



February 13, 2015

**Memorandum**

To: Members of the Board

*Robin M. Gilliam*

From: Robin M. Gilliam, Assistant Director

*Wendy M. Payne*

Director Through: Wendy M. Payne, Executive Director

Subject: Risk Assumed—Insurance Programs [Phase 1]—**TAB G**<sup>1</sup>

**MEETING OBJECTIVE**

To review and approve the revised draft of the proposed standards.

**BRIEFING MATERIALS**

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

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

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<sup>1</sup> 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**

### **Insurance Program Education Session:**

At the December 2014 meeting, representatives from the following insurance programs presented an education session about their current reporting of revenue from premiums, unearned revenue, and estimated losses:

Department of Agriculture (USDA), Risk Management Agency (RMA), Federal Crop Insurance Corp (FCIC):

- Margo E. Erny, Chief Financial Officer (CFO)
- Michael Drewel, Accounting Officer
- Shanda Sander, Special Assistant to CFO
- Tom Worth, Senior Actuary

Department of Homeland Security (DHS), Federal Emergency Management Agency (FEMA), National Flood Insurance Program (NFIP):

- Jennifer Raab, Accountant , OCFO, Financial Statements and Reporting Branch
- Thomas Hayes, Chief Actuary

Department of Transportation, Federal Aviation Administration (FAA), Aviation Insurance Program: Tom Brown, Insurance Examiner

Presentations are available at: <http://www.fasab.gov/projects/active-projects/risk-assumed/>

### **Claims Adjustment Expenses:**

The Board discussed and approved including Claims Adjustment Expenses (CAE) in the Liability for Unpaid Claims if an insurance program's CAE are related to and calculated based on outstanding claims.

### **Liability for Premium Deficiency:<sup>2</sup>**

The Board discussed and approved including a Liability for Premium Deficiency in addition to the Liability for Unpaid Claims. However, the Board suggested further consideration in the following areas:

- 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.

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<sup>2</sup> The name of this liability to be discussed in section IV

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## STAFF ANALYSIS AND RECOMMENDATIONS FOR PROPOSED STANDARDS

### I. Scope Section

#### Staff Analysis

During the October/December 2014 meetings, the Board determined that the following items be included and expanded upon where necessary, but in accordance to other standards:

- Earned/Unearned Premiums
- Borrowing Disclosure
- Appropriations used or returned, and
- Investments and interest earned.

#### Staff Recommendation

Staff recommends including a general statement in the scope section to address that all matters not addressed in this Statement be reported in accordance with other standards.

Therefore, staff revised the scope (number 2) as follows:

This Statement provides general principles that should guide preparers of GPFFRs in accounting for and reporting on premium revenue, related claims and liabilities and other losses of insurance programs. **Matters not addressed in this Statement should be reported in accordance with other standards.**

**Question 1:** Does the Board agree with the revised scope section?

## II. Definitions Section:

### Staff Analysis

During the October 2014 Board meeting, staff recommended moving the *criteria for insurance programs* from the definition of insurance programs [page 3, 4.a] to the basis for conclusions. Some Board members did not agree with that recommendation.

The following was included in the October 2014 proposed standards:

#### **a. Criteria for Insurance Programs**

- i. *Insurance programs are administered by an agency established to do so or within an agency that administers many programs.*
- ii. *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, fees paid, assessments, excise taxes, penalties and/or fines, recoveries, interest received from investments and/or receivables, and/or budget authority including appropriations and borrowing authority.*
- iii. *Insurance programs create a contract, such as an agreement or arrangement, that specifically states:*
  1. *the role the program will play,*
  2. *who the parties are that may contribute funding,*
  3. *the designated population that may be beneficiaries and their responsibilities for receiving compensation for losses,*
  4. *funding requirements,*
  5. *financial compensation to be paid,*
  6. *the adverse event (other than a defaulted debt obligation).*
- iv. *Insurance programs assume risk for the uncertainty of an adverse event occurring and the amount of compensation expected to be paid for losses.*
- v. *Through insurance programs the federal government assumes:*
  1. *all risk for covered losses;*
  2. *partial risk by filling a gap where commercial Insurance companies are not able or willing to provide the insurance; or*
  3. *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.*

**Staff Recommendation**

The criteria for insurance programs were so broad that they would not exclude or include any programs meeting the basic definition. Hence the criteria would have no effect. Except for a.i—as noted below—staff recommends including the following criteria in other definitions:

1. Staff will include **a.i.** in the basis for conclusions because Board members pointed out that most insurance programs are *administered by an agency established to do so or within an agency that administers many programs* and does not need to be a specific criteria for insurance programs.
2. Staff consolidated the criteria in **a.ii.** into the premiums definition.
3. Staff consolidated the criteria in **a.iii – v** into the insurance contract definition.

**Question 2:** Does the Board agree with how the criteria for insurance programs were modified?

### **III. Insurance Program Classifications - Recommended Structure for Proposed Standards**

#### **Staff Analysis**

During the December 2014 meeting discussion about the liability for premium deficiency, the Board directed staff to distinguish between exchange and nonexchange revenue, and short-duration and long-duration contracts.

Staff discovered that most insurance programs engage in exchange transactions by collecting premiums, assessments, and/or fees. Some programs engage in nonexchange revenue by collecting excise taxes such as the Vaccine Injury Compensation Program (VICP) and/or using full subsidies followed by an excise tax to recapture amounts paid, such as the Terrorism Risk Insurance Act (TRIA).

In addition, while life insurance programs may engage in exchange transactions, they issue long-duration contracts.

#### **Staff Recommendation**

Staff recommends the following three classifications:

1. Exchange Transaction—Insurance (presented in Attachment I)
2. Exchange Transaction—Life Insurance
3. Nonexchange Transaction—Insurance

Note that staff intends to clarify application of the draft proposal's provisions to each of these three classes after definitions are developed for classes 2 and 3.

**Question 3:** Does the Board agree with the insurance program classifications?

#### IV. New Name for Liability for Premium Deficiency

##### **Staff Recommendation**

Staff recommends **Liability for Losses on Remaining Coverage** as the new name for the *liability for premium deficiency*. During the October/December 2014 meetings, the Board struggled with the name *liability for premium deficiency* because (1) it is designated by FASB to track the solvency of commercial insurance programs and (2) the timing of the estimate of the losses was confusing.

The name **liability for losses on remaining coverage** provides a clearer representation for estimating probable losses on contracts that are still open at the end of the reporting year for their remaining coverage.

**Question 4:** Does the Board approve the name Liability for Losses for Remaining Coverage?

**V. Disclosure for Breaking Out Insurance Program Information:**

**Staff Analysis**

At the February 2013 meeting, the Board approved moving into a phased approach for risk assumed, with insurance to be addressed in the first phase. Through research with the task force and our December 2014 education session, staff understands that risk is not a single number. Risk assumed revolves around how much revenue is collected and dedicated to cover the many uncertainties and different risk factors covered by each federal insurance program.

Work done on the reporting model has also enlightened staff that users and preparers are looking for the FASAB to connect financial reporting with performance reporting.

**Staff Recommendation**

In order to understand the risk assumed by each insurance program, staff recommends a model based on SFFAS 27<sup>3</sup> (as amended by 43<sup>4</sup>) as presented in the following illustration.

	FY 2XX1	FY 2XX0
<b>ASSETS</b>		
Investments in Treasury securities	\$XXX	\$XXX
Other Assets	XXX	XXX
<b>Total Assets</b>	<b>XXX</b>	<b>XXX</b>
<b>LIABILITIES</b>		
Outstanding debt	\$XXX	\$XXX
Liability for unearned revenue	XXX	XXX
Liability for losses on remaining insurance coverage	XXX	XXX
Other liabilities	XXX	XXX
<b>Total Liabilities</b>	<b>XXX</b>	<b>XXX</b>
<b>Total Net Position</b>	<b>XXX</b>	<b>XXX</b>
<b>Total liabilities and net position</b>	<b>\$XXX</b>	<b>\$XXX</b>

<sup>3</sup> Statement of Federal Financial Accounting Standards 27: Identifying and Reporting Funds from Dedicated Collections (SFFAS 27).

<sup>4</sup> Statement of Federal Financial Accounting Standards 43: Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds (SFFAS 43).



	FY 2XX1	FY 2XX0
<b>CHANGE IN NET POSITION</b>		
Net position, beginning of period	\$XXX	\$XXX
Gross cost of:		
Claims	(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)
Premiums earned	XXX	XXX
Interest earned	XXX	XXX
Net costs	(XXX)	(XXX)
Appropriations used	XXX	XXX
Other financing sources	XXX	XXX
<b>Change in net position, end of period</b>	<b>\$XXX</b>	<b>\$XXX</b>

By presenting the operating picture of the program as connected to financial information, phase I gives the Board the opportunity to set a model for future risk assumed phases. In addition, the combined financial report (CFR) will be able to present a complete economic picture of federal insurance programs by utilizing this standardized break out for insurance program information.

**Question 5:** Does the Board approve the disclosure for breaking out insurance program information?

**VI. Additional Comments:**

**Question 6:** Does the Board have any additional comments on the proposed standards?

## **QUESTIONS FOR THE BOARD:**

**Question 1:** Does the Board agree with the revised scope section?

**Question 2:** Does the Board agree with how the criteria for insurance programs were modified?

**Question 3:** Does the Board agree with the insurance program classifications?

**Question 4:** Does the Board approve the name Liability for Losses for Remaining Coverage?

**Question 5:** Does the Board approve the disclosure for breaking out insurance program information?

**Question 6:** Does the Board have any additional comments on the proposed standards?

## **NEXT STEP:**

Continue developing the proposed exposure draft for insurance programs.

## **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](mailto:gilliamr@fasab.gov) with a cc to [paynew@fasab.gov](mailto:paynew@fasab.gov)

# **TAB G – Attachment 1–**

## **Risk Assumed—Insurance Programs**

### **Proposed Standards**

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## PROPOSED STANDARDS

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### SCOPE

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1. This Statement applies to federal entities that present general purpose federal financial reports (GPFGRs), including the consolidated financial report of the U.S. Government (CFR), in conformance with generally accepted accounting principles (GAAP), as defined by paragraphs 5 through 8 of Statement of Federal Financial Accounting Standards (SFFAS) 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.
2. This Statement provides general principles that should guide preparers of GPFGRs in accounting for and reporting on premium revenue, related claims and liabilities, and other losses of insurance programs. Matters not addressed in this Statement should be reported in accordance with other standards.
3. This Statement rescinds the section: Insurance and Guarantee Programs in Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of The Federal Government*, paragraphs 97-121.

### DEFINITIONS

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4. **Insurance program**—“Insurance program” (program) is used broadly to refer to a program that is authorized by law to accept all or part of the risk for losses by financially compensating a designated population of beneficiaries who incur losses as a result of an adverse event.
5. The following are excluded from Insurance Programs:
  - a. Programs that administer direct loans and loan guarantees.<sup>1</sup>
  - b. Programs that qualify as social insurance.<sup>2</sup>
  - c. Disaster relief programs.
  - d. Entitlement programs
  - e. Programs whose missions are not by statute to provide insurance but which self-insure their own programs.<sup>3</sup>
  - f. Programs whose missions are not by statute to provide insurance but which process claims through an administrative or judicial process.<sup>4</sup>

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<sup>1</sup> Statement of Federal Financial Accounting Standards 2 (SFFAS 2): Accounting for Direct Loans and Loan Guarantees

<sup>2</sup> Programs identified in the Statement of Federal Financial Accounting Standards 17 (SFFAS 17): Accounting for Social Insurance including unemployment insurance.

<sup>3</sup> GAO, Catalogue of Federal Insurance Activities, GAO-05-265R, page 4.

- 1  
2 g. Programs whose missions are not by statute to provide insurance but which  
3 provide security against loss or damage through contractual indemnification of  
4 another party.<sup>5</sup>  
5
- 6 **6. Adverse event**—an “adverse event” may be a single or cyclical event or situation, except  
7 a default of a debt obligation, that causes losses to the beneficiary (ies) as identified in  
8 the insurance contract.
- 9 **7. Claim adjustment expenses (CAE)**—“Claim adjustment expenses (CAE)” are  
10 incremental costs directly attributable to investigating, settling, and/or adjusting claims.  
11 An incremental cost is one that would not have been incurred if the entity had no claims.  
12 These include but are not limited to legal and adjuster’s fees. CAE may be incurred by  
13 employees of the insurance program or through contracts.
- 14 **8. Contract period**—is the period over which adverse events that occur are covered.
- 15 **9. In Force**—contracts that are unexpired as of a given date.
- 16 **10. Incurred but not yet reported (IBNR)**—“Claims incurred but not yet reported (IBNR)”  
17 are estimated claims from adverse events that have occurred as of the end of the  
18 reporting period but have not yet been reported to the insurance program for settlement.
- 19 **11. Insurance claim**—an “insurance claim” is a formal request for payment for losses as  
20 authorized under the insurance contract.
- 21 **12. Insurance contract (contract)**— An “insurance contract (contract)” is a general term  
22 used for an explicit insurance or non-loan guarantee agreement or arrangement between  
23 an insurance program and specific parties such as but not limited to: individuals, state,  
24 local, or foreign governments, other federal agencies, or businesses.
- 25 a. A contract may include and/or identify:  
26 i. the term the insurance contract is in force; that is from inception until its  
27 termination date,  
28 ii. the insurance program’s responsibilities,  
29 iii. the risk assumed by the insurance program as:  
30 1. all risk for covered losses;  
31 2. partial risk by filling a gap where commercial Insurance companies  
32 are not able or willing to provide the insurance; or  
33 3. a timing risk wherein the insurance program provides  
34 compensation for losses in anticipation that future funding sources  
35 will be sufficient to cover all or part of past benefits paid.  
36 iv. the adverse event,  
37 v. the insured party(ies) and their premium requirements,

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<sup>4</sup>Examples may include: 1) an administrative settlement of tort claim resulting from military events, and 2) GSA self-insuring their vehicle fleet instead of using a commercial insurance company.

<sup>5</sup>These 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.

- vi. the beneficiary(ies) and their responsibilities for filing claims, and/or
- vii. the financial compensation.

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

**14. Recoveries**—“ Recoveries” may be 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.

## RECOGNITION AND MEASUREMENT

### REVENUE AND LIABILITY FOR UNEARNED PREMIUMS

**15.** Premiums should be recognized as revenue evenly over the contract period in proportion to the amount of insurance protection provided.

**16.** A liability for unearned premiums should be recognized for the amount of premiums billed by the end of the reporting period that have not yet been earned in proportion to the insurance protection provided during the remaining contract period.

**17.** If premiums are adjusted after the contract period as a result of, but not limited to, claim experience or other experience ratings, the adjustment should be recognized in the reporting period during which the adjustment is made.

### CLAIMS EXPENSE AND 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 reestimated at the end of each reporting period.

- a. The estimated settlement amount includes outflows to liquidate claims that have been reported but not paid, estimated claims incurred but not reported (IBNR), related estimated claim adjustment expenses, and estimated inflows from recoveries not yet realized at the end of the reporting period.

1           b.       If an estimated recovery exceeds the related claim(s) then recognition is limited  
 2                   to the amount of the related claim.<sup>6</sup> Recoveries are not recognized as revenues  
 3                   since they reduce claims expenses.

4   **19.**   Adjustments to the liability for unpaid insurance claims, other than those resulting from  
 5           payments made to liquidate existing liability balances, should be recognized as claims  
 6           expense.

7   LOSSES ON REMAINING INSURANCE COVERAGE AND LIABILITY FOR  
 8   REMAINING INSURANCE COVERAGE

9  
 10  
 11   **20.**   A liability for remaining insurance coverage should be recognized at the end of the  
 12           reporting period if:

13           a.       A net future outflow or other sacrifice of resources during the remaining open  
 14                   contract period is probable, and

15           b.       The net future outflow of sacrifice of resources is measurable.

16   **21.**   The amount of the liability is the excess of the estimated settlement amount for probable  
 17           claims to be incurred during the remaining open contract period less the unearned  
 18           premium at the end of the reporting period. The following should be considered in  
 19           estimating the liability amount:

20           a.       Claims are probable if it is more likely than not that an adverse event will occur  
 21                   during the remaining open contract period for which beneficiaries will be eligible  
 22                   to receive compensation.

23           b.       Management’s judgment supplemented by experience with similar transactions  
 24                   and, in some cases, the views of independent experts will be needed.

25           c.       The probability of future claims is determined by considering a portfolio of  
 26                   contracts rather than individual contracts. A portfolio includes insurance contracts  
 27                   that:

- 28                   i.       Are subject to similar risks, and
- 29                   ii.      Have a similar duration of coverage.

30  
 31           d.       If the portfolio includes a large population of contracts, outflows may be  
 32                   estimated by weighing all possible outcomes by their associated probabilities;  
 33                   that is, the expected value.

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<sup>6</sup> 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 e. If the estimate is a range of amounts and, if due to uncertainty, no amount within  
 2 the range is a better estimate than any other amount within the range, then using  
 3 the mid-point of the range is appropriate.
- 4 f. If the effect of the time value of money is material, the estimated outflow should  
 5 be discounted. (See SFFAS 33, par. 28 - 32 for guidance on selecting discount  
 6 rates.)
- 7 **22.** Adjustments to the liability for remaining insurance coverage should be recognized as  
 8 losses on remaining insurance coverage.

9 **DISCLOSURE REQUIREMENTS**

- 10 **23.** For each major insurance program and collectively for all other insurance programs the  
 11 following information should be disclosed:
- 12 a. Condensed information about the balances at the end of the reporting period for  
 13 assets, liabilities, and net position, including at a minimum balances for :
- 14 i. Investments in Treasury securities,  
 15 ii. Outstanding debt (borrowing),  
 16 iii. Liabilities for:  
 17 1. unearned revenue,  
 18 2. unpaid claims, and  
 19 3. losses on remaining insurance coverage.  
 20  
 21
- 22 b. Condensed information about the net cost and change in net position for the  
 23 reporting period, including at a minimum amounts for:  
 24  
 25 i. Gross cost:  
 26 1. Claims  
 27 2. Claims adjustment expense  
 28 3. Recoveries  
 29 4. Interest expense  
 30 5. Losses on remaining coverage  
 31 6. Other gross costs  
 32
- 33 ii. Premiums earned  
 34 iii. Interest earned  
 35 iv. Net costs  
 36 v. Appropriations used  
 37 vi. Other financing sources  
 38 vii. Change in net position  
 39

- 1 c. Changes in the liability balance for unpaid insurance claims, as follows:
- 2 i. Beginning balance
- 3 ii. Incurred claims attributable to insured adverse events of:
- 4 1. the current fiscal year, and
- 5 2. prior fiscal years
- 6 iii. Paid claims attributable to insured adverse events of:
- 7 1. the current fiscal year, and
- 8 2. prior fiscal years
- 9 iv. Recoveries and other adjustments
- 10 v. Ending balance
- 11
- 12 d. The liability for losses on remaining insurance coverage:
- 13 i. Key provisions of the program’s contracts including specific risk factors
- 14 that may influence the loss or range of loss.
- 15 ii. The basis, methods, and/or assumptions used in estimating the liability
- 16 for losses on remaining insurance coverage or a statement that the
- 17 amount is not measurable.
- 18 iii. If the recognized amount is based on a range of amounts rather than a
- 19 specific amount, the range and the relationship of the recognized
- 20 amount to the range (for example, whether the recognized amount is a
- 21 better estimate than the other amounts in the range or represents the
- 22 mid-point of the range).
- 23 iv. A narrative discussion about the premium pricing policies (in
- 24 accordance with SFFAS 7, par. 46) including the information about risk
- 25 characteristics used in determining premiums.
- 26 v. Other information that would provide an understanding of the nature,
- 27 magnitude, and specific risk factors in calculating the liability for
- 28 remaining insurance coverage.
- 29 vi. If losses on remaining coverage are reasonably possible but not
- 30 probable:
- 31 1. A discussion of the nature of the contingency and key risk
- 32 factors, and
- 33 2. A reasonable estimate of the loss exposure (which may be a
- 34 range) or a statement that the amount is not measurable
- 35 vii. The amount of coverage provided through insurance in force at the end
- 36 of the reporting period, an explanation that this amount represents the
- 37 maximum risk exposure during the remaining contract period, and

1 appropriate narrative to aid in avoiding the misleading inference that  
2 there is a more than remote likelihood of a loss of that amount.

3 e. A narrative discussion, or a reference to one, about borrowing authority including  
4 but not limited to: balances, interest expense, repayment requirements, the ability  
5 to repay borrowing used to fund insurance claims, financing sources for  
6 repayment, and other terms of borrowing authority used in accordance to already  
7 existing standards.

8 f. An explanation for any event(s) that caused a material change in the required  
9 disclosures, such as changes in laws and/or actuarial assumptions.

10  
11  
12

# **TAB G – Appendix A**

**(Optional Reading for Reference)**

## **Risk Assumed: Insurance Programs**

### **Project Decision History and Milestones**

# Risk Assumed: Insurance Programs Project Decision History and Milestones

## 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 programs<sup>1</sup> 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,<sup>2</sup>

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

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

fees paid, excise taxes, penalties and/or fines, recoveries,<sup>3</sup> interest received from investments and/or receivables, and/or budget authority including appropriations and borrowing authority.<sup>4</sup>

- Insurance programs create an agreement<sup>5</sup> 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,<sup>6</sup>
  - 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:
  - 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.

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<sup>3</sup> 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.

<sup>4</sup> 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.

<sup>5</sup> 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.

<sup>6</sup> 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.

### 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.<sup>7</sup>
- c. Disaster relief programs that provide discretionary funding, goods, and/or services are not included as insurance programs.<sup>8</sup>
- 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 activities<sup>9</sup> 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 process<sup>10</sup> 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 party<sup>11</sup> 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.

#### 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.

<sup>7</sup> Includes unemployment insurance as this is captured also in SFFAS 17.

<sup>8</sup> Criteria 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

<sup>9</sup> GAO, Catalogue of Federal Insurance Activities, GAO-05-265R, page 4.

<sup>10</sup> An example is an administrative settlement of tort claim resulting from military events.

<sup>11</sup> These 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.



### **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