SUBCHAPTER A. Examination and Financial Analysis
28 TAC §7.18

1. INTRODUCTION. The Texas Department of Insurance proposes amendments to 28 TAC §7.18, concerning Statements of Statutory Accounting Principles (SSAPs). SSAPs provide guidance to insurers and health maintenance organizations (HMOs), including accountants employed or retained by these entities, on how to properly record business transactions for the purpose of accurate statutory reporting. These insurers and HMOs are referred to collectively as "carriers" in this proposal.

SSAPs provide a nationwide standard method of accounting that state insurance regulators require most carriers to use for statutory financial reporting guidance. Because they create a nationwide standard, SSAPs provide a more consistent reporting of financial information from carriers. SSAPs provide the source of statutory accounting principles for the department when analyzing financial reports and for conducting statutory examinations and rehabilitations of carriers licensed in Texas, except where otherwise provided by state law. However, SSAPs do not preempt individual state legislative or regulatory authority.

The National Association of Insurance Commissioners (NAIC) adopts SSAPs through its maintenance of statutory accounting principles process. Under this process, the NAIC proposes and develops new SSAPs through a series of open meetings in which the public has the opportunity to comment. SSAPs adopted by the NAIC are incorporated into *The Accounting Practices and*

Procedures Manual (Manual), a comprehensive guide to statutory accounting principles published and issued by the NAIC. The SSAPs that have been adopted by the NAIC are incorporated into Texas regulations through adoption by reference in §7.18.

The proposed amendments are necessary to adopt by reference the March 2012 version of the Manual adopted by the NAIC. The March 2012 version of the Manual substantively revises the March 2010 version of the Manual by: (i) adding SSAP No. 94R, which the NAIC finalized on December 7, 2011; (ii) adding SSAP No. 101, which the NAIC finalized on August 30, 2011; and (iii) making five substantive placement revisions, which the NAIC finalized on August 30, 2011.

SSAP No. 94R revises SSAP No. 94 to allow entities to treat non-transferable state tax credits as admitted assets if specific criteria are met. The substantive revisions in SSAP No. 94R are effective for reporting periods ending on or after December 31, 2011.

SSAP No. 101 replaces SSAP No. 10R and SSAP No. 10 and provides revised statutory accounting principles for current and deferred federal and foreign income taxes and current state income taxes. SSAP No. 101 is effective for reporting periods ending on or after January 1, 2012.

Proposed amendments to §7.18(a) and (b) update the reference to the Manual to refer to the March 2012 version of the Manual. A second proposed amendment in subsection (a) corrects a punctuation error in the current rule text. Additionally, the proposed amendments to subsections (b) and (c) delete references to various SSAPs and to Issue Paper No. 99 because these SSAPs and issue paper are now included in the adopted March 2012 version of the Manual. Further, the proposed amendments to §7.18(c) redesignate the subdivisions of subsection (c) to reflect the deletion of paragraph (1). Finally, the proposed amendments to §7.18(c) reflect that the NAIC moved guidance in SSAP No. 96 to SSAP No. 25, which is located in Appendix H of the Manual. The NAIC did this through adoption of a placement revision (Reference No. 2011-13).

The proposed amendments to §7.18(e) reflect structural reorganization within the department; they change “Senior Associate Commissioner” to “Deputy Commissioner” and change “Financial Program” to “Financial Regulation Division.”

The proposal also incorporates nonsubstantive editorial changes to conform to current agency style.

2. FISCAL NOTE. Danny Saenz, deputy commissioner, Financial Regulation Division, has determined that, for each year of the first five years the amended section is in effect, there will be no fiscal implications for state or local government as a result of enforcing or administering the amended section, and there will be no effect on local employment or the local economy.

3. PUBLIC BENEFIT/COST NOTE. Mr. Saenz also has determined that for each year of the first five years the amended section is in effect, the public benefit will be the adoption of an updated Manual that will enable the department to continue efficient financial solvency regulation of insurance in general and the decrease in costs to carriers required to comply with accounting requirements in multiple states. In particular, adoption of the March 2012 version of the Manual will enable the department to continue efficient and effective utilization of existing resources in the analysis and examination of the financial condition of carriers to better ensure financial solvency. Additionally, the adoption and use of the updated Manual will continue to support a more consistent regulatory environment and to provide a central source for accounting guidance. The department does not anticipate that any of the proposed amendments, including the proposed adoption by reference of the 2012 Manual, will result in additional costs to those costs already required of carriers, regardless of size, under the existing rules.

The proposed amendments to §7.18(b) adopt by reference two substantively revised SSAPs: SSAP No. 94R, which allows non-transferable state tax credits to be admitted assets if specific criteria are met; and SSAP No. 101, which provides revised statutory accounting principles for current and deferred federal and foreign income taxes and current state income taxes. None of these substantively revised SSAPs will result in additional costs to those costs already required of carriers, regardless of size, under the existing rules.

Additionally, the proposed amendments to §7.18(b) adopt by reference five substantive placement revisions to the March 2010 version of the Manual that the NAIC adopted on August 30, 2011. These placement revisions are considered substantive only because SSAPs are nullified. However, these placement revisions do not make any changes to the existing guidance. None of these placement revisions will result in additional costs to those costs already required of carriers, regardless of size, under the existing rules.

4. ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL AND MICRO BUSINESSES. In accordance with the Government Code §2006.002, the department has determined that the proposed amendments will not result in any additional costs to those costs that are required of small and micro business carriers under the existing rules for the reasons specified in the Public Benefit/Cost Note part of this proposal. Nevertheless, the rule exempts certain carriers that have historically accounted for their business on a cash basis and have historically posed relatively insubstantial insolvency-related risk to consumers, other carriers, and the state's general economic welfare from compliance with the Manual. Section 7.18(d) exempts any farm mutual insurance company, statewide mutual assessment company, local mutual aid association, or mutual burial association with less than $6 million in annual direct written premiums from compliance with the Manual. Because of the types or methods of operations of these types of carriers, they are more likely to be small or micro business carriers.

Under the Government Code §2006.002(c), before adopting a rule that may have an adverse economic effect on small or micro businesses, an agency is required to prepare in addition to an economic impact statement a regulatory flexibility analysis that includes the agency's consideration of alternative methods of achieving the purpose of the proposed rule. The department has determined that the routine costs to comply with this proposal, i.e., compliance with the Manual in financial filings, will not have an adverse economic effect on small or micro business carriers. Therefore, the department is not required to consider alternative methods of achieving the purpose of these requirements in the proposed rule as required by the Government Code §2006.002(c).

5. TAKINGS IMPACT ASSESSMENT. The department has determined that no private real property interests are affected by this proposal and that this proposal does not restrict or limit an owner's right to property that would otherwise exist in the absence of government action and, therefore, does not constitute a taking or require a takings impact assessment under the Government Code §2007.043.

6. REQUEST FOR PUBLIC COMMENT. To be considered, written comments on the proposal must be submitted no later than 5:00 p.m. on July 30, 2012. All comments should be submitted to Sara Waitt, General Counsel, Mail Code 113-2A, Texas Department of Insurance, P.O. Box 149104, Austin, Texas 78714-9104. An additional copy of the comments should be submitted simultaneously to Danny Saenz, Deputy Commissioner, Financial Regulation Division, Mail Code 305-2A, Texas Department of Insurance, P. O. Box 149104, Austin, Texas 78714-9104. Any request for a public hearing on the proposal should be submitted separately to the Office of the Chief Clerk, Mail Code 113-2A, Texas

Department of Insurance, P.O. Box 149104, Austin, Texas 78714-9104 before the close of the public comment period. If a hearing is held, written and oral comments presented at the hearing will be considered.

7. STATUTORY AUTHORITY. The amendments are proposed under the Insurance Code Chapters 32, 401, 404, 421, 425, 426, 441, 802, 823, 841, 843, 861, and 862, and §36.001. Sections 401.051 and 401.056 mandate that the department examine the financial condition of each carrier organized under the laws of Texas or authorized to transact the business of insurance in Texas and adopt by rule procedures for the filing and adoption of examination reports. Section 404.005(a)(2) authorizes the commissioner to establish standards for evaluating the financial condition of an insurer. Section 421.001(c) requires the commissioner to adopt each current formula recommended by the NAIC for establishing reserves for each line of insurance. Section 425.162 authorizes the commissioner to adopt rules, minimum standards, or limitations that are fair and reasonable as appropriate to supplement and implement the Insurance Code Chapter 425, Subchapter C. Section 426.002 provides that reserves required by §426.001 must be computed in accordance with any rules adopted by the commissioner to adequately protect insureds, secure the solvency of the workers' compensation insurance company, and prevent unreasonably large reserves. Section 441.005 authorizes the commissioner to adopt reasonable rules as necessary to implement and supplement Chapter 441 of the Insurance Code (Supervision and Conservatorship). Section 32.041 requires the department to furnish to the companies the required financial statement forms. Section 802.001 authorizes the commissioner to change the form of any annual statement required to be filed by any kind of insurance company, as necessary, to obtain an accurate indication of the company's condition and method of transacting business and. Section 823.012 authorizes the commissioner to issue rules and orders necessary to implement the provisions of Chapter 823 of the Insurance Code (Insurance Holding Company Systems). Section 843.151 authorizes the commissioner to promulgate rules that are necessary and proper to implement the provisions of Chapter 843 of the Insurance Code (Health Maintenance Organizations). Section 843.155 requires HMOs to file annual reports with the commissioner, which include a financial statement of the HMO, certified by an independent public accountant. Sections 841.004(b), 861.255(b), and 862.001(c) authorize the commissioner to adopt rules defining electronic machines and systems, office equipment, furniture, machines and labor saving devices, and the maximum period for which each such class may be amortized. Section 36.001 provides that the commissioner of insurance may adopt any rules necessary and appropriate to implement the powers and duties of the department under the Insurance Code and other laws of this state.

8. CROSS REFERENCE TO STATUTE. The following statutes are affected by this proposal: Insurance Code Chapters 32, 401, 404, 421, 425, 426, 441, 802, 823, 841, 843, 861, and 862.

9. TEXT.

§7.18. National Association of Insurance Commissioners Accounting Practices and Procedures Manual.

(a) The purpose of this section is to adopt statutory accounting principles, which will provide insurers and health maintenance organizations, including accountants employed or retained by these entities, guidance as how to properly record business transactions for the purpose of accurate statutory reporting. The March 2012 [~~2010~~] version of the *Accounting Practices and Procedures Manual* (Manual) published by the National Association of Insurance Commissioners (NAIC), with the exceptions and modifications set forth in subsections (c) and (d) of this section, will be utilized as the guideline for statutory accounting principles in Texas to the extent the Manual does not conflict with provisions of the Insurance Code or rules of the department. The commissioner [~~Commissioner~~] reserves all authority and discretion to resolve any accounting issues in Texas. When making a determination on the proper accounting treatment for an insurance or health plan transaction, the commissioner will [~~Commissioner shall~~] refer to the sources in paragraphs (1) - (6) of this subsection in the respective order of priority listed. The sources in paragraphs (1) – (3) of this subsection preempt any contrary provisions in the Manual. The department rules that preempt any contrary provisions in the Manual, include, but are not limited to: §§3.1501 - 3.1505, 3.1601 - 3.1608, 3.4505(f), 3.6101, 3.6102, 3.7001 – 3.7009, 3.9101 - 3.9106, 3.9401 – 3.9404, 7.7, 7.85, and 11.803 of this title (relating to Annuity Mortality Tables; Actuarial Opinion and Memorandum Regulation;

General Calculation Requirements for Basic Reserves and Premium Deficiency Reserves; Policy Reserves; Claims Reserves; Minimum Reserve Standards for Individual and Group Accident and Health Insurance; the 2001 CSO Mortality Table; Preferred Mortality Tables; Subordinated Indebtedness, Surplus Debentures, Surplus Notes, Premium Income Notes, Bonds, or Debentures, and Other Contingent Evidences of Indebtedness; Audited Financial Reports; and Investments, Loans, and Other Assets).

(1) - (2) (No change.)

(3) directives, instructions, and orders of the commissioner [~~Commissioner~~];

(4) – (6) (No change.)

(b) The commissioner [~~Commissioner~~] adopts by reference the March 2012 [~~2010~~] version of the Manual, with the exceptions and modifications set forth in subsections (c) and (d) of this section, as the source of accounting principles for the department when analyzing financial reports and for conducting statutory examinations and rehabilitations of insurers and health maintenance organizations licensed in Texas, except where otherwise provided by law. [~~Except as provided in subsection (c)(1)(A) of this section concerning Statement of Statutory Accounting Principles (SSAP) Nos. 5R and 35R,~~] This [~~this~~] Manual that is adopted by reference with the exceptions and modifications specified in subsections (c) and (d) of this section will [~~shall~~] be applied to examinations conducted as of December 31, 2011 [~~2010~~], and thereafter, and also must [~~shall~~]

be used to prepare all financial statements filed with the department for reporting periods beginning on or after December 31, 2011 [~~2010~~].

(c) The commissioner [~~Commissioner~~] adopts the following exceptions and modifications to the Manual: [~~specified in paragraphs (1) and (2) of this subsection. Except as provided in paragraph (1)(A) of this subsection concerning SSAP Nos. 5R and 35R, these exceptions and modifications shall be applied to examinations conducted as of December 31, 2010, and thereafter, and also shall be used to prepare all financial statements filed with the department for reporting periods beginning on or after December 31, 2010.~~]

[~~(1) In addition to the statements of statutory accounting principles in the Manual, the following modifications are adopted by reference:~~]

[~~(A) Statements of Statutory Accounting Principles (SSAP) Nos. 5R, adopted by the NAIC in calendar year 2010, and effective December 31, 2011; 35R, adopted by the NAIC in calendar year 2010, and effective January 1, 2011; and 91R, adopted by the NAIC in calendar year 2010 and effective December 31, 2010. SSAP Nos. 5R and 35R shall be applied to examinations conducted as of December 31, 2011, and January 1, 2011, respectively, and thereafter, and also shall be used to prepare all financial statements filed with the department for reporting periods beginning on or after December 31, 2011, and on or after January 1, 2011, respectively.~~]

[~~(B) Nonsubstantive modifications to SSAP Nos. 9, 43R, 90, 100, and 10R, and Issue Paper No. 99 made by the NAIC in calendar year 2010, as follows:~~]

[~~(i) Ref. No. 2010-07: ASU 2010-09, Subsequent Events - Amendments to Certain Recognition and Disclosure Requirements;~~]

[~~(ii) Ref. No. 2010-01: AVR and IMR Guidance within SSAP No. 43R and SSAP No. 7;~~]

[~~(iii) Ref. No. 2010-02: Clarification of SSAP No. 90 - Accounting for the Impairment or Disposal of Real Estate Investments, paragraph 6;~~]

[~~(iv) Ref. No. 2010-05: ASU 2010-06, Fair Value Measurements and Disclosures - Improving Disclosures about Fair Value Measurements~~]

[~~(v) Ref. No. 2010-09: Income Taxes;~~]

[~~(vi) Ref. No. 2009-20: ASU 2009-02, Omnibus Update – Amendments to Various Topics for Technical Corrections; and 2010-04: ASU 2010-03, Extractive Activities - Oil and Gas; and Ref. No. 2010-04: ASU 2010-03, Extractive Activities – Oil and Gas;~~]

[~~(2) In addition, the following exceptions and modifications are adopted:~~]

(1) [~~(A)~~] Settlement requirements for intercompany transactions are subject to the accounting treatment in Statement of Statutory Accounting Principles (SSAP) No. 25 currently located in Appendix H (previously SSAP No. 96), except that amounts owed to the reporting entity shall be settled by the due date in accordance with the written agreement and the requirements of §7.204 of this title (relating to Commissioner's Approval Required).

Intercompany balances shall be settled within 90 days of the period for which the services are being billed; otherwise the [~~such~~] balances shall be nonadmitted.

(2) [~~(B)~~] Retrospective premiums must be billed within 60 days of computation and audit premiums must be billed within 60 days of the completion of the audit in determining the beginning date from which the 90-day period is calculated to determine admissibility of uncollected premium balances under SSAP No. 6.

(3) [~~(C)~~] Electronic machines, constituting a data processing system or systems and operating systems software used in connection with the business of an insurance company acquired after December 31, 2000, may be an admitted asset as permitted by Insurance Code §§841.004, 861.255, 862.001, and any other applicable law and shall be amortized as provided by the Manual. Property [~~All such property~~] acquired prior to January 1, 2001, may be an admitted asset as permitted by Insurance Code §§841.004, 861.255, 862.001, and any other applicable law, and shall be amortized in full over a period not to exceed ten years.

(4) [~~(D)~~] Furniture, labor-saving devices, machines, and all other office equipment may be admitted as an asset as permitted by the Insurance Code §§841.004, 861.255, 862.001, and any other applicable law and, for [~~such~~] property acquired after December 31, 2000, depreciated in full over a period not to exceed five years. Property [~~All such property~~] acquired prior to January 1, 2001, may be an admitted asset as permitted by Insurance Code

§§841.004, 861.255, 862.001, and any other applicable law, and shall be depreciated in full over a period not to exceed ten years.

(5) [~~(E)~~] All certificates of deposit, of any maturity, may be classified as cash and are subject to the accounting treatment contained in SSAP No. 2, notwithstanding the provisions of SSAP No. 26.

(d) (No change.)

(e) In the event a domestic insurer desires to deviate from the accounting guidance in a Texas statute or any applicable regulation, the insurer must [~~shall~~] file a written request for a permitted accounting practice and obtain approval prior to using the accounting deviation in a financial statement. The [~~Such~~] filing must [~~shall~~] be made with the Deputy [~~Senior Associate~~] Commissioner of the Financial Regulation Division [~~Program~~], Texas Department of Insurance, Mail Code 305-2A, P.O. Box 149104, Austin, Texas 78714-9104 at least 30 days before filing the financial statement that is proposed to be affected by the deviated accounting practice. Insurers must [~~shall~~] not use deviated accounting practice without the department's prior approval.

(f) (No change.)