

SUBCHAPTER A. EXAMINATION AND FINANCIAL ANALYSIS
28 TAC §7.18

1. INTRODUCTION. The Commissioner of Insurance (Commissioner) adopts amendments to §7.18, concerning the adoption by reference of the *Accounting Practices and Procedures Manual*, including new statements of statutory accounting principles. The section is adopted without changes to the proposed text published in the October 29, 2010 issue of the *Texas Register* (35 TexReg 9622).

2. REASONED JUSTIFICATION. The amendments to §7.18 are necessary to adopt by reference the March 2010 version of the *Accounting Practices and Procedures Manual* (Manual) as well as substantive and non-substantive updates to this version of the Manual issued by the National Association of Insurance Commissioners (NAIC) in calendar year 2010. The substantive updates include new statements of statutory accounting principles (SSAPs). The Manual, published and issued by the NAIC, is a comprehensive guide to statutory accounting principles and includes the SSAPs that have been adopted by the NAIC. The 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 adoption. SSAPs provide a nationwide standard

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method of accounting, which most carriers are required to use for statutory financial reporting guidance. Therefore, SSAPs provide for a more consistent reporting of financial information from carriers. However, SSAPs do not preempt individual state legislative or regulatory authority. SSAPs are adopted by the National Association of Insurance Commissioners (NAIC) through its maintenance of the statutory accounting principles process, which involves the developing and proposing of new SSAPs, and adoption by the NAIC in a series of public meetings with the opportunity for public comment. SSAPs provide the source of statutory accounting principles for the Department when analyzing financial reports and for conducting statutory examinations and rehabilitation of carriers licensed in Texas, except where otherwise provided by law. Except for new SSAP Nos. 5R and 35R, the March 2010 version of the Manual and the updates to it must be used to prepare all financial statements filed with the Department for reporting periods ending on or after December 31, 2010. SSAP Nos. 5R and 35R must be used to prepare all financial statements filed with the Department for reporting periods beginning on or after December 31, 2011, and January 1, 2011, respectively.

The following paragraphs provide a brief summary as well as an analysis of the reasons for the amendments.

Amendments to §7.18(a) replace the reference to the March 2008 Manual with the reference to the March 2010 Manual and replace the word “additions” with the word “modifications.” These amendments are necessary to clarify that

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the March 2010 version of the Manual, including the exceptions and modifications specified in §7.18(c) and (d), 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 Department rules of the Department.

Under the amendments to §7.18(b), the Commissioner adopts by reference the March 2010 version of the Manual, with the exceptions and modifications specified in subsections (c) and (d), as the source of accounting principles for the Department when analyzing financial reports and for conducting statutory examinations and rehabilitations of insurers and HMOs licensed in Texas, except where otherwise provided by law. The amendments to §7.18(b) also provide that except for new SSAP Nos. 5R and 35R, the March 2010 version of the Manual, as well as the exceptions and modifications specified in subsections (c) and (d), are required to be (i) applied to examinations conducted as of December 31, 2010, and thereafter; and (ii) used to prepare all financial statements filed with the Department for reporting periods ending on or after December 31, 2010. Under the amendments to §7.18(b), SSAP Nos. 5R and 35R must be (i) applied to examinations conducted as of December 31, 2011, and January 1, 2011, respectively, and thereafter; and (ii) 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.

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These amendments are necessary to clarify the purpose and application of the updated Manual.

Under the amendments to §7.18(c), the Commissioner adopts the exceptions and modifications to the Manual that are specified in §7.18(c)(1) and (2). The amendments provide that except for new SSAPs Nos. 5R and 35R, these exceptions and modifications must be (i) applied to examinations conducted as of December 31, 2010, and thereafter, and (ii) used to prepare all financial statements filed with the Department for reporting periods ending on or after December 31, 2010. Under the amendments to §7.18(c)(1)(A), the following substantively revised SSAPs are adopted by reference: SSAPs Nos. 5R, 35R, and 91R. SSAP No. 5R, which was adopted by the NAIC in October 2010, was revised to include guidance for accounting guarantees that are issued to other entities. SSAP No. 5R is adopted to be effective on December 31, 2011, and must be used to prepare all financial statements filed with the Department for reporting periods beginning on or after December 31, 2011. SSAP No. 35R, which was adopted by the NAIC in October 2010, was revised to eliminate the non-admission criteria for accrued guaranty fund assessments, to incorporate new disclosures for assets, and to include transition guidance for assets. SSAP No. 35R was adopted by the NAIC to be effective on January 1, 2011, and must be used to prepare all financial statements filed with the Department for reporting periods beginning on or after January 1, 2011. SSAP No. 91R, which was adopted by the NAIC in August 2010, specifies updated securities lending

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accounting, reporting, and disclosures. SSAP No. 91R is effective on December 31, 2010, and must be used to prepare all financial statements filed with the Department for reporting periods beginning on or after December 31, 2010. The amendments to §7.18(c)(1)(A) also delete references to SSAP Nos. 98 and 99 because SSAP Nos. 98 and 99 are included in the March 2010 version of the Manual. Additionally, a non-substantive amendment to §7.18(c)(1)(A) deletes from the existing rule the redundant phrase “filed with the Department.” Under amendments to §7.18(c)(1)(B), the Commissioner adopts by reference non-substantive modifications to SSAP Nos. 9, 43R, 90, 100, and 10R, and Issue Paper No. 99 issued by the NAIC in calendar year 2010. These non-substantive modifications clarify language or change disclosures, appendices, or other material referenced in SSAPs already included in the March 2010 version of the Manual. The amendments to §7.18(c)(1)(B) also delete references to the non-substantive modifications to SSAP Nos. 5, 15, 21, 22, 26, 30, 32, 40, 41, 43, 48, 52, 54, 55, 63, 65, 68, 86, and 91, and to the Preamble section of the Manual because the March 2010 version of the Manual includes all of these with the non-substantive modifications. The amendments to §7.18(c)(1)(C) delete references to Actuarial Guidelines 43, 44, and 45, and revisions to Actuarial Guidelines 34 and 39 because these guidelines are included in the March 2010 version of the Manual.

Amendments to §7.18(a), (b), (c), and (c)(2) replace the word “additions” with the word “modifications.” These amendments are necessary to classify

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more accurately the provisions adopted under §7.18(a), (b), (c), and (c)(2). An amendment to §7.18(c)(1) replaces the words “additions and exceptions” with the word “modifications.” This amendment is necessary to classify more accurately the provisions adopted under §7.18(c)(1).

Additionally, amendments to §7.18(e) add the phrases “and obtain approval prior to using the accounting deviation in a financial statement” and “that is proposed to be.” Therefore, §7.18(e) as adopted reads in pertinent part: “In the event a domestic insurer desires to deviate from the accounting guidance in a Texas statute or any applicable regulation, the insurer shall file a written request for a permitted accounting practice *and obtain approval prior to using the accounting deviation in a financial statement.* Such filing shall be made with the Senior Associate Commissioner of the Financial Program, Texas Department of Insurance, . . . at least 30 days before filing the financial statement *that is proposed to be* affected by the deviated accounting practice.” These two amendments are necessary to clarify that a domestic insurer must both timely file a written request for a permitted practice and receive the Department’s approval prior to using the accounting deviation in a financial statement. A third amendment to §7.18(e) also add the phrase “of the Financial Program” to clarify that written requests for a permitted practice must be filed with the Senior Associate Commissioner of the Financial Program.

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3. HOW THE SECTION WILL FUNCTION. The amendments to §7.18(a) clarify that the purpose of this section is to adopt the March 2010 version of the Manual and the exceptions and modifications set forth in subsections (c) and (d) of this section with deference to Texas statutes and regulations. The amendments to §7.18(b) adopt by reference the March 2010 version of the Manual, with the exceptions and modifications set forth in subsections (c) and (d). Additionally, the amendments to §7.18(b) clarify the purpose and applicability of the updated Manual. The amendments to §7.18(b) provide that except for new SSAP Nos. 5R and 35R, the March 2010 version of the Manual, as well as the exceptions and modifications specified in subsections (c) and (d), are required to be (i) applied to examinations conducted as of December 31, 2010, and thereafter; and (ii) used to prepare all financial statements filed with the Department for reporting periods ending on or after December 31, 2010. Under the amendments to §7.18(b), SSAP Nos. 5R and 35R must be (i) applied to examinations conducted as of December 31, 2011, and January 1, 2011, respectively, and thereafter; and (ii) 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. The adopted version of the Manual, combined with the SSAPs adopted by reference in subsection (c)(1), include substantially all SSAPs and modifications to the SSAPs adopted by the NAIC through December 31, 2010. Additionally, amendments to §7.18(a), (b), (c), (c)(1), and (c)(2) more accurately describe the provisions adopted under

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§7.18(a), (b), and (c) as “modifications.” Also, amendments to §7.18(e) clarify that a domestic insurer must both timely file a written request for a permitted practice and receive the Department’s approval prior to using the accounting deviation in a financial statement. Another amendment to §7.18(e) clarifies that written requests for a permitted practice must be filed with the Senior Associate Commissioner of the Financial Program.

4. SUMMARY OF COMMENTS AND AGENCY RESPONSE. The Department did not receive any comments on the published proposal.

5. STATUTORY AUTHORITY. The amendments are adopted under the Insurance Code Chapters 32, 401, 404, 421, 425, 426, 441, 802, 823, 841, 843, 861, 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

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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, as necessary to obtain an accurate indication of the company's condition and method of transacting business, to change the form of any annual statement required to be filed by any kind of insurance company. 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 as are necessary to carry out the provisions of Chapter 843 of the Insurance Code (Health Maintenance Organizations). Section 843.155 requires a health maintenance organization to file an annual report with the Commissioner, which shall include a financial statement of the health maintenance organization 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

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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 Texas Department of Insurance under the Insurance Code and other laws of this state.

6. 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 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 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 shall refer to the sources in paragraphs (1) - (6) of this subsection in the respective order of priority listed.

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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; 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) Texas statutes;

(2) department rules;

(3) directives, instructions, and orders of the Commissioner;

(4) the Manual;

(5) other NAIC handbooks, manuals, and instructions, adopted by the department; and

(6) Generally Accepted Accounting Practices.

(b) The Commissioner adopts by reference the March 2010 version of the Manual, with the exceptions and modifications set forth in subsections (c) and (d)

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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 Manual that is adopted by reference with the exceptions and modifications specified in subsections (c) and (d) of this section 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.

(c) The Commissioner adopts the 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

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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;

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(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:

(A) Settlement requirements for intercompany transactions are subject to the accounting treatment in Statement of Statutory Accounting Principles (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 such balances shall be nonadmitted.

(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.

(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

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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. 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.

(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. 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.

(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) A farm mutual insurance company, statewide mutual assessment company, local mutual aid association, or mutual burial association that has less than \$6 million in annual direct written premiums need not comply with the Manual.

(e) In the event a domestic insurer desires to deviate from the accounting guidance in a Texas statute or any applicable regulation, the insurer shall file a written request for a permitted accounting practice and obtain approval prior to using the accounting deviation in a financial statement. Such filing shall be made with the Senior Associate Commissioner of the Financial 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 shall not use deviated accounting practice without the department's prior approval.

(f) This section shall not be construed to either broaden or restrict the authority provided under the Insurance Code to insurers, including health maintenance organizations.

CERTIFICATION. This agency hereby certifies that the adopted amendments have been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority.

Issued at Austin, Texas, on December 15 2010.


Gene C. Jarmor
General Counsel and Chief Clerk

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IT IS THEREFORE THE ORDER of the Commissioner of Insurance that amendments to §7.18 specified herein, concerning the adoption by reference of the *Accounting Practices and Procedures Manual*, are adopted.

AND IT IS SO ORDERED.



MIKE GEESLIN
COMMISSIONER OF INSURANCE

ATTEST:



Gene C. Jarmon
General Counsel and Chief Clerk

COMMISSIONER'S ORDER NO. **10-1083**
DEC 15 2010