatives that influence payments based on variables unrelated to the ultimate collateral would not qualify as a creditor relationship in substance. Further, consideration should be given to *SSAP No. 86—Derivatives* in determining whether structures with derivatives are subject to specific guidance, such as that for structured notes.

9. Q – Can expected but non-contractual cash flows (e.g., from future leases) be considered in determining the meaningful cash flow practical expedient for non-financial ABS? [SSAP No. 26, paragraph 9.b.]

9.1 A – The example given was a single-family rental where the lease duration is shorter than the duration of the debt security, subjecting the investor to re-leasing risk. The insurer has a high degree of confidence based on its understanding of the market that the property will be able to be re-leased and that the leases (including consideration of unleased time) will produce sufficient cash flows to satisfy all of the interest and at least 50% of the original principal. The question is whether this example qualifies under the practical expedient. Paragraph 9.b. explicitly states that only contractual cash flows are to be considered in assessing qualification under the practical expedient. As such, evaluating qualification under the practical expedient should not include any future leases that are not yet in place and this example would therefore not qualify. However, this does not necessarily mean that the full analysis will require significantly more effort than using the practical expedient in this case. In fact, the analysis the insurer performed to determine that all of the interest and at least 50% of the principal would be satisfied through expected lease payments is likely sufficient to conclude that there are meaningful cashflows, even though the practical expedient is not met.

9.2 This question was brought forward because, although paragraph 9.b. is explicit that only contractual cash flows are included, a paragraph in a prior draft of the issuer paper addressing this topic omitted the word "contractual". This has since been corrected. This question highlights an important point. Issue papers intend to provide key context regarding the discussions leading to the development of new accounting standards. However, any unintended language that conflicts with statements in the SSAP should be disregarded.

9.3 As one more element of clarity coming from the discussions on this topic, the meaningful cash flow practical expedient is that less than 50% of the original principal relies on sale or refinancing risk. In some cases, this has been phrased in the inverse, that all interest and more than 50% of the original principal must be satisfied by the contractual cash flows at investment acquisition for the investment to qualify under the practical expedient. These two phrasings would be expected to have the same meaning, but for the avoidance of doubt, the standard should be interpreted that any outstanding amounts that rely on sale or refinancing at maturity, whether characterized as principal or accrued interest, must be less than 50% of the original principal in order to qualify under the practical expedient.

10. Q – How should hybrid securities be accounted and reported? [SSAP No. 26, paragraph 13]

10.1 A – SSAP No. 26 prior to the principles-based bond definition explicitly scoped in a class of assets referred to as "hybrid securities" which are defined as "securities whose proceeds are accorded some degree of equity treatment by one or more of the nationally recognized statistical rating organizations (NRSRO) and/or which are recognized as regulatory capital by the issuer's primary regulatory authority. Hybrid securities are designed with characteristics of debt and equity and are intended to provide protection to the issuer's senior note holders. Hybrid securities are sometimes referred to as capital securities." During the development of the principles-based bond definition, it was decided to remove the explicit scope-in and instead rely on the new principles to determine whether bond classification is appropriate. As these securities come in several forms, additional clarity on where to report such securities is warranted.

10.2 Equity Securities: Investments that represent shares, units, or an ownership interest in a company or other entity but do not reflect common stock that were previously considered hybrids under SSAP No. 26 are equity investments and shall be captured as preferred stock in scope of *SSAP No. 32—Preferred Stock*. Investments in debt securities are not permitted to be reported in scope of *SSAP No. 30—Unaffiliated Common Stock* or SSAP No. 32.

10.3 Debt Securities: Investments in debt securities previously considered hybrids under SSAP No. 26 (including those debt securities with cumulative interest features) **that qualify** under the principles-based bond definition shall be reported as bonds on Schedule D. An example may include certain debt securities which NRSROs allow to be treated as equity but for which all the principles-based bond definition requirements are present. To be clear, a set maturity date for a debt security is not a requirement for bond classification if the bond otherwise qualifies under the definition. (Perpetual bonds that qualify under the bond definition are permitted as bonds.)

10.4 Investments in debt securities treated as regulatory capital by the issuer's primary regulatory authority, and **that do not qualify** under the principles-based bond definition solely because interest can be cancelled in the event of financial stress in a non-resolution scenario without triggering an act of default are capital notes and shall be captured in *SSAP No. 41—Surplus Notes*. These capital notes are often issued by domestic or foreign banks, and the domestic or foreign bank regulator or the Issuer has the ability to cancel interest or dividends, without future interest accumulation or payment.

10.5 Debt securities other than capital notes (as defined in 10.4 above) that permit the issuing entity to cancel interest without future interest accumulation or payment and without triggering an act of default, or that incorporate other equity components that do not permit bond classification under the principles-based bond definition are non-bond debt securities and shall be captured in scope of *SSAP No. 21—Other Admitted Assets*.

10.6 Debt securities issued by regulated institutions where only the issuer's primary regulator may have regulatory power to cancel or convert to equity all or a portion of the debt and/or its related interest payments, solely **in a resolution scenario** were not previously considered hybrid securities and should continue to be reported as Schedule D bonds, as Issuer Credit Obligations under SSAP No. 26, so long as all principles-based bond definition requirements are met.

10.7 Exhibit A to this Q&A provides a summary of common types of securities and how they are to be treated under this Q&A.

11. Q – When do non-bond debt securities need to be assessed for admittance based on underlying collateral? [SSAP No. 21, paragraph 22]

11.1 A – All debt securities that do not qualify as bonds, regardless of the reason for which they do not qualify, shall be assessed as to the primary source of repayment. If the primary source of repayment is derived through underlying collateral, then the collateral must qualify as an admitted asset in order for the non-bond debt security to be admitted. For example, if the source of repayment is derived from mortgage loans, and the structure failed because it did not reflect a creditor relationship, have substantive credit enhancement or meaningful cash flows, the debt security is permitted to be admitted if the mortgage loans would have qualified as admitted assets if held directly. If the source of repayment is derived from railcar leases, and the structure failed because it did not reflect a creditor relationship, have substantive credit enhancement or meaningful cash flows, the debt security shall be nonadmitted as directly held railcars would not qualify as admitted assets.

Appendix A – Summary of Securities for Application Under Question 10

Bank Debt/Capital & Hybrid Securities Matrix	Bank Issuers					All Issuers	
				Additional Tier 1 Capital			
	Sr. Unsecured OpCo Debt	Sr. Unsecured HoldCo Debt	Tier 2 Capital (Subordinated Debt)	Debt Form	Perpetual Preferred Form	Debt Issued for Partial Equity Treatment from NRSROs	Debt Issued for Partial Equity Treatment from NRSROs
In scope of "hybrid securities" definition in Q&A?	No	Yes*	Yes*	Yes*	Yes*	Yes	Yes
Issuer can cancel interest (or dividend) non-cumulatively without default.**	No	No	No	Yes	Yes	Yes	No
Regulator can force cancellation of interest (or dividends) non-cumulatively without default.	No	No***	No***	Yes	Yes	No	No
Regulator can force write-down or equity conversion of debt.	No	Yes	Yes	Yes	Yes	No	No
Proposed accounting treatment.	SSAP No. 26, Bond Schedule D, Part 1	SSAP No. 26, Bond Schedule D, Part 1	SSAP No. 26, Bond Schedule D, Part 1	SSAP No. 41, Capital Notes Section of Schedule BA	SSAP No. 32, Preferred Stock Schedule D, Part 2	SSAP No. 1, Non-Bond Section of Schedule BA	SSAP No. 26, Bond Schedule D, Part 1

*Bank regulators require a specific amount of debt that is subject to "bail-in" during a resolution. Additional Tier 1 Capital, Tier 2 Capital, and Total Loss Absorbing Capacity (the latter of which includes Sr. Unsecured HoldCo Debt) are all subject to bail-in requirements and count towards various solvency ratio tests.

**Older versions of bank capital exist where the issuer can defer interest on a cumulative basis without triggering a default. These securities would be treated as SSAP No. 26, Schedule D, Bonds, as would any security with cumulative interest features.

***Interest amount can be cancelled or reduced following a write-down of debt in resolution scenario only.

