Brown Plus
ACCOUNTANTS + ADVISORS

2023 Insurance Webinar

December 14, 2023

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Sources of Presentation Content

This presentation will primarily review the most recent Statutory Accounting Principles Working Group and Blanks Working Group meetings throughout 2023.

Below we have added a link to the NAIC Adoptions by the SAPWG, covering recent adoptions through September 21, 2023:

- NAIC Adoptions by the SAPWG PDF

Also, we have added a link to the Blanks Working Group – Adopted modifications to Financial Statements and Instructions:

- https://content.naic.org/cmte_e_app_blanks_related_adopted_mods.htm

To note, the SAP Working Group Fall Meeting is scheduled for November 30 – December 4, 2023, and minutes summarizing actions taken will be available on the NAIC website after the meeting.

ADOPTIONS TO STATUTORY ACCOUNTING GUIDANCE

ADOPTIONS TO STATUTORY ACCOUNTING GUIDANCE

A. SSAP No. 26R—Bonds, SSAP No. 43R—Loan-Backed and Structured Securities, and other affected SSAPs to refine guidance for the principles-based bond project, effective Jan. 1, 2025. ***(Ref #2019-21 – New SAP Concept, See Principles Based Bond Project)***

B. INT 20-01: ASU 2020-04 and 2021-01 – Reference Rate Reform: Adopted proposal to revise the expiration date of INT 20-01 to Dec. 31, 2024. ***(Ref #2023-05 – SAP Clarification)***

C. SAPWG adopted revisions to SSAP No. 34 – Investment Income Due and Accrued, to add disclosures to the annual statement blank to capture the gross, non-admitted and admitted amounts for interest income due and accrued and the cumulative amount of paid-in-kind interest included in current principal balances, effective 12/31/23. **(Ref #2022-17 – SAP Clarification)** .

On March 22, 2023, the Statutory Accounting Principles (E) Working Group adopted, as final, the exposed revisions, with minor edits as illustrated below, to SSAP No. 34 to add additional disclosures to data capture the gross, nonadmitted and admitted amounts for interest income due and to add disclosure of the cumulative amount of paid-in-kind (PIK) interest included in the current principal balance. These disclosures are effective for year-end 2023 reporting.

Disclosures – the following edits to the disclosures in blue shall be made for investment income due and accrued in the financial statements. (SSAP No. 37 captures disclosures for mortgage loans on nonaccrual status pursuant to paragraph 6).

a. The bases by category of investment income for excluding (non-admitting) any investment income due and accrued;
b. Disclose total amount excluded;
c. Disclose the gross, nonadmitted and admitted amounts for interest income due and accrued;
d. Disclose aggregate deferred interest;
e. Disclose cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance.

Adoptions to Statutory Accounting Guidance

D. Additionally, SSAP No. 34—Investment Income Due and Accrued: Adopted revisions to clarify and incorporate a practical expedient to the paid-in-kind (PIK) interest aggregate disclosure for SSAP No. 34 and annual statement instruction purposes, effective 12/31/23. ***(Ref #2023-13 – SAP Clarification)***

The following revision to item (e) of the SSAP No. 34 disclosure was adopted:

Disclose cumulative amounts of paid-in-kind (PIK) interest included in the current principal balance. / par value (FN).

New Footnote: In disclosing the cumulative amount of PIK interest, identify the specific amounts of PIK interest by lot and aggregate the amounts by CUSIP/PPN that have a net increase to the original par value. The net increase includes PIK interest added to the par value less disposals (i.e., repayments; sales) that are first applied to any PIK interest outstanding. As a practical expedient, an insurer may calculate the cumulative amount of PIK interest on a bond by subtracting the original principal / par value from the current principal / par value, but not less than $0.

E. SSAP No. 43R: Adopted revisions to incorporate changes to add collateralized loan obligations (CLOs) to the financial modeling guidance and to clarify that CLOs are not captured as legacy securities, effective 12/31/23. ***(Ref #2023-02-SAP Clarification)***

Adopted revisions to SSAP No. 43R (in blue):

Designation Guidance:

- For Residential Mortgage-Backed Securities (RMBS), Commercial Mortgage-Backed Securities (CMBS) and Collateralized Loan Obligations (CLOs), RMBS/CMBS securities within the scope of this statement, the initial NAIC designation used to determine the carrying value method and the final NAIC designation for reporting purposes is determined using a multi-step process or the NAIC designation assigned by the NAIC Securities Valuation Office. The P&P Manual provides detailed guidance.

ADOPTIONS TO STATUTORY ACCOUNTING GUIDANCE

F. SSAP No. 95—Nonmonetary Transactions and SSAP No. 104R—Share-Based Payments: Adopted, with modification, ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer. The revisions add guidance to include share-based consideration payable to customers, effective 8/13/23. *(Ref #2023-07 – SAP Clarification)*

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

    Intrinsic Value Option for Awards Classified as Liabilities: A reporting entity shall make a policy decision of whether to measure all of its liabilities incurred under share-based payment arrangements (for employee and nonemployee awards) issued in exchange for goods or services at fair value or to measure all such liabilities at intrinsic value. However, the reporting entity shall initially and subsequently measure awards determined to be consideration payable to a customer at fair value

ADOPTIONS TO STATUTORY ACCOUNTING GUIDANCE

G. SAPWG adopted revisions to SSAP No. 25, Affiliates and Other Related Parties, to clarify that any invested asset held by a reporting entity that is issued by an affiliated entity, or which includes the obligations of an affiliated entity, is an affiliated investment. *(Ref #2022-15 – SAP Clarification)*

Proposed edits to SSAP No. 25 (*noted in blue*) :

5. An affiliate is defined as an entity that is within the holding company system or a party that, directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with the reporting entity. An affiliate includes a parent or subsidiary and may also include partnerships, joint ventures, and limited liability companies as defined in *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies*. Those entities are accounted for under the guidance provided in SSAP No. 48, which requires an equity method for all such investments. An affiliate is any person that is directly or indirectly, owned or controlled by the same person or by the same group of persons, that, directly or indirectly, own or control the reporting entity. Any invested asset held by a reporting entity which is issued by an affiliated entity, or which includes the obligations of an affiliated entity is an affiliated investment.

Proposed Annual Statement Reporting Changes*: (These will be captured in a blanks proposal)*

This will be included in the Investment Schedules General Instructions in several places covering several different types of investment, and this revision is proposed to be included in each place under the header "Parent, Subsidiaries and Affiliates."

Parent, Subsidiaries and Affiliates:

Defined by *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*. Any invested asset held by a reporting entity which is issued by an affiliated entity, or which includes the obligations of an affiliated entity is an affiliated investment.

Adoptions to Statutory Accounting Guidance

H. SSAP No. 86 - Derivatives – Revisions adopted with modifications derivative guidance from GAAP literature, related to incorporate the portfolio layer method and the partial-term hedges for statutory accounting, effective January 1, 2023. ***(Ref #2022-09 – New SAP Concept)***

Description of Issue: In August 2017, the FASB issued *ASU 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities*. Under that ASU, the FASB added guidance to incorporate a "last-of-layer" method to make portfolio fair value hedge accounting more accessible for specific assets. Under the last-of-layer approach, for a closed portfolio of prepayable financial assets or one or more beneficial interests secured by a portfolio of prepayable financial instruments, entities were allowed to hedge a stated amount of the asset or assets in the closed portfolio that is anticipated to be outstanding for the designated hedged period. If the requirements for the last-of-layer method were met, prepayment risk is not incorporated into the measurement of the hedged item.

Following are the key proposed edits to SSAP No. 86 (noted in blue)

26. Fair value hedges qualify for hedge accounting if all of the following criteria are met:

   d. The hedged item is specifically identified as either all, or a specific portion, or the partial term of a recognized asset, or all or a specific portion of or a recognized liability or of an unrecognized firm commitment. The hedged item is a single asset or liability (or a specific portion or partial term thereof) or is a portfolio of similar assets or a portfolio of similar liabilities (or a specific portion thereof) or a closed portfolio of assets (pursuant to paragraph 26f and Exhibit A, paragraph 46) where assumed layer or layers is anticipated to be outstanding (or a specific portion thereof) 1. For a partial term hedge of one or more consecutive selected contractual cash flows where the hedged item begins when the first hedge cash flow begins to accrue and ends at the end of the designation hedge period, the assumed maturity of the hedged item occurs at the end of the designated hedge period.

ADOPTIONS TO STATUTORY ACCOUNTING GUIDANCE

I. SSAP No. 100R – Fair Value Measurement of Restricted Securities - Adopted revisions to incorporate updated guidance from restricted securities, effective 3/22/23. **(Ref #2022-16 – SAP Clarification)**

Proposed edits to SSAP No. 100R:

Equity Securities Subject to Contractual Sale Restrictions

15. An equity security that an entity cannot sell on the measurement date because of a contractual sale restriction shall be measured at fair value on the basis of the price in the principal (or most advantageous) market. A contractual sale restriction does not change the market in which that equity security would be sold. A discount applied to the price of an equity security because of a contractual sale restriction is not a characteristic of the equity security. A contractual sale restriction is a characteristic of the reporting entity holding the equity security rather than a characteristic of the asset and, therefore, is not considered in measuring the fair value of an equity security. A contractual sale restriction prohibiting the sale of an equity security is a characteristic of the reporting entity holding the equity security and shall not be separately recognized as its own unit of account.

16. The effect on a fair value measurement arising from a restriction on the sale or use of an asset by a reporting entity will differ depending on whether the restriction would be taken into account by market participants when pricing the asset. When the restriction is a characteristic of the asset, the restriction is a characteristic of the asset and should be considered in measuring the fair value of the asset. For example, an equity security issued through a private placement is not registered and is legally restricted from being sold on a national securities exchange or an over-the-counter market until the shares are registered or the conditions necessary for an exemption from registration have been satisfied. A market participant would sell the private placement equity securities in a different market than the market used for registered equity securities on the measurement date. Because that restriction would be a characteristic of the equity security, a market participant would consider the inability to resell the security on a national securities exchange or an over-the-counter market when pricing the equity security; therefore, the reporting entity that holds the Class A shares acquired through a private placement transaction would consider that restriction a characteristic of the asset, and the reporting entity should measure the fair value of the equity security on the basis of the market price of the similar unrestricted equity security adjusted to reflect the effect of the restriction FN.

Adoptions to Statutory Accounting Guidance

J. SSAP No. 43R and No. 48 – Residuals in Investments – Adoption includes revisions to statutory reporting guidance and annual statement instructions for the reporting of residual interests, so that all residuals are captured on the dedicated Schedule BA – Other Long-term Invested Assets, effective 12/31/23. **(Ref #2023-12 – SAP Clarification)**

Description of Issue:

This agenda item proposes revisions to clarify the scope and reporting for investment structures that represent residual interests or a residual security tranche (collectively referred to as residuals) within statutory accounting principles. Previously, revisions have been incorporated in SSAP No. 43R—Loan-Backed and Structured Securities to address the reporting of residual interests within securitization structures. With these revisions, residual interests, as defined within SSAP No. 43R, were required to be reported on Schedule BA on designated reporting lines beginning year-end 2022. After reviewing the 2022 reporting results, it was identified that the information for residuals may be underrepresented as a result of the various legal forms that residual investments can take. For example, a reporting entity could hold investments that have the substance of residual interests in the form of limited partnerships, joint ventures, or other equity fund investments. To ensure collective and consistent reporting of all residual interests, this agenda item proposes guidance to clarify the reporting of in-substance residuals regardless of the structure of the investment vehicle.

Proposed revisions to SSAP No. 43R & 48, specifically new paragraphs added to both SSAPs. New paragraphs 18-20 in SSAP No. 48 are titled "Residual Interests and Reporting" and the new paragraphs 27-28 added to SSAP No. 43R are titled "Residual Tranches or Interests."

EXPOSED STATUTORY ACCOUNTING PRINCIPLE CONCEPTS AND CLARIFICATIONS TO STATUTORY ACCOUNTING GUIDANCE

Exposed Statutory Accounting Principle Concepts and Clarifications to Statutory Accounting Guidance

A. SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term investments: Exposed revisions to further restrict the investments that are permitted for cash equivalent or short-term investment reporting. These revisions are proposed to ensure that certain investment types are captured on designated Schedule BA reporting lines and to eliminate the potential to design investments to specifically qualify for short-term reporting. ***(Ref #2023-17)***

Key revisions recommended and exposed for comment are as follows:

Cash Equivalents –

CD's with a maturity of less than 12 months at the time of acquisition are reported as cash per paragraph 5.

Regardless of maturity date, the following investments are not permitted to be reported as cash equivalents and shall be reported on the investment schedule that corresponds to the SSAP for which the investment is applicable (below are additions to the para 6):

- Mortgage loans captured in the scope of SSAP No. 37
- All investments that are reported on Schedule BA, including but not limited to:
  - Collateral / Non-collateral loans captured in the scope of SSAP No. 21R
  - Working capital finance investment in the scope of SSAP No. 105R
  - Surplus Notes in the scope of SSAP No. 41R

Exposed Statutory Accounting Principle Concepts and Clarifications to Statutory Accounting Guidance

SSAP No. 2R—Cash, Cash Equivalents, Drafts, and Short-Term investments: Exposed revisions. *(Ref #2023-17) - Continued)*

Key revisions recommended and exposed for comment are as follows:

Short-term investments:

Regardless of maturity date, the following investments are not permitted to be reported as short-term investments and shall be reported on the investment schedule that corresponds to the SSAP for which the investment is applicable (below are additions to the para 14):

- Mortgage loans captured in the scope of SSAP No. 37
- All investments that are reported on Schedule BA, including but not limited to:
  - Collateral / Non-collateral loans captured in the scope of SSAP No. 20R or 21R
  - Working capital finance investment in the scope of SSAP No. 105R
  - Surplus Notes in the scope of SSAP No. 41R
  - All debt securities that do not qualify as bonds in scope of SSAP No. 21R

Exposed Statutory Accounting Principle Concepts and Clarifications to Statutory Accounting Guidance

B. INT 03-02: Modification to an Existing Intercompany Pooling Arrangement: Exposed the intent to nullify INT 03-02, as it is inconsistent with SSAP No. 25—Affiliates and Other Related Parties. ***(Ref #2022-12)***

Purpose – This agenda item was prompted by the recent focus of Statutory Accounting Principles (E) Working Group on related party transactions, recent queries to NAIC about how broadly to apply the guidance in INT 03 02 and the review of the SSAP No. 62R, paragraph INT 03-02 addresses the valuation of bonds in instances when bonds are used instead of cash for the payment among affiliates for amounts due on modifications to existing intercompany reinsurance pooling contracts. The discrepancy between the INT 03-02 and SSAP No. 25 has been identified through recent discussions evaluating related party transactions. Key excerpts of INT 03-02 are in the Authoritative Literature section below.

The primary accounting question that is a concern for this agenda item is INT 03-02, paragraph 11b which asks, "What is the appropriate valuation basis to be used for assets and liabilities that are transferred among affiliates in conjunction with the execution of a new reinsurance agreement(s) that serves to substantively modify an existing intercompany pooling arrangement?"

Exposed Statutory Accounting Principle Concepts and Clarifications to Statutory Accounting Guidance

INT 03-02: Modification to an Existing Intercompany Pooling Arrangement: Exposed the intent to nullify INT 03-02, as it is inconsistent with SSAP No. 25—Affiliates and Other Related Parties. *(Ref #2022-12) (Continued)*

Staff Recommendation: NAIC staff recommends that the Working Group move this item to the active listing, categorized as a SAP clarification, and expose the intent to nullify INT 03-02, as it is inconsistent with SSAP No. 25 guidance regarding economic and non-economic transactions between related parties. The guidance in INT 03-02 can result with in essence, unrecognized gains (dividends) or losses through the using the statutory book valuation when using assets (bonds) to make payments to affiliates for modifications to existing intercompany reinsurance pooling agreements. Treatment of transfers of assets between affiliates should be consistent for all intercompany transactions and there is not a compelling need to be different when valuing assets for intercompany reinsurance transactions.

Exposed Statutory Accounting Principle Concepts and Clarifications to Statutory Accounting Guidance

C. Re-exposed the revisions to SSAP No. 20 Non-admitted assets and SSAP No. 21R – Other Admitted Assets – both SSAP's identify the need for adequate collateral that qualifies as an invested asset. SSAP No. 20 is explicit that the investment asset collateral must qualify as an admitted asset. Recent discussions with state regulators have highlighted that although SSAP No. 21 references the guidance in SSAP No. 20, that it would be beneficial to also note the need for the collateral to qualify as an admitted invested asset. This agenda item recommends a clarification to SSAP No. 21 that the acceptable invested asset collateral, for collateral loans must qualify as admissible invested assets. The revisions require audits and the use of net equity value for valuation assessments when the pledged collateral is in the form of partnerships, limited liability companies, or joint ventures. ***(Ref #2022-11 – SAP Clarification)***

Proposed revisions to para 4. (Collateral Loans) of SSAP No. 21

a. Non-admitted Asset :
   i. For qualifying investments which are pledged as collateral that would be in the scope of SSAP No. 48 or SSAP No. 97 if held directly by the reporting entity, such as joint ventures, partnerships and limited liability companies and investments that would qualify as SCAs if held directly, the proportionate audited equity valuation shall be used for the comparison for the adequacy of pledged collateral. If the collateral loan exceeds the audited equity valuation of these pledged investments, then the excess shall be non-admitted.

Exposed Statutory Accounting Principle Concepts and Clarifications to Statutory Accounting Guidance

C. Re-exposed the revisions to SSAP No. 20 Non-admitted assets and SSAP No. 21R – Other Admitted Assets – *(Ref #2022-11 – SAP Clarification) (Continued)*

Proposed revisions to para 4. (Collateral Loans) of SSAP No. 21

a. Footnote 2 – A qualifying investment defined as those assets listed in Section 3 of Appendix A-001-Investments of Reporting Entities which would if held by the insurer would qualify for admittance. For example, if the collateral would not qualify for admittance under SSAP No. 4 due to encumbrances or other third-party interests, then it does not meet the definition of "qualifying" and the collateral loan, or any portion thereof which is not adequately collateralized, is not permitted to be admitted.

D. Exposure requests industry and regulator comment on a proposal for SSAP No. 48—Joint Ventures, Partnerships, and Limited Liability Companies <u>to further define and provide examples for the investments captured as non-registered private funds, joint ventures, partnerships or limited liability companies, or residual interests and reported based on the underlying characteristics of assets</u>. *(Ref #2023-16)*

E. Exposed revisions to SSAP No. 92 and SSAP No. 102 to <u>remove the transition guidance</u> that was included in the initial adoption of SSAP No. 92 and SSAP No. 102, <u>as it is past the 10-year effective period</u> for that transition. *(Ref #2023-21)*

2023-21 was subsequently adopted was adopted by the SAP Working Group on 10/23/23.

F. Exposed This agenda item has been developed to specifically identify in SSAP No. 30—Unaffiliated Common Stock and SSAP No. 32—Preferred Stock, <u>clarifications to identify that investments that are in substance residual interests shall be reported on Schedule BA on the dedicated reporting line for residuals.</u> *(Ref # 2023-23)*

Poll Question

Is the statutory Principles Based Bond Project effective January 1, 2025?

- ❑ *Yes*
- ❑ *No*

PRINCIPLES-BASED BOND PROJECT (REF# 2019-21)

Principles-based Bond Project

In August, the SAPWG adopted the exposed revisions to SSAP No. 26R, Bonds; SSAP No. 43R, Loan-Backed and Structured Securities; and other SSAPs (e.g., SSAP No. 86, Derivatives, for replication (synthetic asset) transactions) that would incorporate the most recent feedback received from industry stakeholders into the statutory accounting guidance developed for the principles-based bond project. ***(Ref#2019-21), effective January 1, 2025.*** The adopted revisions included:

i. Adding a scope exclusion paragraph in SSAP No. 26R to exclude securities that do not qualify as bonds pursuant to the principles-based bond definition, including first loss positions that lack contractual payments or substantive credit enhancement.

ii. Adding a scope exclusion in SSAP No. 26R to clarify that the accounting requirements for replication (synthetic asset) transactions are addressed in SSAP No. 86 and are not affected by the principles-based bond definition.

iii. Modifying the reference in SSAP No. 26R from “credit rating related” to “credit-quality related” to encompass the broader range of adjustments that align interests of debtholders and issuing entities (e.g., debt to earnings before interest, taxes, depreciation and amortization (EBITDA) ratio, interest coverage ratio, debt service coverage ratio).

iv. Adding a new footnote in SSAP No. 26R to define an exception for nominal interest rate adjustments as too small to be considered when assessing an investment’s substance as a bond. The new footnote includes an example application and clarifies that any adjustments that cause an investment to meet the definition of a structured note would not be considered nominal.

Principles-based Bond Project

v. Incorporating accounting and reporting guidance in SSAP No. 26R for first loss positions, which would be reported on Schedule BA at the lower of amortized cost or fair value consistent with the treatment of residual tranches.

vi. Modifying the guidance in SSAP No. 26R and SSAP No. 43R to clarify that assessments to determine whether an investment qualifies for reporting as a bond on Schedule D-1 are required as of the origination date and to permit the use of current or acquisition information for the assessments at the time of transition.

vii. Modifying the guidance in SSAP No. 26R and SSAP No. 43R to clarify that the transition guidance will be effective January 1, 2025, on a prospective basis and reporting entities do not need to restate the prior year's information for 2025 year-end reporting purposes.

viii. **Exposed through 9/29/23** for public comment, with possible adoption at the Fall meeting, were revisions to SSAP No. 21R, were as follows:

   - Incorporating accounting and reporting guidance in SSAP No. 21R for debt securities that do not qualify as bonds pursuant to the principles-based bond definition in SSAP No. 26R.

WORKING GROUP DIRECTION PROVIDED TO NAIC STAFF

Working Group Direction Provided to NAIC Staff

A. Review Annual Statement Instructions for Accounting Guidance: To proceed with a broad project to review the annual statement instructions and ensure accounting guidance is included within the SSAPs. ***(Ref #2023-01)***

B. Schedule BA Reporting: Directed NAIC staff to sponsor a blanks proposal to revise Schedule BA: Other Long-Term Assets in accordance with the bond project for debt securities that do not qualify as bonds, with formal notice to the Valuation of Securities (E) Task Force and the Capital Adequacy (E) Task Force on the proposal to allow life reporting entities the ability to use existing Schedule BA reporting provisions for Securities Valuation Office (SVO)-assigned designations in determining risk-based capital (RBC) for debt securities that do not qualify as bonds. ***(Ref #2019-21)***

BLANKS WORKING GROUP ADOPTED EDITORIALS

Blanks Working Group Adopted Editorials

A. 2022-17BWG Modified – Add a new disclosure paragraph for Note 8 – Derivative Instruments and Illustration. The new disclosure is to be data captured. Add electronic-only columns related to derivatives with excluded components to Schedule DB, Part A and Part B for both Section 1 and Section 2. Add new code column instructions for Schedule DB, Part A and B *(Effective 2023 Annual filing)*

B. 2023-01BWG - Remove pet insurance from the inland marine line of business and add a new line of business to Appendix – P/C Lines of Business. Add a pet insurance line within the existing property/casualty (P/C) blank for the Underwriting and Investment Exhibits, Exhibit of Premiums and Losses (State Page), and Insurance Expense Exhibit. Add new Schedule P Parts 1 through 4, specific to pet insurance. (**Effective 2024 Quarterly filing**)

C. 2023-02BWG Modified – New supplemental exhibit to identify premiums that are reportable for Market Conduct Annual Statement (MCAS) purposes. Refer to the Data Call and Definitions document for each individual line of business, found at the MCAS webpage. *(New Supplement filing due March 1st)*

SUPPLEMENT FOR THE YEAR 2023 OF THE

MARKET CONDUCT ANNUAL STATEMENT (MCAS) PREMIUM EXHIBIT FOR YEAR

For The Year Ended December 31, 2023
(To Be Filed by March 1)

FOR THE STATE OF:

NAIC Group Code ____________________ NAIC Company Code ____________________

MCAS LINE OF BUSINESS	MCAS Reportable Premium/Considerations (Yes/No)
1. Disability Income	
2. Health	
3. Homeowners	
4. Individual Annuity	
5. Individual Life	
6. Lender-Placed Home and Auto	
7. Long-Term Care	
8. Other Health	
9. Private Flood	
10. Private Passenger Auto	
11. Short-Term Limited Duration Health Plans	
12. Travel	

Blanks Working Group Adopted Editorials

D. 2023-04BWG Modified – Add instructions for the appointed actuary and qualified actuary contacts to the Jurat electronic-only section. *(Effective 2023 Annual filing)*

E. 2023-08BWG – Add clarifying language for mutual insurance companies on Schedule Y, Part 3. Additional instruction will clarify that mutual insurance companies should be included on Schedule Y, Part 3. *(Effective 2023 Annual filing)*

F. 2023-11BWG Modified – Add additional instructions and illustrations to be data captured for Note 7 – Investment Income in the notes to the financial statement to disclose more information on interest. *(Effective 2023 Annual filing)*

Blanks Working Group Adopted Editorials

G. 2022-04BWG - New Supplemental Exhibit for Other Liabilities by Lines of business – Purpose is to capture more granular detail about the business reported on Lines 17.1, 17.2 and 17.3 of the Exhibit of Premiums and Losses. ***(New Supplement filing due March 1)***

SUPPLEMENT FOR THE YEAR 2023 OF THE

EXHIBIT OF OTHER LIABILITIES BY LINES OF BUSINESS

AS REPORTED ON LINE 17 OF THE EXHIBIT OF PREMIUMS AND LOSSES
(To Be Filed by March 1)

NAIC Group Code ________ NAIC Company Code ________

	Direct Business Only			
	Prior Year	Current Year		
	1 Written Premium	2 Written Premium	3 Losses Paid (deducting salvage)	4 Losses Unpaid (Case Base)
1. Completed operations				
2. Errors & omissions (E&O)				
3. Directors & officers (D&O)				
4. Environmental liability				
5. Excess workers' compensation				
6. Commercial excess & umbrella				
7. Personal umbrella				
8. Employment liability				
9. Aggregate write-ins for facilities & premises (CGL)				
10. Internet & cyber liability				
11. Aggregate write-ins for other				
12. Total ASL 17 - other liability (sum of Lines 1 through 11)				
DETAILS OF WRITE-INS				
0901.				
0902.				
0903.				
0998. Summary of remaining write-ins for Line 9 from overflow page				
0999. Totals (Lines 0901 thru 0903 plus 0998)(Line 9 above)				
2501.				
2502.				
2503.				
2598. Summary of remaining write-ins for Line 11 from overflow page				
2599. Totals (Lines 2501 thru 2503 plus 2598)(Line 11 above)				

Blanks Working Group Adopted Editorials

Data required to be segregated and reported for: Exhibit of Other Liabilities by Lines of Business as Reported on Line 17 of the Exhibit of Premiums and Losses. Due March 1 *(739-744/824).*

For Facilities & Premises separately report each category as follows:

1. Construction and Alteration Liability
2. Contractual Liability
3. Elevators and Escalators Liability
4. Liquor Liability
5. Personal Injury Liability
6. Premises and Operations Liability
7. Commercial General Liability (CGL)
8. Comprehensive Personal Liability
9. Day Care Centers
10. Fire Legal Liability
11. Municipal Liability
12. Veterinarian

Blanks Working Group Adopted Editorials

H. *NON - BWG item – But to highlight a new item for RBC preparation –* Affiliated investments – Changes were adopted to revise the instructions and structure of the Affiliated Investment pages (PR003-PR005) to provide consistent treatment of affiliated investments between Health, Life and P&C. *(Effective for 2023 RBC filing)*

Blanks Working Group Adopted Editorials

The following three deferred and re-exposed proposals were adopted by the BWG at their recent meeting on November 7, 2023.

A. Deferred for comment - 2023-05BWG Modified – Changes to the cybersecurity supplement to remove the reference to identity theft insurance from the General Instructions; remove the interrogatory questions from Part 1 that pertain to identity theft insurance; and remove the column for Identity Theft Insurance from Part 2 and Part 3. Remove claims-made and occurrence breakdown, as well as first-party and third-party breakdowns from data collection and remove the question in the interrogatories regarding tail policies.

B. Deferred for comment - 2023-07BWG – Update the code column and delete the LEI column for the following investment schedules: Schedules A, B, BA, D Part 2, D Part 6 and E Part 1.

C. Re-exposed for comment - 2023-06BWG – Split the Schedule D, Part 1 into two sections: one for issuer credit obligations and the other for asset-backed securities (ABS). Update the other parts of the annual statement that reference the bond lines of business.

NAIC ACTIONS IMPACTING STATUTORY TAX REPORTING

INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax

- **Inflation Reduction Act (Act)**
  - Enacted on August 16, 2022
  - Includes a new corporate alternative minimum tax (CAMT) effective for tax years beginning after 2022

- **CAMT**
  - 15% of the corporation's "adjusted financial statement income"
  - Does not include other comprehensive income including unrealized gains and losses on AFS securities
  - Tentative CAMT is based on a comparison of consolidated tentative CAMT to consolidated regular tax

- **CAMT Application**
  - Application made on a tax-controlled group basis
  - Corporations with average annual adjusted financial statement income in excess of $1 billion for three prior taxable years (threshold reduced to $100 million in the case of certain foreign-owned corporations)
  - "Applicable corporation" status – CAMT must be tentatively determined and compared to regular tax liability
  - Once an applicable corporation, always an applicable corporation (with certain exclusions)

- As most reporting entities will not be subject to the CAMT calculation, guidance was developed as an interpretation

INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax (cont.)

- **Categories of Reporting Entities**
  - Nonapplicable reporting entities
  - Applicable reporting entities
  - Applicable reporting entities with tax allocation agreement exclusions

- **Applicable reporting entities**
  - Required to consider CAMT in current and deferred tax computations
    - May or may not result in different current and deferred income taxes
  - Consider intercompany tax allocation agreement (tax sharing agreement)
  - Consolidated tax return considerations
    - Match the CAMT charges reasonably estimated to be paid by reporting entity
    - CAMT credits reasonably estimated to be received by reporting entity

- **CAMT payable should be included in the calculation of current income tax expense**
  - Amount owed as a separate filer, or
  - In accordance with the consolidated tax return group's tax sharing agreement

INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax (Cont.)

- CAMT Credit Deferred Tax Asset (DTA)
  - Non-expiring tax credit carryforward
  - Equal and offsetting to the current CAMT accrued
  - CAMT credit carryforward is a type of DTA

- Valuation allowance (VA) considerations
  - Dependent upon whether part of a consolidated tax return group or a separate filer
  - Accounting policy election to either consider or disregard CAMT when evaluating the need for a VA for non-CAMT DTAs

- Admissibility considerations
  - Consolidated tax return group – credit can only be realized when the group qualifies for the credit
  - Specific admittance guidance for the CAMT credit:
    - CAMT credit is a tax credit DTA that does not expire
    - Ability to utilize the CAMT credit is contingent on the actions and tax paying behaviors of the consolidated tax return group
  - If CAMT credit carryforward does not qualify for admission under 11.b., it is permitted to be recognized as an offset against DTLs under 11.c.

INT 23-03: Inflation Reduction Act – Corporate Alternative Minimum Tax (Cont.)

- Transition Guidance
  - Tax allocation agreements – potential amendments prior to Dec. 31, 2023 (Form D)
  - Initial application of the interpretation shall not be considered a change in accounting principal, but instead application of a new principal for the first time

- Disclosures
  - Type of entity (nonapplicable reporting entity, applicable reporting entity with tax allocation agreement exclusion, or applicable reporting entity)
  - For applicable reporting entities:
    - If the entity has made an accounting policy election to either consider or disregard CAMT when evaluating the need for a VA for its non-CAMT DTAs
    - Any material modifications to the methodology used to project CAMT
  - Other relevant SSAP 101 disclosures, including:
    - Statutory VA
    - Tax planning strategies, including a statement as to whether the reporting entity may be charged with a portion of CAMT incurred by the consolidated group
    - Inclusion of CAMT credit DTAs, including origination dates and expiration of tax credit carryforwards
    - Impact of CAMT –planning strategies

- Effective beginning with year-end 2023 financial statements and periods thereafter

Poll Question

Is your company subject to CAMT?

- ❑ *Yes*
- ❑ *No*
- ❑ *Not Sure*

NAIC Actions Impacting Statutory Tax Reporting

Notice 2023-63, Guidance on Amortization of Specified Research or Experimental Expenditures under Section 174

Released on September 8, 2023, by the Department of Treasury and Internal Revenue Service. Provides interim guidance to be relied upon pending proposed regulations. If taxpayers choose to rely on the notice, it must be applied in full.

The interim guidance provides taxpayers with clarity in determining whether expenditures are specified research or experimental (SRE) expenditures subject to capitalization and amortization under Section 174. SRE expenditures include research and experimental (R&E) expenditures paid or incurred during the taxable year in connection with the taxpayer's trade or business.

Examples of SRE expenditures:

a. Labor costs – including full-time, part-time, and contract employees and independent contractors who perform, supervise, or directly support SRE activities
b. Materials and supplies costs – costs of materials and supplies which are used or consumed in the performance of SRE activities
c. Cost recovery allowances – depreciation, amortization, or depletion allowances with respect to property used in the performance of SRE activities or in the direct support of SRE activities
d. Other costs such as patent costs, certain operation and management costs and travel costs, etc.

NAIC Actions Impacting Statutory Tax Reporting

Notice 2023-63, Guidance on Amortization of Specified Research or Experimental Expenditures under Section 174

The interim guidance also provides taxpayers with clarity in determining whether certain activities constitute software development for purposes of Section 174. The term computer software generally means any computer program or routine that is designed to cause a computer to perform a desired function or set of functions, and the documentation required to describe and maintain that program or routine.

Activities that are treated as software development generally include:

a. Planning the development of the computer software, including identification and documentation of the software requirements
b. Designing the computer software
c. Building a model of the computer software
d. Writing source code and converting it to machine-readable code
e. Testing the computer software and making necessary modifications to address defects identified during testing, but only up until the point in time that:
    i. The computer software is placed in service
    ii. The computer software is ready for sale or licensing to others
    iii. Production of the product master

NAIC Actions Impacting Statutory Tax Reporting

Notice 2023-63, Guidance on Amortization of Specified Research or Experimental Expenditures under Section 174

Considerations for 2023 Year-End:

a. Status of Proposed Regulations – will likely not be issued until early 2024; determine how 174 capitalization previously determined complies to interim guidance under the Notice
b. Accounting Method Changes – The Treasury and IRS anticipate issuing updating procedures that will address situations in which taxpayers have, prior to the issuance of Notice 2023-63, changed methods of accounting to comply with Section 174 as amended by the Tax Cuts and Jobs Act, but whose treatment of SRE expenditures is not entirely consistent with the Notice
c. Research and Development (R&D) Tax Credit – determine eligibility for the R&D tax credit to lessen financial impact of capitalized R&E costs
    i. Software development or modification
    ii. Enhancements or upgrades to policy admin systems

Fixed Assets – Bonus Depreciation

Bonus depreciation phasing out after December 31, 2022

Placed in service year	Bonus depreciation percentage	
	Qualified property in general	Longer production period property and certain aircraft
2022	100%	100%
2023	80%	100%
2024	60%	80%
2025	40%	60%
2026	20%	40%
2027	None	20%

CECL
CURRENT EXPECTED CREDIT LOSSES
ACCOUNTING STANDARD UPDATE (ASU) 2016-13, FINANCIAL INSTRUMENTS – CREDIT LOSSES

Scope of Financial Assets

- Inclusions
  - Held-to-maturity debt securities
  - Premiums and commissions receivable
  - Reinsurance recoverable

- Exceptions
  - Financial assets measured at fair value through net income.
  - Loans and receivables between entities under <u>common control</u>
    - Including insurance or reinsurance agreements issued to related parties under <u>common control</u> (GAAP based definition)
  - US Treasuries and Federal Agency MBS
  - Available for sale debt securities

Reporting Model

- Must estimate expected future credit losses on financial assets with the reserve carried through an allowance account
- The allowance account will be offset by a charge to net income
- The allowance is a valuation account that nets down the cost basis of the asset on the balance sheet
- The allowance is created when assets are acquired
- Assets with similar risk profiles must be pooled and analyzed collectively to arrive at a lifetime estimated loss
  - Rather than waiting for a specific asset to have probable impairment under the previous incurred loss model

Reporting Model: Asset Pooling

- Similar risk characteristics may include:
  - Credit quality or rating
  - Past due status
  - Asset type, size or term
  - Geographic location
  - Vintage
  - Industry of borrower
  - Effective interest rate

- If a pooled asset ceases to share similar risk characteristics, the asset must be removed from the pool and assessed either with another pool, or separately if no other pool shares similar risk characteristics.

- Risk characteristics must be reviewed each reporting period.

MEASUREMENT - DATA

- Need to obtain or use data on historical information for your asset pools.

- Qualitative and quantitative aspects of the data are required to be considered.

- Use this data in an analysis of credit losses for each pool of assets:
    - Historical Data – usually stating point
    - Characteristics of financial assets
    - Current economic conditions

ESTIMATION METHODS

- Loss Rate Method
  - Calculates the average lifetime rate of loss on a pool of financial assets. Historical write off rates are likely the starting point which can then be adjusted for reasonable and supportable forecasts based on management's assessment of the credit environment for its holdings.
  - Need to obtain historical write off information for holdings like bonds or reinsurance.

- Discounted Cash Flow Method
  - The allowance for credit losses should reflect the difference between the amortized cost basis and the present value of expected cash flows.
    - CECL Reserves = Amortized Cost – Discounted expected value of all future cash flows.
  - Not recommended for pool level or portfolio level analysis.
  - Requires management support of assumptions such as prepayments, timing, adjustments, etc.
  - Investment providers or advisors likely to be heavily relied upon for projection of cash flow on holdings.

CECL Considerations for Common Holdings

- Held-to-maturity debt securities (HTM)
  - Required to pool when similar risk characteristics are present.
  - Asses historical write-off information for pools of assets.
  - Adjust historical information for a reasonable and supportable forecast.

- Premiums receivable
  - Must pool premiums receivable with similar risk characteristics.
  - Credit loss allowance is to be based on the portion of premiums receivable balance that has been earned and the premium that is due from the policy.
  - Receivable associated with unearned premium is not included.

- Reinsurance recoverable
  - Required to pool recoverable with similar risk characteristics.
  - Reinsurers may set aside funds in a trust account and have a right to offset provisions or enter into a letter of credit for the benefit of the ceding insurer. Can use letters of credit in analysis if they are not freestanding.
  - Group your receivables from reinsurers by ratings and asses historical information regarding write-offs.
  - Can consider external and internal history.
  - Ceded UEP does not need to be considered.

- Public entity filings we have looked at typically have small reserves for their HTM and reinsurance receivables due to having high quality investments and reinsures.
  - Chubb

Adoption

- Modified retrospective
  - Determine CECL reserves as of 1/01/2023 and make an adjustment to beginning retained earnings.

- Disclosure
  - Disclose which financial assets are net of an allowance for credit loss and the amount of the reserve.
  - Description of how the reserve is determined for each significant financial asset including any notable assumptions.
  - Roll forward of credit loss showing beginning value, changes, and ending value of the reserve.

Available for Sale Debt Securities (AFS)

- ASU 2016-13 also updated guidance for AFS securities.
- Any holding that has fair value less than amortized cost at the balance sheet date must be considered for credit loss.
- Factors such as credit rating, rate of interest, remaining time to maturity, discussions with advisors, and others can be assessed to determine if the decline is credit related.
- Document support for a conclusion that credit loss is not applicable.
- Discounted cash flows are required to measure the amount of credit loss if credit loss is possible.
- The credit loss reserve is netted on the balance sheet against the amortized cost with the changes in the reserve flowing through the income statement. OCI and AOCI for any changes unrelated to credit loss.
- Modified retrospective approach for adoption.

APPLICABILITY

- CECL is effective for private entities that produce GAAP based reports in 2023.
- CECL does NOT apply to Statutory Accounting Principals (SAP) for 2023.
- In the December 2023 meeting of the Statutory Accounting Principles Working Group, it was exposed to reject CECL.
- Adoption of CECL seems unlikely for SAP.

Poll Question

Are you ready to adopt CECL in 2023?

- ❑ *Yes*
- ❑ *No*
- ❑ *It's not applicable because we do not file GAAP reports*

QUESTIONS?

Thank you!

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