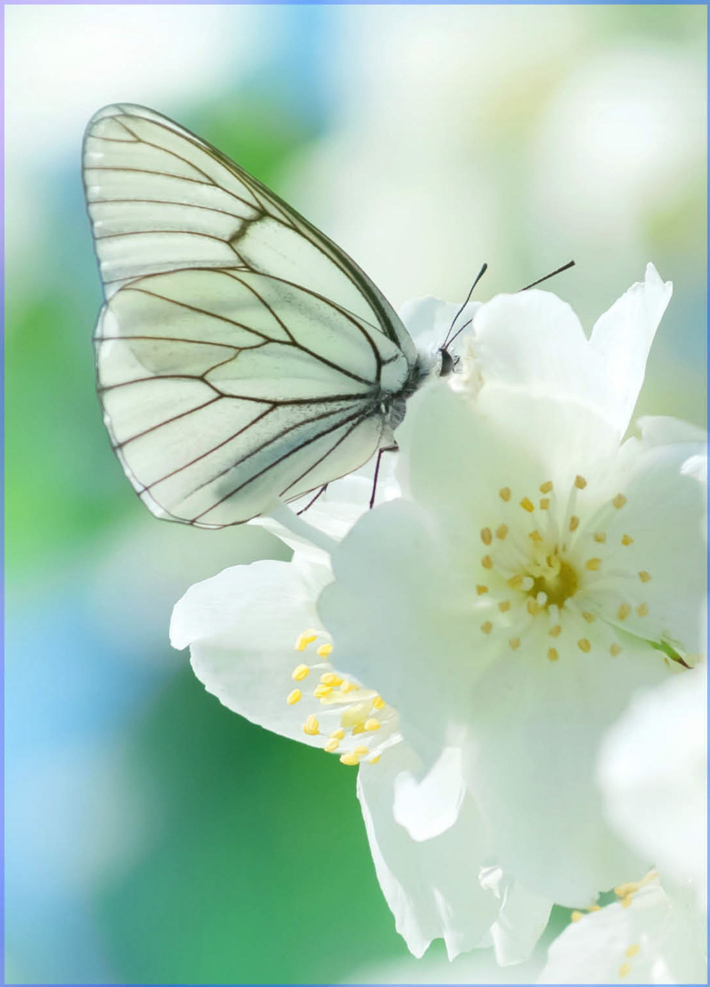
NAIC Spring Meeting

Issues & Trends



Latest actions include exposure of guidance related to negative IMR, tax equity investments and principles-based bond definition.

May 2023

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Contents

1

Meeting highlights

During its Spring meeting and on calls before and after it, the National Association of Insurance Commissioners (NAIC) **adopted** the following guidance.

- SSAP No. 34 to add disclosures for interest income due and accrued and for paid-in-kind (PIK) interest included in the current principal balance.
- Proposal to add a line in the risk-based capital (RBC) calculation to isolate residual tranches reported on Schedule BA and the asset valuation reserve and to add residual tranches to the sensitivity testing exhibits for RBC.

The NAIC **exposed** revisions to the following guidance.

- SSAP No. 21R to clarify that pledged assets must qualify as admitted invested assets for a collateral loan to be admitted.
- SSAP Nos. 21R, 26R, 43R and other affected SSAPs related to the principles-based bond project and a proposal to split Schedule D, Part 1 into two sections.
- INT 23-01 to provide limited-time, optional, statutory accounting guidance that would allow insurers to admit a portion of negative IMR.
- Nullification of INT 03-02 because it is inconsistent with SSAP No. 25 for economic and non-economic related party transactions.

The NAIC **discussed** the following guidance:

- Revisions to SSAP No. 93 to expand current guidance to capture all tax equity investments that qualify under specified criteria and provide general federal business tax credits and state tax credits including state premium tax credit programs.
- Quantitative results for the Economic Scenario Generator field test.
- Amendments to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (PPM) to exclude structured equity and feeder funds from being eligible for the filing exempt process.

Accounting highlights >>	
Conceptual Framework	The Statutory Accounting Principles Working group (SAPWG) reexposed revisions to SSAP No. 5R and its related issue paper to include updates from the FASB conceptual framework to define a liability with modification, deferring to other SSAPs that provide more topic specific contradictory guidance.[1] Comments are due June 9, 2023.
Negative interest maintenance reserve	After the Spring meeting, SAPWG exposed INT 23-01 to provide limited-time, optional, statutory accounting guidance that would allow insurers to admit a portion of negative IMR.[2] Comments are due May 5, 2023.
Collateral loans	SAPWG reexposed revisions to SSAP No. 21R to clarify that pledged assets must qualify as admitted invested assets to be admissible.[3] Comments are due June 9, 2023.
Government assistance	SAPWG exposed revisions to SSAP No. 24 to clarify that even though the general disclosures from ASU 2021-10 were previously adopted, ASU 2021-10 is rejected.[4] Comments are due June 9, 2023.
Affiliated investments	SAPWG adopted revisions to SSAP No. 25 to clarify the definition of an affiliated investment.[5]

1 SSAP No. 5R, Liabilities, Contingencies and Impairments of Assets

2 INT 23-01, 2023 Net Negative (disallowed) Interest Maintenance Reserve

3 SSAP No. 21R, Other Admitted Assets;

4 SSAP No. 24, Discontinued Operations and Unusual or Infrequent items; FASB Accounting Standards Update (ASU) 2021-10 Government Assistance (Topic 832): Disclosures by Business entities about Government Assistance

5 SSAP No. 25, Affiliates and Other Related Parties

Accounting highlights >>	
Principles-based bond definition	SAPWG exposed revisions to SSAP Nos. 21R, 26R, 43R and other affected SSAPs for guidance related to the principles-based bond project.[6] Comments are due June 9, 2023.
Principles-based bond definition – Schedule D reporting	The Blanks Working Group exposed a proposal to split Schedule D, Part 1 into two sections, one to report issuer credit obligations and the other for asset-backed securities. The revisions also update other parts of the Annual Statement that reference the bond lines of business. Comments are due June 30, 2023.
Interest income disclosures	SAPWG adopted revisions to SSAP No. 34 to add disclosures for interest income due and accrued and for PIK interest included in the current principal balance.[7] Revisions are effective for 2023 year-end reporting.
CLO financial modeling	SAPWG exposed revisions to SSAP No. 43R to add collateralized loan obligations (CLOs) to the financial modeling guidance and clarify that CLOs are not included as legacy securities. Comments are due June 9, 2023.
C-2 mortality risk disclosure	SAWPG exposed revisions to SSAP Nos. 51R, 59, and 61R to add detailed disclosures for the net amount at risk to support updates to the life RBC C-2 mortality risk charges.[8] Revisions would be effective for 2023 year-end reporting. Comments are due May 5, 2023.
Derivatives and hedging	SAPWG adopted an issue paper that documents previous adoptions in connection with the review of ASU 2017-12.[9]
New market tax credits and tax equity investments	SAPWG discussed comments on proposed revisions to SSAP No. 93 to expand current guidance to capture all tax equity investments that qualify under specified criteria and provide

6 SSAP No. 26R, Bonds; SSAP No. 43R Loan Backed and Structured Securities

7 SSAP No. 34, Investment income due and accrued

8 SSAP No. 51R, Life Contracts; SSAP No. 59 Credit Life and Accident and Health Insurance Contracts; SSAP No. 61R, Life, Deposit-Type and Accident and Health Reinsurance

9 ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted improvements to Accounting for Hedging Activities

Accounting highlights >>	
	general federal business tax credits and state tax credits including state premium tax credit programs.[10]
Fair value measurement of restricted securities	SAPWG adopted revisions to SSAP No. 100R to adopt, with modification, ASU 2022-03.[11]
Share-based compensation	SAPWG exposed revisions to SSAP No. 104, as well as SSAP Nos. 47 and 95 to adopt, with modification, ASU 2019-08.[12] Comments are due June 9, 2023.
Intercompany pooling	SAPWG reexposed its intent to nullify INT 03-02 because it is inconsistent with SSAP No. 25 for economic and non-economic related party transactions.[13] The nullification would be effective December 31, 2023. Comments are due June 9, 2023.
Reference rate reform	SAPWG exposed revisions to INT 20-01 to extend the expiration date of the guidance to December 31, 2024.[14] Comments are due June 9, 2023.
Corporate alternative minimum tax guidance	After the Spring meeting, SAPWG exposed revisions to INT 22-02 to extend its effective date through second quarter of 2023.[15] The INT provides an exception to insurers from assessing the effects of Corporate Alternative Minimum Tax (CAMT). The INT is proposed to be nullified on July 1, 2023. Comments are due May 5, 2023. SAPWG also directed NAIC staff to continue to work with interested parties on developing

[10] SSAP No. 93, Low-Income Housing Property Tax Credits

[11] SSAP No. 100R, Fair Value; ASU 2022-03 - Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions

[12] SSAP No. 47, Uninsured Plans; SSAP No. 95, Nonmonetary Transactions; SSAP 104, Share Based Payments; 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

[13] INT 03-02, Modification to an Existing Intercompany Pooling Arrangement

[14] INT 20-01, ASU 2020-04 and 2020-01 - Reference Rate Reform

[15] INT 22-022, Third Quarter 2022 through Second Quarter 2023 Reporting of the Inflation Reduction Act - Corporate Alternative Minimum Tax

Accounting highlights >>	
	guidance for the CAMT for periods after the first quarter of 2023.
Accounting guidance in the Annual Statement instructions	SAPWG exposed a proposal to start a project to review the annual and quarterly statement instructions to ensure that all accounting guidance is properly reflected within SSAPs. Comments are due June 9, 2023.
Actuarial highlights >>	
Economic scenario generator – field test results	LATF heard a presentation about the quantitative results of the economic scenario generator from the field test on VM-21 and C-3 Phase II requirements.[16]
Hedge modeling	LATF exposed revisions to hedge modeling language for index credit hedging in VM-21. Comments were due April 12, 2023.
Referrals from Valuations of Securities Task Force	On a call before the Spring meeting, LATF exposed a referral from the Valuation of Securities Task Force (VOSTF) requesting comments about amendments to the definition of structured equity and fund investments. Comments were due March 22, 2023. On a call before the Spring meeting, LATF exposed a referral from VOSTF requesting feedback about the potential for obtaining additional measures of an insurer's investment risk by adding additional modeling capabilities to the NAIC's Securities Valuation Office (SVO). Comments were due April 14, 2023.
Affiliated investments	The Capital Adequacy Task Force adopted revisions to instructions and structure of the RBC calculation for affiliated investments for all lines of business.

[16] VM-21, Requirements for Principle-Based Reserving for Variable Annuities

Risk-based capital >>	
RBC Investment Risk and Evaluation Working Group – collateralized loan obligations	The Risk-Based Capital Investment Risk and Evaluation (RBC IRE) Working Group discussed comments on the Academy's presentation about CLOs.
RBC IRE interim proposal to address arbitrage	The Capital Adequacy Task Force adopted the proposal of the RBC IRE Working Group to add a line in the RBC calculation to isolate residual tranches reported on Schedule BA and the asset valuation reserve and to add residual tranches to the sensitivity testing exhibits for RBC.
Valuation of Securities Task Force >>	
Structured equities and funds	VOSTF discussed proposed amendments to the PPM to exclude structured equity and feeder funds from being eligible for filing exempt process.
Collateralized loan obligation	On a call before the Spring meeting, VOSTF discussed comments received on the NAIC Structured Securities Group (SSG) memorandum about a proposed CLO modeling methodology.
Big data and artificial intelligence >>	
Model and data regulatory questions	The Big Data and Artificial Intelligence (AI) Working Group heard comments about the proposed model and data regulatory questions.

2

Accounting highlights

Conceptual framework

Action. SAPWG reexposed revisions to SSAP No. 5R and its related issue paper to include updates from the FASB conceptual framework to define a liability with modification, deferring to other SSAPs that provide more topic specific contradictory guidance. Comments are due June 9, 2023.

Comprehensive revisions to the definition of a liability would include:

- removing the term ‘probable’ and the phrase ‘in the future as a result of past transactions or events’ in the definition of a liability;
- focusing the primary characteristics of a liability on a present obligation to transfer an economic benefit; and
- clarifying that the guidance only applies if there were no contradictory guidance in other SSAPs.

Negative interest maintenance reserve

Action: After the Spring meeting, SAPWG exposed INT 23-01 to provide limited-time, optional, statutory accounting guidance, that would allow insurers to admit a portion of negative IMR. Comments are due May 5, 2023.

The guidance is a proposed solution for 2023 year-end reporting. It is an exception to the existing guidance in SSAP No. 7 that requires negative IMR to be nonadmitted and includes:

- allowing insurers with an RBC greater than 300% to admit net negative IMR, up to 5% of the insurer’s general account capital and surplus adjusted to exclude any net positive goodwill, EDP equipment and operating system software, net deferred tax assets and admitted net negative IMR;

- limiting admitted negative IMR to IMR generated from losses incurred from the sale of bonds, or other qualifying fixed income investments, that were reported at amortized cost before the sale, and for which the proceeds of the sale were immediately used to acquire bonds, or other qualifying fixed income investments, that will be reported at amortized cost;

- disclosing within the annual and quarterly financial statements:

  - the non-amortized effect on IMR from gains or losses from derivatives that were reported at fair value before their closing, termination, settlement or expiration; and
  - the gross negative IMR, the amounts of negative IMR admitted and nonadmitted, adjusted capital and surplus and the percentage of

adjusted capital and surplus for which the admitted negative IMR represents;

- reporting net negative IMR as a write-in to miscellaneous other-than-invested assets;
- allocating an amount equal to the general account admitted net negative IMR to special surplus;
- prohibiting admitted negative IMR to include losses from derivatives that were reported at fair value before settlement, termination, expiration or closing of the derivative; and
- stating that the admittance of net negative IMR in the general account should not affect the reporting of IMR in the separate account.

At the Spring meeting, SAPWG discussed the treatment of negative IMR, specifically the current nonadmission guidance, based on feedback about adding guardrails to limit the amount of negative IMR that could be admitted.

Interested parties stated that a rising interest rate environment is generally favorable to the financial health of the life insurance industry. However, they expressed concern that without a change to the current treatment of negative IMR, the business environment may give an inappropriate perception of decreased financial strength through lower surplus and RBC ratios.

Interested parties commented on previously discussed guardrails including:

- support for additional demonstrations of reinvestment in fixed income investments, for example by showing that the sum of proceeds from the sale and maturity of bonds and mortgage loans are less than the sum of the cost of acquired bonds and mortgage loans;
- statement that negative IMR should only be allowed if included in asset adequacy testing (AAT);
- concern with:
  - shortening the amortization period because it would obviate one of the main objectives of IMR and introduce practical challenges;
  - limiting negative IMR to a specific percentage of surplus because it would create an arbitrary limit that would penalize strong and weak insurers alike; and
- assertion that the effect of AAT requiring additional reserves is equivalent to restricting surplus available for dividends to stockholders or participating policyowners.

Interested parties proposed two additional guardrails:

- a limit based on the amount of RBC; and
- an opt-in framework with structured governance.

Limiting negative IMR based on the amount of RBC would ensure that negative IMR is admitted only if an insurer's RBC showed that it was financially strong. Interested parties stated that they would work with SAPWG on establishing an appropriate threshold and analyzing what would occur if that threshold was subsequently crossed to ensure there would not be an inappropriate cliff effect.

The opt-in framework could be structured similar to the framework included within SSAP No. 108 that recognizes the prudency of hedging guarantees embedded within variable annuity contracts while also recognizing the non-economic volatility created.[17] This framework could be tailored to include documentation and controls of prudent strategies for investment management, asset liability management, and hedging strategies deemed appropriate and against which future transactions could subsequently be verified as necessary by the insurer's domiciliary regulator.

Some regulators expressed concern over the opt-in framework because it would introduce optionality. SAPWG discussed potential thresholds of capital and surplus that could be used to limit the admission of negative IMR. Some regulators suggested a limit of one percent, while others suggested ten percent, similar to the limit for admissibility of goodwill.

SAPWG directed NAIC staff to work on both an interim solution for 2023 year-end and a long-term solution by:

- drafting a referral to LATF that would:
  - develop a template for reporting within AAT;
  - consider the actual amount of admitted negative IMR that would be used in the AAT;
  - consider cash flows within AAT as well as any liquidity stress test considerations;
  - ensure excessive withdrawals considerations are consistent with actual data; and
  - ensure that any guardrails for assumptions in the AAT are reasonable and consistent with other aspects;
- drafting a referral to the Capital Adequacy Task Force to consider eliminating any admitted net negative IMR from total adjusted capital and consider sensitivity testing with and without negative IMR;
- developing accounting and reporting guidance for 2023 reporting.

After the Spring meeting, the 2023 reporting guidance was exposed in INT 23-01.

Collateral loans

Action. SAPWG reexposed revisions to SSAP No. 21R to clarify that pledged assets must qualify as admitted invested assets to be admissible. Comments are due June 9, 2023.

The revisions would require:

[17] SSAP No. 108, Derivative Hedging Variable Annuity Guarantees

- audited financial statements for collateral in the form of partnerships, LLCs and SCAs in the scope of SSAP Nos. 48 and 97 for collateral loans to be admitted; [18] and

- the use of the proportionate audited equity valuation, and nonadmit the collateral loan in excess of the audited equity valuation of the pledged investments.

Interested parties commented that audits of joint ventures, partnerships, and LLCs:

- while required under SSAP No. 97 and SSAP No. 48 if held directly, are not necessarily suited for assessing the sufficiency of collateral, because an audit does not validate the fair value of the investment, which is a core standard of the collateral guidance; and
- may be unreasonably costly for this narrow purpose.

They also asserted that regulatory concern over arrangements in which the collateral asset or collateral loan may be related to or affiliated with the insurer is addressed by related party reporting that requires a collateral loan involving a related party to be identified as such in the Annual Statement.

Interested parties recommended SAPWG add a footnote to SSAP No. 21 allowing insurers to obtain a fair value assessment from an unrelated third party in place of an audit to record the collateral as an admitted asset.

Some regulators expressed concern with the interested parties' recommendation stating that:

- it is imperative to uphold the existing requirement to obtain an audit of the joint venture, partnership, LLC or subsidiaries, controlled and affiliated entities when held as collateral similarly to the requirement for these investments if held directly to qualify as admitted investments under SSAP Nos 48 and 97; and

- allowing fair value without an audit would lower the collateral requirement standard and allow potential arbitrage with RBC and the admissibility of assets by using a collateral loan as the conduit.

Government assistance

Action. SAPWG exposed revisions to SSAP No. 24 to clarify that even though the general disclosures from ASU 2021-10 were previously adopted, ASU 2021-10 is rejected. Comments are due June 9, 2023.

The proposed revisions are a result of questions received by the NAIC staff about the previously adopted disclosures on government assistance. The primary questions were whether the adoption, with modification, of the disclosures in ASU 2021-10 allowed insurers to use the grant and

[18] SSAP No. 48, Investments in Joint Ventures, Partnerships and Limited Liability Companies; SSAP No. 97, Investments in Subsidiary, Controlled and Affiliated Entities

contribution model to account for government assistance. The proposed revisions clarify that:

- the grant and contributions model is not permitted by rejecting ASU 2021-10; and
- general disclosures about government assistance apply, as previously adopted.

Affiliated investments

Action. SAPWG adopted revisions to SSAP No. 25 to clarify the definition of an affiliated investment.

The revisions clarify that an invested asset held by an insurer that is issued by an affiliated entity, or that includes the obligation of an affiliated entity is an affiliated investment. This change was in response to interested parties' comments to revisions clarifying the application of the existing affiliate definition and new disclosures requirements to be included within the Annual Statement Investment Schedules. Those disclosures required insurers to include a specific designation for investments acquired through, or in, related parties regardless of if they meet the affiliate definition.

Principles-based bond definition

Action. SAPWG exposed revisions to SSAP Nos. 21R, 26R, 43R and other affected SSAPs for guidance related to the principles-based bond project. Comments are due June 9, 2023.

SAPWG responded to comments received from interested parties about previously proposed changes to SSAP Nos. 26R and 21R stating that it made many of the proposed revisions. Revisions to SSAP No. 26R included:

- updating scope to:
  - exclude securities that do not qualify as bonds, including first loss positions that lack contractual payments or substantive credit enhancement; and
  - clarify that replication transactions are addressed in SSAP No. 86 and are not affected by the principles-based bond definition.
- clarifying that the requirement for instruments representing creditor issuer obligation not to vary based on appreciation or depreciation of any underlying collateral value or other non-debt security does not include nominal interest rate adjustments; and
- adding accounting and reporting guidance for first loss positions.

The following revisions were made to both SSAP Nos. 26R and 43R in response to interested parties' comments:

- clarifying that investment assessments are required as of origination and permitting current or acquisition information in determining whether investments qualify at the time of transition; and
- stating that transition guidance would be applied prospectively beginning with the first year of adoption and comparative disclosures would not be required to be restated in the year of adoption.

SAPWG also:

- updated the scope of SSAP No. 43R to exclude residual tranches, interests and first loss positions and to identify that they are captured in SSAP No. 21R and added guidance for residual tranches to SSAP No. 21R;
- stated that securities captured in SSAP No. 21R are reported at lower of amortized cost or fair value with changes in measurement recorded in unrealized gains or losses; and
- proposed changes to reporting lines in Schedule BA to categorize debt securities that do not qualify as bonds under SSAP No. 26R or 43R and are captured in the scope of SSAP No. 21R and to consolidate existing reporting lines.

NAIC staff also recommended further discussion with interested parties about:

- categories for when debt instruments do not meet the principles-based bond definition in SSAP No. 26R as well as the accounting and measurement basis; and
- guidance that limits admittance of debt securities when the source of repayment is derived from the rights to underlying collateral, to the extent that the collateral is an admitted invested asset.

Proposed bond definition – Schedule D reporting

Action. The Blanks Working Group exposed a proposal to split Schedule D, Part 1 into two sections, one to report issuer credit obligations and the other for asset-backed securities. The revisions also update other parts of the Annual Statement that reference the bond lines of business. Comments are due June 30, 2023.

These revisions split Schedule D Part 1 into Schedule D-1-1 for creditor issuer obligations and Schedule D-1-2 for asset backed securities in response to the proposed principles-based bond definition and include more granular categories. The proposal also revises the data elements that would be reported for each category. The categories include:

- for issuer credit obligations in scope of SSAP No. 26R:
  - US Government obligations;
  - Other US Government securities;
  - Non-US sovereign jurisdiction securities;

  - Municipal bonds – general obligation (direct and guaranteed);
  - Municipal Bonds – special revenue;
  - Project finance bonds issued by operating entities;
  - Corporate bonds;
  - Mandatory convertible bonds;
  - Single entity backed obligations;
  - SVO-Identified bond funds – fair value;
  - Bank loans – issues;
  - Bank loans – acquired;
  - Mortgage loans that qualify as SVO-Identified credit tenant loans;
  - Certificates of deposit;
  - Other issuer credit obligations; and
  - Affiliated reporting lines;

- for asset-backed securities in scope of SSAP No. 43R:

  - Financial asset-backed securities – self-liquidating:
    - Agency residential mortgage-backed securities (RMBS) – guaranteed;
    - Agency commercial mortgage-backed securities (CMBS) – guaranteed;
    - Agency RMBS – not guaranteed;
    - Agency CMBS – not guaranteed;
    - Non-agency RMBS;
    - Non-agency CMBS;
    - Non-agency – CLOs, collateralized bond obligation, collateralized debt obligations; and
    - Other financial asset-backed securities – self-liquidating
  - Financial asset-backed securities – not self-liquidating:
    - Equity-backed securities; and
    - Other financial asset-backed – not self-liquidating;
  - Non-financial asset-backed securities (practical expedient):
    - Lease-backed transactions; and
    - Other non-financial asset-backed securities;
  - Non-financial asset-backed securities (full analysis):
    - Lease-backed transactions; and
    - Other non-financial asset-backed securities; and
  - Affiliated reporting lines.

Interest income disclosure

Action. SAPWG adopted revisions to SSAP No. 34 to add disclosures for interest income due and accrued and for PIK interest included in the current principal balance. Revisions are effective for 2023 year-end reporting.

The revisions require disclosure of:

- the gross, nonadmitted and admitted amounts for interest income due and accrued;
- the aggregate deferred interest; and
- the cumulative amounts of PIK interest included in the current principal balance.

Interested parties requested that these revisions have the same effective date as the revised SSAP Nos. 26R and 43R because these revisions are a result of the principles-based bond project. The Working Group acknowledged interested parties' comments but stated that this project is separate from the principles-based bond project and an effective date of 2023 is appropriate.

CLO financial modeling

Action. SAPWG exposed revisions to SSAP No. 43R to add CLOs to the financial modeling guidance and clarify that CLOs are not included as legacy securities. Comments are due June 9, 2023.

The proposed revisions are in response to changes adopted by VOSTF on February 21, 2023, to include CLOs in the SVO financial modeling process.

C-2 mortality risk disclosure

Action. SAWPG exposed revisions to SSAP Nos. 51R, 59, and 61R to add detailed disclosures for the net amount at risk to support updates to the life RBC C-2 mortality risk charges. Revisions would be effective for 2023 year-end reporting. Comments are due May 5, 2023.

The revisions would create a direct link from the financial statements to Life RBC C-2 morality risk charges and would require insurers to disclose for life and credit life insurance the net amount at risk by product characteristics for the following components:

- gross of reinsurance;
- assumed reinsurance;
- ceded reinsurance; and
- amount net of reinsurance amounts.

For individual and industrial life, the categories are based on contract type depending on the degree of pricing flexibility.

For group and individual credit life, the categories are based on the remaining length of the premium rate term by group contract and the degree of pricing flexibility.

The amounts are intended for data capture using the tables and detail line references in the Annual Statement.

Derivatives and hedging

Action. SAPWG adopted an issue paper that documents previous adoptions in connection with its review of ASU 2017-12.

The issue paper documents historical discussions, considerations, and changes made as a result of ASU 2017-12, including:

- documentation and initial assessment of hedge effectiveness;
- determination of hedge effectiveness and measurement of excluded components; and
- application of portfolio layer method and partial-term fair value hedges.

New market tax credit and tax equity investments

SAPWG discussed comments on proposed revisions to SSAP No. 93 to expand current guidance to capture all tax equity investments that qualify under specified criteria and provide general federal business tax credits and state tax credits, including state premium tax credit programs.

Interested parties agreed with:

- having uniform accounting and reporting for equity investments when the return is earned primarily through tax credits; and
- applying proportional amortization method to any type of investment where the return is primarily earned through tax credits.

They also:

- requested SAPWG to consider allowing the amortization of investments and the use of tax credits to be reported in the same income statement line, similar to US GAAP;
- expressed concerns about tax credit investments that are issued in debt form being reporting on Schedule BA, instead of Schedule D.

SAPWG stated that:

- reporting the amortization of investments and the use of tax credits in a single line was previously considered when the presentation in US GAAP was considered;
- the current reporting of amortizing the investment as a component of net investment income or expense and recognizing tax credits used as reduction in the related tax expense was intentional; and
- it will consider changing the current reporting as part of the proposal.

It also expressed its view that tax credit investments should be reported on Schedule BA and not Schedule D.

Next Steps: SAPWG directed NAIC staff to draft revisions to SSAP Nos. 93 and 94 as well as its related issue paper.[19] The proposed guidance would address the tax credits from the New Market Tax Credit Program as well as other qualifying tax equity investments.[20] SAPWG will consider the

[19] SSAP No. 94, Transferable and Non-Transferable State Tax Credits

[20] The New Market Tax Credits Program was established by Congress in December 2000 and permits individual and corporate taxpayers to receive a non-refundable tax credit against federal income taxes for making equity investments in financial intermediaries known as Community Development Entities.

proposed FASB guidance as well as admittance and impairment provisions, recognizing that tax credits cannot be used to provide direct payment to policyholders, but rather are meant to affect a reporting entity's tax liability.

Fair value measurement of restricted securities

Action. SAPWG adopted revisions to SSAP No. 100R to adopt, with modification, ASU 2022-03.

The adopted revisions add guidance for equity securities subject to contractual sale restrictions including:

- the effect on a fair value measurement arising from a restriction on the sale or use of an asset by an insurer will be different depending on whether the restriction will be taken into account by market participants when pricing the asset;
- an equity security that an insurer cannot sell on the measurement date because of a contractual sale restriction will be measured at fair value on the basis of the price in the principal (or most advantageous) market. A contractual sale restriction is not a characteristic of the equity security and is not considered in measuring the fair value of an equity security;
- an equity security with sale restrictions will be considered a restricted equity security and subject to admissibility guidance in SSAP No. 4;[21] and
- insurers will disclose the fair value of equity securities subject to contractual sale restrictions.

Share-based compensation

Action. SAPWG exposed revisions to SSAP No. 104R as well as SSAP Nos. 47 and 95 to adopt, with modification ASU 2019-08. Comments are due June 9, 2023.

Proposed revisions:

- revise the scope of SSAP No.104R to include share-based considerations payable to customers;
- add language to SSAP No.95 to include share-based consideration payable to customers; and
- update the relevant literature of SSAP No. 47 to include the Topic 606 guidance included in ASU 2019-08.[22]

[21] SSAP No. 4, Assets and Nonadmitted Assets

[22] ASC 606, Revenue from Contracts with Customers

Intercompany pooling

Action. SAPWG reexposed its intent to nullify INT 03-02, because it is inconsistent with SSAP No. 25 for economic and non-economic related party transactions. The nullification would be effective December 31, 2023. Comments are due June 9, 2023.

Interested parties commented that INT 03-02 provides a reasonable approach for accounting for intercompany pooling modifications and provides consistency in reporting across insurers. They continued to believe that this INT should not be nullified and stated that nullification could result in inconsistency in accounting.

SAPWG acknowledged interested parties' concerns but maintained that the INT should be nullified, observing that it:

- is inconsistent with SSAP No. 25 guidance about economic and non-economic transactions between related parties; and
- can result in unrecognized dividends (in effect) or losses when using bonds to pay affiliates for modifications to intercompany reinsurance pooling agreements.

SAPWG also stated that treatment of asset transfers between affiliates should be consistent for all intercompany transactions. It requested that interested parties provide specific scenarios that would create inconsistencies and suggest amendments to SSAP No. 62R to prevent them.[23]

Reference rate reform

Action. SAPWG exposed revisions to INT 20-01 to extend the expiration date of the guidance to December 31, 2024. Comments are due June 9, 2023.

INT 20-01 applies to all SSAPs with contracts within the scope of ASU 2020-04, including:[24]

- debt and service agreements under SSAP No. 15 that require reversal and rebooking of the liability as a result of the reference rate reform;[25]
- lease modifications solely caused by the reference rate reform and those eligible for optional expedients under SSAP No. 22R;[26] and
- certain derivative transactions.

The scope of INT 20-01 also includes ASU 2021-01 and allows insurers to apply an optional transitional expedient to derivative instruments modified to change the reference rate used for margining, discounting or contract price

23 SSAP No. 62R, Property and Casualty Reinsurance

24 ASU 2020-04 – Reference Rate Reform

25 SSAP No. 15, Debt and Holding Company Obligations;

26 SSAP No. 22R Leases

alignment resulting from reference rate reform regardless of whether the reference rate is expected to be discontinued.[27] These modifications would not be considered a change in the critical terms requiring dedesignation of the hedging relationship.

Corporate alternative minimum tax guidance

Action. After the Spring meeting, SAPWG exposed revisions to INT 22-02 to extend the effective date through second quarter of 2023. The INT provides an exception to insurers from assessing the effects of CAMT. The INT is proposed to be nullified on July 1, 2023. Comments are due May 5, 2023.

At the Spring meeting, SAPWG stated that the CAMT presents several accounting challenges, and input will be needed on certain decision points including:

- estimating future applicable financial statement income for a group of companies that is not the issuer;
- determining the future period when the CAMT credit can be used;
- evaluating the effect of tax sharing agreements and allocation of the CAMT liability;
- determining the effect of the CAMT deferred tax assets (DTA) in the statutory valuation allowance; and
- accounting for CMAT DTAs in the overall DTA admissibility calculation.

SAPWG will also consider whether to maintain an RBC threshold for the SSAP No. 101, paragraph 11b admissibility test and the overall extent of admissibility of the CAMT DTAs.[28]

The Inflation Reduction Act (IRA) was enacted on August 16, 2022 and included a new CAMT. The IRA, including the CAMT, are effective for tax years beginning after 2022.

Next Step. SAPWG directed NAIC staff to continue to work with interested parties on developing guidance for the CAMT for periods after the expiration of INT 22-02.

Accounting guidance in the Annual Statement instructions

Action. SAPWG exposed a proposal to start a project to review the annual and quarterly statement instructions to ensure that all accounting guidance is properly reflected within SSAPs. Comments are due June 9, 2023.

Annual and quarterly instructions may duplicate or reference accounting guidance, but they are not intended to be a source of accounting guidance.

[27] ASU 2021-01, Reference Rate Reform (topic 848): Scope

[28] SSAP No. 101, Income Taxes

NAIC staff stated that it identified some situations where the instructions provide more detailed accounting guidance than SSAPs. The project will review the instructions to identify any areas where accounting guidance may need to be captured.

3

Actuarial highlights

Non-variable annuities

The VM-22 Subgroup updated LATF on the work that has been done and project plan to completion including key issues and milestone dates.

The Subgroup is targeting a field test in mid-2024 with a proposed earliest effective date of January 1, 2026 with a three year implementation. All insurers would be required to implement VM-22 beginning January 1, 2029. However, this timing is dependent on the work being performed over the economic scenario generator, which needs to be completed before the VM-22 field test. The Subgroup stated that field testing an economic scenario generator materially different than the one ultimately adopted could lead to results different than future reserve levels.

The Subgroup is in the process of reviewing comments received from the last exposure. It highlighted the key issues that have been preliminary identified including:

- aggregating annuities by payout, accumulation or longevity reinsurance reserving categories;
- treating index credit programs differently;
- including an exclusion test allowing insurers that pass the option to use pre-PBR methodology; and
- having a PBR exemption allowing insurers below a certain volume of business to not follow PBR requirements.

On a call before the Spring meeting, the Subgroup discussed thresholds for the PBR exemption that would be based on prior year-end information. It considered exempting insurers having statutory reserves of either greater than one billion or three billion. The Subgroup also discussed whether the exemption would be gross or net of reinsurance. A large majority of the Subgroup voted to exempt insurers with reserves of less than one billion, gross of reinsurance.

On future calls the Subgroup will continue to work on:

- longevity reinsurance, specifically a ‘k-factor’ methodology similar to CRVM;
- an exclusion test carveout for payout annuities; and
- the standard projection amount mechanics.

VM-22 issues that have not yet been resolved include:

- whether the current VM-20/VM-21 proposal from the American Academy of Actuaries (Academy), or a different approach should be used for a reinvestment guardrail;
- the passing level for the stochastic exclusion ratio text;
- the level of minimum index credit hedge margin; and
- whether the standard projection amount should be the minimum reserve floor or disclosure-only.

Economic scenario generator – field test results

LATF heard a presentation about quantitative results of the economic scenario generator from the field test on VM-21 and C-3 Phase II requirements.

The presentation summarized quantitative information to:

- understand the effect on reserves and capital;
- evaluate the effect of hedging programs across field test scenario sets;
- review the range of results across field test participants;
- compare the stability of results over time; and
- inform regulator decision-making on model and calibration choices.

The results presented data from 26 legal entities and included:

- data from two baseline scenarios, one using scenario sets(s) the insurer used for December 31, 2021 statutory reporting and the other modified to use sets with a December 31, 2019 yield curve using a 200 basis points increase across all maturities (Baseline #1 and Baseline #2);
- GEMS baseline equity and corporate model scenarios as of December 31, 2021 and Conning treasury model calibration with generalized fractional floor as of December 31, 2021 (Test 1a) and same test with alternative treasury model calibration with shadow floor as of December 31, 2021 (Test 1b);
- same as Test 1a, but with equity, corporate, and treasury models with a December 31, 2019 starting yield curve modified using a 200 basis point increase across all maturities (Test 2a) and same test with alternative treasury model calibration with shadow floor instead of conning treasury model calibration with generalized fractional floor (Test 2b);
- same as Test 1a, but with Conning's original equity model calibration that had significantly lower gross wealth factor's than the Academy Interest Rate Generator equity model (Test 5a) and same test using December 31, 2019 starting yield curve modified using a 200 basis point increase across all maturities; and

- same as Test 1a but with the American Council for Life Insurer's GEMS equity calibrations.

The results showed that for all of the tests, on average, both reserves and required capital increased, however some participants showed decreases. It was not apparent why some showed decreases, but such decreases were not typical or prevalent. Most participants saw an increase in reserves and required capital results. The increases to capital were a lot more substantial than the increase in reserves.

The largest increase in reserves and capital were from Test 5a and the smallest increases from Test 6. The NAIC staff stated that:

- for every field test run, there was a large range in the reserve and capital effects across participants; and
- some insurers commented that guaranteed benefits were out-of-the money due to the economic environment (favorable stock market), and that field test effects would have been larger if a less favorable environment had been tested.

Next steps: The NAIC staff will present economic scenario generator field test results for VM-20 and C3 Phase I in one to two months after the Spring meeting. LATF will also work with the Academy and interested parties to decide on stylized facts and acceptance criteria before recalibration of the economic scenario generator and a second field test.

Hedge modeling

Action. LATF exposed revisions to hedge modeling language for index credit hedging in VM-21. Comments were due April 12, 2023.

The revisions were proposed by interested parties who stated that:

- index credit hedging is fundamentally different than the dynamic guaranteed minimum benefit (GMxB) that formed concepts supporting VM-21;
- for GMxB contracts, features drive hedging, whereas for indexed products, including registered indexed-linked annuities hedging drives contract features.

The proposal:

- aims to align the index crediting guidance in VM-21 with the draft of VM-22 with some suggestions for technical improvements; and
- adds new definitions for index credit hedge margin, index credit and index crediting strategies.

The proposal also includes a requirement for the index credit hedge margin to be reflected in both best efforts and adjusted runs by reducing the index interest credit hedge payoff by a margin multiple that is adjusted by sufficient and credible insurer experience and accounts for a model error that is no less than one percent multiplicatively of the interest credit. If the insurer does not have sufficient and credible experience, the revisions propose that a 20 percent multiplier be assumed.

Referrals from Valuation of Securities Task Force

Action. On a call before the Spring meeting, LATF exposed a referral from VOSTF requesting comments about amendments to the definition of structured equity and fund investments. Comments were due March 22, 2023.

The proposal would amend the definition in the PPM and will exclude these investments from filling exempt eligibility. The NAIC staff stated that this proposal is looking at assessing a risk designation more consistent with the underlying risk of the investment.

Action. On a call before the Spring meeting, LATF exposed a referral from VOSTF requesting feedback about the potential for obtaining additional measures of insurer's investment risk by adding additional modeling capabilities to the SVO. Comments were due April 14, 2023.

The referral requested responses about the following:

- whether LATF is supportive of creating this capability within the SVO;
- a list of the investment analytical measures and projections that would be most helpful to support LATF's work;
- a description of how the data would be used and why it would be of value;
- other investment data or projection capabilities that would be useful to LATF that could be provided by commercially available data sources or investment models; and
- other thoughts on this initiative.

4 Risk-based capital

Affiliated investments

Action. The Capital Adequacy Task Force adopted revisions to instructions and structure of the RBC calculation for affiliated investments for all lines of business.

The goal of the revisions is to improve the RBC formulas and provide consistency to the treatment of affiliates for all lines of business. Insurers will now be required to calculate RBC using more a granular listing of affiliated investment types.

RBC Investment Risk and Evaluation Working Group – collateralized loan obligations

On a call before the Spring meeting, the RBC IRE Working Group (Working Group) discussed comments on the Academy's presentation about CLOs. The Academy stated that it has been investigating CLOs to understand the risk they pose to life insurers' statutory capital and considerations for establishing capital requirements.

The Academy stated the intersection of CLOs and RBC creates a unique challenge for modelling credit risk. It asked for regulatory guidance to move forward with the project, including:

- how the statistical safety levels should be measured, suggesting that a conditional tail expectation (CTE) type of measure would be more appropriate due to the cliff risk embedded in CLOs;
- where to set the statistical safety level; and
- whether the Working Group believes no RBC arbitrage principle should be applied to the C-1 factor methodology.

The Working Group commented that it prefers a CTE type measure but is looking to the Academy to provide a recommendation on the statistical safety level. One regulator expressed concern with using just historical information and that modelling of potential market situations would be more appropriate. The Working Group also stated that the question about arbitrage would be more appropriate for their parent committee, the Capital Adequacy Task Force.

Interested parties commented there needs to be a data driven solution for the model used for the update of the bond factors to allow RBC to be calculated in the same manner for all securities.

At the Spring meeting, the Academy reported that it is continuing to develop a model for CLOs. Specifically, it is in the process of developing a specification document and trying to answer questions asked on the call before the Spring meeting. It stated there appears to be different definitions of arbitrage and it is working on a document about RBC arbitrage to be released at a later date.

RBC IRE interim proposals – residual tranches

Action. On a call after the Spring meeting, the Capital Adequacy Task Force adopted the proposal of the RBC IRE Working Group to add a line in the RBC calculation to isolate residual tranches reported on Schedule BA and the asset valuation reserve and to add residual tranches to the sensitivity testing exhibits for RBC.

At the Spring meeting, the RBC IRE Working discussed the approach for residual tranches, which includes all asset backed securities. Some regulators questioned whether an interim solution that would apply a higher RBC charge to all residual tranches is needed. They suggested that such determination be made based on the population of securities making up the residual tranches, specifically the magnitude of that population. However, other regulators stated that work on the interim solution is consistent with the charge received from the Financial Condition Committee. The Working Group stated that it will have a regulator-only call to discuss the population of residual tranches based on 2022 Annual Statement filings to determine whether a response to the Financial Condition Committee request for an interim solution is needed. In the interim, the Working Group decided to proceed with structural changes for the interim solution.

Interested parties commented on the proposal. Some stated that although a quantitative analysis is needed to determine a final factor, an interim solution with one RBC charge of 45% is appropriate because residual tranches are highly leveraged to the underlying, typically high yield collateral, and that is not the same risk as holding an S&P 500 security. However, other interested parties questioned if an interim solution is needed due to the materiality of the residual tranches but agreed a long-term solution should be developed. They requested that this solution be data driven to support the model used with an expert engaged along with industry to perform field testing. Some interested parties also suggested that sensitivity testing be used to provide what-if scenarios that can identify individual insurers that may have a high concentration of risk.

On a call after the Spring meeting, the RBC IRE Working Group also discussed adding a line item for residual tranches to the sensitivity testing exhibits for RBC. The updated sensitivity testing could be an additional tool to assist regulators in reviewing insurers' investments in residual tranches. However, some regulators stated that this sensitivity test is not needed or may not be as useful if a separate factor charge for residual tranches is added.

The RBC IRE Working Group previously considered having three designation categories with RBC factors of 30%, 75% and 100% to eliminate RBC arbitrage and potential financial solvency risk. The proposal asserted that the aggregate risk of owning all the underlying corporate loans held in a CLO structure should be the same as owning all of the CLO's tranches resulting in an equivalent RBC effect on both, if it is free from any

RBC arbitrage. It also identified that there is a regulatory issue with the insurer’s ability to potentially materially reduce C-1 capital requirements by securitizing a pool of assets into a CLO.

5 Valuation of Securities Task Force

Structured equities and funds

VOSTF discussed proposed amendments to the PPM to exclude structured equity and feeder funds from being eligible for filing exempt process. The prosed revisions would not change how the investments are classified for reporting by the insurer, but it would ensure that the NAIC designation and category assigned are appropriate for the risk and eliminate RBC arbitrage. The amendments were a result of SVO's concerns with investments in notes issued by, and of equity or limited partnership interests in, a special purpose vehicle, trust, LLC, limited partnership or other legal entity that operates as a feeder fund which itself invests, directly or indirectly, in one or more funds or other equity investments. The SVO's concerns included that these structures may be:

- circumventing regulatory guidance because they introduce an intervening entity as debt issuer resulting in an investment that is in substance an equity investment being treated as a bond;
- receiving an inappropriate rating by relying on credit rating provider ratings that would not be permitted for the fund or equity investments which underly these notes;
- receiving better RBC treatment than what would be received if the investment had been directly reported;
- allowing insurers to exceed investments permitted under state investments law for certain asset classes because structures would permit insurers to hold more underlying equity or fund investments; and
- introducing a lack of transparency due to their complex nature.

Interested parties' expressed concern over the proposal. Their comments included that:

- the ongoing project in the RBC IRE Working Group to determine the appropriate RBC charge for residual tranches of structured investments and the SAPWG principles-based bond definition project would address these regulatory concerns;
- the proposed revision would potentially capture traditional fixed income securities not intended to be in the scope and could be difficult for the SVO to evaluate; and there is a lack of transparency of SVO methodologies and related consistency in designation for similar risk.

Interested parties also commented on the specific examples of structures sited by SVO and how they can be addressed. One interested party also stated that these structures were intended to create a more operationally efficient way for insurers to access certain asset classes. It expressed a view that an unintended consequence may be that lack of these structures could make smaller insurers less competitive.

Next Steps: VOSTF supported having transparency in the process and directed NAIC staff to draft an amendment outlining recommended procedural steps for reviewing filing exempt investment securities for which there are concerns about the assigned NAIC designation. The amendment would also include the steps insurers could take to clarify and rebut the SVO's concerns about the proposed NAIC designation.

Collateralized loan obligations

On a call before the Spring meeting, VOSTF discussed comments received on the SSG memorandum about a proposed CLO modeling methodology. The NAIC staff stated that the SSG is not trying to build a new issue platform, rather a surveillance process, for which there are adequate resources. Similar to the RMBS and CMBS process, SSG does not expect to analyze any new issues. The NAIC staff stated that the main issues from the comment process were prepayments and reinvestments. Although prepayments are not material, they influence two other assumptions in modeling, having the use of principal to pay overcollateralization tests, and the par building process that is sometimes assumed.

The issue around prepayments is around reinvestment. Prepayments allow principal proceeds, which can be reinvested, and if reinvested at a below par price, can create par build-up, which can offset losses in the modelling. VOSTF formed an ad-hoc group to clarify and resolve technical and modelling issues.

At the Spring meeting, VOSTF received an update on the goals and operations of the ad-hoc group working on the CLO modeling project.

Based on interested parties' comments, the ad-hoc group will:

- focus on the pre-payment and discount dynamic to demonstrate the quantitative impact of the proposals on tranche losses; and
- validate the cash flows on 'dummy' scenarios to ensure the methodology is adequately specified.

6 Big data and artificial intelligence

Model and data regulatory questions

The Big Data and AI Working Group heard comments about the proposed Model and Data Regulatory Questions. The Working Group stated that these questions were considered a starting point for discussion and focus on what regulators can ask about data and models used by insurers, including internally developed and third-party models. The questions are separated into three sections:

- main general questions;
- detailed technical questions; and
- definitions.

The first two sections are further sub-divided into questions to insurers:

- about their own models;
- about the use of third-party models; and
- about third-party data purchases.

The Working Group received comments from eight interested parties and the chair summarized policy issues that were identified during the comment period, including:

- using a principles-based approach;
- limiting the scope to higher risk AI models to encourage regulator use;
- prioritizing questions to recognize the importance of model governance;
- aligning information requests with existing state laws;
- avoiding redundancy with state examinations;
- scaling to prevent over burdening smaller insurer's;
- clarifying the intended use of the questions; and
- revising the definitions section to include terminology used throughout the questions and to be consistent across NAIC work steams.

Interested parties appreciated the Working Group's acknowledgement of the comments and that further work will be performed to revise the document. They provided additional comments, including a request that the Working Group:

- consider how confidential information will be treated and how much information is needed because third-party vendors may restrict access to proprietary information;
- focus on analyzing model outcomes, and require insurers to test for unfair discrimination rather than focus on model development;
- take a risk-based approach to regulatory oversight that identifies principles and expectations for AI governance, testing, and monitoring for both internally developed and third-party technology; and
- direct a limited number of questions to specific use cases and differentiate between high-risk and low-risk models to avoid unnecessary barriers to innovation.

Next Steps: The Working Group will review all comments received on the Model and Data Regulatory Questions and will reexpose a draft by the end of May.

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