



June 5, 2015

Memorandum

To: Members of the Board

Robin M. Gilliam

From: Robin M. Gilliam, Assistant Director

Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subject: Risk Assumed—Insurance Programs [Phase 1]—**TAB E**¹

MEETING OBJECTIVE

Review the revised proposed standards to:

1. finalize the measurement guidance for estimating expected losses on remaining coverage, and
2. approve insurance categories.

BRIEFING MATERIALS

This memo discusses revisions to the risk assumed—insurance program draft proposed standards and attachment:

- Attachment I: Proposed Insurance Standards with track changes
- Appendix A: Risk Assumed - Project Decision History and Milestones (Optional Reading for Reference)

¹ The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

BACKGROUND

Staff continued to review the updated proposed insurance standards at the April 2015 Board meeting.

The Board approved the following items:

- The adverse event and IBNR definitions in order to clarify the recognition and measurement of claims incurred but not recorded (IBNR).
- The wording...*“Estimates should be based on...using all available information that existed at the balance sheet date, experience with previous transactions and historical trends, and, as appropriate, the views of independent experts...”* in the recognition and measurement of the liability for losses on remaining coverage.

The Board identified the following changes:

- Liability for unpaid losses: provide more clarity about the timing of a series of events to address the recognition and measurement of IBNR.
- Liability for losses on remaining coverage:
 - Update subsequent event disclosure requirement in reference to SFFAS 39 because events that happen after the balance sheet are subsequent events that will not be recognized.
 - Remove expected cash flows as a single measurement model and replace it with wording such as...*probability assessments affected by trends to determine the most likely estimate, or, if a most likely estimate is not available, then use the expected cash flow method.*
 - Avoid using the word “contingency”—which will remain in SFFAS 5—because this liability is comparing the estimated losses to unearned premiums, whereas SFFAS 5 speaks only to liabilities.
- Premium pricing disclosure: remove the word subsidy and subsidy rate, reword, and provide an illustration.
- “Condensed” insurance program disclosure: reference disclosures that are already available in audited financial statements.
- Consolidated Financial Report disclosures: remove unearned premiums and gross claims and related earned revenue, and reword information about insurance in force.

STAFF ANALYSIS AND RECOMMENDATIONS FOR PROPOSED STANDARDS**I. Recognition and Measurement for Estimated Losses on Remaining Coverage:****Staff Analysis:**

During the February 2015 meeting, the Board agreed that expected losses on remaining coverage should be based on expected cash flows which will naturally determine an appropriate estimate through a prescribed method.

As a result, the following was presented at the April 2015 meeting:

23. *Estimates should be based on expected cash flows using all available information that existed at the balance sheet date, experience with previous transactions and historical trends, and as appropriate, and the views of independent experts. Therefore, expected cash flows should not be adjusted based on actual events that occur subsequent to the balance sheet date that were not estimable using information that existed at the balance sheet date.*

However, some Board members did not agree with expected cash flows as the only method for estimating expected losses on remaining coverage and requested that staff include first a most likely amount, and then expected cash flows as an alternative.

Staff was directed to use wording similar to that found in the FASB proposed revenue standards (606-10-32-8) as a model for drafting these standards:

FASB 606-10-32-8: *An entity shall estimate an amount of variable consideration by using either of the following methods, depending on which method the entity expects to better predict the amount of consideration to which it will be entitled: [ASU 2014-09, paragraph 5]]*

a. The expected value—the expected value is the sum of probability-weighted amounts in a range of possible consideration amounts. An expected value may be an appropriate estimate of the amount of variable consideration if an entity has a large number of contracts with similar characteristics.

B. The most likely amount—the most likely amount is the single most likely amount in a range of possible consideration amounts (that is, the single most likely outcome of the contract). The most likely amount may be an appropriate estimate of the amount of variable consideration if the contract has only two possible outcomes (for example, an entity either achieves a performance bonus or does not).

In addition, there was a significant discussion about the timing of subsequent events in determining losses on remaining coverage. The Board agreed that only information that exists at the balance sheet date would be included, but events occurring between the reporting and publication date should be disclosed. Staff addressed this in the below update.

The Board also agreed to include a standard that discounts claims that will take several years to settle. Staff addressed this in the below update.

Staff Recommendation:

Utilizing the above noted FASB model and the Board's recommendations/approvals, staff is providing the following two options for measurement guidance for losses on remaining coverage:

Option 1: Direct Use of Expected Cash Flow If a Best Estimate is Not Feasible

24. Insurance programs should use all available information existing at the balance sheet date, experience with previous transactions, trends, and, as appropriate, the views of independent experts to estimate the amount necessary to settle claims during the remaining open contract period.
25. The estimate should be the best estimate of the likely outcome. If no amount is a better estimate than another, the expected cash flow method should be used.²

Option 2: Either a Best Estimate or Expected Cash Flows Approach Based on Circumstances

24. Insurance programs should use all available information existing at the balance sheet date, experience with previous transactions, trends, and, as appropriate, the views of independent experts to estimate the amount necessary to settle claims during the remaining open contract period.
25. The estimate should be made using whichever of the following methods would best represent the amount:
 - a. The most likely amount—the most likely amount is based on the likely outcome from all possible outcomes, or
 - b. The expected cash flows—the expected cash flows is the sum of probability weighted amounts in a range of possible amounts.

² The expected cash flow is the sum of probability-weighted amounts in a range of possible amounts.

The paragraphs below would follow either of the above options to complete the recognition and measurement guidance:

26. Adverse events occurring after the balance sheet date but before the financial report is issued are considered subsequent events. Nonrecognized events consist of those subsequent events that provide evidence with respect to conditions that did not exist at the end of the reporting period, but arose subsequent to that date. Adverse events occurring after the reporting period for which no information existed at the balance sheet date should be treated as nonrecognized events and should be considered for disclosure in accordance with SFFAS 39,³ par.15.

27. If the effect of the time value of money is significant, for example, when settlement may occur over several years, then the estimated settlement amount should be discounted. (See SFFAS 33,⁴ par. 28 - 32 for guidance on selecting discount rates.)

Question I: Does the Board approve Option 1 or Option 2 for the measurement guidance for estimating losses on remaining coverage?

³ SFFAS 39: *Subsequent Events: Codification of Accounting and Financial Reporting Standards Contained in the AICPA Statement on Auditing Standards*

⁴ SFFAS 33: *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*

II. Categories for Insurance Programs:

Staff Analysis and Recommendation:

Staff recommends the following categories for insurance programs:

- A. Exchange revenue insurance programs other than life insurance
- B. Nonexchange revenue insurance programs
- C. Life Insurance

Note: Some members have suggested that we classify insurance programs by short- and long-duration categories. The following analysis explains why the above list is more efficient and effective than only separating into short- and long-duration contracts:

A. Exchange revenue insurance programs other than life insurance:

This category includes insurance programs, other than life insurance, that collect revenue through contracts⁵ in exchange for the Government promising to make payments to program participants if adverse events occur.⁶

The following is an example of programs that are included in this category:

Program	Contract/Agreement Length
Crop Insurance (RMA)	12 months
Federal Deposit Insurance Corporation (FDIC)	Annual assessments
Flood Insurance (FEMA)	12 months, some 36 months
Overseas Private Investment Corporation (OPIC)	12 months up to multiple years
Pension Benefit Guaranty Corporation (PBGC)	Annual = premium plan year
Traumatic Servicemembers' Group Life Injury-TSGLI (VA/DOD)	Automatic enrollment with Servicemembers' Group Life Injury-SGLI for additional \$1 a month premium.

⁵ The proposed standards define insurance contract (contract) as follows: *An "insurance contract (contract)" is a general term used for an explicit insurance or non-loan guarantee agreement or arrangement between an insurance program and specific parties such as but not limited to: individuals, state, local, or foreign governments, other federal agencies, or businesses. A contract may include and/or identify...*

⁶ SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, Appendix B, page 84, paragraph 284.

This category is more efficient and effective than separate categories for short- and long-duration agreements/contracts because the standards will:

1. focus attention on the substance of the contract or agreement which—except for life insurance—is likely the same regardless of the duration of the contract,
2. also focus attention on substance by disclosing by portfolios, as noted in par. 27 below, because portfolios provide a vehicle for reporting entities to distinguish and aggregate their short-duration contracts from their long-duration contracts,

Par 27: Specific information **should be disclosed for selected insurance portfolios**, and/or in aggregate for all remaining insurance portfolios, and/or insurance contracts. Selecting insurance portfolios to be presented individually requires judgment. Quantitative and qualitative criteria should be considered in selecting individual portfolios for disaggregated disclosure.

Footnote 4: Portfolios are groupings of insurance programs or contracts that have some meaningful relationship. The groupings may be based on **contract period/duration**, shared risks, management, customers, geographic regions, or other factors.

3. adequately address the greater uncertainty with long-duration contracts through the proposed methods for estimating losses on remaining coverage,
4. avoid arbitrary cutoffs between short- and long-durations which are subjective to each program, and
5. avoid repeating the exact same standards in two categories.

B. Nonexchange revenue insurance programs:

Staff recommends this category because there are insurance programs that collect nonexchange revenue as **demand by the government** instead of within an explicit agreement/contract. In addition, because there are no explicit contracts, there are no contract periods for which to capture losses for remaining coverage.

The following is an example of programs that are included in this category:

Program	Nonexchange Revenue Collected
National Vaccine Injury Compensation Program (HHS-HRSA)	75 cent excise tax on each vaccine sold
Terrorism Risk Insurance Act (Treasury-TRIA)	Mandatory recoupment of the Federal share of compensation through policyholder surcharges

According to SFFAS 5...For federal nonexchange transactions, a liability should be recognized for any unpaid amounts due as of the reporting date...⁷ and therefore, these programs will only recognize adverse events that have happened as of the balance sheet date in the liability for unpaid claims. [Note that SFFAS 39 provides guidance for subsequent events. Nonrecognized events may still result in disclosure under SFFAS 39.]

Because nonexchange transactions under SFFAS 5 general principles would only recognize liabilities for unpaid claims, the standards should be captured in a distinct category and remain consistent with the general principles.

Question II.B – Does the Board approve the nonexchange revenue insurance programs category?

⁷ SFFAS 5, *Accounting for Liabilities of The Federal Government*, page 14, par. 24

C. Life Insurance

Staff recommends including life insurance programs in a separate category because their risk profile is very different from the non-life insurance programs.

The following is an example of programs that are included in this category:

Life Insurance Programs	Acronym	Description
VA:		
National Service Life Insurance Fund	NSLI	For World War II era Veterans
Service-disabled Veterans Insurance Fund	SDVIF	For Veterans separated on or after Apr. 25, 1951 who receive a service-connected disability rating
Service members' Group Life Insurance Fund	SGLI	For members of the Uniformed Services on active duty and Ready reservists
United States Government Life Insurance	USGLI	For Veterans who served in World War I and through October 8, 1940
OPM: Federal Employee Group Life Insurance	FEGLI	For federal employees

Unlike the non-life exchange/nonexchange insurance programs that cover the risk of personal and property damage from an adverse event, “the main purpose of life insurance is to cover the risk of dying too early, or in the case of annuities, the risk of living too long.”⁸

In addition, because life insurance programs will always pay out losses upon death (the adverse event), unlike non-life exchange and nonexchange insurance programs that might not experience an adverse event and loss payout at all during a contract period, life insurance should be a separate and distinct category of standards.

Question II.C: Does the Board approve the life insurance category for insurance programs?

⁸ An Introduction to the Insurance Industry: Insurance Facts and Stats, 2011 edition by A.M. Best Company.

QUESTIONS FOR THE BOARD:

Question I: Does the Board approve Option 1 or Option 2 for the measurement guidance for estimating losses on remaining coverage?

Question II.A: Does the Board approve the exchange revenue insurance programs other than life insurance category?

Question II.B: Does the Board approve the nonexchange revenue insurance programs category?

Question II.C: Does the Board approve the life insurance category for insurance programs?

NEXT STEPS

Continue developing the proposed exposure draft for insurance programs. If approved, develop the life insurance category standards.

MEMBER FEEDBACK

Please contact me as soon as possible to convey your questions or suggestions. Communication before the meeting will help me to prepare answers to your questions in order to make the meeting more productive. You can contact me by telephone at 202-512-7356 or by e-mail at gilliamr@fasab.gov with a cc to paynew@fasab.gov

TAB E
– Attachment 1–

Risk Assumed—Insurance Programs

Updated Proposed Standards

1 **PROPOSED STANDARDS**

2 **SCOPE**

- 3 1. This Statement applies to federal entities that present general purpose federal financial
 4 reports (GPFFRs), including the consolidated financial report of the U.S. Government
 5 (CFR), in conformance with generally accepted accounting principles (GAAP), as defined
 6 by paragraphs 5 through 8 of Statement of Federal Financial Accounting Standards
 7 (SFFAS) 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the*
 8 *Application of Standards Issued by the Financial Accounting Standards Board.*
- 9 2. This Statement provides general principles that should guide preparers of GPFFRs in
 10 accounting for and reporting on premium revenue, related claims and liabilities, and
 11 losses and costs of insurance programs. Items such as revenue types, direct loans and
 12 loan guarantees, borrowing, investing, and/or appropriations used not addressed in this
 13 Statement should be reported in accordance with other standards.
- 14 3. This Statement rescinds the section: Insurance and Guarantee Programs in Federal
 15 Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of The Federal*
 16 *Government*, paragraphs 97-121.

17 **DEFINITIONS**

- 18 4. **Insurance program**—“Insurance program”¹ is used broadly to refer to a program that is
 19 authorized by law to financially compensate a designated population of beneficiaries by
 20 accepting all or part of the risk for losses incurred as a result of an adverse event.
- 21 5. The following are excluded from Insurance Programs:
- 22 a. Programs that administer direct loans and loan guarantees²
 - 23 b. Programs that qualify as social insurance³
 - 24 c. Programs authorized to engage in disaster relief activities⁴
 - 25 d. Entitlement programs⁵
 - 26 e. Programs that self-insure their own activities, but whose missions are not by
 27 statute to provide insurance⁶
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¹ An insurance program is hereinafter referred to as either insurance program or program
² Programs identified in SFFAS 2: *Accounting for Direct Loans and Loan Guarantees*
³ Programs identified in SFFAS 1): *Accounting for Social Insurance* including unemployment insurance.
⁴ The Robert T. Stafford Disaster Relief and Emergency Assistance Act (Public Law 100-707), commonly referred to as the Stafford Act, is the act that authorizes and regulates disaster relief programs.
⁵ Terms defined in the Glossary are shown in **bold-face** the first time they appear.
⁶ GAO-05-265R, *Catalogue of Federal Insurance Activities, Enclosure IV: Description of Accounts With Federal Self-Insurance Activity*

- f. Programs that process claims through an administrative or judicial process, but whose missions are not by statute to provide insurance⁷
- g. Programs that provide security against loss or damage through contractual indemnification of another party, but whose missions are not by statute to provide insurance⁸

6. Adverse event—an “adverse event” may be a single-occurring event or a series of events that cause losses to the beneficiary(ies) as identified in the insurance contract.

7. Claim adjustment expenses (CAE)—“Claim adjustment expenses (CAE)” are incremental costs directly attributable to investigating, settling, and/or adjusting claims. An incremental cost is one that can result only when claims have been incurred. CAE include but are not limited to legal and adjuster’s fees. CAE may be incurred through work performed by federal employees and/or contractors.

8. Contract period—“Contract period” is the period over which adverse events that occur are covered.

9. In Force—“In force” refers to contracts that are unexpired as of a given date.

10. Incurred but not reported (IBNR)—“Claims incurred but not reported (IBNR)” are estimated claims from adverse events that have occurred as of the end of the reporting period but have not yet been reported to the insurance program for settlement.

11. Insurance claim—an “insurance claim” is a formal request for payment for losses as authorized under the insurance contract.

12. Insurance contract (contract)— An “insurance contract (contract)” is a general term used for an explicit insurance or non-loan guarantee agreement or arrangement between an insurance program and specific parties such as but not limited to: individuals, state, local, or foreign governments, other federal agencies, or businesses. A contract may include and/or identify:

- a. the term the insurance contract is in force,
- b. the insurance program’s responsibilities,
- c. the risk assumed by the insurance program, such as:
 - i. all risk for covered losses,
 - ii. partial risk by filling a gap where commercial Insurance companies are not able or willing to provide the insurance, or
 - iii. a timing risk wherein the insurance program provides compensation for losses in anticipation that future funding sources will be sufficient to cover all or part of past benefits paid.
- d. the adverse event,
- e. the insured party(ies) and their premium requirements,
- f. the beneficiary(ies) and their responsibilities for filing claims, and/or

⁷An example may include an administrative settlement or tort claim resulting from military events.

⁸These are administrative settlements for transactions occurring by contractors with Federal Acquisition Regulation authorized indemnification clauses or first responders within programs that do not have a statutory insurance or guarantee mission.

g. the financial compensation.

13. Liability for Losses on Remaining Coverage—the “liability for losses on remaining coverage” is an accrued obligation to beneficiaries attributable to coverage of insured events anticipated to occur after the end of the reporting period through the open contract period.

14. Premiums—“Premiums” is a general term used to refer to exchange revenue⁹ billed by insurance programs. Programs may refer to their exchange revenue by various terms including but not limited to premiums, assessments, and/or fees.

15. Recoveries—“Recoveries” include monies recouped or recovered from:

- a. another agency through an indemnification agreement,
- b. a third party or commercial insurance company to repay all or part of a loss originally paid for by the program,
- c. the sale of salvageable parts through acquisition and disposal or salvage of assets, and/or
- d. adjustments to previously paid insurance claims.

**EXCHANGE REVENUE INSURANCE PROGRAMS
OTHER THAN LIFE INSURANCE**

RECOGNITION AND MEASUREMENT

REVENUE AND LIABILITY FOR UNEARNED PREMIUMS

16. Premiums should be recognized as revenue evenly over the contract period.

17. A liability for unearned premiums should be recognized for the amount of premiums collected and/or due by the end of the reporting period that have not yet been earned in proportion to the insurance protection to be provided during the remaining contract period.

LIABILITY FOR UNPAID INSURANCE CLAIMS

18. A liability for unpaid insurance claims should be recognized for adverse events that occurred before the end of the reporting period. The liability should be initially recorded at the estimated settlement amount and remeasured at the end of each reporting period.

⁹ See SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*; page 14, par. 33 for the exchange revenue definition, and Appendix B *Guidance for the Classification of Transactions*, page 84, par.284 for the classification for exchange revenue insurance programs.

- 1 19. The estimated settlement amount includes:
 2 a. outflows to liquidate:
 3 i. claims that have been reported but not paid,
 4 ii. claims incurred but not reported (IBNR),
 5 1. A series of events causing loss must be completed by the end of
 6 the reporting period to be considered an adverse event of the
 7 reporting period.¹⁰
 8 2. Management should use judgement to determine if an adverse
 9 event creates an IBNR prior to the reporting date.
 10 b. related estimated claim adjustment expenses, and
 11 c. estimated inflows from recoveries not realized at the end of the reporting period.
 12 i. If estimated recoveries exceed the related claims for a group of
 13 contracts then recognition is limited to the amount of the related
 14 claims.¹¹
 15 ii. Recoveries should be recognized as reductions of claims, rather than
 16 as revenue.
 17 20. Adjustments to the liability for unpaid insurance claims, other than those resulting from
 18 payments made to liquidate existing liability balances, should be recognized as claims
 19 expense.

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20 LIABILITY FOR LOSSES ON REMAINING COVERAGE

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 22 21. A liability for losses on remaining coverage should be recognized if the estimated amount
 23 to settle claims for the remaining open contract period, is greater than the related
 24 unearned premiums as of the end of the reporting period.
 25 22. Estimates should be determined by considering groups of contracts rather than individual
 26 contracts, when feasible.
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Deleted: expected cash flows¹²

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¹⁰ If a series of events causing loss begins prior to the reporting date, and additional pending events are required to result in losses, then it is not considered an adverse event and should not be included in the estimated settlement costs for IBNR.

¹¹ Any amount expected to be recovered in excess of the recognized claim, which will result in a gain, should not be recognized until any contingencies relating to the recovery have been resolved because a contingent gain cannot be recognized until realized.

1 **23. Memo Question 1 – Does the Board approve Option 1 or Option 2 for the**
 2 **measurement guidance for estimating losses on remaining coverage?**

Option 1: Direct Use of Expected Cash Flow If a Best Estimate is Not Feasible

1. Insurance programs should use all available information existing at the balance sheet date, experience with previous transactions, trends, and, as appropriate, the views of independent experts to estimate the amount necessary to settle claims during the remaining open contract period.
2. The estimate should be the best estimate of the likely outcome. If no amount is a better estimate than another, the expected cash flow method should be used.¹

Option 2: Either a Best Estimate or Expected Cash Flows Approach Based on Circumstances

24. Insurance programs should use all available information existing at the balance sheet date, experience with previous transactions, trends, and, as appropriate, the views of independent experts to estimate the amount necessary to settle claims during the remaining open contract period.
25. The estimate should be made using whichever of the following methods would best represent the amount:
 - a. The most likely amount—the most likely amount is based on the likely outcome from all possible outcomes, or
 - b. The expected cash flows—the expected cash flows is the sum of probability weighted amounts in a range of possible amounts.

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5 **24. Adverse events occurring after the balance sheet date but before the financial report is**
 6 **issued are considered subsequent events. Nonrecognized events consist of those**
 7 **subsequent events that provide evidence with respect to conditions that did not exist at**
 8 **the end of the reporting period, but arose subsequent to that date. Adverse events**
 9 **occurring after the reporting period for which no information existed at the balance sheet**
 10 **date should be treated as nonrecognized events and should be considered for disclosure**
 11 **in accordance with SFFAS 39,¹³ par.15.**

Deleted: <#>Estimates should be based on expected cash flows using all available information that existed at the balance sheet date, experience with previous transactions and historical trends, and as appropriate, the view of independent experts. Therefore, expected cash flows should not be adjusted based on actual events that occur subsequent to the balance sheet date that were not estimable using information that existed at the balance sheet date.¶¶ <#>¶¶

Deleted: using all available information that existed at the balance sheet date, experience with previous transactions and historical trends, and, as appropriate, the views of independent experts. Therefore, **expected cash flows** should not be adjusted based on actual events that occur subsequent to the balance sheet date that were not estimable using information that existed at the balance sheet date.

¹³ SFFAS 39: Subsequent Events: Codification of Accounting and Financial Reporting Standards Contained in the AICPA Statement on Auditing Standards

1 **25.** ~~If the effect of the time value of money is significant, for example, when settlement may~~
 2 ~~occur over several years, then the estimated settlement amount should be discounted.~~
 3 ~~(See SFFAS 33,¹⁴ par. 28 - 32 for guidance on selecting discount rates.)~~

Deleted: The expected cash flows should be discounted, unless the effect of the time value of money is not significant.

4 **26.** Adjustments to the liability for losses on remaining coverage should be recognized as
 5 losses or gains over the remaining insurance coverage.

6 **COMPONENT REPORTING ENTITY DISCLOSURE REQUIREMENTS**

7 **27.** Specific information should be disclosed for selected insurance portfolios,¹⁵ and/or in
 8 aggregate for all remaining insurance portfolios, and/or insurance contracts. Selecting
 9 insurance portfolios to be presented individually requires judgment. Quantitative and
 10 qualitative criteria should be considered in selecting individual portfolios for
 11 disaggregated disclosure.

12 **28.** Acceptable quantitative criteria may include whether certain groups of contracts are
 13 accumulating large claim expenses or unpaid claim liability balances.

14 **29.** Acceptable qualitative factors may include whether a group of contracts is of immediate
 15 concern to constituents, politically sensitive, and/or controversial.

16 **30.** The following information should be provided for insurance portfolios selected for
 17 disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or
 18 insurance contracts:

19 **a.** A description of what is insured ~~or guaranteed, for whom, and what other~~
 20 ~~government agencies and/or commercial insurance programs administer or~~
 21 ~~assume risk for any part of the program.~~

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22 **b.** Contract duration.

23 **c.** A narrative description of the sources of revenue, such as premiums received
 24 from insureds, non-exchange revenue such as fines or fees, and/or
 25 appropriations

26 **d.** Renewal characteristics such as non-cancelable or guaranteed renewals.

27 **e.** Premium pricing policies (in accordance with SFFAS 7, par. 46) including:

28 **i.** risk characteristics used in determining premiums, and

29 **ii.** requirements to set premium prices that ~~do not cover the full estimated~~
 30 ~~cost to settle claims.~~

Deleted: are not based on full cost or on market price and as a result the premiums that

¹⁴ SFFAS 33: *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*

¹⁵ Portfolios are groupings of insurance programs or contracts that have some meaningful relationship. The groupings may be based on contract period/duration, shared risks, management, customers, geographic regions, or other factors.

- 1 f. A discussion about the liability for losses on remaining coverage to include:
- 2 i. The basis and methods, trend information, and risk assumptions and
3 factors used in determining the estimated settlement costs.
- 4 ii. Subsequent events. (See SFFAS 39, par. 15 for guidance on non-
5 recognized subsequent events)
- 6 iii. Any additional information that would provide an understanding of the
7 nature and magnitude of uncertainty in calculating the liability for losses
8 on remaining coverage.
- 9 g. The amount of coverage provided through insurance in force at the end of the
10 reporting period, including:
- 11 i. A narrative discussion that this amount represents the maximum risk
12 exposure during the remaining contract period, and
- 13 ii. Appropriate information to aid in avoiding the misleading inference that
14 there is a more than remote likelihood of a loss of that amount.
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- 16 **31.** The following information¹⁶ should be provided for insurance portfolios selected for
17 disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or
18 insurance contracts for:
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- 20 a. Gross cost:
- 21 i. Claims expense
- 22 ii. Claims adjustment expense
- 23 iii. Recoveries
- 24 iv. Interest expense
- 25 v. Losses or gains on remaining coverage
- 26 vi. Other gross costs
- 27 b. Total gross cost
- 28 c. Earned Revenue
- 29 i. Premiums earned
- 30 ii. Interest earned
- 31 d. Total Earned Revenue
- 32 e. Net cost
- 33 i. Nonexchange revenue
- 34 ii. Appropriations used
- 35 iii. Other financing sources
- 36 f. Change in net position

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Deleted: mean distribution of possible cash flows for future losses included in the liability for losses on remaining coverage, as well as the high and low amounts in the distribution.

Comment [RG1]: April 2015 BM decided to remove this section because this information is captured elsewhere in audited FS.

Deleted: <#>Information should be provided for insurance portfolios selected for disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or insurance contracts about balances at the end of the reporting period, including at a minimum balances for: ¶
<#>Investments in Treasury securities, ¶
<#>Total Assets ¶
<#>Outstanding debt (borrowing), ¶
<#>Liabilities for: ¶
<#>Unearned premiums, ¶
<#>Unpaid claims, and ¶
<#>Losses on remaining insurance coverage. ¶
<#>Total Liabilities ¶
<#>Unexpended appropriations ¶
<#>Cumulative results of operations ¶

¹⁶ See Illustration I for an example.

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- 32. Changes in the liability balance for unpaid insurance claims should be provided for insurance portfolios selected for disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or insurance contracts as follows:
 - a. Beginning balance
 - b. Incurred claims attributable to insured adverse events of:
 - i. the current fiscal year, and
 - ii. prior fiscal years
 - c. Payments attributable to insured adverse events of:
 - i. the current fiscal year, and
 - ii. prior fiscal years
 - d. Recoveries and other adjustments
 - e. Ending balance
 - 33. A narrative discussion consolidated for all insurance portfolios—or a reference to one to avoid duplication of disclosures—should be provided for:
 - a. borrowing authority including but not limited to: balances, interest expense, repayment requirements, the ability to repay borrowing used to fund insurance claims, financing sources for repayment, and other terms of borrowing authority used in accordance to already existing standards.
 - b. investment activities,
 - c. appropriations requested, used, and/or available to return to Treasury, and
 - d. any event(s) that caused a material change in the required disclosures, such as low probability high impact adverse events, changes in laws and/or actuarial assumptions.

26 **NONEXCHANGE REVENUE INSURANCE PROGRAMS**

27 **RECOGNITION AND MEASUREMENT**

28 **LIABILITY FOR UNPAID INSURANCE CLAIMS**

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- 34. A liability for unpaid insurance claims should be recognized for adverse events that occurred before the end of the reporting period. The liability should be initially recorded at the estimated settlement amount and remeasured at the end of each reporting period.

1 35. The estimated settlement amount includes:

2 a. outflows to liquidate:

3 i. claims that have been reported but not paid,

4 ii. claims incurred but not reported (IBNR).

5 1. A series of events causing loss must be completed by the end of
 6 the reporting period to be considered an adverse event of the
 7 reporting period.¹⁷

8 2. Management should use judgement to determine if an adverse
 9 event creates an IBNR prior to the reporting date.

10 b. related estimated claim adjustment expenses, and

11 c. estimated inflows from recoveries not realized at the end of the reporting period.

12 i. If estimated recoveries exceed the related claims for a group of contracts
 13 then recognition is limited to the amount of the related claims.¹⁸

14 ii. Recoveries should be recognized as reductions of claims, rather than as
 15 revenue.

16 36. Adjustments to the liability for unpaid insurance claims, other than those resulting from
 17 payments made to liquidate existing liability balances, should be recognized as claims
 18 expense.

19 **COMPONENT REPORTING ENTITY DISCLOSURE REQUIREMENTS**

20 37. Specific information should be disclosed for selected insurance portfolios, and/or in
 21 aggregate for all remaining insurance portfolios, and/or insurance contracts. Selecting
 22 insurance portfolios to be presented individually requires judgment. Quantitative and
 23 qualitative criteria should be considered in selecting individual portfolios for
 24 disaggregated disclosure.

25 38. Acceptable quantitative criteria may include whether certain groups of contracts are
 26 accumulating large claim expenses or unpaid claim liability balances.

27 39. Acceptable qualitative factors may include whether a group of contracts is of immediate
 28 concern to constituents, politically sensitive, and/or controversial.

29 40. The following information should be provided for insurance portfolios selected for
 30 disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or
 31 insurance contracts:

32 a. A description of what is insured or guaranteed, for whom, and what other
 33 government agencies and/or commercial insurance programs administer or
 34 assume risk for any part of the program.

¹⁷ If a series of events causing loss begins prior to the reporting date, and additional pending events are required to result in losses, then it is not considered an adverse event and should not be included in the estimated settlement costs for IBNR.

¹⁸ Any amount expected to be recovered in excess of the recognized claim, which will result in a gain, should not be recognized until any contingencies relating to the recovery have been resolved because a contingent gain cannot be recognized until realized.

b. A narrative description of nonexchange revenue collected, if it covers the full estimated costs to settle claims, and, whether other funding sources, such as appropriations, are needed.

41. The following information should be provided for insurance portfolios selected for disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or insurance contracts for:

a. Gross cost:

- i. Claims expense
- ii. Claims adjustment expense
- iii. Recoveries
- iv. Interest expense
- v. Losses or gains on remaining coverage
- vi. Other gross costs

b. Total Gross Cost:

- i. Nonexchange revenue
- ii. Appropriations used
- iii. Other financing sources

c. Change in net position

42. Changes in the liability balance for unpaid insurance claims should be provided for insurance portfolios selected for disaggregated disclosure, and/or aggregated for all remaining insurance portfolios, and/or insurance contracts as follows:

- a. Beginning balance
- b. Incurred claims attributable to insured adverse events of:
 - i. the current fiscal year, and
 - ii. prior fiscal years
- c. Payments attributable to insured adverse events of:
 - i. the current fiscal year, and
 - ii. prior fiscal years
- d. Recoveries and other adjustments
- e. Ending balance

43. A narrative discussion consolidated for all insurance portfolios—or a reference to one to avoid duplication of disclosures—should be provided for:

- a. borrowing authority including but not limited to: balances, interest expense, repayment requirements, the ability to repay borrowing used to fund insurance claims, financing sources for repayment, and other terms of borrowing authority used in accordance to already existing standards.
- b. investment activities,
- c. appropriations requested, used, and/or available to return to Treasury, and

- d. any event(s) that caused a material change in the required disclosures, such as low probability high impact adverse events, changes in laws and/or actuarial assumptions.

FINANCIAL REPORT OF THE US GOVERNMENT DISCLOSURES

44. The U.S. government-wide financial statements should disclose the following information separately for exchange, nonexchange and life insurance programs.¹⁹

- a. a broad description of insurance programs included in the category,
- b. a general reference to component reporting entity²⁰ reports, and
- c. balances for each of the following, including detail for each significant individual insurance program:
 - i. liability for unpaid claims,
 - ii. liability for losses on remaining coverage,
 - iii. total net cost for exchange and life insurance programs,
 - iv. total gross cost for nonexchange programs,
 - v. borrowing by programs and a narrative discussion of repayment requirements including the ability to repay the borrowing, and
 - vi. The amount of insurance in-force at the end of the reporting period and the appropriate information to aid in avoiding the misleading inference that there is a more than remote likelihood of a loss of that amount.

- Deleted:** by insurance
- Deleted:** category
- Deleted:** or selected portfolios of insurance
- Deleted:** break out for insurance programs that are material
- Deleted:** schedule of material
- Deleted:** <#>unearned premiums,¶

Deleted: <#>gross claims expense and related earned revenue,¶

Deleted: the amount of coverage provided through insurance in force at the end of the reporting period, including:¶
 <#>a narrative discussion that this amount represents the maximum risk exposure during the remaining contract period, and ¶

¹⁹ Disclosure is "Reporting information in notes or narrative regarded as an integral part of the basic financial statement."

²⁰ The term "component reporting entity" is used to distinguish between the U.S. Federal government and its components. The U.S. Federal government is composed of organizations that manage resources and are responsible for operations. These include major departments and independent agencies, which are generally divided into sub organizations, i.e., smaller organizational units with a wide variety of titles, including bureaus, administrations, agencies, and corporations

1 **APPENDIX A: BASIS FOR CONCLUSIONS**

2 **PLACE HOLDER**

3 This appendix discusses some factors considered significant by Board members in reaching the
 4 conclusions in this Statement. It includes the reasons for accepting certain approaches and
 5 rejecting others. Individual members gave greater weight to some factors than to others. The
 6 standards enunciated in this Statement—not the material in this appendix—should govern the
 7 accounting for specific transactions, events, or conditions.

10 **APPENDIX B: ILLUSTRATIONS**

11 This appendix is for illustrative purposes only and is not authoritative.

12 **ILLUSTRATION I: Exchange Revenue Insurance Program Disclosure**

	FY 2XX1	FY 2XX0
Net Position, beginning of Period	\$XXX	\$XXX
Gross cost of:		
Claims expense	(XXX)	(XXX)
Claims adjustment expenses	(XXX)	(XXX)
Recoveries	XXX	XXX
Interest expense	(XXX)	(XXX)
Losses on remaining coverage	(XXX)	(XXX)
Other gross costs	(XXX)	(XXX)
Total gross costs	(\$XXX)	(\$XXX)
Exchange Revenue:		
Premiums earned	XXX	XXX
Interest earned	XXX	XXX
Net Cost	(\$XXX)	(\$XXX)
Nonexchange revenue	XXX	XXX
Appropriations used	XXX	XXX
Other financing sources	XXX	XXX
Change in net position, end of period	\$XXX	\$XXX

1 APPENDIX C: ABBREVIATIONS

2 | PLACE HOLDER

3

4	CFR	Consolidated financial report of the U.S. government
5	ED	Exposure draft
6	FASAB	Federal Accounting Standards Advisory Board
7	FASB	Financial Accounting Standards Board
8	GAAP	Generally Accepted Accounting Principles
9	GAO	Government Accountability Office
10	GASB	Governmental Accounting Standards Board
11	IPSASB	International Public Sector Accounting Standards Board
12	OMB	Office of Management and Budget
13	SFAS	Statement of Financial Accounting Standards (FASB)
14	SFFAC	Statement of Federal Financial Accounting Concepts
15	SFFAS	Statement of Federal Financial Accounting Standards

16

17 APPENDIX D: GLOSSARY

18 | PLACE HOLDER

19
20

TAB E – Appendix A

(Optional Reading for Reference)

Risk Assumed: Insurance Programs

Project Decision History and Milestones

Risk Assumed: Insurance Programs Project Decision History and Milestones

April 2015:

Staff continued to review the updated proposed insurance standards at the April 2015 Board meeting.

The Board approved the following items:

- The adverse event and IBNR definitions in order to clarify the recognition and measurement of claims incurred but not recorded (IBNR).
- The wording...*“Estimates should be based on ... using all available information that existed at the balance sheet date, experience with previous transactions and historical trends, and, as appropriate, the views of independent experts...”* in the recognition and measurement of the liability for losses on remaining coverage.

The Board identified the following changes:

- Liability for unpaid losses: provide more clarity about the timing of a series of events to address the recognition and measurement of IBNR.
- Liability for losses on remaining coverage:
 - Update subsequent event disclosure requirement in reference to SFFAS 39 because events that happen after the balance sheet are subsequent events that will not be recognized.
 - Remove expected cash flows as a single measurement model and replace it with wording such as...*probability assessments affected by trends to determine the most likely estimate, or, if a most likely estimate is not available, then use the expected cash flow method.*
 - Avoid using the word “contingency”—which will remain in SFFAS 5—because this liability is comparing the estimated losses to unearned premiums, whereas SFFAS 5 speaks only to liabilities.
- Premium pricing disclosure: remove the word subsidy and subsidy rate, reword, and provide an illustration.
- “Condensed” insurance program disclosure: reference disclosures that are already available in audited financial statements.

- Consolidated Financial Report disclosures: remove unearned premiums and gross claims and related earned revenue, and reword information about insurance in force.

February 2015:

The Board reviewed the proposed standards during the February 2015 meeting and approved the following:

Scope Section #2: add qualifying language to address accounting for such items as borrowing, investing, and appropriations that are found in other Statements to the new sentence—*Matters not addressed in this Statement should be reported in accordance with other standards.*

Criteria for Insurance Programs:

1. Include **a.i.** in the basis for conclusions.
2. Move **a.ii.** criteria as follows:
 - Exchange criteria is now included in the premiums definition,
 - Nonexchange will be presented in a future version,
 - Recoveries is now its own definition, and
 - Investment income and budget authority is included in the disclosure section.
3. Consolidating **a.iii – v** criteria into the insurance contract definition

Insurance Program Classifications: staff will conduct more research to identify and present classifications that will capture all current and future insurance programs.

Liability for Losses for Remaining Coverage: adopt the name Liability for Losses for Remaining Coverage instead of Liability for Premium Deficiency.

Disclosure for Breaking out Insurance Program Information:

- “Major” in relation to “*For each major insurance program*” is hard to define in relation to materiality,
- FASAB, as a standard setting body, cannot define “program,” and “Major category of insurance,” might work better.
- Staff will continue to work on what detail to include and at what level to report it for the component and consolidated financial report (CFR).

Revenue and Measurement: remove the word the word “liability” from unearned revenue.

Paragraph 16: change the word “billed” to “collected or due.”

Paragraph 17: remove paragraph 17 because future adjustments to premiums based on experience ratings should be recognized as normal premium revenue over the contract period and is covered in paragraph 15.

Paragraph 18b: restate the second sentence to read: *Recoveries should **not** be recognized as revenue, but rather as reductions of claims expense.*

Paragraph 21: change the word “less” to “over:”

Paragraph 21 a & d: delete the word “probable” and focus on measuring liabilities using the expected value of estimated outflows net of remaining insurance coverage recognized at the end of the reporting period.

Paragraph 21.b: change 21.b. to read: *Management’s judgment based on experience, and in some cases, the views of independent experts.*

Paragraph 21.e: remove a reference to a range because paragraph 21 will be rewritten to focus on the expected value and all numbers for expected value carry the same weight.

Paragraph 22: update paragraph 22 to read: *Adjustments to the liability for remaining insurance coverage should be recognized as losses **or gains** on remaining insurance coverage.*

Paragraph 23: include a brief description of the insurance programs similar to the standards for loan programs.

Paragraph 23.c: change “paid claims” to “payments.”

December 2014:

Claims Adjustment Expenses: The Board approved including Claims Adjustment Expenses in the Liability for unpaid claims if they are related to claims.

Liability for Premium Deficiency/Net Future Losses: The Board approved including a Liability for Premium Deficiency in addition to the Liability for Unpaid Claims.

Additional Items:

The Board approved:

- Differentiating between insurance programs who receive appropriations to finance subsidies and those who borrow to finance subsidies,

- Classifying revenue for insurance programs that receive subsidies as exchange or non/exchange revenue, and
- Distinguishing between short-duration and long-duration insurance contracts.

October 2014:

Borrowing Disclosure: The Board decided to require insurance programs to disclose their borrowing authority, borrowing balances, interest expense, the ability to repay the borrowing, and explain any material differences in accordance with SFFAS 1, SFFAS 5, and SFFAS 7, but will not prescribe how or where the program will logistically place the disclosures.

Earned/Unearned Premiums: In relation to recognizing and disclosing earned and unearned premiums, the Board directed staff to begin with the revenue standards available in SFFAS 7, paragraphs 36–37, and include in the new standards guidance specific to insurance contracts but consistent with SFFAS 7.

Proposed Standard: In relation to the wording for the proposed standard, staff noted that the criteria for insurance programs will most probably be moved to the Basis for Conclusion section because it did not add anything to the insurance program definition.

The Board requested that staff:

- Rewrite paragraph 19 to allow for more flexibility in aggregating types of insurance programs
- Merge 19a and 19b in order to reduce duplicity and tie any explanations for material differences to the chart line items.
- Rewrite 19g to request a disclosure on how premium prices are determined and contribute to managing risk.

August 2014:

The Board approved changing the name of this phase to Risk Assumed: Insurance Programs.

The Board approved the following definition, criteria, and exclusions:

A. DEFINITION:

Insurance programs¹ are authorized by law to accept all or part of the risk for losses incurred by a designated population of beneficiaries as a result of an adverse event by financially compensating them.

B. CRITERIA:

- Insurance programs are administered by an agency established to do so or within an agency that administers many programs.
- Insurance programs collect exchange or non-exchange revenue that may be earned through, but is not limited to, any or all of the following: premiums,² fees paid, excise taxes, penalties and/or fines, recoveries,³ interest received from investments and/or receivables, and/or budget authority including appropriations and borrowing authority.⁴
- Insurance programs create an agreement⁵ or arrangement that specifically states:
 - the role the program will play,
 - who the parties are that may contribute funding,
 - the designated population that may be beneficiaries and their responsibilities for receiving compensation for losses,⁶
 - funding requirements,
 - financial compensation to be paid,
 - the adverse event (other than a defaulted debt obligation), and
 - if and how much to place in reserves.
- Insurance programs assume risk for the uncertainty of an adverse event occurring (other than a defaulted debt obligation), and the amount of compensation expected to be paid for losses.
- Through insurance programs the federal government assumes:

¹ Insurance programs will also include guarantee programs not designed for loan/debt guarantees.

² The term “premiums” will be used to mean premiums, fees paid, excise taxes, penalties and/or fines.

³ Recoveries may be monies recouped or recovered from: (1) another agency through an indemnification agreement, (2) a third party or commercial insurance company to repay all or part of a loss originally paid for by the program, and/or (3) the sale of salvageable parts through acquisition and disposal or salvage of assets. Recoveries may also be adjustments to already paid claims where the claimant owes money back to the program for a loss that wasn’t realized.

⁴ Sources of funding are broad and the charging of “premiums” (or other fees) is not necessary for a program to qualify as an insurance program.

⁵ Insurance programs may enter into explicit arrangements or agreements with specific individuals, state, local, or foreign governments, other federal agencies, or businesses to carry out their mission.

⁶ Beneficiaries may or may not directly participate in an explicit agreement/arrangement prior to becoming eligible to receive compensation. An example where a beneficiary does directly participate and receives compensation is when a U.S. investor purchases risk insurance for political violence and upon an act of politic violence that impacts their business investment may receive compensation. An example where beneficiaries do not directly participate is when a service provider pays premiums directly to a federal insurance program and upon failure provides a list of customers as beneficiaries whom the program may compensate.

- all risk for covered losses;
- partial risk by filling a gap where commercial Insurance companies are not able or willing to provide the insurance; or
- a timing risk wherein the insurance program provides compensation for losses at the time claims are received and processed in anticipation that future funding sources will be sufficient to cover all or part of past benefits paid.

C. EXCLUSIONS:

- a. Loan guarantee programs as defined in SFFAS 2 (as amended) are not included as insurance programs.
- b. Social insurance programs as defined in SFFAS 17 (as amended) are not included as insurance programs.⁷
- c. Disaster relief programs that provide discretionary funding, goods, and/or services are not included as insurance programs.⁸
- d. Entitlement programs that administer eligibility requirement applications to provide means tested benefits are not included as insurance programs.
- e. “Self-insurance,” where the government assumes the risk of loss for some its own activities⁹ is not included as insurance programs.
- f. Programs whose missions are not by statute to provide insurance but which process claims through an administrative or judicial process¹⁰ are not included as insurance programs.
- g. Programs whose missions are not by statute to provide insurance but which provide security against loss or damage through contractual indemnification of another party¹¹ are not included as insurance programs.

Insurance in Force: The Board agreed to disclose insurance in force—the amount the program would pay out if all contracts experienced maximum loss for the remaining coverage at the end of the reporting period.

⁷ Includes unemployment insurance as this is captured also in SFFAS 17.

⁸Criteria updated due to discussion with Chairman Allen concerning funding that was provided to Washington State mud slide victims in addition to goods and services. In addition, it is the Stafford Act that authorizes and regulates disaster relief programs

⁹ GAO, Catalogue of Federal Insurance Activities, GAO-05-265R, page 4.

¹⁰An example is an administrative settlement of tort claim resulting from military events.

¹¹These are administrative settlements for transactions occurring by contractors with FAR authorized indemnification clauses or first responders within programs that do NOT have a statutory insurance or guarantee mission.

Projections: The Board tentatively agreed not to require projections for insurance programs. However, the Board did agree that the issue for projections would remain open, because they might want to address it for other types of programs in future phases of the risk assumed project.

April 2014

The Board revisited the definition and reviewed the similarities and differences with loan guarantee programs under the Federal Credit Reform Act and asked staff to address the following questions/concerns:

- 1) Distinguish insurance/non-loan guarantee programs from loan guarantee programs in the definition.
- 2) What value does the term “non-loan guarantees” add? Can it be removed from the definition?
- 3) Clarify the exclusion of disaster relief programs in relation to the type of compensation provided.

March 2014:

The Board generally agreed with the insurance/non-loan guarantee definition, upon updates from Mr. Dacey, as well as the characteristics and exclusions presented in the staff memo with the understanding that as staff develops the standard and new information is discovered changes are possible and will be finalized within the standard.

Staff worked with Mr. Dacey to update some of his concerns with the definition.

The following is the revised definition:

A federal insurance/non-loan guarantee program is a program authorized by law to accept all or part of the risk by financially compensating the designated population for losses incurred as a result of an adverse event as defined by the:

- A. law or otherwise enforceable by law,
- B. related regulations,
- C. agency policies, or
- D. explicit arrangements or agreements

December 2013:

1. The Board agreed with staff's recommendation that it would be difficult to apply the FASB proposed insurance contracts definition to federal insurance/guarantee programs
 - Board requested and Staff agreed to present FASB's proposed definition to the Task Force during the development of the federal definition
2. The Board agreed with Staff's next step to develop a general definition and specific characteristics of insurance and guarantee programs.

June 2013:

1. The Board agreed with staff's recommendation to ask the four federal entities identified to respond to specific questions on FASB's insurance contracts proposal. Staff would use those responses to identify application concerns that would be unique to a federal entity.
2. The Board agreed to further narrow the scope to federal insurance and guarantee **programs** rather than contracts to support the structure of the federal environment and president's budget.

February 2013:

The risk assumed project will be addressed in a **phased approach**:

- Phase I: Insurance and Guarantees
- Phase II: Entitlement Programs, including: national defense, security and disaster response; and other potential effects on future outflows, such as regulatory actions, GSE's, etc.
- Phase III: Commitments and Obligations and other risk areas