NAIC Summer Meeting

Issues & Trends

Latest actions include adoption of guidance related to principles-based bond definition, negative interest maintenance reserve, risk-based capital factor for residual tranches and exposure of the guidance on how to assess corporate alternative minimum tax.

September 2023

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Meeting highlights

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

- Revisions to SSAP Nos. 26R, 43R and other SSAPs to add guidance for the principles-based bond definition.
- INT 23-01 to provide optional, temporary guidance for negative (disallowed) interest maintenance reserve (IMR).
- A risk-based capital (RBC) factor for residual tranches reported on Schedule BA.

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 admissible.
- SSAP Nos. 43R and 48 to clarify the scope and reporting of residual interests and residual security tranches.
- Nullification of INT 03-02 because it is inconsistent with SSAP No. 25 for economic and non-economic related party transactions.
- INT 23-02 to provide guidance on how insurers will assess the corporate alternative minimum tax (CAMT) for the third quarter 2023.
- INT 23-03 to provide guidance on assessing the effects of CAMT for periods on or after the 2023 year-end.
- A framework for the regulation of insurer' investments.

The NAIC **discussed** the following guidance:

- Initial observations from filings submitted under Actuarial Guideline 53 adopted in 2022.
- Quantitative results of the economic scenario generator from the field test on C-3 Phase I requirements.
- Proposal to update the definition of an NAIC designation in the Purposes and Procedures Manual (PPM).
- Process for challenging the NAIC designations assigned through the filing exempt (FE) process when the Securities Valuation Office (SVO) determines the Credit Rating Provider (CRP) rating does not represent a reasonable assessment of risk for regulatory purposes.

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Accounting highlights >>	
Short-term investments	The Statutory Accounting Principles Working Group (SAWPG) exposed revisions to SSAP No. 2R to restrict the investments reported as cash equivalents or short-term investment, effective January 1, 2025.[1] Comments are due September 29, 2023.
Conceptual framework	SAPWG adopted revisions to SSAP No. 5R and its related issue paper to include updates from the FASB conceptual framework, with a modification, to define a liability, deferring to other SSAPs that provide more topic specific contradictory guidance.[2]
Asset valuation reserve and interest maintenance reserve	SAPWG exposed a proposal for a long-term project to include additional accounting guidance for the asset valuation reserve (AVR) and IMR into SSAP No. 7.[3] Comments are due September 29, 2023.
Interest maintenance reserve	SAWPG exposed revisions to the Annual Statement instructions to remove guidance that permits the allocation of non-interest related losses to IMR. Comments are due September 29, 2023.
Negative interest maintenance reserve	SAPWG adopted INT 23-01 to provide optional, temporary guidance for negative (disallowed) IMR.[4] The INT is effective through December 31, 2025, and will be automatically nullified on January 1, 2026, but could be nullified earlier or extended based on SAPWG's actions to establish long-term guidance on negative (disallowed) IMR.
Collateral loans	SAPWG reexposed revisions to SSAP No. 21R to clarify that pledged assets must qualify as admitted invested assets for a collateral loan to be admissible.[5] Comments were due September 12, 2023.

[1] SSAP No. 2R, Cash, Cash Equivalents, Drafts and Short-Term Investments

[2] SSAP No. 5R, Liabilities, Contingencies and Impairments of Assets; Issue Paper No. 168 – Updates to the Definition of a Liability

[3] SSAP No. 7, Asset Valuation Reserves and Interest Maintenance Reserves

[4] INT 23-01, Net Negative (Disallowed) Interest Maintenance Reserve

[5] SSAP No. 21R, Other Admitted Assets

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Accounting highlights >>	
Government assistance	SAPWG adopted 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.[6]
Principles-based bond definition	SAPWG adopted revisions to SSAP Nos. 26R, 43R and other SSAPs to add guidance for the principles-based bond definition, effective January 1, 2025.[7] SAPWG exposed revisions to SSAP 21R to provide guidance for the accounting for debt securities that do not qualify as bonds and to propose measurement guidance for residual tranches, interests and first loss positions. Comments are due September 29, 2023. SAPWG directed NAIC staff to sponsor a blanks proposal to revise Schedule BA under the bond project for debt securities that do not qualify as bonds.
Principles-based bond definition – Schedule D reporting	On a call before the Summer meeting, the Blanks Working Group reexposed revisions to Schedule D, Part 1 splitting it 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 October 12, 2023.
Paid-in-kind interest disclosures	SAPWG adopted revisions to SSAP No. 34 to further clarify disclosures and incorporate a practical expedient for the paid-in-kind (PIK) interest aggregate disclosures.[8]
Financial modeling for collateral loan obligations	SAPWG adopted revisions to SSAP No. 43R to add collateral loan obligations (CLOs) to the financial modeling guidance and clarify that CLOs are not included as legacy securities.
Residual interests	SAPWG reexposed revisions to SSAP Nos. 43R and 48 to clarify the scope and reporting of residual interests and residual security tranches.[9] Comments were due September 12, 2023.

[6] SSAP No. 24, Discontinued Operations and Unusual or Infrequent Items; ASU 2021-10, Government Assistance

[7] SSAP No. 26R, Bonds; SSAP No, 43R, Asset-Backed Securities

[8] SSAP No. 34, Investment Income Due and Accrued

[9] SSAP No. 48, Joint Ventures, Partnerships, and Limited Liability Companies

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Accounting highlights >>	
Actuarial Guideline 51	SAPWG exposed revisions to SSAP No. 54R to clarify that gross premium valuation under Appendix A-010 and cash flow testing under Actuarial Guideline 51 (AG 51) are both required.[10] Comments are due September 29, 2023.
Schedule BA reporting categories	SAPWG exposed a request for comments on a proposal to further define and provide examples of investments that are reported by type of investment on Schedule BA based on underlying characteristics of the assets. Comments are due September 29, 2023.
New market tax credits and tax equity investments	SAPWG reexposed revisions to SSAP No. 93 to update guidance for tax credit investments and clarify the scope of SSAP No. 94.[11] The proposed effective date is December 31, 2024. Comments are due September 29, 2023.
Share-based compensation	SAPWG adopted revisions to SSAP No. 104R as well as SSAP Nos. 47 and 95 to adopt, with modification, ASU 2019-08.[12]
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] Comments are due September 29, 2023.
CAMT guidance	SAPWG exposed INT 23-03 to provide guidance on assessing the effects of CAMT for periods on or after the 2023 year-end.[14] Comments were due September 12, 2023.

[10] SSAP No. 54R, Individual and Group Accident and Health Contracts; Appendix A-010, Minimum Reserve Standards for Individual and Group Accident and Health Insurance Contracts; Actuarial Guideline 51, The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves.

[11] SSAP No. 93, Investments in Tax Credit Structures; SSAP No. 94R, State and Federal Tax Credits

[12] SSAP No. 47, Uninsured Plans; SSAP No. 95, Nonmonetary Transactions; SSAP 104R, Share-Based Payments; ASU 2019-08, Codification Improvements to Topic 718 and Topic 606

[13] SSAP No. 25, Affiliates and Other Related Parties; INT 03-02, Modifications to an Existing Intercompany Pooling Arrangement

[14] INT 23-03, Inflation Reduction Act – Corporate Alternative Minimum Tax

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Accounting highlights >>	
Accounting guidance in the Annual Statement instructions	SAPWG discussed a proposal to start a project to review the annual and quarterly statement instructions to ensure that all accounting guidance is reflected within SSAPs.
Actuarial highlights >>	
Non-variable annuities	On a call before the Summer meeting, the VM-22 Subgroup exposed a draft of the structure and methodology of the standard projection amount requirements.[15] Comments were due July 29, 2023.
Modeling of complex assets – insurer filings	The Life Actuarial Task Force (LATF) discussed initial observations from filings submitted under Actuarial Guideline 53 (AG 53) that was adopted in 2022.[16] Life insurers in the scope of AG 53 are required to disclose asset related information. The first submission was due April 2023.
Economic scenario generator – field test results	LATF heard a presentation about the quantitative results of the economic scenario generator from the field test on C-3 Phase I requirements.
Hedge modeling	On a call before the Summer meeting, LATF adopted revisions to hedge modeling language for index credit hedging in VM-21.[17]
IMR template	On a call before the Spring meeting, LATF exposed a template to gather information about how insurers report IMR. Comments were due July 28, 2023.
Risk-based capital >>	
Residual tranches	On a call before the Summer meeting, the Risk-Based Capital Investment Risk and Evaluation (RBC IRE) Working Group adopted a proposal for a new RBC factor for residual tranches reported on Schedule BA. This proposal was also adopted by all of Working Group’s parent committees.

[15] VM-22, Statutory Maximum Valuation Interest Rates for Income Annuities

[16] Actuarial Guideline 53, Application of the Valuation Manual for Testing the Adequacy of Life Insurer Reserves

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

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Risk-based capital >>	
Structured securities	The RBC IRE Working Group heard a presentation from the Academy about proposed principles for RBC for structured securities. These principles included criteria for when an asset class would require a new model and if the securities within an asset class should be modeled individually to determine their C-1 factors.
Repurchase agreements	The Life RBC Working Group exposed a proposal to align the RBC charge for repurchase agreements, currently at 1.26%, with the 0.20% charge for conforming securities lending programs. Comments are due September 29, 2023.
Valuation of Securities Task Force >>	
NAIC designation definition	Before the Summer meeting, the Valuation of Securities Task Force (VOSTF) discussed a proposal to update the definition of an NAIC designation in the PPM.
NAIC designations	VOSTF discussed comments on the proposed process for challenging the NAIC designations assigned through the FE process when the SVO determines the CRP rating does not represent a reasonable assessment of risk for regulatory purposes.
Other developments >>	
Framework for regulation of insurer' investments	The Financial Condition Committee exposed a framework for regulation of insurer' investments. Comments are due October 2, 2023.
Use of algorithms, predictive models, and artificial intelligence systems	The Innovation, Cybersecurity, and Technology Committee received initial comments about the proposed NAIC Model Bulletin: Use of algorithms, predictive models, and artificial intelligence systems by insurers.

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Accounting highlights

Short-term investments

Action. SAWPG exposed revisions to SSAP No. 2R to restrict the investments reported as cash equivalents or short-term investment, effective January 1, 2025. Comments are due September 29, 2023.

The revisions prohibit the following investments to be reported as short-term investments or cash equivalents regardless of maturity date:

- investments that are reported on Schedule BA, including but not limited to:
  - collateral or non-collateral loans in the scope of SSAP No. 21R;
  - surplus notes in the scope of SSAP No. 41R; [18] and
- mortgage loans in the scope of SSAP No. 37.[19]

SAPWG stated that certain types of investments, particularly collateral loans, or other investments reported on Schedule BA, are being designated to meet the parameters for short-term investment reporting. The proposed revisions are designed to:

- ensure that these types of investments are captured on Schedule BA; and
- eliminate the potential to design investments to qualify for short-term investment reporting that could result in:
  - masking the extent of investments held on Schedule BA;
  - obtaining favorable RBC treatment; and
  - having exceptions to state investment limits, or admissibility requirements.

Conceptual framework

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

Comprehensive revisions to the definition of a liability include:

- removing the term 'probable' and the phrase 'in the future as a result of past transactions or events';
- focusing the primary characteristics of a liability on a present obligation to transfer an economic benefit; and

[18] SSAP No. 41R, Surplus Notes

[19] SSAP No. 37, Mortgage Loans

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- clarifying that the guidance only applies if there is no contradictory guidance in other SSAPs.

Asset valuation reserve and interest maintenance reserve

Action. SAPWG exposed a proposal for a long-term project to include additional accounting guidance for AVR and IMR into SSAP No. 7. Comments are due September 29, 2023.

Discussion topics are expected to include:

- allocation between IMR and AVR when credit declines occur;
- bifurcation between IMR and ARV for bonds when credit quality of the investment changes within a designation level;
- update of the guidance about perpetual preferred stock that directs insurers to allocate based on NAIC designation;
- establishment of principle-based concepts to assist insurers with the allocation between IMR and AVR to ensure consistency across insurers;
- clarification of allocation of derivatives held at fair value that are deemed to be hedging interest rate risk;
- clarification about the effect of IMR in reinsurance transactions, particularly with the dissolution of reinsurance agreements when IMR has been initially transferred;
- addition of cross checks to ensure that items are being mapped to the AVR correctly from other schedules; and
- review of overall reporting of IMR and AVR that includes how positive balances in one account effect negative balances in another.

SAPWG stated that this project would also address disconnects between the SSAPs and the IMR and AVR guidance included in the Annual Statement instructions.

Interest maintenance reserve

Action. SAWPG exposed revisions to the Annual Statement instructions to remove guidance that permits the allocation of non-interest related losses to IMR. Comments are due September 29, 2023.

These revisions focus on ensuring that the guidance does not inadvertently permit the allocation of non-interest related changes to IMR. The changes will subsequently be included in SSAP No. 7 as part of the long-term project for IMR and AVR. However, SAPWG proposed that these clarifying edits be made immediately in the Annual Statement instructions because that is where the guidance currently resides.

Negative interest maintenance reserve

Action. SAPWG adopted INT 23-01 to provide optional, temporary guidance for negative (disallowed) IMR. The INT is effective through December 31, 2025, and will be automatically nullified on January 1, 2026,

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but could be nullified earlier or extended based on SAPWG's actions to establish long-term guidance on negative IMR.

The INT:

- allows insurers to admit negative (disallowed) IMR up to 10% of adjusted capital and surplus when RBC is greater than 300% of the authorized control level after adjustment to total adjusted capital to remove admitted positive goodwill, electronic data processing equipment and operating system software, net deferred tax assets (DTA) and admitted net negative (disallowed) IMR;
- instructs insurers to admit negative (disallowed) IMR in the general account (GA) until the capital and surplus percentage limit is reached; then if all negative (disallowed) IMR has not been fully admitted, report the remaining negative (disallowed) IMR in the separate accounts proportionately between insulated and non-insulated separate accounts;
- includes application guidance for reporting of admitting IMR in both the general and separate accounts;
- allows derivative losses to be included in negative IMR that is subject to being admitted if the insurer can demonstrate historical practice in which realized gains from derivatives were also included in IMR (as liabilities) and amortized;
- directs insurers to disclose:
  - net negative (disallowed) IMR in aggregate and allocated between the general account, insulated separate accounts and non-insulated separate accounts;
  - amounts of negative IMR admitted in the general account and reported as an asset in the separate account insulated and non-insulated blank;
  - the calculated adjusted capital and surplus;
  - the percentage of adjusted capital and surplus that the admitted net negative (disallowed) IMR represents (including what is admitted in the general account and what is recognized as an asset in the separate account); and
- adds attestation disclosures that:
  - fixed income investments generating IMR losses comply with the insurer's documented investment or liability management policies;
  - IMR losses for fixed income related derivatives are in accordance with prudent and documented risk management procedures under the insurer's derivative use plans and reflect symmetry with historical treatment in which unrealized derivative gains were reversed to IMR and amortized;
  - any deviation from the insurer's documented investment or liability management policies was either because of a temporary and transitory timing issue or related to a specific event; and
  - asset sales that generated admitted negative IMR were not compelled by liquidity pressures.

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SAPWG directed the formation of a technical group to continue work on a long-term solution for the accounting of negative IMR.

Collateral loans

Action. SAPWG reexposed revisions to SSAP No. 21R to clarify that pledged assets must qualify as admitted invested assets for a collateral loan to be admissible. Comments were due September 12, 2023.

The revisions require:

- audited financial statements for collateral in the form of partnerships, limited liability companies (LLC), and subsidiaries controlled or affiliated entities (SCA) in the scope of SSAP Nos. 48 and 97 for collateral loans to be admitted;[20] and
- the use of the proportionate audited equity valuation, and to nonadmit the collateral loan in excess of the audited equity valuation of the pledged investments.

One interested party commented that the use of book value to measure the adequacy of collateralization, or the ability for a borrower to repay a collateral loan is not supportable because it does not reflect the value at which an asset would be bought or sold. They asserted that proposed revisions could:

- create volatility for insurers and lead borrowers to manage to a metric in the short term that would not provide the highest proceeds to repay the collateral loan; and
- result in undue costs and efforts to the insurers.

The interested party requested SAPWG to consider the likely adverse effects to insurers' decision-making that may result from this proposal in addition to the operational disruptiveness of immediate adoption and suggested that SSAP No. 21:

- allow insurers to elect the use of either fair value or the proportionate audited equity valuation of the pledged investment when evaluating the adequacy of pledged collateral;
- treat the election as an accounting policy election under SSAP No. 3;[21] and
- direct insurers to nonadmit the portion of the collateral loan that exceeds the elected valuation basis of the pledged investments.

Other interested parties supported the revisions proposed by SAPWG but acknowledged they did not fully consider the implication of using net equity value versus fair value in the measurement of pledged collateral. They stated that additional time would be beneficial to consider the suggestion.

The NAIC staff stated that it is a long-standing SSAP view that collateral loans need to be backed by investments that qualify as admitted assets.

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[20] SSAP No. 97, Investments in Subsidiary, Controlled and Affiliated Entities

[21] SSAP No. 3, Accounting Changes and Corrections of Errors

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Some regulators expressed concern about introducing optionality that could lead to inconsistencies across insurers domiciles in different states.

Government assistance

Action. SAPWG adopted 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.

The proposed revisions clarify that:

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

Interested parties agreed with the proposed revisions, but suggested SAPWG clarify that the intent of the revisions is:

- to require disclosure of unusual or infrequent government assistance transactions regardless of how those transactions are accounted for; and
- not to prohibit insurers from accounting for government assistance transactions by using a grant or contribution model.

SAPWG stated that such clarification is not needed because the disclosures are about governance assistance and not the form of accounting for such assistance.

The 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 contribution model to account for government assistance.

Principles-based bond definition

Action. SAPWG adopted revisions to SSAP Nos. 26R, 43R and other SSAPs to add guidance for the principles-based bond definition, effective January 1, 2025.

The principles-based bond definition project included a number of revisions that were discussed and agreed upon in previous meetings. The adoption included the following changes from the most recent exposure:

Revisions to SSAP No. 26R include:

- updating scope to:
  - exclude securities that do not qualify as bonds, including first loss positions that lack contractual payments or substantive credit enhancement; and

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  - clarify that replication transactions are addressed in SSAP No. 86 and are not affected by the principles-based bond definition.[22]

- 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.

Revisions to both SSAP Nos. 26R and 43R included:

- 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.

Revisions to SSAP No. 43R included an update to its scope to exclude residual tranches, interests and first loss positions and to identify that they are captured in SSAP No. 21R.

Action. SAPWG exposed revisions to SSAP 21R to provide guidance for the accounting for debt securities that do not qualify as bonds and to propose measurement guidance for residual tranches, interests and first loss positions. Comments are due September 29, 2023.

Proposed revisions include addressing admissibility for securities in the scope of SSAP No. 21R that do not qualify as bonds under SSAP 26R:

- for debt securities where the primary source of repayment is derived through underlying rights to collateral, the underlying collateral must primarily qualify as admitted assets; and
- residual tranches or first loss positions qualify as admitted assets only to the extent the underlying collateral primarily qualifies as admitted assets.

SAPWG also proposed revisions related to guidance for residual tranches, interests and first loss positions that included requirements to:

- report residual tranches at the lower of adjusted cost or fair value, and report reductions in fair value below adjusted cost as an other-than-temporary impairment;
- treat all cash flows received as a return of investment until the residual tranche book adjusted cost basis of zero, and then treat them as interest income.

The proposed revisions address interested party comments about admissibility of securities in the scope of SSAP No. 21R but not suggestions about accounting for residual tranches.

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[22] SSAP No.86, Derivatives

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SAPWG also discussed suggestions by interested parties to revise Schedule BA reporting for debt securities that do not qualify as bonds, including interested parties' proposal to:

- ensure the reporting categories reflect the related SSAP within the instructions;
- update the reporting columns;
- clarify that investments tagged as debt securities that do not qualify as bonds that are transferred from Schedule D retain the NAIC designation and filing exempt or private letter rating status at the time of transfer;
- remove instructions for tax credit Investments that are no longer valid; and
- report tax credit investments according to their risk categories.

Next step. SAPWG directed NAIC staff to sponsor a blanks proposal to revise Schedule BA in accordance with the bond project for debt securities that do not qualify as bonds. It will also send a notice to VOSTF and the Capital Adequacy Task Force to allow life insurers the ability to use existing Schedule BA reporting provisions for SVO-assigned designations

Proposed bond definition – Schedule D reporting

Action. On a call before the Summer meeting, the Blanks Working Group reexposed revisions to Schedule D, Part 1 splitting it 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 October 12, 2023.

Revisions were made to the original proposal based on comments received from interested parties that included clarifying the categories and information reported in them.

In addition to splitting Schedule D into two categories, the proposal revises the data elements 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 exchange traded funds – fair value;
  - SVO-Identified bond exchange traded funds – systematic value
  - Bonds issued from SEC-Registered business development corps, closed-ended funds and REITs
  - Bank loans – issued;
  - Bank loans – acquired;

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  - 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 (exempt);
    - Agency commercial mortgage-backed securities (CMBS) – guaranteed (exempt);
    - Agency RMBS – not or partially guaranteed (not exempt);
    - Agency CMBS – not or partially guaranteed (not exempt);
    - 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.

For the categories marked exempt, government sponsored mortgage reference securities are not included.

Paid-in-kind interest disclosure

Action. SAPWG adopted revisions to SSAP No. 34 to further clarify disclosures and incorporate a practical expedient for the PIK interest aggregate disclosures.

The revisions add a footnote to SSAP No. 34 stating that for the disclosure of the cumulative amount of PIK interest included in the current principal balance or par value insurers would:

- 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;
- apply any decreasing amounts such as disposals (i.e. repayments or sales) to any PIK interest outstanding first when calculating the net increase that includes PIK interest; and
- allow insurers to use a practical expedient to calculate the cumulative amount of PIK interest on a bond by subtracting the original principal or

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par value from the current principal or par value, not to be less than zero.

The revisions are in response to questions received about how paydowns and disposals would affect PIK interest included in the cumulative balance.

Financial modeling for collateral loan obligations

Action. SAPWG adopted revisions to SSAP No. 43R to add CLOs to the financial modeling guidance and clarify that CLOs are not included as legacy securities.

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

Residual interests

Action. SAPWG reexposed revisions to SSAP Nos. 43R and 48 to clarify the scope and reporting of residual interests and residual security tranches. Comments were due September 12, 2023.

Interested parties suggested clarifying that the definition of a residual would not include:

- private funds that issued debt for liquidity or operating purposes rather than to raise capital backed by a discrete pool of collateral loans;
- real estate funds such as real estate investment trusts or joint ventures;
- non-US registered funds;
- other Issuer Credit Obligations in the proposed bond definition, such as 1940 Act funds, business development company operating entities, and holding companies supported by operating companies.

SAPWG revised the proposed definition based on recommendations from interested parties to ensure consistent reporting classification for residuals.

Interested parties also recommended an effective date of six months after the adoption to allow time for insurers to consider the guidance, develop accounting policies and identify the residuals under the new definition. SAPWG did not agree to delay the effective date because that would go beyond the year-end 2023.

The proposed revisions are a result of a VOSTF referral and discussion at the Spring meeting that suggested residuals may be underreported because of the many legal forms of residual investments.

Actuarial Guideline 51

Action. SAPWG exposed revisions to SSAP No. 54R to clarify that gross premium valuation under Appendix A-010 and cash flow testing under AG 51 are both required. Comments are due September 29, 2023.

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Proposed revisions:

- clarify an insurer's accident and health reserves in total must be adequate under a gross premium valuation;
- state that:
  - requirements of AG 51 provide a test that indicates whether reserves in addition to the requirements of A-010 are indicated; and
  - AG 51 does not change the base requirements of A-010; and
- include exhibits illustrating interaction between SSAP No. 54R, A-010 and AG 51.

These revisions are a result of diversity in practice across insurers of long-term care insurance with regard to how guidance in AG 51 about determining when additional reserve may be necessary interacts with guidance on accident and health insurance reserve adequacy in SSAP 54R and Appendix A-010.

Schedule BA reporting categories

Action. SAPWG exposed a request for comments on a proposal to further define and provide examples of investments that are reported by type of investment on Schedule BA based on underlying characteristics of the assets. Comments are due September 29, 2023.

Examples were requested of investments with the following characteristics:

- bonds / fixed income instruments;
- common stocks;
- real estate;
- mortgage loans; and
- other.

SAPWG stated that variations exist across insurers on the types of investments that are included within each category of Schedule BA. This exposure is intended to improve the Annual Statement instructions and examples for reporting investments based on the underlying characteristics of assets.

New market tax credits and tax equity investments

Action. SAPWG reexposed revisions to SSAP No. 93 to update guidance for tax credit investments and clarify the scope of SSAP No. 94. Their proposed effective date is December 31, 2024. Comments are due September 29, 2023.

The proposed revisions to SSAP No. 93 include:

- clarifying that investments that do not meet the conditions of investments in a tax credit structure would be captured under either SSAP No. 48 or SSAP No. 26R based on the nature of the structure;

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- providing guidance for tax credits and other tax benefits previously included in SSAP No. 94;
- updating examples in Exhibit A to illustrate application of the proportional amortization method; and
- stating that all revisions would apply retrospectively.

While the revisions do not change criteria to admit the tax credit investment, they clarify that insurers are required to annually assess the future utilization of the investment's current portion of unallocated tax credits against the estimated tax liabilities for both the tax year in which the tax credits can be initially utilized as well as any applicable carryback periods.

Proposed revisions to SSAP 94R include:

- clarifying that the scope includes:
  - state and federal tax credits purchased by the insurer without being an investor in the entity for which the tax credit was purchased; and
  - tax credits allocated from investments not within the scope of SSAP 93R; and
- updating the detailed exhibits to better illustrate the accounting for transferable tax credits purchased at a discount.

Interested parties stated that they agree with having uniformity in accounting and reporting for equity and debt investments for which the return is earned primarily through tax credits. They also agreed with using the proportional amortization method for these types of investments.

The revisions to SSAP No. 94 were responsive to interested parties' comments. However, SAPWG did not make a change suggested by interested parties that would allow purchased federal tax credits to be initially reported as other than invested asset and then transferred to a DTA, if not used in the same period it was purchased. It stated that allocated and purchased tax credits are substantially the same assets no matter how they are acquired and should not reported differently.

Share-based compensation

Action. SAPWG adopted revisions to SSAP No. 104R as well as SSAP Nos. 47 and 95 to adopt, with modification, ASU 2019-08.

Revisions include:

- 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 reject the Topic 606 guidance included in ASU 2019-08.[23]

[23] ASC 606, Revenue from Contracts with Customers

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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. Comments are due September 29, 2023.

Interested parties continued to express concerns with the nullification of this guidance. They stated that requiring the transfer of assets that support insurance liabilities at fair will result in several issues including conflicts with SSAP No. 63.[24]

SAPWG asked that interested parties provide specific scenarios that would create inconsistencies and suggested amendments to SSAP No. 62R to prevent inconsistencies. NAIC staff will work with interested parties to develop recommendations for future discussion.[25]

Application of CAMT to third quarter 2023

Action. SAPWG exposed revisions to INT 23-02 to provide guidance on how insurers will assess the effects of CAMT for the third quarter 2023. Comments were due September 12, 2023.

The proposed interpretation:

- allows insurers not to assess the effects on the insurer's valuation allowance and deferred tax assets from the CAMT;
- includes a subsequent event exception; and
- direct insurers to disclose:
  - any information available about their applicable entity status; and
  - the estimate for the CAMT 2023 liabilities for third quarter 2023, if available or that a reasonable estimate is not feasible.

Corporate alternative minimum tax guidance

Action. SAPWG exposed INT 23-03 to provide guidance on assessing the effects of CAMT for periods on or after the 2023 year-end. Comments were due September 12, 2023.

The exposed INT 23-03:

- does not revise SSAP No. 101, rather clarifies existing guidance;[26]
- relies on tax sharing agreements (TSA) to allocate the consolidated CAMT for purposes of admittance calculation; and
- introduces a principles-based approach that could be applied by all insurers.

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24 SSAP No. 63, Underwriting Pools

25 SSAP No. 62R, Property and Casualty Reinsurance

26 SSAP No. 101, Income Taxes

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INT 23-03 would apply to insurers that are not subject to CAMT, those that are subject to CAMT, and those that may or may not meet the TSA exclusions.

To meet the exclusion, the TSA would:

- exclude the insurer from charges for any portion of the group's CAMT; and
- not allocate any portion of the group's CAMT credit carryover to the insurer.

The insurer would also have to reasonably expect or have knowledge that the parties liable for the CAMT payables under the TSA are meeting their obligations.

Insurers that meet the TSA CAMT exclusion would not be required to calculate or recognize CAMT in their current or deferred tax computation. Insurers that do not meet the TSA exclusion, are included in a consolidated tax return and are subject to a qualifying TSA, will recognize the amount of CAMT payable (expense) or CAMT tax credit carryforward in accordance with the TSA.

The INT provides guidance for recognition of CAMT payable, DTA and statutory valuation allowance (SVA) that is consistent with SSAP No. 101. It states that the determination of a SVA would depend on whether the insurer is a part of a tax-controlled group or a stand-unaffiliated corporation:

- if part of a tax-controlled group, the insurer would use the SVA assessment for the CAMT credit carryforward completed at the group level; or
- if part of stand-alone unaffiliated corporation, the insurer would estimate the SVA for all deferred taxes, including CAMT credit carryforward, in determining their total adjusted gross DTA.

Insurers would be allowed to make an accounting policy election to either consider or disregard CAMT when evaluating the need for a SVA for its non-CAMT DTAs.

The INT proposes that the DTA for a CAMT tax credit allocated to the insurer be an admitted asset subject to the following admissibility guidance:

- it is a CAMT payor or is part of a tax-controlled group that is a CAMT payor; and
- the use of the CAMT tax credit is contingent on the actions of the tax-controlled group that may potentially put the group below the CAMT threshold prohibiting it from being utilized.

The INT also proposes that insurers that meet or exceed the top line of the Realization Threshold Limitation Table in SSAP No. 101 would not be required to take the CAMT into account when calculating the with and without tax liability for purposes of determining the amount expected to be realized under SSAP No. 101, paragraph 11.b.i.

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SAPWG considered whether or not to allow CAMT to be admitted under paragraph 11.c, thus treating it similar to other DTAs and decided to allow CAMT to be treated the same as other DTAs under SSAP No. 101.

INT proposed transition guidance that would allow insurers to rely on amended TSA agreements filed by year end with the domiciliary regulator while it is in review provided that the domiciliary regulator confirms that it does not object to the new TSA amendment.

Insurers would also be required to disclose whether it is a non-applicable entity, an applicable entity with TSA exceptions or an applicable entity. For applicable entities without TSA exclusions, insurers would also disclose:

- the accounting policy election made to consider or disregard CAMT when evaluating the need for a valuation allowance for its non-CAMT DTAs;
- application of the Realization Threshold Limitations Table for the CAMT; and
- material modifications to projections.

Insurers would continue to be subject to all disclosures required by SSAP No. 101.

Accounting guidance in the Annual Statement instructions

SAPWG discussed a proposal to start a project to review the annual and quarterly statement instructions to ensure that all accounting guidance is reflected within SSAPs.

SAPWG stated that the Annual Statement instructions are not intended to be a source of accounting guidance. It received comments about topics where accounting guidance is included in the Annual Statement instructions that should be considered for inclusion in the SSAPs. These included:

- IMR/AVR guidance;
- Schedule F penalties; and
- health insurer specific presentation of:
  - co-payments and deductibles;
  - fee-for-service revenue;
  - gains or loss on fixed assets.

Next Steps: SAPWG directed NAIC staff to proceed with a broad project to review the Annual Statement instructions and ensure accounting guidance is included within the SSAPs.

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3

Actuarial highlights

Non-variable annuities

Action. On a call before the Summer meeting, the VM-22 Subgroup exposed a draft of the structure and methodology of the standard projection amount requirements. Comments were due July 29, 2023.

At the Summer meeting, the VM-22 Subgroup reported to LATF on the progress of their work. It stated that they have discussed all comments received from the last exposure of VM-22. Although the updated document has not been exposed, it has been made available on the subgroup's website.

The goal is for VM-22 to be effective January 1, 2026 with a three-year implementation. All insurers would be required to implement VM-22 beginning January 1, 2029. This timing assumes the ability to conduct a field test in 2024 which is dependent on the work being performed over the economic scenario generator, which needs to be completed before the VM-22 field test.

Next step. The VM-22 Subgroup will hear from the Society of Actuaries mortality drafting group about standard projection mortality assumptions for payout annuities, deferred annuities and structured settlements.

Modeling of complex assets – insurer filings

LATF discussed initial observations from filings submitted under Actuarial Guideline 53 adopted in 2022. The guideline requires disclosures of asset related information for life insurers in its scope. The first submission was due April 2023.

The initial review was focused on identifying insurers with outlier net yield assumptions. Regulators stated that they are concerned that assuming high net yields will result in more favorable asset adequacy analysis results and a conclusion that lower amount of assets are needed for reserves to be considered adequate. The regulator group working on the review of filings is engaging with domestic regulators with the goal of decreasing higher net yield assumptions by discussing findings with relevant insurers and removing them from the outlier list.

Next steps. Regulators will be requesting additional information from certain ceding insurers, particularly if an assuming insurer does not submit a VM-30 actuarial memorandum to the state.[27] They will also work on a guidance document for year-end 2023 to clarify and fill in gaps identified during reviews of the year-end 2022 filings, including:

[27] VM-30, Actuarial Opinions and Memorandum Requirements

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- sensitivity test for currently held equities;
- structured asset information by tranche and related payments in-kind;
- information about asset allocation in future projection years;
- template clarification and updates; and
- information to ensure less volatility in classification as projected high net yield asset.

Regulators stated that phase one of the reviews has been focused on insurers with outlying net yield assumptions. Phase two of the reviews will focus on incomplete documentation and narrative answers to identify best and outlying practices.

Economic scenario generator – field test results

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

The presentation summarized quantitative information to:

- understand the effect on capital;
- review the range of results across field test participants;
- compare the stability of results over time;
- evaluate the use of alternative metrics; and
- inform regulator decision-making on model and calibration choices.

The report stated that while at the end of 2021 there were 752 insurers that reported using Life RBC blank, 613 of these insurers reported less than one dollar of C3 Phase 1 capital with total C3 Phase 1 capital amounting to approximately $3 billion.

The results of the field test presented data from 24 legal entities and that represented approximately 19% of the industry and included the following observations:

- The field test results produced from the Conning economic scenario generator showed, on average, an significant increase to capital compared to the baseline scenarios. However, many field test participants held little or no C3 Phase I capital in their baseline runs.
- The participant results for 200 scenarios from the latest version of the Academy Interest Rate Generator prescribed in VM-20 and VM-21 were mixed. Some insurers saw an increase, but it was mostly offset by decreases in other insurers.

The report also stated that when producing capital results using a limited number of scenarios, outlier scenarios that are included in the scenario set can have outsized effect on the results, particularly with scenario sets that have increased volatility or broader distribution.

Next steps: The Generator of Economic Scenarios (GOES) Subgroup will develop recommendations to LATF for reserve and capital frameworks-specific implementation issues and GOES model governance framework. A more comprehensive set of GOES acceptance criteria is planned to be

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exposed in September. Also, a second industry field test is planned, but will not occur before Spring 2024.

Hedge modeling

Action. On a call before the Summer meeting, LATF adopted revisions to hedge modeling language for index credit hedging in VM-21.

The revisions:

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

The revisions also include 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 1.5% multiplicatively of the portion of the index credit that is hedged. If the insurer does not have sufficient and credible experience, a margin of at least 20% is assumed.

When discussing the minimum index credit hedging error, interested parties recommended a 1% minimum stating that a higher minimum error could penalize insurers with a very tight hedging strategy. Some regulators agreed with the 1% minimum while others preferred the minimum to be 2%. As a compromise, LATF adopted a minimum index credit hedging error of 1.5%.

Interest maintenance reserve template

Action. On a call before the Spring meeting, LATF exposed a template to gather information about how insurers report IMR. Comments were due July 28, 2023.

The focus of the template is on insurers that have a total negative IMR balance but could also be useful for insurers with positive balances. The template is intended to be optional and completed at the request of the regulators.

At the Summer meeting LATF heard comments about the proposed template. Interested parties provided technical comments on the template and expressed concern that the template combines concepts from both principle-based reserves (PBR) and the Actuarial Opinion Memorandum. They stated that:

- parts relevant for PBR would be in the purview of the Qualified Actuary, and the PBR report is not due until April, 1 whereas the template is due on February 28; and
- some information that is requested by the template is not currently the responsibility of the Appointed Actuary and should be collected elsewhere.

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Interested parties also asked whether:

- the template would be considered part of the actuarial opinion memorandum; and how it would be referenced; and
- the intent would be for the insurer to maintain the template and make it available upon request.

LATF responded that it was not the intention for the template to be due on February 28.

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Risk-based capital

Residual tranches

Action. On a call before the Summer meeting, the RBC IRE Working Group adopted a proposal for a new RBC factor for residual tranches reported on Schedule BA. This proposal was also adopted by all of the Working Group's parent committees.

The proposal keeps the current 30% RBC factor for 2023 year-end reporting and adds a 15% sensitivity test. Beginning with 2024 year-end reporting, the factor will increase to 45%.

Regulators commented that changing the RBC factor for year-end 2023 reporting would be disruptive and may result in insurers divesting assets at suppressed prices. They stated that the 15% sensitivity testing factor will allow regulators to see the effect that a 45% factor would have. The Working Group stated that the new factor will remain in effect unless it receives information that indicates a factor of above or below the 45% is appropriate.

Structured securities

The RBC IRE Working Group heard a presentation from the Academy about proposed RBC principles for structured securities. These principles included criteria for when an asset class would require a new model and if the securities within an asset class should be modeled individually to determine their C-1 factors.

The Academy stated that for an asset class to be considered for a new C-1 factor it should first meet the following attributes:

- material or likely material in the future across the industry;
- the modeled risk needs to be incorporated in C-1, for example, liquidity alone would not be sufficient justification because C-1 does not measure liquidity risk; and
- expected benefits of a more precise calculation outweighs the expected cost of building and using a new model.

If the above criteria are met, a flowchart would be used to determine if existing C-1 factors can be used or if new factors would need to be developed. The Academy stressed that preference is given to a simpler solution: if an existing factor can be used, it should be used. Based on the flowchart presented, a new factor would be developed when an asset class does not have similar risks to an existing C-1 asset class (for example, structured securities may not be considered similar to corporate bonds because their tail risk increases more quickly) and there is sufficient data available to create a new model. If an asset class for which a new factor is being considered has comparable attributes, (for example, can be grouped by similar risks based on CRP ratings) a new C-1 factor should be created.

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The Academy stated that individual assets should only be modeled when the asset class does not have comparable attributes and it is practical to model the securities individually.

The Academy also proposed the following seven candidate principles to govern the process of creating new C-1 factors:

- the purpose of RBC is to help regulators identify weakly capitalized insurers, therefore small inaccuracies in RBC requirements may not justify a change to the RBC formula;
- RBC measures the effect of risk on statutory surplus;
- RBC arbitrage can only be measured for asset-backed securities (ABS) where the underlying collateral has an established asset class specific C-1 requirement;
- the motivation behind creating an ABS structure should have no bearing on its C-1 requirements;
- C-1 requirements on ABS should treat the collateral as a dynamic pool of assets, incorporating future trading activity that is likely to occur based on historical data or mandated by the structure's legal documents;
- RBC is based on the holdings of an insurer; and
- C-1 requirements for ABS should be calibrated to different risk measures where appropriate.

Next Step. The Academy requested that regulators provide feedback on these principles including whether other principles may be needed.

Repurchase agreements

Action. The Life RBC Working Group exposed a proposal to align the RBC charge for repurchase agreements, currently at 1.26%, with the 0.20% charge for conforming securities lending programs. Comments are due September 29, 2023.

Interested parties commented the 0.20% charge would apply only to repurchase agreements that meet the conforming program criteria. Such program is managed against clear operational and risk guidelines, including maintaining a liquid reinvestment portfolio.

An additional RBC charge of 2% would be applied to all overcollateralized amounts which is the difference between the collateral received under the secured borrowing and the fair value of the securities sold. A 2% charge is in line with the unsecured credit exposures insurers would assume on their bond portfolios.

With the enhanced guidelines, interested parties believe the liquidity risk is significantly reduced and therefore a lower charge is appropriate. All other repurchase agreements that to do not meet the conforming guidelines will maintain the 1.26% RBC charge.

Interested parties also proposed enhancements for both reporting and RBC instructions to align with the change in charge for repurchase agreements.

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5 Valuation of Securities Task Force

NAIC designation definition

Before the Summer meeting, VOSTF discussed a proposal to update the definition of an NAIC designation in the PPM.

The revisions include clarifying the meaning of NAIC designations, including their use, their purpose and the risks they address. The proposal consolidates the instructions defining an NAIC designation to create a single, uniform definition that includes updates addressing questions raised about the purpose of NAIC designations versus CRP ratings. The SVO also recommended consolidating the current NAIC designation subscript 's' definition for other nonpayment risks into Part One of the PPM because application of subscript 's' to assign an NAIC designation for other nonpayment risks signifies a change in the meaning of the designation and is the policy of the Task Force.

Interested parties agreed that the meaning of the NAIC designations should be clarified but expressed concern that the proposed language does not reflect that there are other risks of nonpayment.

At the Summer meeting the Task Force stated that they are continuing to work with interested parties on refinements to the definition. Their comments also included:

- reassurance that nothing in the update changes the scope of responsibility for the SVO;
- statement that the designation should reflect the likelihood of timely and full payment of principle and scheduled period interest, as appropriate;
- agreement with comments that:
  - additional refinements are needed including adding a summary of overall regulatory objectives of the NAIC designation;
  - loss given default should be considered when assigning a designation;
- statement that tail risk should be considered for certain asset class structures.

Interested parties stated that if tail risk is included, it is important that it be treated consistent across asset classes. They said although they expect to have additional comments about the use of loss given defaults and tail risk, considering loss given defaults may be appropriate in certain situations.

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NAIC designations

VOSTF discussed comments on the proposed process for challenging the NAIC designations assigned through the FE process when the SVO determines the CRP rating does not represent a reasonable assessment of risk for regulatory purposes.

VOSTF stated that the purpose of the proposal is to provide the checks and balances needed over the CRP ratings and to provide regulators with comfort that the investment risk assessments are reasonable. It is not intended to replace CRP ratings, but rather create certainty for industry on a go forward basis.

SVO outlined the proposed process as follows:

- SVO will notify an insurer if it has identified an FE eligible security with a CRP rating that is 3 or more notches different than its NAIC Designation equivalent current rating;
- the insurer will have 120 days to appeal and provide additional information to the SVO to support why the CRP rating should be maintained;
- after information is submitted, it will take 90 days or longer to review the information submitted by the insurer; and
- if it is determined that the CRP rating should be excluded from FE for that security, the insurer will have another 120 days to decide if it agrees with an SVO designation or if it decides to acquire a different CRP rating.

SVO stated that the proposal allows sufficient notice period to let the insurer decide whether or not it wants to appeal and provide additional information before any action is taken. It further stated that it could take up to a year for the actual rating to change.

Interested parties expressed concern with the proposal. Their comments included:

- stating the proposed amendment could lead to uncertainty and market disruption
- requesting more transparency about the process;
- observing that the current process could allow the same security held across multiple insurers in different states of domicile to be handled differently;
- suggesting the SVO may be working with incomplete information about individual securities;
- requesting that the SVO provide public disclosures about:
  - rating agency methodologies that they do not believe are fit for the NAIC's purpose with analytical support for such views on each CRP rating methodology in question;
  - its approach for assigning a designation to the security when CRP rating is challenged; and
  - securities affected as a result of the challenge to CRP rating methodology;

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- requesting that:
  - The scope of the SVO review be limited to certain asset classes;
  - a separate appeal process be created with oversight from an independent party to ensure due process for insurers;
  - VOSTF or another sub-group be given oversight to ensure consistency of process or provide an independent review;
  - an independent review of the SVO be conducted;
  - the effect of the bond project be considered on the regulatory concerns designed to be addressed by this proposal; and
  - a cost and benefit analysis be performed.

In response to comments received the SVO stated that they would:

- publish a generic summary of the reason for this amendment and confirm that it maintains the confidentiality of the issue, rating agency and rating;
- provide to the Task Force the number of ratings challenged and the average number of notches of the change;
- request that an independent third party be engaged to perform a periodic review on the reasonability of the SVO analysis, its operational process in supporting systems; and
- provide the Executive Committee with a private and public assessment and recommendations from the review.

VOSTF asked NAIC staff to continue working with interested parties in response to their comments, specifically to create greater transparency, and clarity of the appeals process when challenging the CRP ratings.

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6 Other developments

Framework for regulation of insurer investments

Action. The Financial Condition Committee exposed a framework for regulation of insurer' investments. Comments are due October 2, 2023.

The intent of the framework is to highlight areas where the insurance regulatory framework for investments could be enhanced. The proposed framework includes modernizing the SVO by:

- eliminating or reducing blind reliance on CRPs but continuing to use CRPs with the implementation of a strong due diligence framework and focusing primarily on holistic due diligence around CRP usage;
- retaining the ability within the SVO to perform individualized credit assessments and using regulatory discretion when needed, under well-documented and governed parameters;
- enhancing the SVO's portfolio risk analysis capabilities with investments with a risk analytics tool and corresponding personnel that could perform both insurer-specific risk analysis at the request of the regulators, and industry-wide risk analytics to use in macroprudential efforts;
- enhancing structured asset modeling capabilities;
- building out a broad policy advisory function that could consider and recommend future policy charges to regulators under a holistic lens, considering effect from all affected processes; and
- considering the establishment of a broad investment working group that could act in an advisory capacity to various investment processes with more intensive regulator engagement and analysis on a confidential basis, similar to the financial analysis working group, that would review:
  - bond reporting analysis under the principles-based bond definition;
  - challenges to individual designations provided by CRPs; and
  - work provided by external consultants for investment-related projects for broad impacts to the framework.

The framework also proposes the following guidelines for RBC IRE Working Group:

- changes in RBC factors should consider market effects and consistency across asset classes in determining when and how to implement such changes; and
- consider and address areas where inconsistencies in treatment across asset classes incentivize a particular legal form.

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Use of algorithms, predictive models, and artificial intelligence systems

The Innovation, Cybersecurity, and Technology Committee received initial comments about the proposed NAIC Model Bulletin: Use of algorithms, predictive models, and artificial intelligence systems by insurers. The Committee developed this bulletin in response to the need for a framework around the use of artificial intelligence (AI) systems in insurance.

The bulletin provides regulatory guidance and expectations about how insurers should govern their development and use of AI systems. It also discusses information and documentation that insurers can expect to provide to the regulator when evaluating the insurer's development and use of these systems, organized into four sections:

- background and authority;
- definitions of terms such as algorithm, artificial intelligence, bias, big data and machine learning;
- regulatory guidance and expectations that establishes general guidelines, guidelines for governance, risk management and internal controls, third-party AI systems; and
- regulatory oversight and examination considerations.

Initial comments were provided by interested parties, including consumer representatives on the model bulletin's language on third-party oversight, definitions and principal-based approach to setting governance expectations. Some interested parties agreed with the principal-based approach of the bulletin; however, others stated it should be more specific about what insurers should be doing and include requirements for testing of outcomes. Many interested parties expressed concern with the current guidance for third-party vendors. Other comments also included:

- requesting to clarify some of the definitions for bias and algorithm; and
- making the overall scope of the bulletin more specific.

Next Steps: The Working Group will review all comments received on the bulletin and will reexpose a draft by the end of September.

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Kathy Bachman

Maureen Downie

Lauren Lokensgard

Rebecca Rachlin

Olga Roberts

KPMG Financial Reporting View
frv.kpmg.us

kpmg.com/socialmedia

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